

[Title]

Breakdown of contractual negotiations

[Deciding Court]

Tokyo High Court

[Date of Decision]

1 February 1994

[Case No.]

Case Nos. 418 (ne) and 1156 of 1992

[Case Name]

Claim for damages and concurrent incidental appeal

[Source]

Hanrei Jiho No. 1490, p. 87

[Parties]

Appellant/ Incidental Appellee: Junya Seki, Prinnet Co., Ltd.

versus

Appellee/ Incidental Appellant: The Mitsubishi Bank, Ltd.

[Summary of Facts]

In September 1988, the plaintiff Company X1 applied for finance of approximately JPY 3.4 billion as funds for equipment from the defendant Bank Y, which was its main bank, having formulated a project (hereinafter, “the plant venture project in this case”) to establish a new plant in an industrial complex that was being developed by Prefectural Public Enterprises Agency A (not a party to this action). Bank Y initially expressed reservations that the financing was an excessive investment in equipment for Company X1, which had annual business of approximately JPY 530 million, but ultimately approved financing of JPY 370 million only (hereinafter, “the financing”) as funds for the purchase of land. Having communicated this to X2, the representative of Company X1, through Y’s Branch Manager B (not a party to this action) on 7 November of the same year, Y provided Company X1 with a finance certificate (hereinafter, “the finance certificate”) on 9th of the same month on which were recorded specifics of such details as the finance amount, the loan period, the rate of interest, the security, and the guarantors, to be submitted to Prefectural Public Enterprises Agency A.

At about the time Bank Y was conducting internal discussions, Company X1 was making an application to Prefectural Public Enterprises Agency A for the

required land and deliberating on the procurement of the remaining funds. Around the time that the finance certificate was issued, however, bank Y received information that company X1 was to change its main bank to Bank C (not a party to this action), and that there had been talk of Bank C taking on Company X1's liabilities. When, on November 11 of the same year, B, who was aware of the information, notified X2 that, were X1 to change its main bank to Bank C, Bank Y was resigned to conceding this; X2 appeared to be accept this, so B took it that Company X1 had withdrawn from the financing and would transfer its dealings to Bank C. However, in reality, the relationship between X1 and Bank C was no more than one exploring the possibility of finance, and in fact neither X1 nor X2 had resolved to change main banks. Moreover, neither on that day, nor at any subsequent time, did Bank Y request the return of the finance certificate that had already been issued, or make any mention of doing so.

Ten days later, on the 22nd of the same month, X2 again requested that B effect the financing from Bank Y because procurement of funds from Bank D, a non-party, would not be achievable without the support of a main bank. From the abovementioned sequence of events and the explanation of X2, B understood this to be a proposal for bridging finance until X1's liabilities were taken on by Bank C in the near future, and consented to that proposal. Further, on the 30th of the same month when X2 and Bank Y's Deputy Branch Manager E (not a party to this action) went to Prefectural Public Enterprises Agency A and were given an explanation on matters such as the contract and payment of the land price, E made a firm commitment to the relevant officer of Prefectural Public Enterprises Agency A to the effect that Bank Y would definitely remit the purchase price.

However, on 8 December of the same year, when Company X1's land transfer application had passed through the review of Prefectural Public Enterprises Agency A's Land Allotment Committee, it was discovered that talks on Company X1's liabilities being taken on by Bank C had not progressed at all, so B notified X1 to the effect that if that were true, there was no possibility that the financing could be provided (hereinafter, "the finance refusal"). Consequently, Company X1 managed to raise emergency funds through such means as the sale of shares it held, a short-term advance from Bank Y and a loan from Credit Union F, a non-party, and paid the land purchase price to Prefectural Public Enterprises Agency A. On the 12th of the same month Company X1 proposed to Bank Y the scaling down of the plant venture project in this case, in response to which Bank Y showed openness to discussion. However, a construction works project that X1 had already commissioned to Construction Company G (not a party to this action) was in a state such that changes were impossible, and ultimately Company X1 paid the contract price to Construction Company G by means of a loan from Bank

D. Subsequently, on the 28th of the same month financing approval was granted by H, a non-party financial institution affiliated with Bank C, and on the 30th of the same month notice came from Bank Y that it was prepared to effect the financing, but Company X1 turned down both of these and in January of the following year finally abandoned the plant venture project in this case.

In this action, based on the foregoing course of events, X1 and X2 argued that a finance contract had been formed between Company X1 and Bank Y and that the finance refusal by Bank Y constituted tortious conduct towards Company X1 and X2, and sought payment by Bank Y to Company X1 of JPY 360 million that would have come from financing from Bank Y and other banks and lost expenditure for the land purchase price and contract price with G, etc.; and to X2 of JPY 12 million in damages for pain and suffering for damage to health.

The court at first instance recognized the claim up to a total of JPY1.5 million only, being part recovery of revenue stamp fees, etc., in respect of X1, and part recovery of the damages for pain and suffering in respect of X2. In response, X1 and X2 appealed, and Bank Y also made an incidental appeal.

[Summary of Decision]

Set aside in part; incidental appeal allowed in part.

(i) “In a case where a bank that has had ongoing dealings with an enterprise as its so-called main bank has received a finance application from the enterprise for the funds necessary for a new business project and, having knowledge of the specific details of that project, is in the middle of continuing negotiations with an aim to concluding a consumption loan contract with the enterprise and, even at a stage where there has been no exchange of money and the consumption loan contract cannot be said to have been formed, it has reached specific agreement on lending conditions as to the finance amount; the time for performance; the loan period; the rate of interest; the object of the security; the type of security interest; and the guarantors, and the bank has made a definite promise to provide the finance (hereinafter, “the financing promise”) by issuing a finance certificate on which it is recorded that it will provide finance pursuant to the above lending conditions, if the financing promise is broken and so realization of the new business project of the enterprise becomes impossible or significantly difficult and the enterprise has, for example, no choice but to cancel measures taken in reliance on the financing promise in order to realize the said project, such as a contract with a third party or a legal relationship that can be seen as substantively

identical to such, and circumstances are thus such that, for example, the enterprise will incur loss, and when, moreover, said bank has unilaterally taken action to break the financing promise despite that it knows or should know of such circumstances, unless exceptionally there is cause for taking such action that can be approved as commercially legitimate, where the enterprise has incurred loss of the aforementioned kind, it must be taken that said bank bears the liability to compensate for such pursuant to the *Civil Code Arts. 709 and 715.*”

(ii) “It can be deduced that” the finance promise between Company X1 and Bank Y “had been made at the stage of negotiations with Company X1, even before issue of the finance certificate”. Further, judging from the course of negotiations that resulted in the finance refusal and the circumstances that resulted in Company X1’s discontinuance of the plant venture project in this case, “it must be said that ultimately, the discontinuance of the plant venture project in this case by Company X1 resulted from the fact that Bank Y did not provide financing according to the initial financing promise; there was a relationship of cause and effect between the discontinuance of the plant venture project in this case and the finance refusal”. Additionally, there was no evidence sufficient to accept the proposal by Company X1 to change main banks and withdraw the finance application that Bank Y contended. As for Bank Y’s assertion that its failure to take back the finance certificate was in consideration of the situation were Company X1 to receive financing from another bank: because there was no relevant request by Company X1 and the intentions of Bank Y had not been manifested to Company X1, “that cannot constitute grounds to repudiate Company X1’s belief that it would receive financing according to the finance certificate”. Further, Branch Manager B’s understanding that Company X1 had first withdrawn its finance application and later applied for bridging finance “was merely a unilateral assumption made without conducting sufficient investigation or examination of the facts and further, without confirming same with X2 or Company X1; because it cannot be said that B’s having assumed such could be blamed on either Company X1 or X2 it cannot be said that there was cause for unilaterally breaking the financing promise that can be approved as commercially legitimate”. Because “although both the contract with Prefectural Public Enterprises Agency A for the purchase of land for the plant and the contract with Construction Company G for construction work on the plant were concluded after the finance refusal, the basis of each contract was already formed prior to the finance refusal”, it could not be said that Company X1 should not have concluded either contract. Accordingly, “it must be said that B, Bank Y’s branch manager, unilaterally broke the financing promise” and “pursuant to the *Civil Code Art. 715*, Bank Y is liable to compensate Company X1 for losses incurred in having no choice but to dissolve its above relations with Prefectural Public Enterprises Agency A and Construction

Company G”.

(iii) Looked at from another angle, however, “the lack of consideration given to the procurement of working capital funds by Company X1 and the excessive nature of such project also contributed to X1 having no choice but to discontinue the plant venture project in this case” and because in particular at the time of concluding the contract with Construction Company G, the difficulty of procuring funds was already clear, Company X1 “had a duty under the principle of good faith to minimize losses as far as possible, such as by concluding works contracts based on a scaling down of the plant” and so was comparatively negligent to the extent of 60% in relation to Prefectural Public Enterprises Agency A and 90% in relation to Construction Company G. Further, as to the damages for pain and suffering by X2, because the financing promise and the finance refusal were not made towards X2, given that “X2 had not contended or established that the factual circumstances were sufficient such that it be accepted that the finance refusal also constituted a tortious act towards X2”, X2’s argument that there had been a tortious act could not be recognized; only the claim for approximately JPY 35 million by Company X1 was recognized.