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PRECONTRACTUAL LIABILITY IN EU AND CROATIAN LAW

Precontractual liability is not harmonised in EU law. Authors shall explore different models adopted in EU countries, EU soft law and compare that to the current state of Croatian law, especially after the adoption of the new Croatian Obligations Act in 2006. The article explores legal nature, scholarly writings, judicial practice and especially the extent of damages which may be awarded to the injured party based on precontractual liability in EU countries and under Croatian law. The crucial issue is whether a party can seek compensation of the reliance interest (negative interest) only or of the expectation interest (positive interest) as well.

Key words: *Culpa in contrahendo*.– *Precontractual liability*.– *Reliance interest*.– *Expectation interest*

1. INTRODUCTION

Precontractual liability or *culpa in contrahendo* differs in national laws and it is not harmonized until now in European Union (hereinafter: EU) countries. Authors shall examine whether Croatian legislature regulated precontractual liability, and conditions for its application. Special focus of the work is the extent of damages which a claimant may ask based on the precontractual liability. More precisely, authors shall seek the answer in judicial practice and legal literature whether claimant is entitled to ask recovery of damages for reliance interest and expectation interest. Reliance interest corresponds to negative interest of the party, where damage covers only expenses and loss caused

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to the injured party by its reliance on the misrepresentation, promise, or undertaking in question. Positive interest corresponds to expectation interest of the injured party that a contract shall be concluded and properly fulfilled. Possible solutions and proposal for further practice in Croatian law shall be explored based on EU legal sources which deal with issue of precontractual liability. Namely, authors shall compare solutions adopted in the Principles of European contract law (further in text: PECL),¹ Model Rules of Draft Common Frame of Reference (further in text: DCFR)² and Proposal for a Regulation of the European Parliament and of the Council on a Common European Sales Law (further in text: CESL).³

2. LEGAL NATURE OF PRECONTRACTUAL LIABILITY

While most of the EU civil law countries recognize precontractual liability in various models, common law countries traditionally do not.⁴ The issue of precontractual liability is not harmonised until now in EU countries. It depends on the applicable national law which of the different mechanisms of parties' protection shall apply.

- 1 Prepared by the Commission on European Contract Law, 1999, http://frontpage.cbs.dk/law/commission_on_european_contract_law/pecl_full_text.htm, last visited 10 July 2012.
- 2 Principles, Definitions and Model Rules of European Private Law, Draft Common Frame of Reference, Outline Edition, prepared by Study Group on a European Civil Code and The Research Group on EC Private Law (Acquis Group), http://ec.europa.eu/justice/contract/files/european-private-law_en.pdf, last visited 11 July 2012.
- 3 Proposal for a Regulation of the European Parliament and of the Council on a Common European Sales Law, COM(2011) 635 final, Brussels, 11. 10. 2011., <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2011:0635:FIN:EN:PDF>, last visited 10 July 2012.
- 4 J. Cartwright, M. Hesselink, *Precontractual liability in European Private Law*, Cambridge 2008, 457–461. For arguments that common law countries adopted mechanisms which have the same functions as the concept of precontractual liability see F. Kessler, E. Fine: „Culpa in contrahendo, bargaining in good faith, and freedom of contract: a comparative study“, 77 *Harv. L. Rev.*, 401. Authors argue that concepts of the increased duty to disclose, the concept of estoppel, the notion of an implied subsidiary promise, the colourful doctrine of „instinct with an obligation,“ all impose similar rights and obligations for the parties in negotiations as the culpa in contrahendo doctrine.

The origin of precontractual liability in EU civil law countries is the fundamental work of German author Jhering in 1861.⁵ His doctrine lies on the thought that although no contract between the parties exists in the stage of negotiations, they are still in some sort of legal relationship. This liability is routed in the principle of *good faith* and duty of care which is required from the parties not only in performing contractual duties, but also in the stage of negotiations and formation of the contract. Jhering's theory can be divided into two main premises. The first is that precontractual liability falls in the sphere of contract, where a party in breach commits contractual fault.⁶ It means that the injured party must prove that it suffered damage due to the *culpa* of the party in breach, where the degree of guilt is negligence.⁷ The second is that rules of tort liability should apply on the rules for recovering of damages, but that it should be restrained solely on the party's negative, i.e. reliance interest.⁸ Thus, Jhering's theory combines elements of contract and tort, both with defined limits.

Due to its immense influence on civil law countries, Jhering's theory resulted in different and often confusing solutions in EU countries. There are three predominant doctrines in EU national laws⁹ which define legal nature of the precontractual liability as: contractual,¹⁰ extra-contractual (tort)¹¹ or as a separate, third ground for civil liability.¹² However, only some jurisdictions actually adopted provisions which deal with precontractual liability,¹³ while many derive this doctrine from the general principles of law and apply it as a judge-

5 R. Jhering, „Culpa in contrahendo oder Schadenersatz bei nichtigen oder nicht zur Perfektion gelangten Verträgen“, *Jherings Jahrbücher für die Dogmatik des Bürgerlichen Rechts*. 4 1861.

6 Y. Ben-Dror, „The Perennial Ambiguity of Culpa in Contrahendo“, 27 *Am. J. L. Hist.*, 142, 193.

7 *Ibid.*, 147.

8 On Jhering's theory see F. Kessler, E. Fine, *op. cit. fn. 4*, 404; N. A. Nedzel, „A comparative study of good faith, fair dealing, and precontractual liability“ 12 *Tul. Eur. & Civ. L.F.* 97, 113; Y. Ben-Dror, *op. cit. fn. 6*, 149.

9 J. Cartwright, M. Hesselink, *op. cit. fn. 6*, 459.

10 For example Germany and Austria. See generally J. Cartwright, M. Hesselink, *op. cit. fn. 4*.

11 *Ibid.* For example France and Spain.

12 *Ibid.* For example Greece.

13 *Ibid.* For example Germany (from 2001), Italy, Portugal and Greece.

made doctrine.¹⁴ The most restrictive law on precontractual liability is considered to be English law since it does not recognize this type of liability at all, while the most expansive law is considered to be Dutch law, which under certain conditions even allows the compensation of expectation interest of the injured party.¹⁵

As to the extent of damages which may be rewarded, civil law countries are also greatly influenced by Jhering's doctrine. Almost all EU countries adopted in their judicial practice that the injured party may seek solely the recovery of reliance interest.¹⁶ Exception is Dutch law.¹⁷

In addition to the precontractual liability, a plaintiff could seek the remedy based on the unjust enrichment, misrepresentation, specific promise, general obligation of fair dealing and other.¹⁸ It is the same situation in Croatian law. However, boundaries between these liabilities are not always clear. For example, a party may choose to invoke precontractual liability or it can try to avoid precontractual liability by claiming pure tort liability. This would for example be the case where claimant would try to prove that the defendant had the intention to cause damage by conducting mock negotiations. Such a claim differs

14 *Ibid.* For example Austria, Switzerland, Denmark, Norway and Sweden.

15 J. Cartwright, M. Hesselink, *op. cit.* fn. 4, 461–470.

16 For example: Austria, Germany, France, Greece, Italy etc. See generally J. Cartwright, M. Hesselink, *op. cit.* fn. 4.

17 M. W. Hesselink, G. J. P. de Vries, *Principles of European Contract Law*, Hague 2001, 128. Landmark case decision for precontractual liability in Netherland is Dutch Supreme Court 18 June 1982, *Nederlandse Jurisprudentie* 1983, 723 (*Plas/Valburg*). In further cases (Dutch Supreme Court 23 October 1987, *Nederlandse Jurisprudentie* 1988, 1017 and 31 May 1991, *Nederlandse Jurisprudentie* 1991, 647) Dutch Supreme Court developed a special doctrine which recognizes three different stages of negotiations which have different legal consequences for the parties involved in negotiations. The specific solution of Dutch law is that in the so called third stage of negotiations the parties are no longer free to break-off the negotiations, and consequently, if a party in breach refuses to conclude the contract, the injured party may seek the compensation of the positive interest, i.e. the expectation interest. In order to be considered that negotiations are in this third stage, it is necessary that the injured party was entitled to expect that a contract which was bargained shall be concluded between the parties.

18 See generally in: E. A. Farnsworth, „Precontractual liability and preliminary agreements: fair dealing and failed negotiations“, 87 *Colum. L. Rev.*, 217; J. Cartwright, M. Hesselink, *op. cit.* fn. 4.

from precontractual liability because beside the allegation that the defendant conducted negotiations without the intention to conclude a contract it contains an additional claim that the defendant had an intention to cause damage (e.g. loss of profit). If claimant succeeds in invoking pure tort liability it may be able to seek both reliance interest and expectation interest, which can be much more favourable for him/her. However, these other grounds of liability fall outside the scope of this work.

3. PRECONTRACTUAL LIABILITY UNDER EU LEGAL SOURCES

Since Croatia belongs to the circle of civil law-based EU countries, authors shall examine whether EU legal sources and practice of the European Court of Justice (further in text: ECJ) provide any guide for unifying the approach for precontractual liability. Notably, EU legal sources which cover the issue of precontractual liability have non-obligatory legal nature, which means that they shall be applied solely if parties agree on their application. In addition, authors shall examine solutions adopted in CISG.

3.1. Precontractual liability under PECL

PECL is the first attempt to create common set of general principles of private law in EU countries, which greatly influenced the creation of DCFR.¹⁹ Precontractual liability is adopted in PECL as a particular application of the general principle of good faith.²⁰ As the main rule, PECL confirms that parties are free to negotiate without obligation to conclude the contract.²¹ However, PECL recognized exemptions from this rule, and it divided grounds for precontractual liability on liability for negotiations contrary to good faith in article 2:301 and on

19 See more in N. Jansen, R. Zimmermann, „Contract formation and mistake in European contract law: A genetic comparison of transnational model rules“, 31 *Oxford J. Legal Stud.*, 625.

20 H. Flechtner, „Comparing the general good faith provisions of the PECL and the UCC: appearance and reality“, 13 *Pace Int'l L. Rev.* 295, 306.

21 PECL explicitly provides that a party in negotiation „[...] is not liable for failure to reach an agreement.“ (article 2:301/1 of PECL).

liability for breach of the confidentiality in the course of negotiations in article 2:302.

Article 2:301 of PECL deals with situations where parties entered into negotiations but the contract was not concluded. In that case the party shall be liable if it conducted negotiations or broke off negotiations contrary to good faith.²² As a presumption, it is considered that a party acted in bad faith if it entered or continued negotiations „[...] with no real intention of reaching an agreement with the other party.“²³

The extent of damages based on this ground of precontractual liability is not precisely defined. PECL only provides that a party acting in bad faith is „[...] liable for the losses caused to the other party“.²⁴ Commentary of PECL, however, explicitly states that the injured party could ask solely the compensation of the reliance interest (negative interest), and in no way the expectation interest (positive interest).²⁵ Commentary decisively excluded the application of the article 9:502 of PECL on the negotiations,²⁶ which deals with general measures for damages where the compensation for the loss of profit, i.e. the expectation interest is included as well. Although expectation interest is excluded, extent of damages under the reliance interest is set broadly. It

22 Article 2:301/2 of PECL.

23 Article 2:301/3 of PECL.

24 Article 2:301/2 of PECL.

25 The Commission on European Contract law, O. Lando, H. Beale, *The Principles of European Contract Law, Parts I and II*, Hague 1999, 191. Also in D. Busch, E. Hondious, H. van Kooten, H. Schelhaas, W. Schrama (eds.), *The Principles of European Contract Law and Dutch law: A Commentary*, Nijmegen 2002, 130. For the commentary which supports that PECL does not allow to the injured party to seek expectation interest, but makes the comparison with Dutch law which allows the compensation of expectation interest if the parties entered into so-called third stage of negotiations see M. W. Hesselink, G. J. P. de Vries, *op. cit.* fn 17, 128. The same solution was already provided in UNIDROIT Principles of international Commercial Contracts which served as a role-model for PECL. See *UNIDROIT: Principles of international Commercial Contracts*, Rome 1994, 51. Two subsequently amendments of the UNIDROIT Principles with their official commentaries confirm this standpoint. For UNIDROIT Principles see generally R. Zimmermann, „The UNIDROIT Principles of international commercial contracts 2004 in comparative perspective“, 21 *Tul. Eur. & Civ. L.F.* 1, 5; E. A. Farnsworth, „Duties of Good Faith and Fair Dealing under the Unidroit Principles, Relevant International Conventions, and National Laws“, 3 *Tul. J. Intl. & Comp. L.* 47, 51 1995, 56.

26 The Commission on European Contract law, O. Lando, H. Beale, *op. cit.* fn 25, 191.

includes incurred expenses, work performed, loss of transactions made because of reliance that the contract shall be concluded and even the loss of opportunity.²⁷

Article 2:302 of PECL regulates situations where party disclosed confidential information²⁸ which were given in the course of negotiations or used them for its own purposes, regardless of whether the contract was subsequently concluded or not. Legal nature of this duty is considered to be contractual,²⁹ as it is expressly set by PECL. If not, the injured party would have to prove that there was an oral or written agreement between the parties not to disclose or use information which were considered as confidential. In each case, parties in negotiations should pay attention on defining which set of information are confidential, in order to avoid arguments that other party was not aware that certain information fall within the confidentiality requirement.³⁰

Remedy for the breach of confidentiality in the course of negotiations can include „[...] *compensation for loss suffered and restitution of the benefit received by the other party.*“³¹ Restitution of the benefit is a specific remedy, on which the injured party is entitled even in cases when no actual damage occurred.³²

3.2. Precontractual liability under CISG

CISG is the most important source today for international commercial sales contracts. However, CISG does not expressly govern the precontractual liability. Also, the predominant opinion of legal scholars

27 *Ibid.*

28 See generally about the need for protection of confidentially in the course of negotiations in: G. Forbin, „How is confidential information to be managed during precontractual negotiations?“, *I. B. L. J.*, 4/5 1998, 477–493; M. Fontaine, „Confidentiality clauses in international contracts“, *I. B. L. J.*, 1 1991, 3–94.

29 O. Lando, „The common core of European Private Law and the Principles of European Contract Law“, 21 *Hastings Int'l & Comp. L. Rev.* 809, 815.

30 However, it is argued that a party should be able to recognize which information should be kept as confidential, based on the judgment of the character of the given information and party's professional status, even if the other party did not expressly define it as confidential. See more in The Commission on European Contract law, O. Lando, H. Beale, *op. cit.* fn 25, 194

31 Article 2:302 of PECL.

32 The Commission on European Contract law, O. Lando, H. Beale, *op. cit.* fn 25, 194.

is that precontractual liability is not within the scope of the CISG.³³ The issue of existence, scope and extent of damages in precontractual liability are left for domestic law applicable to the contract.³⁴ It must be noted that there was a proposal for introducing the *culpa in contrahendo* into CISG, but the draftsmen of the CISG explicitly refused to incorporate it.³⁵

3.3. Precontractual liability in the practice of European Court of Justice

The practice of the ECJ is very scarce in the area of precontractual liability. The most relevant decision in this area was brought on 17 September 2002, C- 334/00 *Tacony v Wagner* [2002] ECR I-7357. The parties negotiated to conclude a contract for the delivery of a moulding plant but this never occurred allegedly due to the defendant's breach of his duty to negotiate honestly and in good faith. The Italian court referred to the ECJ with a preliminary question whether an action for precontractual liability falls under the regime of the Brussels I Regulation,³⁶ i.e. whether the precontractual duty falls under tort or

33 P. Schlechtriem, I. Schwenzer (eds.), *Commentary on the UN Convention on the International Sale of Goods (CISG)*, Oxford 2005, 182; A. H. Kritzer, *Guide to Practical Applications of the United Nations Convention on Contracts for the International Sale of Goods*, Hague 1994, <http://cisgw3.law.pace.edu/cisg/biblio/kritzer2.html#contract>, last visited 23 July 2012. For the detailed analysis of differing views on whether CISG covers the pre-contractual liability see L. Spagnolo, „Opening Pandora's Box: Good Faith and Precontractual Liability in the CISG“, 21 *Temp. Int'l & Comp. L.J.*, 261. For the opposite opinion see D. M. Goderre, „International negotiations gone sour: precontractual liability under the United Nations Sales Convention“, 66 *U. Cin. L. Rev.* 257. Author argues that precontractual liability is triggered under the doctrine of detrimental reliance in article 8(3) of the CISG.

34 For differing opinion see M. J. Bonell, „The UNIDROIT Principles of international commercial contracts and the harmonisation of International Sales Law“, 36 *R.J.T.* 335, 349; A. M. Garro, „The gap-filling role of the UNIDROIT Principles in international sales law: some comments on the interplay between the Principles and the CISG“, 69 *Tul. L. Rev.* 1149, 1169. Authors argue that the gap in CISG concerning the precontractual liability should be fulfilled by the application of the UNIDROIT Principles which govern the precontractual liability as previously described.

35 P. Schlechtriem, I. Schwenzer (eds.), *op. cit.* fn 33, 183.

36 Council Regulation (EC) No 44/2001 of 22 December 2000 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters, *Official Journal L 12*, 16.1.2001, p. 1–23.

contractual disputes in purpose of determining competent jurisdiction which should resolve the dispute (Italian or German court). ECJ qualified precontractual liability as a non-contractual obligation arising out of tort or delict for the purpose of determining jurisdiction.³⁷

Further, Rome II Regulation³⁸ puts precontractual liability in the sphere of non-contractual obligations as well. Besides the rule for determining the applicable law,³⁹ Rome II Regulation stipulates in paragraph 30 of the preamble that *culpa in contrahendo* should be treated as an autonomous concept and should not be necessarily interpreted within the meaning of national law. Although Rome II Regulation recognizes the specifics of precontractual liability, trying to detach it from the strict rules of national law, it is highly questionable that judges shall prefer some non-defined EU standards over national law, especially if the national law provides the rules for precontractual liability. Thus, the final outcome of the dispute depends heavily on the national law and its substantive rules on *culpa in contrahendo*.

3.4. Precontractual liability under DCFR and CESL

Final academic DCFR contains principles, definitions and model rules of European contract law. Legal nature of DCFR is ambiguous and legal authors dispute whether it is actually a draft for a European civil code or it is just a academic research which should facilitate in drafting such a code.⁴⁰ Three main purposes of DCFR are defined as: a possible model for a political Common Frame of Reference, legal science, research and education and as a possible source of inspiration.⁴¹ Regardless of its legal nature, parties can choose the application

37 C- 334/00 *Taccony v Wagner* [2002] ECR I-7357, para 26, 27

38 Regulation (EC) No 864/2007 of the European Parliament and of the Council of 11 July 2007 on the law applicable to non-contractual obligations (Rome II), *Official Journal L* 199, 31.7.2007, p. 40-49.

39 As the main rule for determining the applicable law to the dispute, Article 12 of Rome II Regulation provides: „*The law applicable to a non-contractual obligation arising out of dealings prior to the conclusion of a contract, regardless of whether the contract was actually concluded or not, shall be the law that applies to the contract or that would have been applicable to it had it been entered into.*“

40 For the dispute on the legal nature of DCFR see generally N. Jansen, R. Zimmermann, „A European civil code in all but name“: discussing the nature and purposes of the draft common frame of reference“, *C.L.J.*, 69(1) 2010, 98-112.

41 Principles, Definitions and Model Rules of European Private Law, Draft Common Frame of Reference, Outline Edition, *op. cit.* fn 2, 6-8.

of model rules on their contract, and thus, it is necessary to see how DCFR regulates precontractual liability.

DCFR regulates liability for negotiations in II.–3:301 and duty of confidentiality in negotiations in II.–3:301. These provisions have substantially the same approach as PECL and UNIDROIT Principles on precontractual liability. When comparing, it should be noted that DCFR contains some additional mechanisms for parties' protection. It is, thus, expressly stated that parties are not allowed to exclude or limit the liability for negotiations in bad faith.⁴² Also, in the duty of confidentiality, DCFR inserted definition on what should be considered as confidential information, where it is important that confidentiality of the information is presumed not only when one party expressly defined it as confidential, but also whenever „[...] *from its nature or the circumstances in which it was obtained, the party receiving the information knows or could reasonably be expected to know is confidential to the other party.*“⁴³ Additionally, DCFR explicitly gave the right to injured party to obtain a court injunction in order to prohibit the party in breach to disclose the confidential information.⁴⁴ DCFR are equally ambiguous as to the extent of damages,⁴⁵ though it is considered it includes the compensation of the reliance interest solely.⁴⁶

Although it was expected that DCFR shall serve as a starting point and a source of inspiration for new legislative proposals in the area of consumer law, as it is the current CESL, it has been argued that due to significant differences between them, „[...] *there has been no, or very little, interaction between the two projects.*“⁴⁷ In addition, the actual link between DCFR and CESL has officially not been clarified.

42 II.–3:301/2 of DCFR. The same approach is taken in PECL and UNIDROIT Principles, but DCFR explicitly inserted this provision in the wording of model rules.

43 II.–3:302/2 of DCFR.

44 II.–3:302/3 of DCFR. Again, commentators on PECL and UNIDROIT Principles consider that parties have this right, but DCFR explicitly provided for it, thus leaving no room for differing opinions.

45 M. J. Hesselink, „The common frame of reference as a source of European private law“, *Tul. L. Rev.*, 83 2009, 919, 952.

46 See in M. J. Doris, *Dispute Avoidance and European Contract Law: Dealing with divergence*, Groningen 2008, 49–52.

47 R. Zimmermann, „The present state of European private law“, *57 Am. J. Comp. L.* 479, 487.

The goal of CESL is to create a single horizontal instrument for the protection of consumers which would connect earlier directives on consumer protection.⁴⁸ CESL is currently in the phase of proposal, and it is still to be seen whether it shall finally be adopted.⁴⁹ If adopted, its application will be optional, i.e. it shall be applied on the contract solely by parties' choice.⁵⁰ The area of application is further defined by territorial, material and personal scope. As to territorial scope, CESL is applied to contracts with cross-border element, where at least one party has its habitual residence in one of the Member States.⁵¹ As to the personal scope, CESL can be applied to contracts between traders, and to consumer contracts.⁵² Finally, material scope of the application of CESL is restricted to the sale of goods contracts, contracts for the supply of digital content and their related services contracts.⁵³

CESL has no explicit provision for conducting negotiations in good faith or for breach of duty of confidentiality concerning the information given in the course of negotiations. Although precontractual liability is frequently mentioned in the wording of CESL, it relates exclusively to matters of which information is one trader obliged to provide to other trader or to consumer before concluding the contract,⁵⁴ which is particularly important in distant sales contracts. Consequently, if parties choose CESL as the set of rules applicable to their contract, national laws shall apply on the issue of existence, scope and damages which can be awarded for precontractual liability, unless otherwise agreed by the parties.

48 *Ibid.*

49 Proposal consists of three main parts: regulation, Annex I which contains the contract law rules and Annex II which contains standard information notice.

50 Article 3 of CESL.

51 Article 4 of CESL.

52 Article 1 of CESL.

53 Article 5 of CESL.

54 Sets of information which a trader is obliged to provide to a consumer before conclusion of a distant contract are provided from articles 13 – 21 of Annex I of CESL. These information include main characteristics of the goods, the total price and additional charges and costs, the identity and address of the trader, the contract terms, the rights of withdrawal etc. These articles have mandatory nature in the meaning that if the application of CESL is chosen, parties cannot derogate from these provision to the detriment of the consumer (Article 21 of Annex I of CESL). Sets of information which a trader is obliged to provide to another trader before conclusion of a contract are provided in article 23 of Annex I of CESL.

4. PRECONTRACTUAL LIABILITY UNDER CROATIAN LAW

Croatia adopted the concept of precontractual liability in Croatian Obligations Act (further in text: COA)⁵⁵ in the article 251. Current solution on precontractual liability is in force since 1st January 2006, and it was made on basis of article 2:301 and 2:302 of PECL.⁵⁶ However, the concept of precontractual liability is in Croatia adopted much earlier, although with narrower application, in former Obligations Act.⁵⁷ It provided only two situations which could trigger the liability, and these were if the party entered into negotiations without real intention to conclude the contract, and if the party broke-off the negotiations without justified reason.⁵⁸ In the COA currently in force, as it shall be demonstrated, liability can be triggered not just in these two cases, but whenever one party negotiates contrary to good faith. Liability for breach of confidential information given in the course of negotiations is in Croatian law inserted by the new COA in 2006.

4.1. *Legal nature of precontractual liability*

There are different opinions on the legal nature of precontractual liability in Croatia. Some authors consider that precontractual liability is a part of extra-contractual, i.e. tort liability,⁵⁹ while others consider that precontractual liability forms a separate ground of civil liability.⁶⁰ However, regardless the legal nature, Croatian legal scholars agree that the rules for extra-contractual liability apply as *lex generalis*

55 Official Gazette of the Republic of Croatia, No. 35/05, 41/08, 125/11.

56 I. Crnić, *Zakon o obveznim odnosima*, Zagreb 2005, 82; V. Gorenc (*et. al.*), *Komentar Zakona o obveznim odnosima*, Zagreb 2005, 347.

57 Sl.l. 29/78, 39/85, 57/89; Official Gazette of the Republic of Croatia, No 53/91, 73/91, 58/93, 111/93, 3/94, 107/95, 7/96, 112/99, 129/00, 88/01. It was in force until 1st of January 2006.

58 Article 30 of the former Obligations Act.

59 R. Knez, „Predugovorna odgovornost“, *Pravo u gospodarstvu*, 35 1996, 868; J. Barbić, *Sklapanje ugovora po Zakonu o obveznim odnosima*, Zagreb 1980, 14; V. Gorenc (*et. al.*), *op. cit.* fn. 56, 347.

60 M. Vedriš, P. Klarić, *Građansko pravo*, Zagreb 2008, 606; M. Baretić, „Predugovorna odgovornost“, *Zbornik Pravnog fakulteta u Zagrebu*, 49 1999, 54; O. Jelčić, „Pravni učinci pregovora i ponude“, *Zbornik Pravnog fakulteta u Rijeci*, 20 (2) 1999, 599.

on all issues which are not covered in the provisions on precontractual liability.⁶¹ The most important issue not covered by the article 251 of the COA dealing with precontractual liability is the extent of damages which should be awarded to the injured party. Since general provisions on tort liability provide the right of the injured party to claim both for the compensation of reliance and expectation interest,⁶² authors shall explore impact of this fact on the answer whether the extent of damages incurred by precontractual liability includes both reliance and expectation interest.

4.2. Conditions for precontractual liability

Conditions which must be met for invoking precontractual liability are regulated in article 251 of the COA. There must exist: 1) persons in obligatory relationship of damage liability, 2) conduct of negotiations and damaging act, 3) illegality, 4) causal link, 5) damage.⁶³ Liability may be invoked if these conditions cumulatively exist.

4.2.1 Persons in obligatory relationship of damage liability

In a precontractual relationship these persons are the negotiating parties. Damage liability will primarily be incurred by the person who caused the damage.⁶⁴

4.2.2. Conduct of negotiations and damaging act

Croatian legislature adopts fundamental principle that the parties are free to negotiate without obligation to conclude the contract.⁶⁵ However, if a party negotiated or broke-off negotiations contrary to the principle of good faith, it is responsible for the damage caused to the

61 R. Knez, *op. cit.* fn 59, 878; J. Barbić, *op.cit.* fn. 59, 14; M. Baretić, *op. cit* fn. 60., 61; M. Vedriš, P. Klarić, *op.cit.* fn. 60, 609; O. Jelčić, *op. cit* fn. 60., 599; G. Mihelčić, „Ugovorna i predugovorna odgovornost za neimovinsku štetu prema novom Zakonu o obveznim odnosima“, *Informator* 5356–5357/2005, 17.

62 Article 1046 of the COA.

63 I. Crnić, J. Matić, *Odštetno pravo*, Zagreb 2008, 4, 5.

64 *Ibid.*, 4.

65 Article 251/1 of COA.

other party.⁶⁶ It is presumed that a party negotiated in bad faith if it negotiated without real intention to conclude the contract.⁶⁷

Importantly, it is considered that a party did not break-off negotiations contrary to good faith if it concluded the contract with another offeror, i.e. if it simultaneously negotiated with more than one party.⁶⁸ This is because the party intended to conclude the contract, although it turned out with another offeror, thus not falling under the accusation that it negotiated without real intention to conclude the contract.

Criterion for determining whether negotiations between the parties existed at all are discussed in a 2007 court decision of the Supreme Court of Croatia.⁶⁹ In that case one party claimed damages, i.e. expenses for legal representation, stating that the other party conducted negotiation without real intention of concluding the contract. Supreme Court rejected plaintiff's claim finding that no actual negotiations occurred between the parties. It stated that in order for negotiations to exist, it is necessary that parties exchange information and standpoints on the content of the future contract, that they are involved in mutual correspondence whether in person or by representatives, that they are acquainted with legal and economic consequences of the future contract for each party and etc.

Duty of confidentiality is inserted by the new COA in 2006, also in correspondence to the PECL. It provides that parties are obliged not to disclose confidential information given in the course of negotiations or use them for their own purposes, unless otherwise agreed.⁷⁰

4.2.3. *Illegality*

The claimant must prove that the defendant broke the principle of good faith during negotiations or that the defendant had no intention to conclude a contract. The general rule and principle in Article 8 of the COA forbids causing damage.⁷¹ Illegality will always exist when

66 Article 251/2 of COA.

67 Article 251/3 of COA.

68 Decision of the Regional Court in Zagreb, Gž-560/05, from 7 February 2006.

69 Decision of the Supreme Court of the Republic of Croatia, Rev 1151/06-2, from 30 October 2007.

70 Article 251/4 of COA.

71 I. Crnić, J. Matić, *op. cit.* fn. 63, 6.

a person negligently or intentionally acts contrary to a legal rule. In order that precontractual liability is triggered, injured party must prove both the breach of the rule and the fault of the party in breach.

Simple fault will exist when the damaging party did not use the attention which would have been used by a careful person (the attention of a good businessman).⁷² The general rule on damage liability stipulated in COA states that simple fault (*culpa levis*) is presumed.⁷³ However, precontractual liability is an exception from this rule. In precontractual liability cases, fault (simple or grave) must be proven by the claimant (the injured party).⁷⁴

Simple fault will exist when the damaging party did not use the attention which would have been used by a careful person (the attention of a good businessman).⁷⁵ In precontractual liability, the injured party will prove that fault exists if it proves that the damaging party negotiated or broke-off negotiations contrary to the principle of good faith.⁷⁶ Simple fault or carelessness is objectified and the court compares the behaviour of the damaging party to the behaviour of another person in equal or similar circumstances.⁷⁷ The yardstick for fault is objective negligence. In cases of precontractual liability the careful person would probably be an honest businessman who acts in good faith and shares all relevant information with the other party. If the claimant succeeds to show that the defendant acted below the set standard of care, fault will exist.

Further, it is presumed that a party negotiated in bad faith if it negotiated without real intention to conclude the contract.⁷⁸ It will be hard to prove for the injured party that there was no real intention because that is the inner connection between the damaging party and the cause of damage or the absence of such connection. For example, the lack of real intention will be held to exist if the damaging party was insolvent for conclusion of the contract which it negotiated.⁷⁹ Grave fault (*culpa lata*) is practically equal to intent in consequences.

72 V. Gorenc (*et. al.*), *op. cit.* fn. 56, 347; Article 10 of COA.

73 Article 1045/2 of COA.

74 M. Vedriš, P. Klarić, *op.cit.* fn. 60, 610.

75 V. Gorenc (*et. al.*), *op. cit.* fn. 56, 347; Article 10 of COA.

76 M. Vedriš, P. Klarić, *op.cit.* fn. 60, 608.

77 *Ibid.*, 599; V. Gorenc (*et. al.*), *op. cit.* fn. 56, 1624.

78 Article 251/3 of COA.

79 V. Gorenc (*et. al.*), *op. cit.* fn. 56, 347; Article 251/3 of COA.

4.2.4. Causal link

The definition of causal link does not exist in Croatian law. Causal link must exist between the damaging act and damage. There is no method which the courts might use to determine its existence between the damaging act and damage. If this element does not exist, liability will not be incurred. The resulting damage must be a consequence of the damaging act.⁸⁰ The behaviour of the damaging party is crucial. Claimant must prove that the defendant breached the good faith principle which directly resulted in damage. Causal link is a chain of consequences which must not be broken by some other human act (for example a faulty act of the claimant). If it is, the defendant will not be held liable.

However, damage may be caused by many different causes known as factual causes. The defendant will try to prove that the damage resulted due to functioning of the market, overall business crisis or bad business organisation of the claimant. The judge makes a selection between all of these causes by choosing only those which are legally relevant or the principal cause of damage. This is done by the application of the adequacy theory.⁸¹ Only those causes which according to the normally expected course of events could have caused such damage will be accepted. That is, only the typical causes which lead to such damage. It is uncertain how wide should be the observing field, the judge sets that. But the narrower the observing field which serves as a standard for comparison, the closer the judge gets to the case at hand and the objective circumstances which are observed and tested become more adequate to the original case.

The judges rarely analyse it in their judgments, they mostly conclude a causal link (or adequate causal link) exists or if it does not they explain why.⁸² Scholarly writings mostly neglect this element of non-contractual liability. However, if adequate causal link is sought after, then causality must be determined in a two-step analysis – first factual causation and second adequate causation. This first test helps to estab-

80 Stipulated in Article 1045/1 of COA.

81 I. Crnić, J. Matić, *op. cit.* fn. 63, 6; B. Vizner, *Komentar Zakona o obveznim (obligacionim) odnosima*, Knjiga 2., Zagreb 1978., 675.

82 E.g. the decision of the County Court in Dubrovnik number Gž–2447/06 from 11 September 2008.

lish all the possible causes of damage. However, these can be plentiful. The second step narrows this variety down. Adequacy serves to limit liability to only legally relevant causes. It determines the scope of liability. It is undisputable the injured party must prove causation.⁸³ More precisely, in the frame of the two-step causal inquiry, claimant must prove the factual causation while adequate causation is determined by the court based on the given factual proof. The judge must determine whether the damage that occurred is indeed a typical consequence of such damaging act or whether it was highly probable to occur.

*„According to the adequacy theory, the relevant cause among many different events which could be considered as causes of a certain consequence is only that one which is typical for creation of certain damage. The typical cause is the one which regularly leads to certain damage. It is that event for which the experience of life shows that when it appears, the occurrence of certain consequence may be commonly expected together with it. According to that theory all other accidental occasions which intervene with regular events and have thus entered the group of causes preceding the damage but which are not typical for it, should be excluded.“*⁸⁴ That is why it seems that judges determine the existence of causal link based on the circumstances of the case and laws of nature. The truth is adequate causal link is a legal question which depends on the assessment and conviction of the judge.⁸⁵

The causal inquiry differs if the damaging party acted with intent or with simple fault. When damage was caused by intent then causal adequacy does not have to be examined at all because all intentionally caused damage is automatically adequate to the damage.⁸⁶ Therefore, if the claimant has succeeded in proving that the defendant negotiated without the real intention to conclude the contract (as stipulated in Article 251/3 COA) adequate causal link will not have to be proven.

83 Decision of the Supreme Court of the Republic of Croatia, Rev 1216/06–2 from 11 July 2007.

84 Decision of the Constitutional Court, U-III / 49 / 2008 of 24 June 2008, published in *Official Gazette of the Republic of Croatia* 78/08, para 5.

85 Decision of the Supreme Court of the Republic of Croatia, Rev 1216/06–2 from 11 July 2007.

86 This is so for example in Germany but it is a purely logical explanation applicable in Croatia as well. See Palandt *Bürgerliches Gesetzbuch*/ Ch. Grüneberg, *Beck'sche Kurz Kommentare Vorb v § 249*, Band 7, 69. Auflage, Verlag C.H. Beck 2010, 276, para 27.

If this is a link between the damaging act and damage, then obviously the damaging act or illegality of it as well as damage must be proven first. This will also facilitate the finding of the causal link because fault and causation are proportional. The faultier certain act is, the easier it will be to establish causal link.

4.2.5. Damage

Article 251 of COA does not stipulate the extent of damages which an injured party can seek. Thus, it is left to legal scholars and judicial practice to answer whether the injured party is entitled to reliance interest only or to compensation of expectation interest as well.

As to legal scholars, the majority argues that an injured party is entitled to seek only the compensation of reliance, but not the expectation interest.⁸⁷ Available judicial practice based on the former⁸⁸ Obligations Act supports this standpoint. In particular, High Commercial Court of Croatia confirmed that the injured party is not entitled to request for the conclusion of the contract or the compensation of the expectation interest, but it can only seek reliance interest.⁸⁹ Thus, we can conclude that in Croatia the compensation of expectation interest based on precontractual liability is excluded by the majority of legal scholars and current judicial practice. This standpoint is com-

87 V. Gorenc (*et. al.*), *op. cit.* fn. 56, 348; M. Vedriš, P. Klarić, *op.cit.* fn. 60, 609; R. Knez, *op. cit.* fn 59, 878; J. Barbić, *op.cit.* fn. 59, 18; O. Jelčić, *op. cit* fn. 60., 603; G. Mihelčić, *op.cit.* fn. 61, 17. For opposite opinion see generally M. Baretić, *op. cit.* fn. 60.

88 To the best knowledge of authors, there is no relevant judicial practice based on the article 251 of new COA until now.

89 Decision of the High Commercial Court of the Republic of Croatia, Pž-1881/00 from 14 November 2000. In particular, the Court found that the party is not entitled to seek the formation of the limited liability company. That could be claimed solely on the basis of the preliminary agreement, which in particular case was not concluded. Earlier decisions which support this standpoint are: Municipal Court in Zadar, GŽ-864/91 from 06 November 1991, *Pregled sudske prakse* – 52/72; Supreme Court of the Republic of Croatia, Rev-70/88 from 28 February 1989, *Pregled sudske prakse* –46/66; An example of reliance interest upon which the party is entitled to ask is the restitution of the amount of money received by the other party to make preparations for the future contract.

pletely in accordance with the basic principle of the freedom of contract.⁹⁰ The threat of expectation interest would impede this freedom.

Duty of confidentiality during negotiations provides that parties are obliged not to disclose confidential information or use them for their own purposes, unless otherwise agreed.⁹¹ Remedies for the breach of the duty of confidentiality include compensation of damages and restitution of benefit received by the other party.⁹²

As to the costs of negotiations Article 251/6 of COA provides that each party pays its own costs while mutual costs are divided between the parties, if nothing else is agreed.

5. CONCLUSION

Precontractual liability is not harmonised in EU law. German author Jehring had the immense influence on the development of precontractual liability doctrine. Almost all EU countries adopt precontractual liability, with the only exception of common law countries. However, models adopted greatly differ in defining the legal nature of the precontractual liability while an overall majority agrees that the extent of damages should only cover reliance interest. The only exception is Dutch law which considers that expectation interest should also be awarded. Analysed non-obligatory legal sources PECL and DCFR adopted substantially the same rules for precontractual liability. These texts carefully left outside the explicit answer as to whether parties may seek reliance and expectation interest. It is left to legal doctrine to answer this question and for now it is considered that only reliance interest may be sought. Croatian law complies with these findings. Both judicial practice and legal scholars agree that only reliance interest can be compensated. Differences arise solely as to the issue of legal nature. Some scholars consider it as a part of tort liability and others as a separate and special ground of civil liability. To conclude, Croatian law in this respect completely complies with the current trends in EU law.

90 Article 251/1 COA.

91 Article 251/4 of COA.

92 Article 251/5 of COA.

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PREDUGOVORNA ODGOVORNOST U PRAVU EU I HRVATSKOM PRAVU

Sažetak

Predugovorna odgovornost nije harmonizirana unutar prava Europske Unije. Autorice će ispitati različita rješenja o predugovornoj odgovornosti u državama članicama EU i usporediti ih sa prihvaćenim rješenjem u hrvatskom pravu, posebice nakon usvajanja novog Zakona o obveznim odnosima u siječnju 2006. U članku se ispituje pravna narav, sudska praksa i stajališta pravnih stručnjaka te posebice opseg naknade štete koju se može potraživati temeljem povrede predugovornih obveza vođenja pregovora, čuvanja poslovne tajne i drugo. Postavlja se ključno pitanje može li oštećena strana tražiti samo naknadu stvarne štete ili je ovlaštena potraživati i naknadu izmakle dobiti.

Ključne riječi: *Culpa in contrahendo*.– *Predugovorna odgovornost*.– *Stvarna šteta*.– *Izmakla dobit*.