

# PRELIMINARY AGREEMENTS IN INTERNATIONAL CONTRACT NEGOTIATION

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Portugal . . . a taste of sun . . . Fresh . . . Calm . . . Mild  
. . . . Come to where the flavor is . . . America's ultimate  
taste . . . . The successful range for men of the world all over  
the world.<sup>1</sup>

If brains and money are spent on constructing them, it is because those apparently innocent sentences are the first steps in precontractual negotiations. But from the moment such an invitation to deal becomes known to a reader to the moment the negotiations are concluded in the form of a definitive contract, various legal relations may be established between the parties. In many everyday contracts, the stages of negotiation and conclusion coincide and consist of an instant meeting of offer and acceptance. In other instances, negotiations may be longer and more elaborate. Offers and counter-offers may be exchanged and discussed for months or years . . . you do not buy a Concorde as you would buy a car. The legal consequences of the discussion may even become more precise and authoritative if, during the negotiations, the parties come to an agreement in order to prepare the conclusion. Such agreements may have the legal effect of a binding contract; they are distinguishable from the definitive contract only by their object, which is to prepare the latter.

Negotiation of business and industrial contracts offers many examples of such preliminary agreements. This practice is recognized under various titles: letters of intent, options, promises, etc. But the legal effect of a contract does not depend on the label given to it by the parties, but on its content. In spite of their growing practical importance, preliminary agreements have received little attention in legal writings,<sup>2</sup>

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1. Various phrases taken from *Time* magazine advertisements.

2. Italian Law: BALBI, *IL CONTRATTO ESTIMATORIA*, (2d ed. 1960); VISALLI, *IL CONTRATTO ESTIMATORIO*, (1964); ALABISO, *IL CONTRATTO PRELIMINARE*, (1966); RASCIO, *IL CONTRATTO PRELIMINARE*, (1967). German law: HENRICH, *VORVERTRAG, OPTIONSVERTRAG, VORRECHTSVERTRAG: EINE DOGMATISCH-SYSTEMATISCHE UNTERSUCHUNG DER*

whereas the classical mechanisms of "offer-acceptance" have been widely studied.<sup>3</sup> This lack of recognition may be one of the reasons why negotiators frequently underestimate the legal problems raised by such preliminary agreements and why negotiators sometimes even ignore the fact that they have made such an agreement.

The existence and consequences of preliminary agreements are of particular interest in the course of negotiating an international contract. Various legal systems accord differing legal consequences to the different stages of negotiation. It is therefore important to know which law is applicable to particular negotiations, especially when there could be a question of the existence of a preliminary contract. It may well happen that the negotiators have entered into a preliminary contract without being conscious of it. Such will be the case, for instance, under French law, where the principle of consensualism implies that a contract is concluded when a party demonstrates the existence of a meeting of minds, without any further condition being required. This rule applies to any contract including preliminary agreements, and may thus lead to the imposition of contractually binding obligations upon the negotiators simply because, in the course of discussion, they have expressed an agreement on certain points.

This article will discuss the issues raised by preliminary contracts in general, and point out solutions developed by the main European continental systems, with an emphasis on French law. This discussion will attempt to analyze the possible content and consequences of preliminary contracts, which appear to depend upon the contract's object. A preliminary agreement may relate either to the negotiation or to the conclusion of the definitive contract.

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VERTRAG-LICHEN BINDUNGEN VOR UND ZU EINEM VERTRAGSSCHLUSS, (1965). Swiss law: STÜBER, *Der Vorvertrag zur Aktiengesellschaft* (1973). French law: MOUSSERON, *La Durée dans la formation des contrats*, ETUDES OFFERTES À ALFRED JAUFFRET 509-24, (1974); RIEG, *La "Punctuation": Contribution à L'étude de la Formation Successive du Contrat*, *Etudes Offertes à Alfred Jauffret* 593-608 (1974).

3. Besides numerous national studies, the main comparative approaches to the problem are: FORMATION OF CONTRACTS: A STUDY OF THE COMMON CORE OF LEGAL SYSTEMS (Schlesinger ed. 1968); LA FORMATION DU CONTRAT: HARMONISATION DU DROIT DES AFFAIRES DANS LES PAYS DU MARCHÉ COMMUN (Rodiere ed. 1976); Kessler & Fine, *Culpa in Contrahendo, Bargaining in Good Faith and Freedom of Contract: A comparative study*, 77 HARV. L. REV. 401 (1964); VON MEHREN, THE CIVIL LAW SYSTEM (1979); Von Mehren, *The French Civil Code and Contract: A Comparative Analysis of Formation and Form*, 15 LA. L. REV. 687 (1955); NUSSBAUM, *Comparative Aspects of the Anglo-American Offer-and-Acceptance Doctrine*, 36 COLUM. L. REV. 920 (1936); Tunc, *La Possibilité de Comparer le Contrat dans des Systèmes Juridiques à Structures Economiques Differentes*, 27 RABELS ZEITSCHRIFT FÜR AUSLÄNDISCHES UND INTERNATIONALES PRIVATRECHT 478 (1962).

## I. PRELIMINARY AGREEMENTS RELATING TO THE NEGOTIATION OF THE DEFINITIVE CONTRACT

Persons contemplating the conclusion of a future contract may seek to define the conditions of the negotiation itself in a preparatory agreement. The object of a preliminary agreement may be to address two kinds of concerns: either the parties wish to obligate themselves to undertake negotiations; or they wish to organize their mutual obligations during the negotiation.

### A. *Preliminary Agreements Obligating the Parties to Negotiate*

When the parties think it useful to obligate themselves to negotiate a future contract, it is generally because they wish in this way to increase the chances of concluding the contract. The effectiveness of this preliminary agreement depends on whether or not it includes a right of preference for the benefit of the other party.

#### 1. *Obligation to negotiate without a right of preference*

Typical practices in the negotiation of industrial contracts provide numerous examples of such agreements relating to the conditions of the negotiation itself: “[C]onsidering the urgency of this project . . . the contract will be signed as soon as possible after the initial discussions and every effort will be made to make this possible . . . .”<sup>4</sup>

The agreement might also contain further details designed to define its content: it might give specifications as to time, place or cost of the negotiations. This might include a time-table for the negotiations, or arrangements for the financial consequences of a hypothetical breakdown in the discussions (e.g., the determination and allocation of costs of the preliminary studies). One might find, with respect to delays in negotiation, the following clause:

Considering the urgency of this project . . . the contract will be signed as soon as possible after the initial discussions, and every effort will be made to make this possible within thirty days of the beginning of the initial discussions.

Similarly, a typical clause dealing with the arrangements and refunds of the costs of the preliminary studies may read as follows:

Within sixty days following the date hereof the parties shall .

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4. The clauses cited in this article are excerpts from contracts examined by the Working Group on International Contracts, of which the author is a member. See M. Fontaine, *Etude du Groupe de Travail Contrats Internationaux: Les Lettres d'Intention*, DROIT ET PRACTIQUE DU COMMERCE INTERNATIONAL (International Trade Law & Practice) 73, 76-116 (1977).

appoint a team comprised of a mutually agreed number of representatives of each party to undertake feasibility studies for the establishment . . . of a facility to produce the aforesaid products. . . . The cost of the study agreed to by the parties in advance shall be shared equally by the parties at the conclusion of the study. If the project is implemented, the agreed costs will be borne by [a specified party]. [I]f the project is not implemented the agreed cost, after the net billing settlements, will be borne equally by the parties.

The legal consequences of such agreements may vary according to the legal system under which they are interpreted. The contractual nature of such an agreement is recognized by the principal continental European systems.

For instance, French law and French legal writers know this type of preliminary agreement under the name of "agreement of principle," which is a contract obligating the parties to make an offer or to continue an already existing negotiation relating to a contract, the object of which is only partially determined. This form of preliminary agreement was recognized as positive law in a decision of the French *Cour de Cassation* (Supreme Court). At the end of World War II, the management of Renault wrote to one Mr. Marchal, a former employee who was seeking to be rehired: "We will consider with you the possibility of employment as soon as the resumption of automobile activity allows." This they did not do. At the request of Mr. Marchal, the courts found that a contract existed, the object of which was not an obligation to conclude the labor contract, but to negotiate it. Mr. Marchal was allocated damages for Renault's failure to perform.<sup>5</sup>

The existence of such a contract to negotiate has also been recognized to exist in the course of negotiating the creation of a corporation.<sup>6</sup> One Rouayroux proposed orally to one Pennec the creation of a corporation to build a hospital. The exact nature of the corporation was to be agreed upon later. Pennec hired an architect to draft the plans of the buildings, and asked for the necessary administrative authorizations. But when Rouayroux showed him a proposal for the corporation, Pennec refused to sign or even discuss the proposal and ordered work on the building stopped. The Court of Appeals, affirmed by the Supreme Court, found that the parties' behavior indicated the existence of a contract. Pennec was held liable for breach of this preliminary

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5. *Marchal v. Renault*, *Cour de Cassation*, March 24, 1958, *Semaine juridique*, 1958, II, 10868, note Carbonnier.

6. *Cass. civ. comm.*, Oct. 8, 1963, *Bull. civ. I*, p. 359, No. 419. *See also, e.g.*, *Cass. civ. comm.*, Apr. 16, 1973, *Bull. civ. III*, p. 207, No. 287 (Obligation to communicate the conditions of a rental).

agreement since he refused to engage in any serious discussion and did not even make any counter-proposal relating to the incorporation. He was ordered to pay damages to Rouayroux, and to bear the architect's fees and the costs of the already-realized work.

The contractual nature of such preliminary agreements is also recognized under Belgian<sup>7</sup> and Italian law.<sup>8</sup> Such a contractual obligation to negotiate must be performed in good faith. The parties are thus considered to have the duty of *diligentia in contrahendo*, so dear to Ihering, who overemphasized the concept by giving it a systematic character and consequently considering it part of every negotiation.<sup>9</sup> In the absence of such an agreement, misbehavior during negotiations may give rise, under most systems, only to possible tort liability if it may be qualified as such.<sup>10</sup>

English legal writers and case law do not seem to recognize the idea of a "contract to negotiate." Such an agreement would be regarded as void because of the uncertainty of the terms of the future contract. English courts apparently have never granted a remedy in contract for the failure to negotiate in good faith after conclusion of a "letter of intent" or "agreement of principle." An evolution toward the admission of such a possibility is, nevertheless, conceivable.<sup>11</sup>

Under English law, the conduct of the parties during the precontractual negotiations may be a source of tortious or *delictual* liability in cases where incorrect or misleading statements are made, fraudulently

7. SCHRANS, PREADVIES OVER PRAECONTRACTUEL VERHOUDINGEN NAAR BELGISH RECHT IN VERENIGING VOOR DE VERGELIJKENDE STUDIE VAN HET RECHT VAN BELGIE EN NEDERLAND 23 (1967); Van Uytvanck, *La Pratique d'Entreprises Belges en Matière de Contrat International*, LE CONTRAT ÉCONOMIQUE INTERNATIONAL, at 397 (1975).

8. GORLA, IL CONTRATTO: PROBLEMI FONDAMENTALI TRATTATI CON IL METODO COMPARATIVO E CASISTICO (1954); V.R. SCHMIDT, *Der Abschluss des Vertrages nach dem Italienischen Zivilgesetzbuch von 1942*, 1 FESTSCHRIFT FÜR NIPPERDEY 701 (1965).

9. VON IHERING, *Culpa in contrahendo, oder Schaden-ersatz bei nichtigen oder nicht zu Perfektion gelangten Verträgen*, 4 JAHRBUCH FÜR DIE DOGMATIK DES HEUTIGEN RÖMISCHEN UND DEUTSCHEN PRIVATRECHTS 1 (1861).

10. French law: J. SCHMIDT, LA SANCTION DE LA FAUTE PRÉCONTRACTUELLE, 1 REVUE TRIMESTRIELLE DE DROIT CIVIL 46 (1974); Belgian law: DE PAGE, TRAITÉ ÉLÉMENTAIRE DE DROIT CIVIL BELGE §§ 501 & 509 (Vol. II, 3d ed. 1964). The Italian civil code gives a statutory basis to the obligation to negotiate in good faith (art. 1337), but the sanction is tortious liability (cass. it. June 23, 1964. Giust; civ. mass. 1964, 755); German law admits contractual liability: Serick, *La Responsabilité Civile en Droit Allemand*, Revue Internationale de Droit Comparé 560-71 (1955); ESSER, 1 SCHULDRECHT 372 (1975).

11. The problem of the contractual nature of a "letter of intent" has been posed in *Snelling v. Snelling* [1972] 2 All. E.R. 79, 85. It has been there decided: "Then it is said that this arrangement was essentially a statement of mutual intention for the future and no more, or in other words, that it was in substance a letter of intent." See also *Letters of Intent. Questions on English Law*, INT'L TRADE LAW & PRACTICE 519 (1976); Dugdale & Lowe, *Contracts to Contract and Contracts to Negotiate*, J. BUS. L. 28, 28-37 (1976); CHITTY, CONTRACTS § 81 (23rd ed.); Goetz & Scott, *Enforcing Promises: An Examination of the Basis of Contract*, 89 YALE L.J. 1261, 1261-1322 (1980).

or even negligently.<sup>12</sup>

In this context, it is useful to note that the choice of judge (or arbitrator) is extremely important to the solution of this problem. The problem of determining whether a given agreement is or is not a contract is a question of fact. The judge qualifies a given situation according to his own national rules of law and procedure (*lege fori*). It is thus possible, for example, that an agreement may be considered a binding contract by a French judge, whereas it would be refused any binding effect by an English judge.<sup>13</sup>

The admission by some legal systems of the existence of a contract to negotiate might, however, be dangerous for the negotiators, in view of the breadth of interpretation which judges might give it. Think of the many cases where the classic expression appears: "leave your address, we'll be in touch." Such an expression is a means, without saying it expressly, of getting rid of someone who wants to negotiate and ultimately conclude a contract. It certainly does not mean that the party wishes to bind himself, anymore than that he undertakes to negotiate. Indeed, a party should express his real intentions in order to avoid double meanings and the dangers just mentioned. Statements limiting liability "without obligation on a part" are thus advisable.

The parties' intention not to create legally binding relations does not produce, however, the same consequences under all legal systems.<sup>14</sup> English courts assume that the parties meant to create legally enforceable rights and obligations under their agreement, but will take into account a contrary intention expressed or necessarily implied. Under English law, the crucial element in determining enforceability is the analysis of the parties' real intention.<sup>15</sup> English law gives full significance to the notion that a contract is understood to be an agreement

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12. *Courtney & Fairbairn Ltd. v. Tolaini Bros. Ltd.*, [1975] 1 W.L.R. 297; *Esso Petroleum Co. Ltd. v. Mardon*, [1975] 2 All. E.R. 5. See STREET, *THE LAW OF TORTS* § 5 (6th ed. 1976).

13. Reese, *Choice of Law: Rules or Approaches*, 57 CORNELL L. REV. Q. 315, 315-34 (1972); Von Mehren, *Recent Trends in Choice of Law Methodology*, 60 CORNELL L. REV. Q. 927, 927-68 (1975); LAGARDE, *L'interprétation Par Le Juge des Règles Écrites en Droit International Privé Français*, TRAVAUX DE L'ASSOCIATION HENRI CAPITANT, vol. xxix, 1978 at 346.

14. ZWEIGERT, *Du Sérieux de la Promesse: Remarques de Droit Comparé sur la Distinction des Actes qui Obligent de Ceux Qui n'Obligent Pas*, REVUE INTERNATIONALE DE DROIT COMPARÉ (1964); McGovern, *The Enforcement of Informal Contracts in the Later Middle Ages; An Examination of the Basis of Contract*, 89 YALE L.J. 1261, 1261-1322 (1980).

15. G. CHESIRE, H.S. FITFOOT & M.P. FURMSTON, *LAW OF CONTRACT* 102 (9th Ed. 1976); 9 H.S.G. HALSBURY, *THE LAWS OF ENGLAND; Macaulay, Non-Contractual Relations in Business: A Preliminary Study*, 28 Sm. Soc. Rev. 55, 55-67 (1963); *Rose and Frank Co. v. J.R. Crompton* [1923] 2 K.B. 261.

designed to produce legal consequences.<sup>16</sup>

Although the classical continental doctrine incorporates the same definition, more recent legal writers show that the parties' intentions are not the sole criteria of contract. An agreement only creates an objective situation for which the law recognizes certain consequences. Thus, an agreement may produce legal effects independently of the parties' intention.<sup>17</sup> French case law, for example, recognizes the existence of a contract even when an agreement is expressly said to be binding "in honor" and meant not to produce any legal consequences.

It has been decided, for instance, that when a debtor to whom a creditor has granted relief from a debt declares "in honor" that he will pay when he is better off, he undertakes a contractual obligation to pay.<sup>18</sup> More recently, in a suit designed to solve a problem of jurisdiction under the Brussels Convention of September 27, 1968 relative to the jurisdiction and enforcement of civil and commercial decisions in the European Economic Community (EEC), the question was raised whether a "letter of intent" was a contract. In this letter of intent, it was said that a given corporation would "do the necessary" so that another (affiliate) corporation "would have sufficient funds to face its obligations" toward a given bank arising from a current account. The Paris Court of Appeals held that the corporation had an obligation in contract to "guarantee" the balance of its affiliate's account.<sup>19</sup>

Under the EEC commercial law, the European Communities Commission has qualified a "Gentlemen's Agreement" without signature as being an illegal antitrust agreement prohibited by Article 85-1 of the Rome Treaty. The "Gentlemen's Agreement" was designed to extend to the Common Market an agreement relating to prices, delivery quotas, and production limitations.<sup>20</sup> As for the relations between the parties, such an agreement would not be enforceable, not necessarily because it was meant not to be binding, but because of its illegal object. The national courts of the EEC Member States may derive civil consequences from the Community's decisions based on Articles 85 and 86 of the Rome Treaty.

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16. See CHESHIRE, FITFOOT & FURMSTON, *supra* note 15. D. & G. DE KERSTRAT, *LES CONTRATS EN DROIT ANGLAIS* 102 (1973).

17. WILLOWEIT, *ABGRENZUNG UND RECHTLICHE RELEVANZ NICHT RECHTSGESCHÄFTLICHER VEREINBARUNGEN* (1969); GORLA, *IL CONTRATTO*, (1954); ROUHETTE, *Contribution à l'Étude Critique de la Notion de Contrat*, Thèse Poul L'Obtention du Grade de Docteur En Droit, Université de Paris, 1965.

18. Aix, June 11, 1872, *Recueil Dalloz*.

19. *Uniputz Mosbacher v. Banque Nationale de Paris*, 1980 *Recueil Dalloz-Sirey*. See also *Oppetit, L'engagement d'Honneur*, 1979 *Recueil Dalloz-Sirey*.

20. Decision No. 69/24/EEC from July 16, 1969, *Entente internationale de la quinine*; *JOCE*, No. L. 192/1969.

Negotiators should thus be aware of those solutions and know that a continental judge, faced with the problem of the existence of a preliminary contract, may admit its existence even if a contrary intention is expressed.

The existence of such an "agreement of principle" or agreement to negotiate raises the question of the sanction for failure to perform. It was held in France that when there had been a breach of contract, a combined order of damages with interest was made in accordance with Article 1184 of the French Civil Code. The existence of an "agreement of principle" creates a contractual ground to the liability for non-performance, but cannot lead to an authoritative conclusion of the projected definitive contract. The breach of the negotiations, without serious discussion or formulation of a counter-offer, may be grounds for such liability.

The judge would have to consider whether the obligation has in fact been performed by a party, whether an actual failure to perform has been concealed by the device of an offer which is laughably low or excessive, or whether the bargaining is really nonconstructive. In determining whether the separate act amounts to performance or not, the judge must take into account what would have been correct performance of the obligation. But he cannot go beyond that, substituting his own judgments for those of the contracting parties or substituting his judgment for negotiations which never took place. One can imagine that in a climate of very enthusiastic judicial intervention, the judge might himself find a contract which had been neither negotiated nor, *a fortiori*, concluded. Such an authoritative solution is not admitted under French contract law.<sup>21</sup> Thus, the preliminary contract of negotiation does not necessarily lead to the conclusion of a definitive contract even through litigation.

## 2. *Obligation to negotiate with a right of preference*

This type of obligation existed under Roman law, and is presently a part of most civil law systems. French positive law, for instance, recognizes this type of preparatory agreement as a "preference agreement." The "preference agreement" is not a mere offer, but an actual contract, created by a meeting of minds between the "promisor" and the "beneficiary" upon a right of preference granted by the former to the latter as to the conclusion of a future contract.<sup>22</sup>

21. See J. SCHMIDT, *supra* note 10.

22. J. BARTET, *Le Pacte de Préférence*, Thesis Paris, (1932); J. BALBAA, *La Préemption en Droit comparé*, Thesis Dijon (1938); Voirin, *Le Pacte de Préférence*, 1 SEMAINE JURIDIQUE 1192 (1954).

Those contracts obligate one or both parties to offer the other party, in preference to third persons, the conclusion of a future contract, under the same conditions as those proposed by or to the third persons. As the conditions of the definitive future contract are not yet identified at the time of the conclusion of the "preference agreement," the latter must be distinguished from the option contract, by which at least one of the parties gives his definitive consent to the future contract. (*See below*).

Such "agreements of preference" are found to have, with respect to independent contracts, wide application in real property law (for instance, between neighboring landowners or between the lessor and his lessee concerning a possible future sale of land). One comes across them also in relation to the transfer of capital or debenture issues in a company:

[A] participant may offer to sell all of the shares owned by it and its affiliate(s) in both companies to a specified third party, or all or part of such shares to one or more specified participants holding shares in such companies, provided that the participants other than the offeror holding shares in those companies are first given an opportunity to purchase the shares on the same terms and conditions as offered to the third party or the specified participant(s). . . .<sup>23</sup>

"Preference clauses" also appear in many "long term" contracts, but for a different purpose. In publishing contracts, for instance, a clause frequently grants a right of preference to the publisher for the publication of future works of the author. In industrial agreements, by such "clauses of preference" one party (a supplier, for instance) gains the certainty of performing on the condition that he falls into line with the competition, whereas the other party (a receiver, for instance) gains the certainty of being able "to stock up" in preference to third parties as long as he does not refuse the offer of the first party. This last type of clause is known as the "first refusal clause." In first refusal clauses, the obligor has a duty to reserve his future offers for the obligee and, consequently, to make the conclusion of certain contracts with third party competitors dependent on the former's refusal. One comes across such clauses in various economic environments, some of which have been listed by the Working Group on International Contracts, and may be quoted here. For instance, two firms are working together to de-

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23. M. Fontaine, *Les Clauses de L'Offre Concurrente, du Client le Plus Favorisé et la Clause de Premier Refus dans le Contrats Internationaux*, INT'L TRADE LAW & PRACTICE 185 (1978).

velop a certain product. One of them gives the other the benefit of a first refusal clause, in respect of raw materials and products:

Taking into account the specific nature of the materials and products necessary for the plant's functioning, *X* will consult *Y* with regard to the acquisition of such materials and products. If the terms offered by *Y* to supply materials of such description are of the same order as the offers of the competitor whose technical data is the closest to that of *Y*, *X* undertakes to give *Y* priority to supply the said raw materials and products.

In another example, firm *A* assigns a manufacturing license to a foreign partner *B*. When considering exporting some of its products to another foreign country *Z*, *B* grants to *C* (*A*'s subsidiary in country *Z*), a right of first refusal to distribute its products in the country:

In all cases where *B* exports from country *X* to country *Z*, *B*'s vehicles and/or *B*'s vehicle parts manufactured by *B*, under this agreement *B* . . . must first offer the sale of *B*'s vehicle parts to the firm *C*, or such other company that has the right to act as distributor of *A*'s products in country *Z*. If *B* and *C* or such other company are not in agreement as to the whole of the conditions and terms of a distribution contract, *B* will have the right to offer such a contract to any other person, enterprise, or company on more favorable terms or conditions than those offered to *C* or any other company which would have the right to act as distributor of *A*'s products in country *Z*.

In a contract of firm undertaking, a company grants to a consortium of banks a right of first refusal regarding certain further possible issues:

In the event of the company raising further loans in Switzerland at a later date, The Banks have a right of preference to make such loans on the same terms.

The existence of such agreements or preference clauses raises the question of their legal consequences. Their effect is simply to burden the obligor to the benefit of the creditor with a certain obligation under the threat of certain sanctions. The obligation is to make an offer on the same terms as an offer made by a third party, or with the possibility of deviating from a specified condition (for example, as to price or delivery delays, etc.). This duty is binding if, during a specified period, a certain situation arises.

The obligation to make an offer created by the preference agreement is binding only to the extent that certain conditions are fulfilled,

concerning essentially the existence of an offer by a third-party. As a result, many problems arise over information about third-party offers and over comparing the behavior of third parties with that of the original parties.

The initial question with respect to information about third party offers is whether communication of negotiations to another partner is not in itself contrary to the essential nature of business. Generally, the preference agreement creates a duty to disclose the contents of the offer, if not its source, or all the business relations that led up to it.

In comparing competitive offers, the first question concerns who is to make the decision. It might be both parties or else a "third-party expert" (*i.e.*, an independent assessor) acting under the supervision of the arbitrator or judge. Sometimes provisions are inserted to regulate the procedure, such as the period of time to be spent in making the comparison and in reaching a decision.

What sanction is involved where the party under an obligation of preference fails to perform, *e.g.*, contracts with a third person without making an offer to his contractor?

In principle, the remedy cannot be the annulment of the contract made with the third party, as the annulment would be based on a prior contract, and contracts are considered to have no effect in regard to third parties who participate in a subsequent set of relations, but not the original bargain: "*Res inter alios acta, aliis neque nocere, neque prodesse potest.*" There is, however, always the exception of the bad faith of the third party; in the event of fraudulent collaboration between him and the "promissor", their contract may be declared void on the basis of the principle "*fraus omnia corrumpit.*" Such was the solution in a 1926 French Supreme Court case.<sup>24</sup> There the beneficiary of a preference agreement learned of a possible conclusion of the definitive contract between the promissor and a third person and addressed a protest to both of them. In spite of this, the defendants completed the projected contract. Answering the beneficiary's demand, the Court decided that the contract was void and ordered that the promissor complete it with the beneficiary. Furthermore, the beneficiary could obtain damages with interest from the promissor for breach of contract (the preference agreement), and from the third party for tortious conduct.<sup>25</sup>

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24. Cass. req., Jan. 12, 1926, Dalloz Hebdom. 1926, p. 116.

25. R. Demogue, *Les Effets du Pacte de Préférence*, REVUE TRIMESTRIELLE DROIT CIVIL 394 (1926), note 9 Cass. req. Jan. 12, 1926, D.H. 1926, 116.

## B. *Preliminary Contracts Establishing Obligations During the Negotiation*

It may seem appropriate to the negotiators to set out their reciprocal obligations during the negotiations and even after their conclusion. In some cases, preliminary contracts aim at allowing the parties to examine their reciprocal ability to perform the definitive contract. The obligations provided for in the preliminary contract are, in these cases, identical to those of the definitive contract. In other instances, the object of the preliminary contract is to provide for the parties' specific obligations relating to the negotiations themselves.

### 1. *Preliminary contracts with content identical to the definitive contract*

Such contracts have sometimes been qualified as provisional contracts, because they are designed to last only for the duration of the negotiation, and to rule the parties' actions during that period. In order to allow one or both of the parties to appreciate whether the conclusion of the definitive contract is possible, a provisional contract is concluded having the same object and creating obligations of the same nature as the definitive one.<sup>26</sup> The intention to make a provisional contract must, however, be expressed. This is the case for all trial contracts (*contrats à l'essai*). The provisional or trial contract of employment, for instance, creates for the parties, broadly speaking, the same obligations as the definitive one; the principal difference being the duration of the contract's effects and, sometimes, a special organization of the revocation of such an agreement, as provided by the national labor law systems.<sup>27</sup> The provisional contracts of insurance are similarly designed to cover the short period (usually several days to three months), during which the client wishes to be insured, whereas the insurer wants to prepare more precise conditions of the definitive contract, if he agrees to conclude it. The end of the negotiation, whatever its results may be, implies the end of the provisional contract's effects. But if the negotiation is successful, the definitive contract will follow the provisional one.

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26. Most of the European Romano-Germanic systems provide for rules relating to the trial sale and decide that the effects of the contract are suspended until the results of the trial sale are deemed satisfactory: Italian law: civil code, art. 1521 (*vendita di prova*); Swiss civil code: art. 223; German BGB, art. 495; Austrian civil code (ABGB), art. 1080. The English Sale of Goods Act of 1893 (sect. 18) provides for a similar solution.

27. Most of the national labor laws require precise conditions to be satisfied by a labor contract on trial, especially as to its duration (Germany, Act of June 21, 1869, § 127b: maximum three months; Belgium, Act of March 10, 1900 §§ 3bis & 5bis: the duration is variable according to the employee's professional qualification; Netherlands, civil code art. 1639: maximum two months. Under French law, the length of the trial period depends on the duration of the definitive labor contract (art. L. 122-177 Labor Code).

The identity of their contents then raises the problem of the possible retroactivity of the final contract back to the date of the provisional one. This is generally the case in labor relations, when the "trial period" is included in the employee's length of service.

2. *Preliminary contracts with content different from the definitive contract*

Such preliminary contracts aim to create for the parties specific obligations relating to the conduct of the negotiations themselves. They are useful in that they facilitate an action for liability on the grounds of a contractual wrong. In their absence, most of the civil law systems will recognize only tort liability as a possible sanction for misbehavior during negotiations.

The most frequent and typical example of such preliminary contracts is found in the negotiation of contracts for the sale of technology. The possessor of the know-how,<sup>28</sup> who wants to sell his secret, is virtually forced to disclose it during the negotiation. His partner would be unlikely to agree to enter into such a contract, or undertake heavy financial obligations, if he has no way of evaluating the reality or efficiency of the proposed technique. But after having disclosed the know-how, its possessor risks seeing his unscrupulous partner using or disclosing it to third parties, in spite of a failure of the negotiation and the non-conclusion of the projected final contract.

This problem may be solved by the conclusion of a preliminary contract, creating for the recipient of the disclosure the obligation not to further disclose the know-how and not to exploit it during the negotiations or after their failure.<sup>29</sup>

The duration of such a provisional contract is determined by the results of the negotiation. If the negotiation fails, the obligations not to disclose or exploit will survive definitively, at least as long as the know-how continues to have any economic value. If the negotiation succeeds, the definitive contract will follow and replace the provisional one. In this case, the obligation not to disclose will survive, but as a part of the definitive contract, and will obviously be performed, since it is the secret character of the know-how which makes it valuable to its

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28. TURNER, *THE LAW OF TRADE SECRETS*, 1962; The World Intellectual Property Organization (WIPO) gives a definition of know-how in the Model Law for Developing Countries on Inventions, § 53/1: "[P]roceedings of production of information relating to the use and application of industrial technology."; DELEUZE, *LE CONTRAT DE TRANSFERT DE PROCESSUS TECHNOLOGIQUE: KNOW HOW*, (2nd ed. 1979) at 31.

29. BLANCO-WHITE, *AGREEMENT FOR SALE OF "KNOW-HOW"* (1962); DESSEMONTET, *THE LEGAL PROTECTION OF KNOW-HOW IN THE UNITED STATES OF AMERICA*, (2nd ed); R. FABRE, *LE KNOW HOW: SA RÉSERVATION EN DROIT COMMUN* (1976).

beneficiary. The obligation not to exploit, on the contrary, will disappear since the definitive contract has as its object such exploitation and frequently expressly provides for an obligation to exploit.

In the absence of such a provisional contract under most civil law systems, the unfair disclosure or use of the know-how after the unsuccessful end of the negotiation could be sanctioned only in tort.<sup>30</sup> The provisional contract therefore adds a contractual basis for the sanction.

Other provisional contracts may go further, and create for the negotiators specific obligations which do not usually exist between them as a matter of good faith, and could not, therefore, become the basis for liability in tort. For instance, the preliminary contract may provide for an obligation not to negotiate simultaneously with third persons during the negotiation of the projected contract. Such parallel negotiations occur frequently and are necessary for the normal development of competition. In the absence of a contractual prohibition, they cannot be forbidden as contrary to the principle of good faith in bargaining.

In practice, one comes across clauses providing for such a prohibition and organizing a right of exclusive negotiation:

We have taken due note of the fact that your group envisages the possibility of buying . . . shares of corporations . . . and trademarks . . . . In order to allow you to examine this possibility, we undertake the irrevocable obligation towards your group not to conduct any negotiation nor to sell to a potential buyer all or part of the shares or trademarks listed above, until . . . .<sup>31</sup>

The effects of such a provisional agreement cease at the end of the negotiation, whether it is successful or not. As such obligations are specific to the negotiation, there may not be a question of the definitive contract being retroactive to the date of the conclusion of the preliminary agreement.

The final question as to preliminary agreements relating to the negotiation is to determine their role after the conclusion of the definitive contract. In practice, the problem is often solved by providing in the definitive contract that all the documents and agreements made prior to the conclusion will be of no effect after the main contract is signed. The following example is illustrative:

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30. English case law seems to consider that when the possessor of the know-how has disclosed it during the negotiations, the use of that information is forbidden on the basis of an implied contract; see TURNER, *supra* note 28, at 280; Comment, *Misappropriation of Trade Secrets*, 53 TUL. L. REV. 215, 229-33 (1978).

31. See FONTAINE, *supra* note 4, at 96.

This contract shall constitute the entire agreement between the parties hereto and shall supersede all prior contracts, agreements and negotiations between the parties whether written or oral relative to the project prior to the effective date of this contract.<sup>32</sup>

In the absence of such an express provision, the relations between the definitive and the provisional contracts will be determined according to the interpretation of the parties' intention. The preliminary agreements relating to the negotiation will be useful, at least, to facilitate the interpretation of the definitive contract.

## II. PRELIMINARY CONTRACTS RELATING TO THE CONCLUSION OF THE DEFINITIVE CONTRACT

Such preliminary contracts may be classified into two categories, according to their closeness to the definitive contract which they precede. Some of them are designed only to facilitate the conclusion of the definitive contract, whereas others are intended to create an obligation to conclude it.

### A. *Preliminary Contracts Relating to the Conclusion of the Definitive Contract*

Facilitating the conclusion may be realized mainly by two different techniques: either the negotiation of the future contract is divided, or it is unified for a whole series of future contracts.

#### 1. *The conclusion is facilitated by a division of the negotiation.*

It happens in practice that the negotiations are carried out in several successive stages dealing with separate points of the definitive contract, which may even be discussed by separate groups of negotiators.<sup>33</sup> The problem arises, then, in determining the consequences of a partial agreement reached on one of those points, toward the conclusion of the definitive contract. The negotiators may be interested in setting out the answer to this question in the partial agreement itself, in order to avoid further difficulties which may be created by its normal legal solution. Any "point by point" negotiation raises this problem of the effectiveness of the partial agreements, which should be considered by the parties with care, because of the diversity of the national legal solutions it receives. The relation between the partial and the definitive contract

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32. See RIEG, *supra* note 2.

33. Cass. civ. com. April 17, 1980, *Semaine juridique*, ed. Commerce et Ind. (1980), No. 8848.

may be governed by two possible solutions: the partial agreement may be considered as either sufficient or insufficient, for the formation of the definitive one.

In French law, for instance, the formation of a contract may be the result of a partial agreement if the points remaining in discussion are merely secondary. A recent case relating to the negotiation of an international contract has been decided by the French Supreme Court: a seller sent a telex to a buyer abroad, expressing his agreement as to the merchandise, the price, and the payment by a letter of credit, followed by another telex requiring a given time limit for the letter of credit. The buyer sent a letter of credit with a different duration. Then the seller refused to deliver the goods on the grounds that the contract of sale had not been formed. The Court Appeals of Rouen, affirmed by the Supreme Court, held that the seller was liable for breach of a contract formed by the first telex relating to the essential elements of the deal.<sup>34</sup>

This solution is grounded on a strict interpretation of Article 1583 of the French Civil Code: "The sale is complete between the parties and ownership immediately transferred to the buyer, when they have agreed upon the matter and the price." By neglecting the elements other than the matter and the price, the Code thus admits that the agreement on the essential elements is necessary and sufficient for the contract to be formed. Although Article 1583 is the only provision relating to this problem, the principle may be applied to any contract. Thus, the difficult point is to determine what are the essential elements of a given contract. Always essential are the elements necessary for the realization of the contract's economic aim. The contracting parties may, however, decide that any other element is essential for them and is, therefore, a condition of the formation of the contract. It is thus useful for them to make clear what value they attach to the discussed points.

The same solution is expressly given by the Swiss Code of Obligations (Article 2):

If the parties have reached an agreement on all the essential points, they are presumed to have undertaken definitive obligations, even if they have reserved some secondary points. In the absence of agreement, the secondary points are fixed by the judge in accordance with the nature of the business.<sup>35</sup>

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34. SCHÖENBERGER-JÄGGI, KOMMENTAR ZUM SCHWEIZERISCHEN ZIVILGESETZBUCH, 3. Aufl. Obligationenrecht, Band V, art. 2, (1973).

35. POLANDT, BÜRGERLICHES GESETZBUCH §§ 145 & 154 (1982).

The German Civil Code (Article 154), provides for an opposite solution:

[A]s long as the parties have not agreed upon all points of a contract on which, according to the declaration even of one party, agreement is to be reached, the contract is, in case of doubt, not concluded. An understanding concerning particular points is not binding, even if it has been reduced to writing . . . . If it has been agreed to reduce the contemplated contract to documentary form, the contract is, in case of doubt, not concluded until the document has been executed.

The draftsmen of the German Civil Code (BGB) have thus decided that agreement on some of the points of the contract is subject to agreement on the other points; as long as the agreement is not complete, the definitive contract is not concluded.<sup>36</sup>

As the solutions may thus vary according to the legal system applicable to the negotiation, the negotiators should establish, in a preliminary contract, the relationship between the partial and the definitive agreement.

During the negotiation of some complex contracts, such as a contract of sale of the entire assets of an industrial operation, the parties may consider that they have reached a point of no return in the negotiation, and decide that the agreement already realized about certain elements will be considered as a definitive contract, in spite of the fact that other points remain under discussion. A "letter of intent" is then frequently written spelling out the agreed points and providing for an arbitration clause for the elaboration of the secondary elements in case the parties could not reach an agreement about them in a fixed period of time. The following examples are illustrative:

We have the intention to entrust you with the complementary work necessary to determine the feasibility of a light gas engine, following your telex . . . relating to your technical and financial proposition answering our consultation, which has received the agreement of our technical department. . . . The definitive contract will be sent to you as soon as the modification to the contract . . . will be ready. You are authorized by the present letter to begin work listed hereunder up to the amount of . . . . We ask you to confirm your agreement by sending back a copy of the present letter signed by you.

In this example, the negotiation is much advanced, but a series of problems remain unsolved. Nevertheless, considering the urgency of the project and the near certainty of the final agreement, the parties

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36. See FONTAINE, *supra* note 4, at 98.

decide that they are already bound in a definitive manner and can even begin the performance of the main contract.

In other instances, the parties provide that the effectiveness of the partial agreement is subject to final agreement to be reached on all the discussed points:

We hereby inform you that your company has been awarded by our organization an order for equipment, as described in your tender. As some inconsistencies exist between your proposal and our requirements, we kindly invite you to review the technical aspects and contract terms with us . . . . In case no agreement is reached on all terms and no contract is signed before [a specified date] . . . we reserve the right to cancel this award, without any right for indemnification on your part.<sup>37</sup>

The differences in the legal systems are minimized in that they agree that it is possible for the parties to stipulate that the contemplated writing (or other formality) shall be conditional, *i.e.*, that there will be no contract unless and until the contemplated formality is observed. The refusal of one of the parties to execute the writing raises the question of his possible liability for damages suffered through reasonable reliance on the future conclusion of the contract.<sup>38</sup> In the above instance, such liability is excluded by an express provision; otherwise, the problem should be solved according to the law applicable to the preparatory agreement.<sup>39</sup>

## 2. *The conclusion is facilitated by a unification of the negotiation.*

The parties who foresee making a large number of contracts in the future may view them separately, each contract being made and negotiated individually. As the number of business operations grows and the technicalities involved in performance increase, a need for standardization<sup>40</sup> soon begins to make itself felt, and the parties reach the point where each has its own "general conditions" of purchase (on the back of the order) or sale (on the back of the delivery slip or invoice). This is known as the "battle of the forms." However, exchanging such docu-

37. See *Letters of Intent*, *supra* note 11, at 508.

38. See SCHLESINGER, *supra* note 3, at 178.

39. See Litvinoff, *Stipulations as to Liability and as to Damages*, 52 TUL. L. REV. 258, 258-98 (1978).

40. See generally, Friedman, MacCaulay & Rehbinder, *Impact of Large Scale Business Enterprise upon Contract*, INT'L. ENCYCL. COMP. L., vol. 7, chap 3; Council of Europe, *Les Conditions Générales du Contrat*, Actes du 8<sup>e</sup> Colloque de Droit européen, Univ. Neuchatel, (1979); Neumayer, *Les Conditions Générales des Contrats-Contrats d'Adhésion*, RECUEIL DES TRAVAUX SUISSES AU 7<sup>e</sup> CONGRÈS INTERNATIONAL DROIT COMPARÉ (1970); Gluck, *Standard Form Contracts: The Contract Theory Reconsidered*, 28 INT'L & COMP. L. Q. 72 (1979). Von Caemmerer, *Standard Contract Provisions and Standard Form Contracts in German Law*, 8 VICT. U. WELLINGTON L. REV. 235, 235-45 (1976-77).

ments, whose terms most likely do not coincide, without any kind of negotiation would lead to difficult problems in the event of litigation. Accordingly, the interested parties who are anxious to have between them a considerable volume of contracts, may decide to meet to settle once and for all the terms of the numerous contracts which they will make in the future, and to impose this framework upon all such contracts. In this way, form contracts emerge as an instrument of unification of the negotiations of future contracts.

The form contract defines the principal rules for negotiation of agreements that the parties contemplate they will soon make. Relating to contracts of performance or contracts of execution, it provides the framework for making agreements as to ordinary orders for the supply of goods or services.<sup>41</sup> The form contract generally is meant to standardize the merchandise and services of the future contractual relations, as well as conditions applying to them. The contract may impose certain conditions on supply contracts, for example, as to the organization of deliveries, transport, insurance, guarantees, payment and arbitration. It may also contain other terms related to further agreements made between one of the contracting parties and third parties concerning resale with respect to price and guarantees, and the participation of suppliers in promoting and maintaining distributed goods. Thus the party to such a form contract undertakes the obligation not to conclude contracts that conflict with the form contract's terms.

This separation of the operation into, on the one hand, a form contract generally well-detailed and discussed and presented as a binding contract, and, on the other numerous contracts of performance made rapidly by sending an order and communicating by telex or telephone, is a well-established process in the distribution sector (and most notably in contracts for the supply of goods). It is a form that has extended into manufacturing operations with respect to subcontracts. A form contract for subcontracting lays down the terms and organization of the numerous business agreements to be made in the future. The process repeats itself in the same manner in the realm of provision of services.<sup>42</sup>

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41. See MOUSSERON, *supra* note 2, at 515.

42. SEUBE, *Le Contrat de Fourniture*, Thèse, Université de Montpellier, Faculté de Droit et Des Sciences Economiques (1970); Mousseron & Seube, *À Propos des Contrats d'Assistance et de Fourniture*, RECUEIL DALLOZ-SIREY (June 20, 1973), at 38; Rodiere & Champaud, *À Propos des Contrats des "Pompistes de Marque,"* SEMAINE JURIDIQUE, vol. I, (1968) at 1983; CAWTHRA, *Long Term Supply Agreements in the EEC*, 74 LAW & SOC. GAZ. 739 (1977); De Marino, *Analisis del Concepto de Suministro*, REV. DERECHES MERCANTIL, (1962), at 27; Giannastasio, *La Somministrazione*, 24 TRATTATO DI DIRITTO CIVILE E COMMERCIALE, (CICU & MESSINEO, ED., 1960); KAHN, LIEFERUNG-SVERTRAG (1893).

It should be noted that under French law, a collective labor agreement may also be considered as a form contract relating to the conclusion of individual labor contracts. This is due to the fact that the collective labor agreement is, under this system, binding upon employers who should not conclude labor contracts contrary to the collective agreement. Any such provision of the labor contract is void and replaced by the correct provision of the collective agreement.<sup>43</sup>

There are other provisions which can be added to the principal agreements organizing future contracts, examples are contracts for a manufacturing license, loans of materials, loans of money, or contracts of guarantee, all of which appear notably in "beer contracts"<sup>44</sup> which are today referred to as "contracts for supply and assistance."

Under French law, such a form contract is entirely distinct from the definitive contracts of which it is the necessary precursor.<sup>45</sup> Certain comments concerning the parties and the relations arising from the form contract ought to be made before turning to its terms and effects.

The parties to the form contract are, in most cases, the parties to the contracts of performance. Thus, in a contract of supply, the supplier and the purchaser prepare the agreement of sale that they will make in the future. But it also happens, although more rarely, that the parties who make the form contract and those who make the contract of performance are not the same.

The parties to the collective labor agreement, for instance, are different from those who conclude the individual labor contracts. Nevertheless, the effects of the collective agreement are binding upon persons who have not participated in its conclusion. Such situations are interesting exceptions to the principle of privity of contract.<sup>46</sup>

More important is the case of resale clauses. The party who made the form contract and who is going to enter into contracts of performance will be bound to insert in the latter the terms contained in the former. In conclusion, the form contract creates for this party the negative obligation not to enter contracts that contain terms other than those stipulated.

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43. ROUJOU DE BOUBEE, *Essai Sur L'acte Juridique Collectif*, Paris 1961; Schregle, *La Négociation Collective en Europe Occidentale*, REVUE DROIT SOCIAL 204 (1978).

44. "Beer contracts", so called in French case law, denote contracts of exclusivity between supplier and retailer at determinable prices. They were first used in the sale of beer.

45. Cass. civ. com. Jan. 29, 1968, Recueil Dalloz-Sirey 341; See MOUSSERON & SEUBE, *supra* note 42, at 199.

46. ROUHETTE, *L'Extension à des Tiers des Effets d'un Accord de Volonté (les Accords Collectifs en Droit Français)*, RAPPORTS AUX 13<sup>e</sup> JOURNÉES JURIDIQUES FRANCO-YOUGOSLAVES, (1979). See also, e.g., the agreements on specialization and collective purchase authorized by the European Coal and Steel Community on June 15, 1967, in JOURNAL OFFICIEL DES COMMUNAUTÉS EUROPÉENNES 2512-17 (1967).

The specific effect of form contracts is to create obligations with respect to the methods of concluding and the contents of those contracts of performance that will follow them. Those obligations are relative either to the making of contracts of performance, if the form contract has created a duty so to make them, or to the methods of concluding these contracts of performance (whether or not their conclusion is itself obligatory). For example: "Silence on receipt of the offer will be considered to amount to acceptance." Or there may be a duty as to the contents of future contracts of performance where the latter are direct (between the parties who made the drafting contract) or proximate (between a party to the drafting contract and a third person, for instance, in case of resale).

In French law, the question has been asked whether the form contract must provide for the price of the performance contracts. Three recent decisions of the French Supreme Court caused much alarm within the business community by stating that the price has to be determined or at least determinable in any contract creating an obligation to pay, including form contracts.<sup>47</sup> In the absence of a determinable price, the contract is void. A price is considered as being determinable when it may be calculated according to "serious, precise and objective data" independently of a party's unilateral will.<sup>48</sup> The negotiators of form contracts must, therefore, keep in mind this condition and choose a formula for computing in accordance with it. The reference to the "market price" or "the price used by the most important competitors" is valid under the condition that those competitors might be precisely identified and that the parties persuade the judge that this is an objective reference.<sup>49</sup>

The parties should take into account these solutions while negotiating an international contract subject to French law or which may be enforceable in France. The Paris Court of Appeals has, in effect, declared void an arbitration decision as contrary to public policy in that it has permitted, in an international contract, a price unilaterally set by

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47. Cass. civ. com. Oct. 11, 1978, *Société Européenne de Brasserie v. Portella, Société Anonyme Brasserie Guillaume Tell v. Portella, Société Européenne de Brasserie Eurobra* RECUEIL DALLOZ-SIREY, (1979), 135, note HOUIN; Cass. civ. com. Oct. 11, (1978), *Société Européenne de Brasserie v. Portella, Seddik v. Société Européenne de Brasserie*, SEMAINE JURIDIQUE, (1979), II, 19034, note LOUSSOUARN.

48. Cass. comm. April 27, 1971, RECUEIL DALLOZ-SIREY, (1972), 353 Cass. civ. comm. June 21, 1976, BULLETIN DES ARRÊTS DE LA COUR DE CASSATION, IV, at 179 (1976).

49. See MERCADAL, *La Détermination du Prix dans Les Contrats*, *Chronique des Jurisprudences Nationales Relatives aux contrats internationaux*, INT'L TRADE LAW & PRACTICE, 443 (1979); BERNINI, *Techniques for Resolving Problems in Forming and Performing Long-term Contracts*, INT'L TRADE LAW & PRACTICE 487, 487-98, 631-45 (1976).

the buyer.<sup>50</sup>

*B. Preliminary Contracts Obligating the Parties to Conclude the Definitive Contract*

The practical problem to be solved is how to grant a party a "right to the conclusion" of a future projected contract. Under some legal systems this aim may be reached by means of an irrevocable offer if it is admitted that acceptance forms the contract even against the offeror's will.<sup>51</sup> Under some systems, this mechanism would not be satisfactory, as the withdrawal of even an irrevocable offer allows the offeree only an action in tort, not specific performance. This solution, found for instance under the French law, is based on the principle that a unilateral act of will (*e.g.*, an offer) is incapable of creating obligations.<sup>52</sup> (It also explains the revocability of offers under French law.) Thus, to give rise to an enforceable "right to conclusion," it is necessary to have a preliminary contract providing for an obligation to conclude the definitive one. Such a preliminary agreement is generally known as an "option" or a "promise to contract."<sup>53</sup>

Under French law, the preparatory contract of a promise to contract is defined as an agreement for the purpose of creating for either one of the parties (the unilateral promise), or both parties (the bilateral promise) the obligation to conclude a certain contract under certain conditions.<sup>54</sup>

German and Austrian laws analyze an option as an offer, irrevocable for a certain period of time. But the parties may create the condition precedent that the optionee, by exercising the power conferred upon him, perfects the contractual relationship.<sup>55</sup>

Another important consequence is derived under French and Italian law from the distinction between an offer and an "option contract": an offer does not create any obligation; it is neither assignable nor

50. Judgment of Nov. 3, 1977, 1978 REVUE DE L'ARBITRAGE 486.

51. Such would be the solution under German law (§ 145 of the BUNDESGESETZBLATT [BGB]); See Neumayer, German Report, in Schlesinger, *supra* note 3, at vol. I, A-11, 780-82; RIEG, Le Rôle de la volonté dans l'Acte Juridique en Droit Civil Francais et Allemand 441 (1961).

52. J. SCHMIDT, *supra* note 10, at 46-73.

53. See HENRICH, *supra* note 2; SCHUMANN, DIE OPTION (1969); CESARO, IL CONTRATTO E L'OPZIONE (1969); LALAGUNA, *La funcion Negocial de la Promesa de Venta*, 2, MEL. CASTAN-TOBENAS 303-39 (1969); FIESCHI-VIVET, *La Promesse de Contrat*, Thesis, Lyons Law School, (1973); Boyer, *Les Promesses Synallagmatiques de Vente - Contribution à la Théorie des Avant-Contrats*, REVUE TRIMESTRIELLE DE DROIT CIVIL (1949); Litvinoff, *Of the Promise of Sale and Contract to Sell*, 34 LA. L. REV. 1017-76 (1974).

54. 2 GHESTIN, TRAITÉ DE DROIT CIVIL, LES OBLIGATIONS, LE CONTRAT (1980).

55. Neumayer, German-Swiss Report, in Schlesinger, *supra* note 3, at vol. I, A 10, 782-83.

transferable on the death of the offeror or the offeree. On the other hand, an option creates an enforceable right to the conclusion of the definitive contract, which is assignable and transferable (unless the definitive contract is *intuitu personae*).<sup>56</sup>

By undertaking to hold an offer open for a limited period of time, the offeror intends merely to give up his normal right of revocation and not to grant a right to the conclusion. It is sometimes difficult to apply the distinction to a factual situation. The qualification of the facts is a matter of interpretation of the parties' intent. It is thus necessary to analyze whether the offeror intended to make a mere offer or to grant a right of option relating to the definitive contract. In the latter case, a right of option must be accepted by the beneficiary. The option is, in effect, a contract. This is what distinguishes it from an offer. It happens not infrequently that the instrument which contains the unilateral promise only mentions the promisor's undertaking, and does not even bear the signature of the optionee. However, acceptance and the date thereof may be established by all available means.<sup>57</sup>

The option must necessarily specify the nature of the contract it anticipates, the object it concerns, and the price (of the anticipated contract, not of the option). In other words, the essential elements of the main contract and the undertakings by which the promisor has now engaged himself must have reached a stage where only the exercise of the option by the beneficiary remains for the main contract to become binding. If the beneficiary of the option does not exercise the option within the allotted time, the promise is not binding. For instance, a patent license contract between a French licensor and an American licensee may contain the following clause: "X grants to T, on terms hereinafter defined, an option to acquire a sub-license for the manufacture of licensed products in the United States and its territories and possessions under the terms and conditions hereinafter defined." The effects of the promise are binding to the extent that within the terms of the main contract, one of the parties has already undertaken obligations and, *a fortiori*, this is even more the case when both parties have done so.

In effect, French law distinguishes between unilateral and bilateral options (*promesse unilaterale* or *promesse synallagmatique*). It should be noted that those two terms are employed in the civil law systems

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56. GORLA, *Problemi Sulla Cedibilità dell'Offerta Contrattuale (di Scambio), dell'Opzione e del Contratto Preliminare*, RIV. DIRITTO CIV. (1963); Bonassies, French Rep., in Schlesinger, *supra* note 3, at vol. 2, B-1, 924-27.

57. See Boyer, *Promesse de Vente*, ENCYCLOPÉDIE DALLOZ DROIT CIVIL, No. 11-15; Gorla, *Note sulla Distinzione fra Opzione a Proposta Irrevocabile*, STUDI IN MEMORIA DI G.B. FUNAIOLI 124-44 (1961).

with a meaning entirely different from the common law. They do not refer, as in the common law, to the formation of contracts, but to their effects. Those contracts which typically produce legal obligations only for one party (*e.g.*, a contract of donation) are called unilateral contracts, whereas contracts creating reciprocal obligations for both parties are bilateral ones (*synallagmatiques*). The unilateral promise to contract creates an obligation to make a contract in the future for only one of the parties (the promissor). The other party (the beneficiary) retains his freedom, having the power (if he wishes to use it) to exercise the option. Exercising the option is the crucial point between two periods, both governed by the promise to contract but at which point the effect of the contract changes substantially.

Before the option is exercised, the *in rem* rights which a contract can create do not arise when the parties are only at the preparatory stage of making the promise. He who promises to sell his building continues to be its owner and to be liable for all risks attached thereto. Thus, the only effects that one can identify as arising from the promise are personal obligations. These are, essentially, to be performed by the promissor, whose position can be analyzed in two ways.

First, the promissor is committed to concluding the main contract if the optionee exercises his right during the option period (express or implied). Second, the promissor must refrain from any act which would hinder the realization of the main contract; in particular, he must not contract with a third party.<sup>58</sup>

If he did not comply with this obligation, contractual liability would be incurred and an order made for damages with interest. A third party contractor could be jointly liable, if, knowing that the promise had been made, he acted as an accomplice in the promissor's non-performance. Moreover, in this last case, the courts would go so far as to declare that the third party's contract was invalid in respect of the beneficiary of the promise.<sup>59</sup> The rationale for this is generally taken to be based upon the concept of fraud: *fraus omnia corrumpit*. According to others, it should more accurately be related to the sanctioning of a tort in civil law, based on Article 1382 of the French Civil Code.<sup>60</sup>

What are the beneficiary's obligations in a unilateral option contract? Although the option contract provides most often for remuneration to be paid by the beneficiary to the promissor, under French law an enforceable option may be granted gratuitously. Curiously enough,

58. See Boyer, *supra* note 57, at 94-97.

59. Cass. civ. comm., April 10, 1948, 1948 RECUEIL DALLOZ-SIREY 421, note LENOAN.

60. MOREL, *La Violation d'Une Promesse de Vente*, MÉLANGES H. CAPITANT 541 (1939).

the validity of such gratuitous options has never been discussed on the grounds of lack of consideration ("cause"). One may assume that the consideration is to be found in the promisor's interest in concluding the definitive contract.<sup>61</sup>

The exercising of the option forms the main contract, with all the consequences that involves. Thus the conditions of validity of the main contract are to be satisfied as of the date the option is exercised.

On the other hand, the effects of a bilateral promise to contract are more disputable. This contract is characterized by the creation of an obligation to contract for both parties by the promise. The problem which consequently arises is the independence of the bilateral promise as opposed to the main contract itself.

For a long time, the idea of a bilateral promise independent from the main contract was rejected by an almost unanimous body of doctrine and case law. Article 1589 of the French Civil Code lends support to this proposition. "A promise of sale amounts to a sale when there is agreement between the two parties as to the object to be sold and the price."<sup>62</sup>

In other words, the concept of the bilateral promise of a consensual contract would appear to be useless. The parties do not have any need to rely on such an analysis in order to make the desired arrangements. When they want to delay the coming into operation of their duties and consequent liability, it is not necessary to rely on the complex idea of two successive contracts. It is much simpler to talk about contracts which are conditional, or which reserve the transfer of ownership, etc.

The modern French legal writers and case law are drawn towards the conclusion that it is impossible to integrate the moment when the main contract is made with that act in which the mutual promises are exchanged. Most often, the parties use the mechanism of a bilateral promise in case either the main contract cannot be immediately concluded (*e.g.*, lack of an administrative authorization), or because in the option agreement they contemplate further essential formalities (*e.g.*, an act under seal; *acte notarié*). In all these cases, the further element contemplated cannot be analyzed as a condition precedent to the main contract because the parties undertake to carry out the formality (*e.g.*, to obtain the necessary authorization or sign the act under seal). Thus,

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61. But French law admits other instances of jural acts without consideration: *see* Bonassies, French Rep., in Schlesinger, *supra* note 3, at vol. 1, A-10, at 778.

62. *See* Boyer, *supra* note 57, at 15; Blomeyer, *La Promesse de Vente Vaut Vente Zur Geschichte der Durchgriffs die Vorträgen*, MEL. RAAPE 269, 269-305 (1948).

the bilateral option has to be correctly analyzed as a preliminary contract distinct from the definitive one. The latter will be formed when the contemplated formalities are accomplished.<sup>63</sup>

Because it brings about the mutual meeting of minds necessary to the formation of the definitive contract, the bilateral promise is, in effect, the preliminary contract which appears to be as close as possible to the definitive one. All the precontractual agreements relating to the conclusion of the definitive contract are interesting examples of the theory of "contractual ensembles" recently analyzed by the French legal writers.<sup>64</sup>

The phenomenon of preliminary agreements is linked to the growing complexity of the precontractual negotiations, which itself reflects the complexity of business contracts. Preliminary agreements are designed to solve the conflict experienced by each negotiator: to remain free from specific obligations or liabilities as long as possible, while getting some security from the other party. By the conclusion of the definitive contract, the parties give up their freedom for security. The preliminary agreement allows them to find some security outside of the definitive contract. This security derives from the application of contract law to the preliminary agreements: obligations which have been created must be enforced.

This implies, however, that the preliminary agreement may be recognized as a binding contract. This problem, as well as the links which may exist between the preliminary and the definitive contract, cannot be solved definitively: in the absence of a uniform international law of contracts, over one hundred and fifty possible systems of solution exist in the world. Thus, the international aspects of the negotiation add a new element of complexity to the difficulties inherent in the situation.

This study has sketched out the problems posed by the preliminary agreements in international negotiations; it did not have the unrealistic ambition of solving them. Solutions can be sought only to clearly posed problems. It is hoped that this study will contribute to enlightening and encouraging lawyers to take further interest in applying comparative law.

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63. See FIESCHI-VIVET, *supra* note 53, at 73.

64. TEYSSIE, *LES GROUPES DE CONTRATS* (1975).