

LEGAL LIABILITY OF THE CONTRACT PROVISIONS BASED ON THE REFERENCE STATED IN ANOTHER CONTRACT

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Abstract: The author deals with the question of the legal liability of the "ancillary" contract, i.e. the attention is paid to the rights and obligations arising out of a contract concluded between other contracting parties. Furthermore, we focus on the manner of the "main" contract conclusion, while the "main" contract is only contains a reference to the "ancillary" contract and the consent of the parties to the "main" contract to the rights and obligations established by the "ancillary" contract. We discuss the legal liability of the "ancillary" contract as well as the rights and obligations established by the "ancillary" contract, while pointing to the provisions of the two contracts for the purpose of legally binding of the "ancillary" contract. In addition to the basic legislation, the author also points to the decisions of a court regarding the specific case that addresses the issue in question.

Keywords: legal liability, reference to the provisions of another contract, contractual freedom, court decision.

1 Introduction

The primary reason for writing this paper was a fact that it often occurs the situation in the Slovak Republic in which the contracting parties conclude the "main" contract, while this "main" contract contains only a reference to the "ancillary" contract and the consent of the contracting parties to the "main" contract to the rights and obligations established by the "ancillary" contract; thus they consider the rights and obligations of the "ancillary" contract as legally binding also for the "main" contract.

In this paper, it is necessary to clarify the terms as follows:

- (a) the main contract,
- (b) the ancillary contracts.

The main contract is a legally binding relationship between the contracting parties to this legally binding relationship, the provisions of which contain a reference to another legally binding relationship between the other contracting parties. At the same time, it also contains the consent of the contracting parties to this main legally binding relationship with the rights and obligations of other legal binding relationship established between other contracting parties.

An ancillary contract means a legally binding relationship between the contracting parties. The provisions of the main contract refer to the legally binding relationship of the ancillary contract established between other contracting parties and the rights and obligations of the ancillary contract are also applicable to the contracting parties of the main contract, based on the reference and the consent as stated in the main contract.

This paper focuses on the legal regulation of the above mentioned issues and, on the other hand, points out the decisions of the courts in a specific legal matter closely related to the addressed issue.

In the Slovak Republic, it often occurs the situation in which the contracting parties to the main contract refer to the ancillary contract and they consider the rights and obligations established by ancillary contract a legally binding also for the main contract. This is not always the case and therefore, we have decided to write this paper.

The basic legal regulation is included in Act no. 513/1991 Coll. Commercial Code, as amended (hereinafter referred to as the "Commercial Code") and Act no. 40/1964 Coll. Civil Code, as amended (hereinafter referred to as the "Civil Code").

However, the comprehensive legal framework of the issue in question is absent in the Slovak Republic. Under the comprehensive legal framework, we understand both the definition of the relevant concepts and the determination of the specific legal regime, as well as, the determination of the conditions of the legal liability of ancillary contract for the participants of the main contract.

2 Legal liability of the ancillary contract

In this part of the paper, we point to a specific example of the subject matter. Later on, on the basis of this example, we will draw a general conclusion.

In the context of a practical example, we point to a work contract the subject of which is defined as follows:

The Contractor undertakes to construct a work with a title the "Reconstruction and Restoration of the Manor in the Village", Project Code XYZ, under the conditions established in this contract, to the extent of the project documentation and in accordance with the terms and conditions specified in:

- the building permit issued for the realization of the work;
- Funding Agreement no. 123, as amended, concluded between the beneficiary (client) and the provider of a non-refundable financial contribution (NFC), i.e. the Ministry of Construction and Regional Development,
- the Guide for the beneficiaries of NFC from the Regional Operational Programme.

In our case, the main contract is a work contract under which the contractor undertakes to make the work "Reconstruction and Restoration of the Manor in the Village" Project code XYZ for the client.

The ancillary contract is the Funding Agreement no. 123, as amended, which was concluded between the client and the provider of a non-refundable financial contribution, i.e. the Ministry of Construction and Regional Development, thus another contracting party than a contractor.

Based on the provisions on the subject of the work, it is clear that the contractor, *inter alia*, undertakes to carry out the work in accordance with the Funding Agreement no. 123, as amended (hereinafter referred to as the "Funding Agreement"), which was concluded between the client and the provider of a non-refundable financial contribution, i.e. the Ministry of Construction and Regional Development.

Taking into account the provision on subject of the work, it is clear that the Funding Agreement, together with its General Terms and Conditions, undoubtedly also applies to the contracting parties to the work contract, i.e. also to legally binding relationship established by the work contract.

It is necessary to state that the Funding Agreement is not an annex to a work contract.

Based on the above mentioned, it is also clear that the Funding Agreement has to apply also to the legal relationship of the contracting parties to the main contract, whether it forms an annex to a work contract or not and whether the contractor leaned about this contract or not (in this case, the contractor is not a contracting party of the ancillary contract, and thus the contractor can decide whether to learn about the ancillary contract or not).

The work contract also involves provision as follows: The work contract shall enter into force on the date of its signature by both contracting parties and shall take effect on the date of signing the Funding Agreement between the client and the Ministry of

Construction and Regional Development of the Slovak Republic as the provider of the NFC.

The previous provision of the work contract says that the work contract takes effect on the date of signing the Funding Agreement between the client and the Ministry of Construction and Regional Development of the Slovak Republic as the provider of the NFC. This makes it clear that also the Funding Agreement relates to the contractor and that the contractor was informed about this Funding Agreement. If the contractor was not informed about Funding Agreement, this could be perceived as a result of the Contractor's own decision not to be informed about this Funding Agreement.

There is no need for the Funding Agreement to be annexed to the work contract in order to be applied also to the contractor.

Based on the above mentioned facts, it is clear that:

- the contractor has given his/ her consent to the Funding Agreement,
- the contractor has undertaken to perform the work in accordance with the Funding Agreement,
- the contractor has committed to complying with the terms and conditions of the Funding Agreement.

The only significant condition for the Funding Agreement to become a binding on the parties to the main contract is that this Funding Agreement was clearly and definitely specified in the work contract. Based on above mentioned facts and provisions of the work contract, that condition was fulfilled in the presented case study.

Since the Slovak legal regulation does not contain any provision of the law that would deal with the situation in question, we refer to the provision of Section 273, paragraph 1 of the Commercial Code: *"A part of the contract content may also be determined by the reference to the general business terms and conditions drawn up by professional or interest-based organizations or by reference to other business terms and conditions that are known to the contracting parties or that are attached to the contract."*¹

Based on the cited Commercial Code provision and an analogous legal interpretation, it is clear that to make the Funding Agreement a legally binding, it does not have to be an annex to the contract. It is sufficient to make a reference to the Funding Agreement in the work contract.

At the same time, we state that the Funding Agreement was publicly available at the time of signing the contract, thus it has to be considered that it was known to the contractor. However, if the Funding Agreement was not known at the time of signing the work contract and that Funding Agreement was defined and specified in the work contract, the contractor would be compulsory, before signing the work contract, to request the Funding Agreement. Otherwise, it is supposed that the contractor is familiar with the term and conditions of the Funding Agreement.²

In addition to the above mentioned references to the Funding Agreement, the work contract also included the information as follows: The subject of the contract is implemented under the Regional Operational Program, Priority Axis 3 Strengthening the Cultural Potential of the Regions and the Tourism Infrastructure, Measure 3.1b Strengthening the Cultural Potential of the Regions – interventions in cultural monuments, the name of the project "Reconstruction and Restoration of the Manor in the Village" and therefore, the contractor undertakes:

- a) to accept the change of this contract if this change is caused by changes in the Funding Agreement concluded between the client and the Ministry of Construction and Regional

Development of the Slovak Republic or by changes in the Guide for the beneficiaries of NFC from the Regional Operational Programme,

- b) to endure the performance of the control/ audit/ verification related to the subject of performance during the validity and effectiveness of the Funding Agreement concluded between the client and the provider of non-refundable financial contributions. The control/ audit/ verification may be performed by the authorized persons in accordance with the General Terms and Conditions. The contractor is obliged to provide authorized persons with all the necessary co-operation. The contractor is also required to define this obligation in contracts with the subcontractors.

According to the above mentioned provision, it is again clear that the work under the work contract was to be carried out under the terms of the work contract itself, but also under the Funding Agreement, and therefore, inter alia, the terms of the Funding Agreement were known as well as binding on the contractor.

Before signing the contract, the contractor had the opportunity to learn about the Funding Agreement.

At the same time, it should be noted that it is absolutely irrelevant whether the contractor had an opportunity to interfere in the relationship between the client and the ministry or not, since the contractor had the opportunity to learn about all the documents before signing the contract.

In the contractor's opinion the invoice payment was not directly dependent on the financial resources from the non-repayable financial contribution, however, the financing was directly dependent on the financial resources from the non-repayable financial contribution from the Regional Operation Programme. Even if the financial resources were paid directly by the client to the contractor, it would be a breach of the Funding Agreement. These facts were available to the contractor prior to the conclusion of the work contract and hence, the contractor had the opportunity to get acquainted with them and to decide whether to conclude the contract in question or not.

The court in the given court proceedings found that the Funding Agreement had been concluded earlier than a work contract and therefore, the contractor was in a position to learn about this agreement at any time prior to the conclusion of the work contract.

The following facts have resulted from the conclusions of the court.

Despite the fact that the contractor knew the process of providing the financial contribution, as well as the payment due according to the Funding Agreement; in accordance with the work contract, the contractor has committed to a maturity of 90-day with respect to the client. In this regard, it is necessary to resolve the discrepancy in the client's and contractor's interpretations of the payment of remuneration for the work performed. The contractor claimed that the maturity of the remuneration for the work is to be set according to the work contract and the client claimed, that maturity is to be set in accordance with the Funding Agreement.

In spite of all above facts, as well as the discrepancy in the client's and contractor's interpretations of the payment; the court declares that it is necessary to prioritize the work contract since the subject of the work in the work contract is "Reconstruction and Restoration of the Manor in the Village", Project Code XYZ, under the conditions established in this Contract, to the extent of the project documentation and in accordance with the terms and conditions specified in:

- the building permit issued for the realization of the work;
- Funding Agreement no. 123, as amended, concluded between the beneficiary and the provider of a non-

¹ § 273 par. 1 of the Commercial Code

² (see comment on the Commercial Code - Mária Patakyová)

refundable financial contribution (NFC), i.e. the Ministry of Construction and Regional Development;

- the Guide for the beneficiaries of NFC from the Regional Operational Programme.

In relation to the fact that the work contract also contains the following provision, the work contract shall enter into force on the date of signature by both contracting parties and shall take effect on the date of signing the Funding Agreement between the client and the Ministry of Construction and Regional Development of the Slovak Republic, the provider of NFC, the court declares that there is a condition on the basis of which it cannot automatically be concluded that this contract also governs the rights and obligations of the contractor.

In relation to the analogous application of the provisions of § 273 par. 1 of the Commercial Code: *"A part of the contract content may also be determined by the reference to the general business terms and conditions prepared by professional organizations or interest groups or by reference to other business terms and conditions that are known to the contracting parties or attached to the contract."* the court declares that this provision is not relevant in this context, even though, there is no other legislation. The basic legal reasoning of the court is that the Funding Agreement cannot be called a general business conditions. However, in terms of the declared decision, the court did not provide any statement to the analogous application of the above provision. At the same time, the court declares, that if the court accepted the argument that it was a matter of general business terms and conditions, it would be necessary to consider that the work contract as such contains a payment due agreement. Therefore, the Funding Agreement cannot be legally binding since it also contains a payment due agreement, which is different from one in the work contract.

In the light of the above, it is clear that the contractor, *inter alia*, has:

- agreed to perform the work in accordance with the Funding Agreement, as amended;
- endorsed the manner of financing, i.e. repayment in the form of a non-repayable financial contribution;
- agreed with the manner of financing in terms of the Funding Agreement, as amended.

Despite all the facts, the courts acting at all levels declare that the Funding Agreement is not legally binding on contracting parties to the main contract, i.e. the work contract.

Such situation is very common in the Slovak Republic. The contracting parties to the main contract refer to an ancillary contract and thus, they consider the rights and obligations arising from the ancillary contract to be a legally binding also for the main contract. It is clear that, despite the unambiguous and certain reference to an ancillary contract, it is not legally binding on the contracting parties. Since this situation is very common in practice, it is appropriate to adopt legislation, which would set the precise conditions for such cases.

3 Conclusion

In the Slovak Republic it is very common that the contracting parties to the main contract refer to an ancillary contract and thus, they consider the rights and obligations arising from the ancillary contract to be legally binding also on the parties of the main contract. However, this very simple transfer of rights and obligations of the ancillary contract to the main contract is not legally binding in all situations and the rights and obligations of the ancillary contract cannot be fully taken over by the parties to the main contract.

In practice, however, the addressed situation is very common and that is why the jurisprudence should respond to the practical issues and try to resolve the current issue by adopting a new legislation.

The paper focuses on the legal regulation of the above mentioned issues and, on the other hand, points out the decisions of the courts in a specific legal matter related to the addressed issue.

A need to amend the Act is also evident from the interest of the professional public and the general public in the use of the transfer of rights and obligations of the ancillary contract to the main contract in the Slovak Republic.

Literature:

1. Act No. 513/1991 Coll. Commercial Code Act, as amended.
2. Act No. 40/1964 Coll. Civil Code Act of Slovak Republic, as amended.
3. Act No. 89/2012 Coll. Civil Code Act of Czech Republic, as amended.

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