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The Development of the Concept of Pre-contractual Duties in Estonian Law

The knowledge that there are pre-contractual duties that could lead to a liability if breached is new to Estonian lawyers. The relevant regulation was introduced with the new Law of Obligations Act¹, which entered into force on 1 July 2002 and thoroughly altered the existing understanding and concepts of contract law, torts, and other obligations.

The Law of Obligations Act (LOA) contains specific regulation on pre-contractual duties (LOA § 14). As a general rule, LOA § 14 (1) requires the parties who have started negotiations over the conclusion of a contract to “take reasonable account of each other’s interests and rights”. This leads specifically to an obligation to negotiate in good faith, which in turn amounts to a prohibition to start or continue negotiations without willingness to conclude a contract and precludes the party from ending the negotiations in bad faith without concluding a contract (LOA § 14 (3)). The general principle of acting in good faith during the pre-contractual relations in LOA § 14 (1) is also a source of specific disclosure requirements. The negotiating parties are first required to ensure that the information provided by them to the other party in the pre-contractual phase is true and correct (LOA § 14 (2), first sentence). This leads to liability for any incorrect information submitted during the negotiations, provided that such information influenced the decision to enter into contract or to do so under the agreed terms. The pre-contractual duties related to disclosure of information are not limited to the liability for incorrect information. In addition, the law requires the negotiating parties to actively disclose to the other party all information the knowledge of which is evidently material to the other party in consideration of the purpose of the contract (§ 14 (2), second sentence). The source of the regulation of pre-contractual duties in LOA § 14 has mainly been the German concept of liability under *culpa in contrahendo*, as set out in § 241 (2) and § 311 (2) of the BGB², but the legislator was also influenced by the regulations of pre-contractual duties in the Principles of European Contract Law (articles 2:301 (4) and 2:302) and in the Principles of International Commercial Contracts (articles 2.1.15 and 2.1.16).³

The existence of specific duties between the parties prior to conclusion of the contract was to some extent acknowledged also before the new LOA. Such specific pre-contractual duties were mainly recognised with respect to the disclosure requirements in the pre-contractual phase. However, such duties were largely accepted only where the negotiations had led to conclusion of a contract. In such cases, the duties were conceived not as pre-contractual but, rather, as duties arising under the contract. That the duties in question ought to have been performed prior to the conclusion of the contract was not considered to be important. As the liability

¹ Võlaõigusseadus. – RT I 2001, 81, 487; 2007, 56, 375 (in Estonian). Available in English at <http://www.just.ee/23295> (30.06.2008).

² P. Varul et al. Võlaõigusseadus. Kommenteeritud väljaanne I. (Law of Obligations Act I. Commented edition). Tallinn: Juura 2006, commentary 2 to § 14, p. 58 (in Estonian).

³ *Ibid.*, commentary 2 to § 14, p. 58.

for a possible breach of such duties was contractual by its nature, no specific discussion existed regarding the pre-contractual duties or liability. A good example is a case decided by the Civil Chamber of the Supreme Court in 2001.⁴ A buyer of a house, which was still under construction at the time it was bought, claimed damages from the seller. The claim was mainly based on the fact that the constructive elements of floors and ceilings of the house were made of timber and not from concrete. The buyer claimed that prior to the conclusion of the contract the seller had shown her the project details and blueprints of the house, which provided for a concrete structure. The notarised sales agreement that the parties concluded later on made no reference to the blueprints or specific characteristics of the house, which was sold on an 'as is' basis. Nonetheless, the buyer based her claim on defective performance and argued that the house did not conform to the contract. The Supreme Court obviously did not accept this argument, as it concluded that the mere fact that the floors were constructed from timber and not from concrete did not amount to a defect of the house, as the floors conformed to the applicable construction standards. The Court was obviously of the opinion that the provision of the project providing for concrete floors did not become a part of the sales contract as a contractual promise regarding the quality characteristics of the house. This did not lead to dismissal of the claim, though, as the Court accepted the seller's liability on the basis of a different argument. The Supreme Court pointed out that, irrespective of whether there was an agreement on the nature of the floors, the seller, who had disclosed the blueprints, was under a duty to inform the buyer that the house was not constructed in accordance with these. The seller was hence found to be in breach of the contract. This conclusion seemed so evident that the court did not even bother to ponder on the existence of such disclosure requirements, nor did it reflect on their pre-contractual nature.

1. The nature of pre-contractual liability, between tort and contract

When the new LOA entered into force and introduced a thorough regulation of the duties arising in the pre-contractual phase, the practice had only limited understanding of the purpose of the pre-contractual duties, the cases wherein the breach of such duties would be relevant, and the nature of the liability arising thereunder.⁵ It took some time before the courts and practising lawyers discovered the concept and its practical applications. The constant stream of case law in the last few years has shown that the regulation has not remained a mere concept on paper. A number of decisions from the Supreme Court have developed the concept of pre-contractual liability and amount to a growing legal certainty in the field.

The first issue the courts had to settle with respect to pre-contractual duties was the nature of the pre-contractual liability. Two principal concepts were discussed in the literature. The first of them saw the pre-contractual liability as part of tort law.⁶ In accordance with this concept, the respective duties, listed in LOA § 14, were nothing more than a specific form of a general duty of care the breach of which leads to a liability under the general principles of tort law. A concurring concept entailed the opinion that the pre-contractual relationship and the specific duties arising under it between the negotiating parties leads to a specific legal relationship between the parties (an obligation, or *võlasuhe* in Estonian⁷) the nature of which lies between that of contract and tort.⁸ This is, of course, a concept that is apparently similar to the German understanding of pre-contractual liability (*culpa in contrahendo*), which, as noted above, also served as a basis for the Estonian regulation.

It has to be admitted that, as far as the practical outcome is concerned, there is little difference in whether the breach of pre-contractual duties leads to the liability under a tort or to a quasi-contractual liability. The main difference between these two concepts in Estonian law is that the tort liability is a liability for negligence whereas the quasi-contractual liability for the breach of an obligation is strict liability where any breach leads to a liability except where the breach was attributable to *force majeure* and hence excusable. However, there cannot be very many cases in practice where such a fine distinction is of importance. This is largely because most of the pre-contractual duties can be breached only out of negligence. With respect to such duties, the tort law concept would not lead to a less 'strict' liability than the concept of a quasi-contractual liability, which does not require negligence as a precondition for liability. Nonetheless, there are situations where the choice of concept is indeed relevant. The most important among such cases is the liability for incorrect information provided to the other party during the pre-contractual negotiations. Under a tort concept, the party who provided such information

⁴ CCSCd 30.112007, 3-2-1-131-05. – RT III 2005, 43, 425 (in Estonian).

⁵ A notable exception was an introductory article by I. Kull. Sissejuhatus probleemide: lepingueelne vastutus (*culpa in contrahendo*) (Introduction into a Problem: Pre-contractual Liability (*culpa in contrahendo*)). – Juridica 1994, pp. 214–215 (in Estonian).

⁶ J. Lahe. Lepingueelsete kohustuste ning eellepingu rikkumisest tulenev tsiviilõiguslik vastutus (Civil Liability arising from the Breach of Pre-contractual Obligations and Pre-contracts). – Juridica 2004/10, pp. 681–687 (in Estonian).

⁷ The Estonian institute of an obligation (*võlasuhe*) is very similar to the German *Schuldverhältnis*.

⁸ I. Kull, M. Käerdi, V. Kõve. Võlaõigus I. Üldosa (Law of Obligations I. General Part). Tallinn: Juura 2004, p. 80 (in Estonian).

could be held liable only if he knew or ought to have known that the information provided to the other party was incorrect or if it could at least be proved that the information provided was negligently left uncontrolled by that party. In the quasi-contractual strict liability regime, the risk of liability for incorrect information lies entirely with the party who provided the information, who would be liable irrespective of whether said party knew or could have known of the incorrectness or whether the incorrect information was provided negligently.

The nature of the pre-contractual liability was clarified by the Supreme Court in the decision regarding breach of the duty to negotiate in good faith (addressed in the following section of this paper). The Supreme Court supported the concept of the liability in pre-contractual relations being quasi-contractual and therefore not leading to a tort. Negotiations regarding the conclusion of a contract between the parties lead to creation of an obligation⁹ between the parties negotiating. Under Estonian law, the breach of duties arising under an obligation created under the law entitles the parties to the same remedies as the breach of any contractual obligation. As a result, the liability for breach of the pre-contractual obligations is based on the same principles and provisions as the liability for breach of the obligations arising under the contract. Most notably, the pre-contractual liability is a strict liability, as is liability under a contract, and not a liability for negligence, as with the general tort liability.¹⁰

2. Duty to negotiate in good faith

The essence of the pre-contractual liability and the nature of the pre-contractual duties was first under scrutiny with regard to the duty to negotiate in good faith. The leading case for this practice is the decision of the Civil Chamber of the Supreme Court from 15 January 2007 (case No. 3-2-1-89-06).¹¹ The case had to do with the preliminary contract regarding the purchase of a plot of land. Under the contract, the seller agreed to sell a plot of land, which was to be created through division of a larger plot, to the purchaser for an agreed purchase price. Under Estonian law, such a contract would have required notarisation for validity, but the parties ignored this requirement knowingly (the seller was a real-estate developer and the purchaser was a lawyer). Later on, as the division of land was effected, the parties got into an argument regarding the conformity of the plot intended for the purchaser. The plot was smaller than what was agreed in the preliminary contract, and the purchaser wanted the price to be reduced accordingly. As a result, the seller refused to complete the sale and enter into a duly notarised agreement. The purchaser claimed for specific performance and alternatively for damages because of the non-performance. He calculated such damages on the basis of a difference between the agreed price and the market price for the plot.

With regard to the specific performance, the courts unanimously concluded that the claim was unfounded, as the agreement was invalid because of the non-compliance with the requirements as to form. A far more interesting argument arose with respect to the claim for damages. The purchaser claimed that the seller had breached the pre-contractual duty to negotiate in good faith when refusing to enter into the final notarised agreement, which was necessary to complete the sale. In the purchaser's opinion, such refusal amounted to a bad-faith interruption of negotiations, which is prohibited in accordance with LOA § 14 (3). The courts consequently had to clarify the content of the obligation to negotiate in good faith. It was first held that negotiations in bad faith preclude the party entering into the negotiations without a willingness to enter into the contract and the negotiations being held for purposes not consistent with the principle of good faith, such as with the aim of obtaining sensitive business information from the other party that such party would not disclose but for the negotiations or in order to prevent the other party entering into an agreement with a concurring third party.¹² In addition, the law prohibits the parties from terminating the negotiations in bad faith (LOA § 14 (3), second sentence). The essence of such bad-faith termination of negotiations was under particular scrutiny in the above-mentioned decision of the Supreme Court.¹³ The court stressed that, in determining whether negotiations not leading to conclusion of a contract were terminated in bad faith, one has to bear in mind that mere negotiations do not create an obligation to conclude a contract. In this connection, LOA § 14 (3), first sentence, provides explicitly that the mere fact that the negotiations are ended and do not lead to the conclusion of a contract does not create 'legal consequences' for the negotiating parties. This means that the parties have no pre-contractual obligation under the law to enter into a contract. Such obligation can only be created by entering into a (valid) 'pre-contract'. On the other hand, the prohibition of terminating the negotiations in bad faith (as set out in LOA § 14 (3), second sentence) evidences that, even in the absence of an obligation to conclude a contract, a termination of negotiations and refusal to conclude a contract can lead to a breach of pre-contractual obligations and to a corresponding liability. The question of whether the

⁹ In the sense of III-1:101 DCFR.

¹⁰ P. Varul et al. (Note 2), commentary 4.6 to § 14, p. 62.

¹¹ RT III 2007, 3, 23 (in Estonian).

¹² *Ibid.*, Sec. 15.

¹³ *Ibid.*

negotiations have been terminated in bad faith depends mainly on the state of the negotiations at the time of their termination and on whether the other party could reasonably expect the conclusion of the contract.^{*14} It is evident that such expectation is dependent on how far the negotiations have proceeded.^{*15} If, at some point in their negotiations, the parties have acknowledged that they have agreed on the essential conditions of their contract, such acknowledgement would normally be sufficient to create reasonable expectation that the contract would indeed be concluded under the agreed terms. Any subsequent termination of the negotiations and refusal to conclude the contract would hence be contrary to good faith and amount to a breach of pre-contractual obligations under LOA § 14 (3), second sentence. The breach of pre-contractual obligations and bad faith termination is particularly evident where the acknowledgement or agreement to enter into the contract on agreed terms is documented in a pre-contract, memorandum of understanding, or similar document and the negotiations are terminated without valid grounds, despite such acknowledgement. This applies even when such a document is not valid because of the non-fulfilment of requirements concerning form, as was the case in the above-mentioned decision of the Supreme Court.^{*16}

A different issue is the question regarding the consequences of negotiations in bad faith. In considering this, the courts have concluded that, since an obligation to conclude a contract can be created only on the basis of a valid pre-contract, the pre-contractual duty to negotiate in good faith and the attendant prohibition from terminating negotiations in bad faith cannot lead to the compensation of the positive interest. A party who suffered damages because the other party started or terminated negotiations in bad faith cannot therefore file a claim with the goal of being placed in the situation that would have existed if the parties had concluded a contract. In the decision discussed above, the Supreme Court stressed that, although the purchaser could rely on the conclusion of the contract on the basis of the state of the negotiations and agreements evidenced in the invalid pre-contract and the termination of negotiations by the seller was hence performed in bad faith, the purchaser could not claim damages on the basis of the profits lost because of the non-conclusion of the intended contract. The pre-contractual duty to negotiate in good faith merely protects the reliance interest of the parties. Consequently, in the case of a breach, the aggrieved party is to be put in a situation as would have existed if that party had not relied on the negotiations being held in good faith.^{*17} This would mainly lead to the compensation of expenses that the party incurred during the negotiations, such as cost of time, travel costs, or costs related to the drafting of the contract.^{*18} In addition to this, the courts have recognised that in certain cases the protection of reliance interest can lead to compensation of expenses that the aggrieved party has made in reasonable reliance on the conclusion of the contract, such as costs, break fees, or similar expenses under the agreements that the party has entered in reliance on the conclusion.^{*19} It is clear that, prior to the contract's conclusion, such reliance can exist only under special circumstances, mainly where the other party has acknowledged that agreement has been reached in all essential respects, such that the conclusion of the contract is a mere formality. Even in such cases, only reasonable expenses incurred in reliance on such acknowledgement can be recovered as damages.

3. Duty to ensure the validity of a contract

The pre-contractual duties of the parties can involve an obligation to ensure that the contract concluded as a result of such negotiations is valid. Such duty is seldom explicitly stipulated in law. There is also no specific regulation to this effect in Estonian law. The fact that there must be pre-contractual duties regarding the guarantee of validity can be deduced from the various provisions that entitle a party to damages if a contract concluded with the other party is void or becomes invalid (such as through a successful avoidance) for reasons attributable to the other party.

In Estonian law, such regulation can first be found with respect to invalid contracts. A party is entitled to damages in accordance with LOA § 15 (2) if a contract concluded by that party is invalid because of factors attributable to the other party. The same applies if that other party knew or ought to have known of the circumstances leading to invalidity but did not disclose them prior to conclusion of the contract. Similar regulation exists with respect to avoidable contracts. A party who avoids a contract because of a mistake, fraud, or undue influence is entitled to damages in accordance with § 101 of the General Part of the Civil Code Act^{*20} (GPCCA) if such

¹⁴ P. Varul et al. (Note 2), commentary 4.4 to § 14, p. 61.

¹⁵ CCSCd 3-2-1-89-06 (Note 11), Sec. 16.

¹⁶ *Ibid.*, Sec. 15.

¹⁷ *Ibid.*, Sec. 16.

¹⁸ *Ibid.*

¹⁹ *Ibid.*: financing costs or interest payments under financing arrangements entered into in reliance of the conclusion of the contract, costs of valuation of the object of the contract for financing purposes, etc.

²⁰ Tsiviilseadustiku üldosa seadus. – RT I 2002, 35, 216; 2007, 24, 128 (in Estonian). Available in English at <http://www.just.ee/23295> (30.06.2008).

mistake, fraud, or undue influence was caused by the other party or if that other party knew or ought to have known of such circumstances but did not disclose them to the party influenced by such circumstances. Specific rules exist for cases where the invalidity of a contract is due to non-compliance with the form requirements. In LOA § 15 (1) it is provided that, if a party is responsible for preparation of the contract or had to inform the other party of the circumstances related to the conclusion of the contract and the contract is found invalid due to non-compliance with the form requirements, said party is responsible for the damages that the other party sustained because of reliance on the validity of the contract. Responsibility for the preparation of the contract or provision of information regarding the circumstances surrounding the conclusion is usually created when a professional party negotiates with a non-professional who can hence rely on a professional's knowledge to take all steps necessary for due preparation of the contract documentation and for a valid conclusion.^{*21} In practice, the provisions of LOA § 15 (1) have mainly been applied with respect to liability proceeding from invalid (pre-)contracts in the real-estate deals that were entered into in a non-notarised form on the initiative of a professional seller.^{*22} In the above decision of the Supreme Court where the pre-contract related to the purchase of a plot of land was found void because of non-adherence to the form requirements, the purchaser of the plot claimed that as a professional real-estate developer the seller was responsible for preparing the contract documentation.^{*23} One of the major issues in cases related to liability under LOA § 15 (1) has been the fact that since the requirement to notarise a real-estate contract and the consequences of non-adherence to this requirement are generally known, a purchaser who is prepared to enter into a real-estate agreement in a non-notarised form would be acting with gross negligence. As to the issue of how such negligence on the part of the purchaser influences the seller's liability under LOA § 15 (1), the courts have ruled that the reliance by the purchaser on the validity of the contract and the corresponding seller's liability should be excluded only if the purchaser knowingly enters into an invalid agreement.^{*24} If the positive knowledge of the purchaser cannot be proved, simple negligence or even gross negligence is not sufficient to exclude the seller's liability under LOA § 15 (1).^{*25}

With respect to the liability arising due to the breach of duties regarding ensuring of the validity of a contract, the law again protects merely the reliance interest and not the positive interest of the parties; this is generally the case where pre-contractual duties are concerned. In particular, the liability under an invalid contract does not protect the interest toward fulfilment of the contract and cannot lead to a situation where the party entitled to damages because of the invalidity is put in a situation that would have existed if the contract had been valid.^{*26} The law protects reliance on the validity of a concluded contract. If such reliance is not realised, on account of breach of the above-mentioned pre-contractual duties by the other party, the latter is responsible for damages. Such damages again involve the expenses related to negotiations.^{*27} As was discussed above, the damages can also be calculated on the basis of expenses incurred in reliance on the contract. Such expenses become damages if and insofar as they lose their purpose because of the invalidity of the contract. The courts have pointed out that in the case of a contract that has already been concluded (even though it is invalid) the reliance of a party on the validity of the contract is, as a rule, stronger than in the case where negotiations have not yet amounted to conclusion of the contract.^{*28} This means that, in general, any dispositions made by a party to an invalid contract can be deemed to have been performed in reasonable reliance on a contract such that the related expenses are collectable as damages, provided that the party who incurred such expenses did not know of the invalidity.^{*29} As an example, it has been found reasonable that a purchaser of a plot of land who does not know that the pre-contract concluded with the seller is invalid incurs expenses in the amount of approximately €4000 for the planning and design work related to the plot^{*30} whereas the same expenses can seldom be incurred in reasonable reliance on a contract prior to its conclusion irrespective of the state of negotiations.

²¹ P. Varul et al. (Note 2), commentary 4.1 to § 15, p. 66.

²² From the practice of the Supreme Court: the CCSCd 19.06.2007, 3-2-1-70-07 (RT III 2007, 26, 220; in Estonian)), Sec. 12–13 and CCSCd 3-2-1-89-06 (Note 11), Sec. 14.

²³ CCSCd 3-2-1-89-06 (Note 11), Sec. 16.

²⁴ In the case underlying the CCSCd 3-2-1-89-06, the positive knowledge of invalidity was established in case of a purchaser who was a professional lawyer.

²⁵ CCSCd 3-2-1-70-07 (Note 22), Sec. 12.

²⁶ CCSCd 3-2-1-89-06 (Note 11), Sec. 16.

²⁷ Loss of time, travel expenses, expenses for the legal aid, etc., see CCSCd 3-2-1-89-06 (Note 11), Sec. 16.

²⁸ *Ibid.*

²⁹ *Ibid.*

³⁰ S. CCSCd 3-2-1-70-07 (Note 22), Sec. 12.

4. Pre-contractual disclosure requirements and liability for incorrect information

The most important group of pre-contractual duties relates to pre-contractual disclosure requirements and to liability for incorrect information provided to a party during the pre-contractual negotiations.

The question of whether there the parties to a contract should in any way be under an obligation to disclose certain information to the other party in a pre-contractual phase is a matter of great debate among proponents of the various legal systems in Europe. The spectrum of possible solutions starts with the relatively wide disclosure requirements under the German law (disclosure of all material information that the other party can await in good faith) to the approach of England and Wales, with almost no disclosure at all required. This diversity is also reflected in the fragmented regulation of pre-contractual disclosure requirements in articles 3:101–3:106 of Book II of the DCFR, which avoids any references to general disclosure requirements and limits itself to a catalogue of duties to disclose certain specific information, mainly in B-to-C relations.

With regard to pre-contractual information duties, the Estonian law has chosen the German approach, with an explicit regulation of such pre-contractual duties by recognising a general information duty with wide disclosure requirements based on the principle of good faith and fair dealings. As a general rule, LOA § 15 (2), first sentence, provides that each of the negotiating parties is bound to disclose to the other party any information the knowledge of which is apparently material to that other party. This duty is, however, not unlimited. In accordance with LOA § 15 (2), second sentence, the disclosure is required only if and insofar as the other party could have reasonably expected the disclosure in accordance with the principles of good faith and fair dealings. The question of when disclosure of particular circumstances can be expected in accordance with the principles of good faith can be determined in accordance with the principles set out in GPCCA § 95. This provides that, in determining whether disclosure is required, account has to be taken of whether the interest of the other party in the particular information was apparent to the party from whom disclosure is expected, whether the parties have special expertise and knowledge, the costs of obtaining the information, and whether the other party could have obtained the information from another source.

In addition to disclosure in accordance with LOA § 15 (2), the law requires that any information, related to the contract, that is provided to the other party prior to conclusion of the contract is to be true and correct (LOA § 15 (1), second sentence).

Liability for breach of pre-contractual disclosure requirements is somewhat different from liability for breach of other pre-contractual duties, most notably of the duty to negotiate in good faith or of the duty to ensure the validity of the contract. This is mainly due to the fact that, although there can be situations wherein a breach of disclosure requirements or provision of incorrect information by the other party is discovered prior to the conclusion of the contract and leads to the termination of the negotiations^{*31}, the insufficient disclosure or provision of incorrect information would, as a rule, become relevant only if such circumstances are discovered after the parties have concluded a valid contract.

First and foremost, this leads to the question of whether there is room and need at all for the pre-contractual liability in situations where the negotiations have been successful and have ended with the conclusion of a valid contract. If the pre-contractual liability would still be of relevance in such circumstances, its relationship and possible concurrence with the contractual remedies would have to be cleared.

5. Pre-contractual disclosure requirements and liability under the contract

For a number of cases it can indeed be concluded that the breach of pre-contractual duties would lose its relevance if a valid contract is concluded. This is most evident if the breach relates to the disclosure of incorrect information related to the object of the contract. As a general rule, such information would form a part of the parties' agreement as a contractual promise. Any incorrectness of such information would then amount to a breach of a contract and entitle the recipient party to contractual remedies for non-performance. As an example, if a seller of a used car has declared to the potential purchaser, prior to conclusion of a sales agreement, that the car has no accident record, this statement becomes part of the agreement even if this statement is not made in the agreement documented upon conclusion. If the purchaser discovers after conclusion of the agreement that the statement was incorrect, he is entitled to contractual remedies for non-performance.^{*32}

³¹ S. CCSCd 3-2-1-89-06 (Note 11), Sec. 15.

³² Example from P. Varul et al. (Note 2), commentary 3.3.1 to § 217, p. 42.

In this case, the pre-contractual liability for provision of incorrect information is irrelevant, as the purchaser has sufficient remedies for non-performance of the contractual promise. On the other hand, a contract could contain a merger clause that would, in most cases³³, prevent the parties from making recourse to measures for breach of pre-contractual disclosure requirements. In such a case, there is also no recourse to pre-contractual liability, as this is excluded by the contract itself.

There are cases, however, wherein the contractual remedies for non-performance do not provide adequate protection in the event of a breach of pre-contractual obligations. In general terms, this applies in situations wherein the contractual expectations of a party that are partly based on promises given or information provided by the other party in the pre-contractual phase are not fulfilled but the traditional contractual remedies for non-performance fall short because the information or promises have not amounted to a contractual promise. In the Estonian practice, such cases have arisen mainly in connection with sales agreements.

The first of these notable cases was referred to at the beginning of this article and involved a purchase of a house by a seller who was, on the basis of drawings of the house presented to her, convinced that the house had concrete floors.³⁴ As a valid sales agreement existed between the parties, the courts were first bound to examine whether the purchaser was entitled to contractual remedies due to the non-conformity of the purchased house with the agreement. The courts were not convinced that this was the case, as the house was not unfit for the purposes for which a house would usually be used, nor was it of a lower quality than similar, comparable houses. The courts were also of the opinion that the mere fact that the purchaser was able to look at the drawings of the house did not necessarily lead to the conclusion that all information and technical data contained in such drawings amounted to a contractual promise such that any discrepancy from the drawings presented would have amounted to non-conformity of the house with the sales agreement. These arguments make sense in a situation in which the agreement itself contained no references to the drawings. However, as we saw, this did not mean that the purchaser was left entirely without protection. In this particular case, the Supreme Court concluded that, although the house sold by the seller might have conformed to the agreement, the seller had breached a duty to inform the purchaser about the material changes undertaken in the course of construction, compared to the drawings that were introduced to the purchaser.

A similar case was decided by the Supreme Court a few years later.³⁵ This time, a purchaser of a flat claimed he was, at some point during the pre-contractual negotiations, shown the drawings of the house. The drawings indicated that there would be a glass wall directly opposite the front door to the purchaser's flat. In addition, the drawings allegedly provided that there would be a doorway in the wall with access to a public balcony providing great views of an adjacent church. The purchaser claimed to have been prepared to purchase the flat for the agreed price precisely because of the above factors; however, none of this information was contained in the notarised sales agreement, which defined the object of the sale only through references to the flat. As it came out later, the drawings that were shown to the purchaser had already been changed during the time of the conclusion of the sales agreement with the purchaser. The glass wall was indeed constructed, but it was not transparent. The balcony was sold as part of a neighbouring flat and was not publicly accessible. Again the courts had apparent difficulties in acknowledging that the object of the sale was not in conformance with the agreement.³⁶ The case was therefore mainly heard as a dispute over the alleged breach of pre-contractual disclosure requirements.³⁷

The concurrence of the pre-contractual liability for undue disclosure or provision of incorrect information and contractual liability for non-conformity with a contract is most clearly evidenced in the latest case concerning pre-contractual liability, decided on by the Supreme Court.³⁸ In this case, the purchaser acquired a plot of land for the purposes of constructing a family home. The plot was fairly small and had a size of only 907 m². This was correctly reflected in the sales agreement and corresponded to the information contained in the Land Register. The purchaser had inspected the plot with the seller prior to conclusion of the contract. The plot was partly surrounded by a fence. The purchaser rightfully claimed that it had assumed that the fence marked the border of the plot, which therefore in the inspection did not appear to be so small at all. It was only after the conclusion of the contract that the purchaser discovered that to a large extent the fence was located on neighbouring plots that belonged to the seller. In fact, the area of the land bordered by the fence was 1162 m² — that is, 22% larger than the 907 m² plot that was the object of the sale. Consequently, the purchaser claimed for reduction of the purchase price. The claim was based on the alleged non-conformity of the plot with the agreement. This was rightfully denied by the courts, as it would have precluded the object

³³ There can be exceptions where the adherence to the merger clause would be contrary to good faith, for example if the seller knowingly provided incorrect information to the purchaser and included a merger clause to the contract in order to avoid liability, in such case the seller could be prevented from relying on the merger clause, see P. Varul et al. (Note 2), commentary 3.3.1 to § 217, p. 42.

³⁴ CCSCd 3-2-1-89-06 (Note 11).

³⁵ CCSCd 19.11.2007, 3-2-1-111-07. – RT III 2007, 41, 324 (in Estonian).

³⁶ *Ibid.*, Sec. 13.

³⁷ *Ibid.*, Sec 14. In the end the purchaser was not successful with its claims, however this was mainly due to the insufficient evidence brought by the purchaser to support its claims.

³⁸ CCSCd 12.12.2007, 3-2-1-113-07. – RT III 2007, 46, 373 (in Estonian).

of the sales agreement being a plot with an area of 1162 m².^{*39} Quite clearly, this was not the case. The non-performance by the purchaser was again based on non-fulfilment of the contractual disclosure requirements, as the principle of good faith would have required the seller to disclose to the purchaser that, contrary to the obvious appearance, the fence was not constructed on the border.

These examples show that in specific cases the pre-contractual liability can indeed supplement the liability for the breach of contractual liabilities. If the contract has been validly concluded, the breach of pre-contractual duties becomes relevant where the contractual expectations of a party are based on the breach of pre-contractual disclosure requirements or incorrect information provided to that party prior to conclusion of the contract. The pre-contractual duties are important where the non-disclosure of specific circumstances or promises or expectations resulting from incorrect information provided to the purchaser do not become part of the agreement. In such cases, the party who relied on the information should be entitled to concurrent remedies irrespective of whether the duties with respect of which the breach occurred are contractual or pre-contractual in nature.

6. Remedies for breach of pre-contractual disclosure requirements

The exact nature of the remedies that are available to a party to a valid contract in the event of breach of the pre-contractual obligations related to disclosure or provision of correct information is not self-evident. Indeed, there are a number of concurring remedies available.

First one has to bear in mind that the breach of pre-contractual disclosure requirements or provision of incorrect information would normally amount to a fundamental mistake or fraud, which would enable the affected party to avoid the contract. Under Estonian law, the concept of a legally relevant mistake (which can lead to avoidance of the contract) is closely related to the breach of pre-contractual disclosure requirements. The law enables avoidance of a contract that was entered into under a fundamental mistake, if the mistake was caused by or known to the other party or in cases of a shared mistake (GPCCA § 92 (3)). A mistake deemed to be caused by the other party is defined as a mistake that was caused by (incorrect) information given by the other party or through non-disclosure of information, provided that the other party would have been required to disclose such information in accordance with the principle of good faith (GPCCA § 92 (3) 1)). A mistake 'known to the other party' entitles the party given the mistaken understanding to avoid the contract if the other party knew or ought to have known the mistake but contrary to the principle of good faith did not disclose said mistake (GPCCA § 92 (3) 2). It is evident that in both of these cases the other party who causes a mistake through misrepresentation or knows of the mistake but leaves it undisclosed simultaneously breaches its pre-contractual obligations under LOA § 14 (1) and (2). The same is true in the case of fraud — i.e., in cases where the above misrepresentations are fraudulent in nature (GPCCA § 94). On the other hand, breach of pre-contractual duties regarding the disclosure and provision of correct information always seems to entitle the affected party to avoid the contract if the mistake caused through misrepresentations by the other party was fundamental or amounted to a fraud. As a result, the first remedy for a party affected by the breach of pre-contractual duties regarding the disclosure or provision of correct information is the avoidance of the contract. If the contract is avoided, the avoiding party is also entitled to damages in accordance with GPCCA § 101. Typically in cases of breach of pre-contractual duties, such damages are only awarded for the purposes of putting the avoiding party into the position it would have had if it had not entered into the contract (GPCCA § 101 (1)). Therefore, only the negative interest or reliance on the validity of the contract is protected and the costs of negotiating and entering into contract or dispositions made in reliance on the contract are recoverable.

If the contract is not avoided or cannot be avoided, the situation is somewhat more complex. As discussed above, the first question then would be whether a misrepresentation that has occurred through provision of incorrect information on breach of pre-contractual disclosure requirements amounts to a contractual promise. In such cases, the party affected by the misrepresentation would be entitled to contractual remedies for non-performance. If this is not the case, the affected party should be entitled to remedies because of the breach of the pre-contractual duties.^{*40}

In Estonian law, the primary remedy for breach of pre-contractual duties is the claim for damages.^{*41} The nature of such a claim and the damages to which the other party is entitled in the event of breach of the pre-contractual duties was discussed above with respect to cases where the breach led to termination of negotiations or invalidity of a concluded contract. However, it remains to be shown that the interests protected by

³⁹ *Ibid.*, Sec. 10.

⁴⁰ In the DCFR this is simply procured by enabling the mistaken party (or the party affected by the fraud) to claim damages irrespective of the avoidance of the contract (see DCFR II.-7:304).

⁴¹ P. Varul et al. (Note 2), commentary 4.6.1 to § 14, p. 62.

the pre-contractual duties and the respective damages can be different if the parties reach agreement and a contract is validly concluded despite the pre-contractual breach. This is already evident from the general purpose for which the damages are rewarded — to help the aggrieved person into a position that would have existed but for the breach that led to the liability for damages. In cases where the conclusion of a contract was influenced by a breach of the pre-contractual disclosure requirements but the contract is valid, the compensation of damages resulting from such breach can lead to two, fundamentally different situations, depending on the circumstances of the case.

The party who entered into the contract under the influence of a misrepresentation by the other party could claim that he would not have entered into the contract if the other party had disclosed correct information or had not omitted to disclose certain circumstances. This could be a valid claim in the above-mentioned case where the seller omitted to disclose to the purchaser that the fence that was thought to mark the border was indeed located on the neighbouring plot. Here the pre-contractual duties seem to protect the negative interest and the compensation of damages would require the party influenced by the misrepresentation to be placed in a situation as would have existed if said party had not concluded the contract. An apparent concurrence of remedies occurs here between the claim for damages and avoidance of the contract, based on the mistake or fraud.^{*42} In order to avoid contradictions, it may be advisable not to grant damages that would lead to restitution and *de facto* termination of the contract where the contract in question cannot be avoided because of the mistake or fraud under the relevant provisions.

In a number of cases where the pre-contractual disclosure requirements are breached, the affected party is not interested in restitution or avoidance. It is often the case that the party whose decision to enter into the contract was influenced by a misrepresentation by the other party would have concluded the contract even if the relevant information had been properly disclosed. On the other hand, the party who has discovered the misrepresentation might be interested in keeping to the contract, provided that said party is able to reduce the price or otherwise provided with adequate compensation. In such cases, the parties often claim that they would have entered into the contract under the different conditions and mainly for the different price, less the negative value of the circumstances not properly disclosed. If damages are sought here, they seem to lead to compensation of the positive interest, as the damaged party is put in a situation that would have existed if the contract and the related pre-contractual obligations would have been properly fulfilled. It is therefore apparent that there can be pre-contractual duties that protect essentially the same interests as the contract itself. At least this is true with respect to the pre-contractual duties that require disclosure of certain material circumstances related to the object of the contract or that sanction provision of incorrect information related to the intended contract. In such cases, the contractual expectations of the affected party (and the related positive interest) are based on the misrepresentation. The compensation of damages for pre-contractual misrepresentation would lead to a situation that would have existed if such contractual expectations would have been fulfilled; this can be described as compensation of the positive interest. This is most evident in the case described under article 4:117 in the full-text version of the Principles of European Contract Law: A developer buys a plot of land in reliance on a statement by the seller that the land is not subject to any third-party rights. In fact, there is a right of way running across the site and it would cost £10,000 to divert the path. The purchaser cannot avoid the contract, as its mistake is not serious enough but is awarded damages in the amount of £10,000 under article 4:117 because of the seller's misrepresentation. In the Estonian cases discussed above where the purchaser's decision to enter into the contract was influenced by incorrect information provided by the seller, the courts also concluded that the purchaser is in principle entitled to damages that can be calculated as the difference between the value that the object of the sale would have had if the information provided to the purchaser had been correct and the actual value of the object. In the case of the sale of the plot with a misleading fence, the Supreme Court issued reference that the purchaser can claim damages due to the breach of pre-contractual obligations as can be calculated under the same principles as reduction of the purchase price — that is, on the basis of the reduced market value compared to the value the plot would have had if the fence had actually marked its border.^{*43}

⁴² *Ibid.*, commentary 4.7.3 to § 14, p. 64.

⁴³ CCSCd 3-2-1-113-07 (Note 38), Sec. 12.

7. The borderline between contractual and pre-contractual liability

In practice, this has led to the question of whether it is at all appropriate to speak of a pre-contractual liability when the breach of pre-contractual duties is discovered after the conclusion of the contract and does not lead to its invalidity. In legal theory it has been suggested that under such circumstances the pre-contractual duties are to be treated as duties under the contract such that their breach would lead to non-performance of the contract and to the contractual liability and remedies.^{*44} This idea has now been picked up by the Supreme Court, which has ruled that if the breach of pre-contractual obligations is discovered after the conclusion of a valid contract the relationship between the parties is to be viewed as a uniform contractual relationship the contents of which are, in addition to the obligations arising from the contract itself also the obligations that existed between the parties prior to conclusion of the contract.^{*45} For the above examples this would mean that, in addition to an obligation to ensure that the object of sale conforms with the agreement, the seller would be under the contractual obligation to assure that any information provided by it with respect to the object of the sale prior to conclusion of the contract is correct and no material information has been left undisclosed to the purchaser in a manner counter to good faith.

The idea of treating pre-contractual obligations as obligations arising under the contract is mainly aimed at helping the affected party to satisfaction with, in addition to the claim for damages, contractual remedies such as reduction of purchase price or termination of the contract in cases of material breach. As such remedies are only available under the contract and as a result of non-performance of contractual obligations, they could not be used in cases of a breach of a mere pre-contractual obligation.^{*46} As the above cases show, there is indeed need for such specific remedies as one would otherwise need to adapt the claim for damages to achieve the same results as price reduction or even termination. Even more important is the need to ensure that the solution of the case is not dependent on whether a particular non-performance qualifies as pre-contractual or contractual breach. For contractual breach there is often specific regulation in place that limits or adapts the remedies or the liability regime under a particular contract. It would be advisable often to apply this specific regulation also in the case of pre-contractual liability. This is mainly due to the fact that on many occasions the two categories of contractual and pre-contractual liability are almost impossible to distinguish. One should consider only the question of whether the incorrect information provided in the pre-contractual phase has amounted to a contractual promise or not.

The Estonian practice shows that there are a number of cases at the borderline between contractual and pre-contractual liability. Such cases should not be decided on the basis of whether a pre-contractual misrepresentation has amounted to a contractual promise and to corresponding non-performance of the contract, as this is indeed often difficult to prove. The practice also shows that the provisions related to non-performance of contracts often need assistance from the realm of pre-contractual liability, mainly in cases where the conclusion of the contract has been influenced by pre-contractual misrepresentations. It seems that a more general and less specific scheme of regulation of pre-contractual duties, such as the one adopted in Estonia, is able to offer more flexible solutions for these cases than does regulation that is limited to a catalogue of very specific pre-contractual information duties, such as in Chapter 3 of Book II of the DCFR.

⁴⁴ I. Kull, M. Käerdi, V. Kõve (Note 8), p. 81.

⁴⁵ CCSCd 3-2-1-111-07 (Note 35), Sec. 14.

⁴⁶ P. Varul et al. (Note 2), commentary 4.6.1 to § 14, p. 62.