Chronicle terminated negotiations - Has a contract already been reached? (part 1)

René van de Klift

1. Introduction

Already in 1957, the Dutch Supreme Court ruled that contract negotiations are governed by the principle of good faith. As a result, parties negotiating the conclusion of a contract must allow their conduct to be determined in part by the legitimate interests of their counterparty.

The legitimate interests of a counterparty may entail that the termination of negotiations is unacceptable in the given circumstances. If a party nonetheless terminates the negotiations it will be obliged to compensate the damages of its counterparty. As a result, there is a relatively high level of litigation in the Netherlands about terminated negotiations.

In this chronicle, I will discuss judgments by Dutch courts on terminated negotiations, handed down from January 2020 to February 2023.

In this first part of this chronicle, I will discuss judgments addressing the question of whether a contract had already been reached when negotiations were terminated. In the second part, I will discuss judgments addressing the question of whether the termination of negotiations was unacceptable. And finally, in the third part, I will discuss judgments addressing the question of whether the terminating party had to reimburse its counterparty's negotiation costs.

2. Has an agreement been reached?

2.1. Introduction

The judgments studied show that the disappointed party's primary position is often that a contract had already been

reached when the negotiations were terminated. This is because the threshold for claiming lost profits as damages is lower in the contractual phase than in the negotiating phase. In the contractual phase, the disappointed party only has to prove that its counterparty has imputably failed to perform the contract. In the negotiation phase, the disappointed party has to show that the termination of the negotiations was unacceptable. The Dutch Supreme Court ruled that the standard to be applied in this respect is strict. Therefore, Dutch courts will not rule too easily that the termination is unacceptable.

2.2. Consensus

A contract is formed by an offer and its acceptance. Whether a contract has been concluded depends on what the parties have stated and inferred from each other's conduct and could reasonably have inferred in the given circumstances. An important circumstance to be considered in this assessment concerns the nature and scope of the contract envisaged by the parties.

In a decision of 25 August 2020, the 's-Hertogenbosch Court of Appeal considered that the parties were negotiating an extensive package of contracts. These involved far-reaching potential commitments: large sums of money, machinery and other items, a lease, employees and debtors. According to the court, the nature and scope of these envisaged contracts implied that the seller could not reasonably infer from a single word or summary confirmation from the buyer that the buyer wanted to be bound by such far-reaching potential commitments.

Another circumstance to be considered in assessing what the parties were reasonably entitled to infer from each other's statements and conduct concerns the capacity and physical condition of the counterparty.

In a case in which the 's-Hertogenbosch Court of Appeal ruled on 16 August 2022, a professional buyer intended to enter into a contract that had characteristics of a long-term cooperation and a property development project. However, its counterparty was an elderly couple with no business interest whose husband suffered from dementia. According to the court, such a party will usually not want to enter into the agreement envisaged by the professional buyer. Rather, such a party will want to be able to sell the property at short notice in order to arrange suitable accommodation and care in time. According to the court, the professional buyer had to be aware of this and take it into account when assessing the elderly couple's statements.

2.3. Essentials of a contract

A contract may already have been concluded if the parties have not yet agreed on all its parts. It is then required that the parties have already agreed on the essentials of the contract. According to the Dutch Supreme Court, the answer to the question of what the essentials of the contract are depends on the intention of the parties. This intention must be determined based on the meaning of what the parties have and have not agreed, the existence or non-existence of the parties'

intention to negotiate further and the further circumstances of the case. Once again, one of the circumstances to be taken into account in this assessment concerns the nature and scope of the envisaged contract.

In a decision dated 4 May 2021, the Hague Court of Appeal ruled that a perfect contract had not yet been reached, despite the fact that the parties had already agreed on the price and remediation costs of two plots of land. This was because it was not a simple purchase contract. The parties intended to conclude a contract on the sale of two plots of land zoned for business activities as land for housing development with a serious financial interest. In such a transaction, according to the court, not only the price and the property play an essential role, but also other factors, such as the delivery date. And the parties had not yet agreed on the delivery date. Such a gap could not be filled on the basis of the additional effect of the principle of reasonableness and fairness, according to the court.

In a judgment dated 6 September 2022, the Arnhem-Leeuwarden Court of Appeal considered that the parties were negotiating an investment in the form of a joint venture, in which both parties would acquire shares. According to the court, the nature of such a contract generally requires consultation and negotiation on various aspects and tax and legal advice before agreement is reached and the contract can be deemed to have been concluded. This implies, according to the court, that an agreement on an investment in this form cannot be assumed too quickly. At the very least, agreement must have been reached on the exact amount that will be invested, in shares or otherwise, who will make that investment, in what mutual relationship, and the further terms and conditions. This was not yet the case.

2.4 Conditions

Parties are free to shape the negotiation phase by making arrangements to that end. In practice, conditions are therefore widely used by negotiating parties to avoid being too quickly bound to the negotiation result.

A common condition is the condition of approval. This condition may be formulated as a condition of completion or as a condition precedent. In the first case, the contract only comes into being after the condition has been fulfilled. In the second case, the contract has already been concluded, but the obligations contained therein can only be enforced after the condition has been fulfilled.

It follows from the judgments studied that the disappointed party often argues that the condition made should be regarded as a condition precedent, because in that case the disappointed party can take the position that the condition should be regarded as fulfilled on the basis of the principle of reasonableness and fairness because the terminating party prevented the fulfilment of the condition. If the Courts follow the disappointed party's reasoning, then the contract has come into effect. The disappointed party can then demand performance of the contract by its counterparty and, if the latter fails to do so, the

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disappointed party can claim lost profits as damages from its counterparty.

Whether in a given case a party has made or parties have agreed a condition of completion or a condition precedent, must be determined by interpretation. In a ruling on 6 April 2021, the Arnhem-Leeuwarden Court of Appeal considered that the negotiator on behalf of the tenant was neither a member of the management board nor otherwise authorised to conclude leases on behalf of the tenant. The landlord also knew this. The negotiator had repeatedly made the condition of approval by the management board. By doing so, according to the court, the negotiator had clearly indicated to the landlord that the will for the intended lease contract ultimately had to come from the management board. The landlord had also understood this to be the case, as he had asked the negotiator when management approval could be expected. Also the negotiator had, in his communication with the landlord, not characterized the condition made as a condition precedent. Therefore, according to the court, the condition had to be classified as a completion condition: without the approval of the management board, no contract comes into being.

3. In conclusion

It follows from the above that ultimately the circumstances of the case determine the answer to the question of whether a contract had already been reached at the time the negotiations were terminated. To avoid being too quickly bound by the outcome of negotiations, conditions can be used and are often used in practice. However, it is then important that the condition is made in good time and in terms that cannot be misunderstood. And preferably recorded in writing in, for instance, a letter of intent to avoid misunderstandings later on.

If you have any questions about terminated negotiations, please contact René van de Klift.

vandeklift@dvdw.nl