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NEGOTIATIONS OF CONTRACTS FROM A PERSPECTIVE OF LEGAL CERTAINTY IN INTERNATIONAL BUSINESS TRANSACTIONS*[1]

Značaj pregovora za zaključenje ugovora iz perspektive pravne sigurnosti međunarodnog poslovnog prometa

Abstract

In this paper the authors analyze the legal regime applicable to negotiations in comparative law, with a special emphasis on the solutions adopted in uniform law. The general hypothesis of the paper is that the differences in rules on negotiations in various legal systems are likely to jeopardize legal certainty in international business transactions as they may lead to unexpected outcomes in the field of pre-contractual liability. For that reason, the advance understanding of the applicable law to negotiations is of utmost importance in international business transactions as it may significantly affect party's overall cost calculation and liability, in particular in case of failed negotiations. Upon examining the approaches to negotiations taken by two major legal systems (civil law and common law), the content of the sources of uniform contract law and the practice of courts and arbitral tribunals, the authors conclude that, irrespective of the law applicable to negotiations, the parties may exercise critical impact on the legal framework of their negotiations by concluding different kinds of agreements on negotiations. However, in doing so, the parties need to be aware of the importance of predictability of the solutions to be applied, since predictability is one of the crucial elements of legal certainty in international business transactions.

Key words: *legal certainty, international trade, contract law, negotiations, pre-contractual liability, good faith, freedom of contracting*

Sažetak

U ovom radu autori analiziraju pravni režim pregovora u uporednom pravu, sa posebnim osvrtom na rešenja uniformnog prava. Rad se zasniva na hipotezi da razlike u pravilima o pregovorima u različitim pravnim sistemima mogu da ugroze pravnu sigurnost međunarodnog poslovnog prometa jer mogu da dovedu do neočekivanih ishoda na polju predugovorne odgovornosti, i s njom povezanih dodatnih troškova. Na osnovu ispitivanja razlika u pristupu pravnom uređenju pregovora u dva velika pravna sistema (kontinentalnom i anglosaksonskom), sadržaju pravila o predugovornoj odgovornosti u izvorima uniformnog ugovornog prava i sudske i arbitražne prakse, autori zaključuju da, bez obzira na pravo merodavno za pregovore, strane mogu da presudno utiču na pravno oblikovanje svojih pregovora kroz zaključenje različitih oblika sporazuma o pregovorima. Pri tome, treba da imaju u vidu značaj predvidljivosti merodavnih pravnih rešenja, jer je predvidljivost jedan od ključnih elemenata pravne sigurnosti u međunarodnom poslovnom prometu.

Ključne reči: *pravna sigurnost, međunarodna trgovina, ugovorno pravo, pregovori, predugovorna odgovornost, princip savesnosti i poštenja, sloboda ugovaranja*

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Introduction

In modern international business, the conclusion of contracts of significant value, complex content or nature, as well as the contracts which provide for extension of their performance over a longer period of time is normally preceded by negotiations. It can hardly be imagined that certain international commercial contracts, such as contracts for transfer of technology, long-term business cooperation, franchising, distribution, performance of construction works and similar are concluded without prior negotiations. As a matter of principle, negotiations are fundamentally important for a contract, since their course and outcome define not only the conclusion of a contract, but also its content and, consequently, its performance. Apart from this basic role, the negotiations may have a crucial impact on the interpretation of a contract [13, pp. 495-505].

The negotiation process *de facto* begins already in the first moment where the parties mutually express their common interests with respect to the conclusion of a certain contract. During the negotiations, the parties analyze the possibilities for conclusion of the contract, exchange their points of view, discuss the questions relevant for a particular contractual relationship, such as the realization of any previously necessary studies, financing terms, insurance, appropriation of necessary licenses, hiring third persons capable of providing a certain professional assistance or performing a certain service. Additionally, the parties negotiate specific clauses of the future contract, especially those relating to the time limitations and the dynamics of performance of obligations, means and place of performance, quality and quantity of goods or type of services to be rendered, price to be paid, method and place of payment, necessary guarantees, effects of hardship and *force majeure* on the performance of contractual obligations, applicable law, dispute resolution mechanism etc. The questions discussed during negotiations are numerous and diverse and they relate to both factual and legal circumstances that may be important for the conclusion of a contract [14, pp. 258 et seq.].

Business in a globalized world brings together negotiating partners from very different cultures and business traditions, with a wide range of negotiating styles and experience. While this variety is a foundation of today's vibrant trading community, it also increases the chances for costly misunderstandings that impede the smooth flow of business [7, passim.]. The certainty with respect to the legal regime applicable to negotiations is particularly important in international business transactions, which, by definition, include conclusion of contracts with partners from foreign markets. Naturally, parties to international transactions often find themselves in a situation where the negotiations that they undertake are governed by a law other than the law of the country of their nationality. It is therefore necessary to critically examine the approaches taken in comparative law with respect to the basic legal principles of negotiations and the legal nature of agreements made during negotiations in order to assess to what extent possible differences in this field of law may affect legal certainty in international business transactions.

Freedom of negotiation and the principle of good faith

Parties' liability. An important issue which arises when negotiations fail is that of determining if and to what extent the parties must respect certain obligations, even in the period before the conclusion of the contract. The approach to this problem varies substantially from one legal system to another [3, p. 110], and this issue is, not surprisingly, considered as "among the most sensitive in comparative law" [22, p. 300].

Civil law systems. In civil law countries, two basic principles apply to negotiations: freedom of negotiation and the principle of good faith. The principle of freedom of negotiation means that the negotiations do not oblige the parties to conclude the contract and that each party may withdraw from the negotiations whenever it wants. Freedom of negotiation is based on the general principle of *freedom of contracting* which, among other, entails the freedom to decide whether to conclude or not to conclude a contract. Accordingly, each party is free to decide whether it wants to conclude the contract that is the subject-matter of negotiations and, as a matter of

principle, it can withdraw from the negotiations without any legal consequences.

Nevertheless, the freedom of negotiation is not absolute. The negotiations must be led in good faith, in a correct way and they should be aimed at the conclusion of the contract. In civil law countries, this requirement stems from the principle of good faith, which is one of the basic principles of contract law. The negotiations must not be used for realization of forbidden or immoral goals, such as the betray of trust of the other party and the abuse of its business secrets, negotiation without the intent to conclude a contract and with the aim to prevent the other party from making a business deal with a third person, extension or delay of negotiations with the aforementioned aim, as well as unilateral cessation of negotiations in the advanced stage without a justified reason [20, pp. 143 et seq.]. In most general terms, the negotiations can generally be led freely and stopped whenever the parties so wish, but if one of the parties is acting *mala fide* and it causes damage to the other party, the party acting *mala fide* shall be liable for the damage caused [18, pp. 854-865]. A general view on the rules of pre-contractual liability in civil law countries allows for the conclusion that these rules, whether they are provided for by the law or established by case law, are based on the principle of good faith [6, pp. 5-69]. The parties are obliged to observe this principle not only during the conclusion and performance of the contract, but also during negotiations. Therefore, the parties must lead the negotiations in a scrupulous and loyal way and in good faith.[2]

Common law systems. Unlike civil law countries, common law countries, and especially English law, take restrictive approach to pre-contractual liability. In these countries, pursuant to the traditional principle that the offer is revocable, the dominant concept is the one that each party may legitimately protect its interests during negotiations and is free to stop the negotiations at any point, up until the moment of conclusion of the contract [9, pp. 58 et seq.]. In English law, the principle of good faith is not considered to be a general principle so, consequently, English law does not set an obligation to observe this principle during negotiations.[3] On these bases, there is generally no liability for the cessation of negotiations in common law countries, so the negotiating parties may withdraw from negotiations for any reason whatsoever, or they do not even have to state any reason at all for their withdrawal. However, in English law pre-contractual liability exists in case of *negligent misrepresentation* during negotiations [17, pp. 172 et seq.]. In that sense, the *House of Lords* in the case *Hedley Byrne Co., Ltd.* v. *Heller & Partners, Ltd.*[4] has extended the application of the rules on liability for damage caused by a tort to the case of negotiations during which one party, relying on the statement of the other party and taking account of the special relationship that had existed between these two parties, was falsely led to believe that the contract would be concluded and, thus, suffered damage.[5] Similar situations in the USA and Australia may also be addressed by the notion of promissory or equitable estoppel [19, p. 275].

Uniform contract law. Parties negotiating international contracts frequently submit their agreement to neutral rules which do not favour any of them. In that respect, they often provide for the law of a third country (for example Swiss law) as the law applicable to the contract. However, it commonly happens that the parties are not familiar with a law of a third country chosen by them, so that some of the rules or principles of this law are not complying with the parties' intentions and expectations. For these reasons, there is an increasing need among business people for uniform transnational rules which they can apply to their international contracts as a neutral legal framework. An attempt to set out uniform rules adapted to the needs of international commerce has been made in UNIDROIT Principles of International Commercial Contracts (UNIDROIT Principles) [11], [22].

2 See: [4, p. 31], where the following position of the French jurisprudence is reported: "négociations doivent être menées de bonne foi: si chaque partie reste libre de conclure ou pas le contrat définitif, elle engagera sa responsabilité si elle a rompu sans raison légitime, brutalement et unilatéralement des pourparlers avancés".

3 This standpoint has been confirmed in the case *Martin Walford v. Charles Miles* (1992), 1 *Weekly Law Reports*, p. 174, where it was explicitly underlined that: "the concept of a duty to carry on negotiations in good faith is inherently repugnant to the adversarial position of the parties when involved in negotiations. Each party to the negotiations is entitled to pursue his (or her) own interest, so long as he avoids making misrepresentations."

4 Law reports, Appeal case (1964), p. 465, cited in [1, p. 246].

5 The same principle was applied in the case *Caparo Industries plc* v. *Dickman and Others* (1990), 1 All England Law Reports, 568. See [17, p.173].

The UNIDROIT Principles are gaining an increasing practical importance. Already in 2004, on the occasion of the publication of the second edition of the Principles, the Governing Council of UNIDROIT observed that "the success in practice of the UNIDROIT Principles over the last ten years has surpassed the most optimistic expectations" [21, p. viii]. Even though this assertion may have sounded too audacious at the time it was pronounced, the current statistics confirm its validity, since the UNIDROIT Principles are becoming widely accepted by courts and, particularly arbitrations.[6] The Unilex database lists 152 court decisions and 170 arbitral awards where the Principles were applied in the period from 1994 to date.[7] What is more, the UNIDROIT Principles have made another significant and noteworthy practical influence, as they served as a source of inspiration for reforms of national contract laws in different parts of the world [22, p. 17].

With regard to the rules relevant for negotiations, UNIDROIT Principles mainly follow the civil law approach, but by relying on the treshold of 'bad faith', they offer "an intermediate solution that should be acceptable to parties from most legal orders" [22, p. 300].

Under Article 2.1.15. of the UNIDROIT Principles:

"(1) A party is free to negotiate and is not liable for failure to reach an agreement.

(2) However, a party who negotiates or breaks off negotiations in bad faith is liable for the losses caused to the other party.

(3) It is bad faith, in particular, for a party to enter into or continue negotiations when intending not to reach an agreement with the other party."

As to the actual meaning of good faith in the context of negotiations, the official commentary to the UNIDROIT Principles says that: "A party's right to enter into negotiations and to decide on the terms to be negotiated is, however, not limited, and must not conflict with the principle of good faith and fair dealing... One particular instance of negotiating in bad faith which is expressly indicated in para (3) of this article is that where a party enters into negotiations or continues to negotiate without any intention of concluding an agreement with the other party. Other instances occur when one party has deliberately or by negligence misled the other party as to the nature or terms of the proposed contract, either by misrepresenting facts, or by not disclosing facts which, given the nature of the parties and/or the contract, should have been disclosed..." [11, p. 60].

The relevance of good faith negotiations under UNIDROIT Principles was underlined in the practice of International Centre for Settlement of Investment Disputes (ICSID), in a dispute between US company and the Republic of Turkey. The dispute arose out of failed negotiations between US company – Claimant in this case, and Turkey as a Respondent. Namely, in 1994 Claimant started negotiations with Respondent to develop the energy sector in Turkey which were followed by granting of a Concession Contract to build a coal mine and a power plant in 1998. However, the subsequent negotiations were delayed by repeated changes in Turkey's legal framework for the energy sector that culminated in the termination of the investment project in 2001. Although no mining operations were undertaken nor was construction commenced, Claimant expended millions of dollars in the late 1990s on an initial feasibility study, follow-up studies and several rounds of negotiations with government agencies. Hence, Claimant initiated proceedings before ICSID requesting, *inter alia*, damages for Respondent's unjustified breach of negotiations. Respondent argued that, absent evidence to the contrary, negotiations must be presumed to have been carried out in good faith and in the light of Art. 2.1.15 UNIDROIT Principles, there was no obligation to reach an agreement or liability for failure to do so. Nevertheless, the Arbitral Tribunal found that Respondent's continuous changes in the legislative environment breached the fair and equitable standard under the U.S.-Turkey BIT, which mandates host States to provide a stable and predictable business environment for foreign investors. Consequently, Claimant was awarded with damages.[8]

Serbian law. The Serbian Law on Contracts and Torts contains rules on negotiations which are in every respect

6 In arbitration, the UNIDROIT Principles apply within their scope to the exclusion of any particular national law, subject only to the application of those rules of domestic law which are mandatory. More on the application of the UNIDROIT Principles, see [10, pp. 5 et seq.].

7 See http://www.unilex.info./

8 See *PSEG Global & Others v. Republic of Turkey*, ARB/02/5, 19.01.2007, available at Unilex website.

adapted to contemporary tendencies in comparative law and to the needs of modern business [16, pp. 264 et seq.]. Pursuant to Art. 30 of the Law:

"(1) Negotiations preceding the entering into contract shall not be binding, and each party shall at any moment be free to interrupt them.

(2) However, a party conducting negotiations without intending to enter into contract shall be liable for damage caused by conducting such negotiations.

(3) A party conducting negotiations with intent to conclude a contract, but afterwards withdrawing from them without a justified reason, thus causing damage to the other party shall be equally liable for damage.

(4) Unless otherwise agreed, each party shall bear their own expenses relating to preparations for entering into contract, while joint expenses shall be shared equally between the parties."

Even a cursory look at the aforecited rules of the Law on Contracts and Torts is sufficient to see the great resemblance between the solutions contained in the Law and the relevant uniform law rules. In that respect, it is particularly worth mentioning that the Law on Contracts and Torts was drafted long before the cited uniform law rules (in 1978), which is yet another confirmation of the fact that the Serbian legislator succeeded in trying to find the optimal solutions in the matter of legal regime of contract negotiations.

Agreements on negotiations

Different types of agreements. In international commerce, particularly in the context of complex dealings, a rather common practice is to sign documents that provide for the issues relevant for negotiating procedure. These are presented under various names: letter of intent (LOI), memorandum of understanding (MOU), letter of understanding (LOU), preparatory agreement, heads of agreement, temporary agreement, etc. These documents serve to establish the important elements of the negotiation procedure. The most typical examples of these elements are: reasons and goals of negotiations, time of commencement of negotiations, dynamics of negotiations, time limit for completion of negotiations, place of negotiations, form in which the negotiating parties will exchange their points of view, questions already settled and questions to be settled during negotiations, obligations of each party during negotiations (e.g. preparation of a certain study, acquisition of certain documents, hiring certain experts) etc. Other than that, some of the frequently used clauses in the agreements on negotiations are the exclusivity clause and the confidentiality clause.

Legal nature. In many cases, these kind of agreements leave ambiguity as to their binding nature and represent a true "*terra incognita*" in contract law. The doctrine of contract law pays little attention to their legal nature, meaning and effect. The aforementioned questions have not been settled in national laws and sources of uniform law either, and the opinions expressed in case law are extremely divergent [6, pp. 5-69].

Legal nature of the agreements on negotiation is questionable: are they legally non-binding expressions of will or do they represent the documents of *contractual* character? From the standpoint of classical contract law theories, an *a priori* simple answer can be given – negotiations do not oblige the parties to conclude the contract, and the parties are not bound by the acts that they undertake during negotiations, up until the moment of conclusion of the contract. This answer is logical, since the basic purpose of negotiations consists in giving an opportunity to each party to assess the circumstances important for a potential contract and to decide, on the basis of such assessment, whether it wants to conclude the contract or no. However, this stance may be challenged if one would be to consider this problem through the lenses of complex agreements on negotiations in modern business, as these often contain clauses that strictly and precisely define the obligations of the negotiating parties with respect to specific issues in the negotiation process. In these cases, one may reasonably ask whether the agreements of the aforementioned kind, bearing in mind the unambiguously expressed meeting of the minds of the negotiating parties with respect to the commitment to a certain precisely defined performance, may be considered as *contracts*, which would in turn render the liability for their violation a contractual one.

The difficulties in answering the said questions stem from the differences in approach of national laws to the issue of pre-contractual liability and the fact that in practice these agreements differ from case to case not only by their form, but also by their purpose. It is impossible to determine the binding character of this type of documents in general terms; this will depend primarily of the wording of the agreement and the applicable law [3, p. 110]. For these reasons, the agreements on negotiations and the problems arising therefrom must be seen in the light of the relevant circumstances of each particular case.

Case law. With respect to the question raised, different approaches can be identified in case law. In this paper we will attempt to provide a general overview of some typical situations where the problem of binding nature of negotiations agreements is likely to arise.

In the *Dupuis* case before the Commercial court of Brussels, the respondent (*Dupuis*), acting against the general agreement on takeover of a company concluded during the negotiations with the claimant, *GBL et Hachette*, performed the takeover of another company – *Editions Mondiales*. The Commercial court of Brussels found that the general agreement in the case at hand created a contractual obligation to lead the negotiations in good faith. According to the Court, the respondent did not act in good faith when it suddenly withdrew from negotiations, contrary to the obligations under the general agreement, and concluded the contract with the third person. In that sense, the Court concluded that the said general agreement represented a contractual basis of liability for cessation of negotiations. However, even though the Court that Dupuis had the contractual liability, the claim with respect to the transfer of shares to the claimant *GBL et Hachette*, was not granted because the general agreement did not stipulate the duty to *conclude the contract*, but rather to *lead the negotiations* in good faith.[9]

Unlike the Commercial court of Brussels, the Court of Appeals of Brussels in the case *FMC Corporation* took a restrictive view with respect to the legal nature of the letter of intent, which was disputed in the case at hand. According to the Court, a letter of intent *cannot* form a basis of contractual liability until the parties do not reach an agreement with respect to all essential elements of the contract.[10]

The aforementioned question was also discussed in the decision of an International Chamber of Commerce (ICC) tribunal in the case of a joint venture in Iran. A Swedish manufacturer of trucks and an Iranian company signed a Memorandum of Understanding concerning the supply to the Iranian party of trucks and respective spare parts, the organization of the purchaser of an after-sales service, the setting-up of a joint venture and a future cooperation in the assembly of trucks. Thereafter, the supplier did not implement the MOU, failing to set up the joint venture. In the dispute, the Iranian party contended that the MOU did bind the parties, while the Swedish supplier sustained that such document did not bind them, since it had not agreed upon the specific contracts to be negotiated in the framework of such general scheme. The arbitral tribunal awarded damages to the Iranian party for the loss of the ability to enjoy the probable benefits of the aborted projects. In that respect, the tribunal invoked Article 5.1.4(2) of the UNIDROIT Principles[11] and concluded that rules that the expression of the intent to conclude a contract in general terms contained in the memorandum of understanding *binds* the parties to put their best efforts in order to conclude the contract. Pursuant to the decision of the tribunal, the respondent was obliged to recover damages caused to the claimant by breaching the obligation to put its best efforts in order to conclude the contract provided for in the memorandum of understanding.[12]

In another ICC case, a US supplier of telecommunications systems and a Middle Eastern supplier of cables entered into an agreement whereby the parties undertook to negotiate in good faith the supply of cables to the US party if the latter succeeded in becoming prime contractor for a telecommunications expansion project. The agreement did not contain a choice-of-law clause. The US supplier obtained the contract and became prime contractor, but the

9 Comm. Bruxelles, 24 juin 1985, Journal des Tribunaux (Bruxelles), 1986, p. 236.

10 Bruxelles, 14 juin 1984, Revue de droit commercial belge, 1985, p. 472.

11 This article stipulates: "To the extent that an obligation of a party involves a duty of best efforts in the performance of an activity, that party is bound to make such efforts as would be made by a reasonable person of the same kind in the same circumstances".

12 ICC case 8331/96, in ICA Bull., 2/1999, p. 67. Cited in [3, p. 105].

parties were not able to reach an agreement on the supply of cables. The question as to whether the undertaking to negotiate in good faith was valid and enforceable. The arbitral tribunal took the stance that, in determining the applicable law, it should prefer a legal system that would satisfy the expectations of the parties, i.e., a legal system under which the agreement would be considered valid. The tribunal decided in favor of New York law, after having ascertained that under such law the agreement would be enforceable. In addition, the tribunal emphasized that this result was in conformity with general principles of the law of international trade as expressed in the UNIDROIT Principles.[13]

On the other hand, the traditional position of English law with regarding the refusal of pre-contractual liability is systematically applied by the English courts to the agreements on negotiations in modern business transactions. English courts refuse to give any legal effect to this kind of agreements. Two decisions of English courts illustrate this standpoint. In one of the cases, *Cleveland Bridge* informed, by means of a letter of intent, *British Steel* of its willingness to conclude a contract with them and authorized them at the same time to begin the performance of that contract. The Court came to the conclusion that, in that case, no contract was concluded after the letter of intent was sent, despite the fact that one of the parties started to perform.[14] In another case, *Waldorf v. Miles*, the House of Lords invoked the freedom of the negotiating parties to decide whether they want to conclude the contract or not and pointed out that English law does not recognize contracts which stipulate the commitment to conclude a contract, which includes the agreements on negotiations.[15] This decision was heavily criticized in English doctrine [6, p. 50].

Consensual exclusion of obligations arising out of negotiations. In certain cases, the parties decide to include in their agreements on negotiations a clause which expressly provides for exclusion of any obligations that might arise from negotiations. An example of such clause would be the following provision of a letter of intent: "All of the terms and conditions of the proposed transactions would be stated in the Purchase Agreement, to be negotiated, agreed and executed by the Parties. Neither Party intends to be bound by any oral or written statements or correspondence concerning the Purchase Agreement arising the course of negotiations, including this letter of intent, notwithstanding that the same may be expressed in terms signifying a partial, preliminary or interim agreement between the Parties", or the following provision of a memorandum of understanding: "The present MOU is not legally binding the parties. The exact terms and conditions of the future cooperation will be negotiated in due course and laid down in a contract, should circumstances permit".[16] These clauses express the will of the negotiating parties to "dislocate" their agreement from the legal domain (*opting out clause*) and to conclude some sort of a "gentlemen's agreement" deprived of *legal* sanctions [2, pp. 115-157]. In that context, questions may be raised as to the validity of the clause excluding any legal effect of the agreement concluded.

Comparative law shows different approaches to this question. The French law starts from the rule contained in the Code of Civil Procedure which allows to the parties to bind the court by their legal characterizations,[17] so in the light of that provision it is considered that the parties are entitled to exclude, by means of their equivocal expressions of will, the contractual character of their agreement [12, p. 58]. French law generally admits the validity of "gentlemen's agreements" and other "moral commitments", but the court is not automatically bound by the characterization of the parties with respect to the legally non-binding nature of their agreement if the circumstances of a specific case lead to conclude otherwise [6, p. 51]. The Belgian legal doctrine points out that the court must respect the equivocal will of the parties to deprive their agreement of legal effects, but only to the extent that this is not contrary to public policy and mandatory norms [6, p. 51]. On the other hand, the Dutch authors consider that "gentlemen's agreements" do not have the legal force of a contract, which does not necessarily mean that they are deprived of any legal effect

13 ICC award 8540/96, published on the Unilex website [cited in 3, p. 104].

14 *British Steel Corp. v. Clevland Bridge & Engineering Co.*, (1984), All England Law Reports, p. 504.

15 1 Weekly Law Reports, p. 174 (1992).

16 The examples of clauses given pursuant to [8, pp. 49-50].

17 *Code français de procédure civil*, Art. 12(4).

[23, pp. 214-254]. In contrast to the somewhat reserved attitude of the civil law countries towards legal effect of these agreements, English law widely accepts the validity of the clauses which exclude legal effects of the agreement concluded (*subject to contract clauses*).[18] Finally, according to the views expressed in American law, this kind of clauses is considered valid, although certain acts of the parties may nevertheless lead to their invalidity.[19]

The overview of the approaches taken in comparative law on the issue of the clauses which serve to exclude pre-contractual liability shows great diversity and considerable hesitance in taking a firm stance with respect to their admittance or challenge of their validity. The only exception is English law, which admits this type of clauses without reservation. For these reasons, it may be concluded that the validity and legal effect of "gentlemen's agreements" primarily depend on the principles and solutions regarding the negotiations and pre-contractual liability in general accepted by the applicable law.

Confidentiality agreements

During the negotiations, parties often conclude agreements by virtue of which they commit to keep the information disclosed during negotiations confidential. Such an agreement may be phrased as a clause inserted into the text of am agreement on negotiations (*confidentiality clause*), or as a separate agreement – confidentiality agreement. In any event, the duty of confidentiality may bind just one or both negotiating parties. The duty of confidentiality is particularly often in negotiating transfer of technology agreements and know-how licenses, joint ventures, contracts for acquisition of company, distribution contracts, as well as other contracts which require disclosure of confidential information in order to enable the other party to assess all the circumstances relevant for the conclusion of the contract.

In practice, confidentiality clauses are often phrased in very broad terms: "The terms and conditions of this Agreement shall be treated as confidential and such terms and conditions shall not be disclosed in whole or in part by either of the Parties without the prior consent of the other Party", "The Parties agree to keep confidential all business and technical information relating to and acquired in the course of their activities connected with the present MOU", "You shall hold secret all know-how and other confidential information disclosed to you by the Company or its employees".[20]

Duty of confidentiality of the parties who negotiate the contract is provided for by the UNIDROIT Principles under which: "Where information is given as confidential by one party in the course of negotiations, the other party is under duty not to disclose that information or to use it improperly for its own purposes, whether or not a contract is subsequently concluded. Where appropriate, the remedy for breach of that duty may include compensation based on the benefit received by the other party" (Article 2.1.16).

One of the key problems in practice with respect to confidentiality clauses as they are usually drafted in practice is to define what the confidential information is. As long as the party expressly declares that the information is to be considered confidential, it is clear that the receiving party is obliged to treat it as confidential. However, even in the absence of such an express declaration, the receiving party may be under a duty of confidentiality. This is the case where, in view of the particular nature of the information or the professional qualifications of the parties, it would be contrary to the principle of good faith and fair dealing for the receiving party to disclose it, or to use it for its own purposes after the breaking off negotiations [11, pp. 62-63]. Other problems that usually arise with respect to the confidentiality during negotiations are primarily related to the duration of duty of confidentiality and to the remedies of the aggrieved party in case of breach of confidentiality [6, pp. 304-311].

Agreements on certain aspects of negotiations

In certain cases, the negotiating parties insert in their agreements on negotiations the clauses which oblige one or both parties not to enter parallel negotiations with

18 See: [6, p. 51]. For more examples, see *Rose and Frank Co v. Crompton Brothers Ltd* (1925), Law reports, Appeal cases, 445; *Walford v. Miles* (1992), Law reports, Appeal cases, 128.

19 See in that sense: *Texaco Inc. v. Pennzoil Co*, 784 Federal Reporter (Second Series), 1133 (2nd Cir. 1986); [5, pp. 155-172].

20 The examples of the clauses given pursuant to [8, pp. 241 et seq.].

third persons aimed at concluding the same contract – exclusivity clause. As a rule, the duty of exclusivity is time-limited and usually refers to a certain deadline or the realization or fulfillment of certain preconditions during the negotiations. The exclusivity clause contains clearly defined essential elements with respect to which the meeting of the minds of the negotiating parties has been achieved. Consequently, the confidentiality clause represents an agreement of a contractual nature, irrespective of the circumstance that the duty of confidentiality binds just one or both parties.

This being said, one may ask whether the duty of exclusivity exists even when it is not expressly provided for, i.e. whether the duty of a negotiating party to refrain from entering parallel negotiations during the initial negotiations stems from the very principle of good faith and, consequently, exists even in absence of an express agreement. It seems that the answer to that question is in principle negative. Parallel negotiations represent a common practice in business transactions on competitive markets and they constitute an expression of the freedom of contracting, pursuant to which each party is free to choose its contracting partner. For these reasons, the freedom to engage in parallel negotiations aimed at conclusion of the same contract should generally not be denied. However, the problem must be assessed in the light of all relevant circumstances of each particular case. Consequently, the aforestated general conclusion may be nuanced. For example, if the parties stipulated, in their agreement on negotiations, hard commitments with respect to the negotiation process, including the duty to put their best efforts into concluding the contract and to lead the negotiations in good faith, the unilateral withdrawal from negotiations of a party wishing to conclude a contract with a third person may, if the other circumstances of the case allow for such a conclusion, represent the violation of the principle of good faith, irrespective of the fact that the exclusivity clause had not been expressly stipulated [6, pp. 32-33].

Agreements on negotiations often include a clause which sets the time limits and the dynamics of negotiations, as well as the deadlines for conclusion of a contract. An example of such clause is contained in the following provision of a letter of intent: "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 30 days of the beginning of the initial discussions". These clauses may provide for conditions and modalities of cessation of negotiations: "Within 120 days after completion of the feasibility study, each party shall inform the other as to whether it wishes to implement the project. In the event either party fails to so inform the other or decides not to implement the project, this letter of understanding shall be thereupon deemed terminated and neither party shall have any obligation thereafter to the other (subject to surviving secrecy obligations)...".

Other possible clauses whereby the parties set up rules for future negotiations are those by which the parties grant each other a right of first refusal [3, p. 111], provide for the reimbursement of certain expenses in case of failure to conclude the contract, agree on organization and costs of feasibility studies, etc. [6, pp. 32-38].

Recommendations to negotiators

Considering the indicated differences in comparative law it can be difficult to determine the extent of the parties' liability during negotiations without analyzing the legal system applicable in a specific case. Therefore, as a first step, the negotiators should identify the rules that govern the type of negotiation agreement in question in order to verify whether these rules conform to the expectations of the parties and whether there are mandatory rules that cannot be derogated by contract [3, p. 106]. It is equally important to define the dispute resolution mechanism in case the negotiations fail, as this is, in terms of legal certainty, a very sensitive phase in the development of a business transaction. To that end it is highly recommended to opt for arbitration as the preferred dispute resolution mechanism, since the international (or should we say a-national) character of this mechanism seems the best suited for the international character of the legal relation between the parties to international business transactions [15, pp. 31-47].

Upon identifying the legal framework in which the agreement is to be placed and the jurisdiction for eventual disputes, the negotiators should start to draft the terms of the agreement. The agreement should define in the most precise possible way the intents of each parties during negotiations and, as well as the scope of each particular clause in order to avoid any possible misunderstanding. The parties can explicitly state that certain (or all) statements in the agreement are not legally binding. The example of such type of clauses could be: "All of the terms and conditions of the proposed transaction would be stated in the Agreement, to be negotiated, agreed and executed by the parties. Neither party intends to be bound by any oral or written statements or correspondence concerning the Agreement during the course of negotiations". In the same context, the parties may expressly provide that a certain issue on which the meeting of the minds is not achieved during negotiations is of substantial importance for the contract, so without that meeting of the minds the negotiations do not bind the parties. Similarly, the parties may provide that the binding character of an agreement depends on a certain requirement of form (e.g. signing of a document in written form), they may enter the "subject to contract" clause etc. [8, p. 58]. On the contrary, the parties can expressly state that certain undertakings, as for example exclusivity and confidentiality duties, are legally binding, providing for the legal consequences and remedies in case of their breach. Before drafting these and similar clauses, the negotiating parties must always check whether they would be valid pursuant to the law applicable to their agreement.

Model contracts/clauses drafted by international organizations normally represent a result of a worldwide compromise offering companies engaged in international trade set of simple, fair and well-balanced rules that can help them negotiate and draft international contracts. Thus, model contracts and standard clauses are a very valuable tool for drafting the key elements of the agreement in question. In that respect, it should be noted that to date, the ICC has published fourteen model contracts: the ICC Model Commercial Agency Contract (ICC Publication No. 496), the ICC Model Distributorship Contract (ICC Publication No. 518), the Model Occasional Intermediary Contract (ICC Publication No. 619), the ICC Model International Sale Contract – manufactured goods intended for resale – (ICC Publication No. 556), the ICC Model International Franchising Contract (ICC Publication No. 712), the ICC Short Form Model Contracts International Commercial Agency and International Distributorship (ICC Publication No. 634), the ICC Model Contract for Turnkey Supply of an Industrial Plant (ICC Publication No. 653), the ICC Model Selective Distributorship Contract (ICC Publication No. 657), the ICC Model Mergers & Acquisitions Contract 1 – Share Purchase Agreement (ICC Publication No. 656), the ICC Model Confidentiality Agreement (ICC Publication No. 664), the ICC Model Turnkey Contract for Major Projects (ICC Publication No. 659), the ICC Model International Trademark Licence (ICC Publication No. 673), the ICC Model Transfer of Technology Contract (ICC Publication No. 674), The ICC Model Subcontract – ICC Model Back-to-back Subcontract to ICC Model Turnkey Contract for Major Projects (ICC Publication No. 706). As far as the texts prepared by the ICC are concerned, the recently published Principles to Facilitate Commercial Negotiations are particularly important in the matter of negotiations, since they offer a practical guideline for negotiators in cross-border transactions.[21] Apart from ICC, model contracts are also drafted by the International Trade Centre (ITC), which published a series of Model Contracts that take into account the increasing sophistication of international trade transactions and incorporate internationally recognized standards and best practices [10, foreword].

While model contracts certainly are of great importance for drafting and negotiating a particular contract, they should not be used without the appropriate knowledge on how to adapt them to the specific needs of the parties. That is why the parties should prepare the negotiations with the assistance of a lawyer who will make sure that the undertakings of the parties are lawful and effective. The same need for a close cooperation between the businessman and the lawyer exists during the whole negotiation stage, so that the parties are able to fully understand the legal aspects and especially legal consequences of the proposed

21 See http://www.iccwbo.org/News/Articles/2013/New-ICC-business-principles-help-traders-navigate-world-of-international-deal-making/

solutions. The assistance of the lawyer from the very beginning is particularly important where the contract is to be governed by a law different from the laws of negotiators. In such a case, the optimal solution would be to require advices of a lawyer from the country whose law is to be applied or who is otherwise familiar with the rules applicable to the agreement in question [3, p. 109].

Conclusion

The overview of rules and practices regarding negotiations in comparative law shows that two major legal systems – civil law system and common law system – take diverging approaches with respect to the legal effect of negotiations. These divergences in approach primarily stem from the different treatment of the principle of good faith in two respective legal systems. Serbian contract law, typically for a civil law system, provides for pre-contractual liability of the party which negotiates in bad faith. Therefore, the parties coming from civil law background should not encounter major differences in the legal regime applicable to the negotiations in the event that Serbian law governs the negotiations in which they take part. However, the same does not apply for the parties coming from common law countries.

In any event, in light of the principle of freedom of contracting, negotiating parties are allowed to shape the legal regime applicable to their negotiations by derogating from the provisions contained in the relevant contract law. This may be done by concluding different kind of agreements on negotiations. If the negotiating parties decide to establish a special regime for their negotiations, they should be strongly encouraged to resort to model contracts or model clauses drafted by one of the international organizations that promote unification of business law.

Whatever path the negotiating parties decide to take in creating the legal framework for their negotiations, they should be aware that the predictability of solutions is of the utmost importance in international business relations. Bearing in mind that such transactions involve parties from foreign markets and that such contracts are often governed by foreign law, the predictability of the applicable legal regime is an indispensable element of legal certainty in international trade. This is particularly true in case of failed negotiations, as under some national laws – such an outcome may result in party's liability for the damages suffered by its negotiating partner. Consequently, business people should, before entering into negotiations, take into account the potential costs of failed negotiations.

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