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Liability for a *Culpa in Contrahendo* in Korean law in light of the Hyundai Group Case


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In 2010, Hyundai Group, backed by Hyundai Merchant Marine, was named the preferred bidder for the 34.88 percent stake in Hyundai Engineering & Construction (Hyundai E&C). However, questions were raised about Hyundai Group's ability to fund its bid. In particular, Korea Exchange Bank (KEB) and eight other creditors questioned the nature of the 1.2 trillion won loan Hyundai Group obtained from French investment bank Natixis SA and repeatedly demanded that Hyundai Group submit detailed documentation regarding the loan. In response, Hyundai Group reiterated that the loans were legitimate, but the suspicion persisted. Then, Hyundai Group signed a memorandum of understanding (MOU) with the creditors and paid performance guarantee deposits of 275.5 billion won. However, the creditors terminated the MOU on the grounds that Hyundai Group failed to determine the sources of the 1.2 trillion won in question. Hyundai Group filed a lawsuit against Korea Exchange Bank (KEB) and other creditors to get its performance guarantee deposits back, and on July 25th, 2013, the Seoul Central District Court ruled in part for Hyundai Group and ordered the creditors to return 206.6 billion won.

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Generally, the parties enter into preliminary contract negotiations before such are reduced to a formal and binding contract. The doctrine of *culpa in contrahendo* (fault in negotiating) imposes duties on the negotiating parties during preliminary negotiations, including duties to negotiate in good faith, to disclose, to take reasonable care, and to protect. In addition, a party may face liability for *culpa in contrahendo*, a new type of liability, if such party breaches the aforementioned duties and thereby causes damages to the other party in the course of negotiation. The Hyundai Group case is closely related to this so-called liability for *culpa in contrahendo*.

The compensation system under the Korean Civil Code provides two categories of liabilities: contractual liability or tort liability. A trust relationship comes into existence when a party creates the expectation that a contract would be forthcoming. If a relationship of trust and confidence comes into existence, the promisor is bound by the duty of good faith to protect any injurious reliance by the other party, and if any injurious reliance occurs, the promisor will be held liable for *culpa in contrahendo*. However, if any party causes damages to the other party before a relationship of trust and confidence comes into existence, such party will be held liable under tort law.

As soon as a party begins to prepare the performance of the contract, a trust relationship binding the parties comes into existence. The purpose infused within this trust relationship is manifested through the notion of good faith that serves to safeguard contracting parties from unjust behavior and encourage smooth negotiations. As a result, this duty of good faith is strongly encouraged in the negotiation process of contractual agreements so that the legal interests and rights of the contracting parties are duly protected and not infringed upon. These implied obligations are: (i) the duties to protect each other's persons, property or interests; (ii) the duties to disclose such matters that are clearly important for the other party's decision; and (iii) the duties to cooperate if any consent, permit, or authorisation is required to have an enforceable contract.

A repudiation of an obligation, which gives rise to the right to terminate a contractual agreement, may not itself amount to a breach if the contracting parties have complete freedom over the agreement. While, the contractual agreement may not be subject to termination entirely based on such repudiation, the costs incurred in establishing this agreement may be claimed under negligence. It is therefore crucial to recognise the significance of construing contractual agreements narrowly.

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