Journal of Civil Law Studies

Volume 10
Number 1 *Journal of Civil Law Studies - 2017*

Article 11

3-6-2018

The Interaction of Good Faith with Contract Performance, Dissolution, and Damages in the Louisiana Supreme Court

Jumoke Dara

Olivier Moréteau
Louisiana State University Law Center, moreteau@lsu.edu

Follow this and additional works at: https://digitalcommons.law.lsu.edu/jcls

Part of the Civil Law Commons

Repository Citation
Jumoke Dara and Olivier Moréteau, *The Interaction of Good Faith with Contract Performance, Dissolution, and Damages in the Louisiana Supreme Court*, 10 J. Civ. L. Stud. (2018)
Available at: https://digitalcommons.law.lsu.edu/jcls/vol10/iss1/11

This Civil Law in Louisiana is brought to you for free and open access by the Law Reviews and Journals at LSU Law Digital Commons. It has been accepted for inclusion in Journal of Civil Law Studies by an authorized editor of LSU Law Digital Commons. For more information, please contact kayla.reed@law.lsu.edu.

The Interaction of Good Faith with Contract Performance, Dissolution, and Damages in the Louisiana Supreme Court

Jumoke Joy Dara[*] and Olivier Moréteau[†]

I. Background 261
II. Decision of the Court 263
III. Commentary 266
A. The Duty of Good Faith in Contract Performance 266
B. The Duty of Good Faith in Contract Dissolution 268

Keywords: good faith, contract law, contract performance, contract dissolution

It is a general rule, in civil law jurisdictions, that contracts must be performed in good faith. However, the fundamental nature of the good faith principle remains a matter for scholarly debate. The case of *Lamar Contractors, Inc. v. Kacco, Inc.*[1] illustrates how the principle that all contracts must be performed in good faith[2] interacts with contract dissolution and allocation of damages.

I. Background

In this case, Lamar Contractors, Inc. was a general contractor on a construction project. Lamar hired a subcontractor named Kacco, Inc. The subcontractor was to provide metal framing and drywall

---

∗ J.D. candidate (May 2018), Paul M. Hebert Law Center, Louisiana State University.
† Professor of Law, Russell B. Long Eminent Scholars Academic Chair, Director of the Center of Civil Law Studies, Louisiana State University. The authors thank Christabelle Lefebvre for her careful editing.

1. Lamar Contractors, Inc. v. Kacco, Inc. 2015-1430 (La. 05/03/16), 189 So. 3d 394 (2016).
2. LA. CIV. CODE art. 1983 (2017).

work for the construction project. The subcontractor contract included a "pay-if-paid" payment provision; it allowed Lamar ten days to give payment to the subcontractors after receipt of the payment from the owner.

Kacco began work on the project in October 2010, but had regular problems providing manpower and paying for supplies. On November 9, 2010, a Lamar representative sent a certified letter to Kacco expressing concerns regarding the timely completion of the project. Kacco responded by email and explained that the account had been put on hold. Additionally, Kacco was unable to pay a portion of the balance due to insufficient funds. It requested that Lamar issue a joint check to Kacco and the supplier. Lamar agreed, on the condition that Kacco pay a ten percent back charge for the cost of purchased materials. Kacco refused and during the waiting period was able to pay the debt down; it then continued to work through the months of November and December of that same year. An invoice was submitted for the forty-five percent of work completed, and Lamar made payment prior to receiving funds from the owner.

On January 13, 2011, Lamar sent notice addressing the same concerns regarding Kacco's inability to perform the work required under the contract. Kacco asked Lamar to be allowed to finish the job. Kacco completed the metal framing and stud work; however, upon inspection of the work, Lamar found deficiencies.

Later, on January 31, 2011, Kacco notified Lamar that it was awaiting payment for the December invoice to pay the supplier and order the required materials to complete the work. Lamar had received payment from the owner on January 26, 2011, but was not required, under the contract with Kacco, to remit payment until ten business days later, on February 5, 2011.

Lamar sent notice on February 3, 2011, to Kacco stating that the subcontract would be terminated if Kacco did not provide sufficient manpower and materials within forty-eight hours. Kacco did not re-

spond or return to the job site. Two days later, by a letter dated February 5, 2011, Lamar declared the contract terminated, and subsequently hired another subcontractor to complete the work.

Lamar sued Kacco for failure to perform the contract. Kacco filed a reconventional demand against Lamar for failure to pay Kacco for the work performed under the contract, alleging that their failure to pay caused them to fail to perform the contract. The district court ruled that Kacco failed to perform the contract and was liable to Lamar, awarding damages in the amount of $24,116.67 plus interest and attorney's fees. Additionally, the district court entered a judgment in the amount of $60,020 plus interest in favor of Kacco on the reconventional demand. The judgment notes that Kacco failed to provide sufficient materials to complete the work. However, Lamar negligently withheld payments for completed work by Kacco, which contributed to Kacco's inability to perform. The ruling was based on Louisiana Civil Code article 2003.[3] Lamar appealed the judgment, which was affirmed in its entirety. Upon Lamar's application, certiorari was granted, thereby allowing the Louisiana Supreme Court to pronounce for the first time on article 2003 after the 1984 revision of the law of obligations.

II. DECISION OF THE COURT

The Supreme Court limited its ruling to answering the sole issue presented in the appeal: "whether the district court erred in reducing Lamar's damages for breach of contract [sic] based on a finding that Lamar's negligence contributed to Kacco's breach of the contract

3. LA. CIV. CODE art. 2003 (2017):

An obligee may not recover damages when his own bad faith has caused the obligor's failure to perform or when, at the time of the contract, he has concealed from the obligor facts that he knew or should have known would cause a failure.

If the obligee's negligence contributes to the obligor's failure to perform, the damages are reduced in proportion to that negligence.

[sic]."[4] As the judgment states, "our sole focus is on whether Lamar's actions during the relevant time frame contributed to that breach for purposes of La. Civ. Code article 2003."[5] Indeed, looking into jurisprudence based on pre-revision article 1934, the predecessor to article 2003, the Court concludes that "an obligor cannot establish an obligee has contributed to the obligor's failure to perform unless the obligor can prove the obligee itself failed to perform duties owed under the contract."[6]

The Court rightly restates the requirement in article 2003 paragraph 2 when saying that "Kacco must demonstrate that Lamar failed to perform its obligation under the contract, which in turn contributed to Kacco's breach of the contract."[7] The Courts, then, reviews what it describes as the "undisputed facts"[8]:

> [O]n January 31, 2011, Kacco notified Lamar that Kacco was waiting on the payment of its December invoice to pay the supplier and order the necessary supplies to complete the punch list. Lamar had received payment from the owner on January 26, 2011. However, pursuant to the terms of the contract, Lamar was not required to make payment to Kacco until February 9, 2011, ten business days later.[9]

With respect, the Court should have noted February 5 if computing correctly, a detail that has its importance. The following paragraph also needs to be quoted for its full terms:

> On February 3, 2011, during this ten-day period, Lamar advised Kacco that Kacco's contract would be terminated if Kacco did not provide sufficient manpower and materials within forty-eight hours. Kacco did not respond to Lamar or return to the job site. Lamar *officially terminated* Kacco's subcontract in a letter dated February 5, 2011. Thus, the contract was terminated on February 5, 2011, *before* Lamar's

---

4. *Lamar*, 89 So. 3d at 397. Note the confusing usage of the common law terminology "breach of contract" rather than the civil law "failure to perform."
5. *Id.*
6. *Id.* at 398.
7. *Id.*
8. *Id.*
9. *Id.*

> obligation to make payment to Kacco became due on February 9, 2011.[10]

Based on the Court's reading of the facts, assuming that the contract was validly terminated on February 5, given the fact that performance by the obligee was due on February 9, the Court could rightly conclude the following:

> Under these circumstances, it is clear Lamar did not violate any obligation owed under the contract to make payment to Kacco and could not have negligently contributed to Kacco's breach of its obligations under the contract. Accordingly, the district court erred in applying the provisions of La. Civ. Code art. 2003 to reduce Lamar's award of damages.[11]

Therefore, the judgment of the court of appeal was vacated and the case was remanded to the district court for the sole purpose of entering an amended judgment in favor of Lamar, for the full amount of damages and with no reduction for contributory negligence.

However, the problem is that *based on the facts as they appear in the judgment*, nothing (other than the unilateral declaration by Lamar) warrants that the contract had been *officially terminated* on February 5, and this date comes close to the precise moment when Lamar actually owed payment to Kacco. Though the Court seems, on the face of its reading of the facts, to have correctly applied the rule in article 2003 paragraph 2, a closer look shows the following:

- That there was valid termination of contract can be doubted, absence of termination supporting the challenged judgment;
- If the contract had been validly terminated, the proximity of the date of termination with the due date of performance by the obligee casts doubts as to the obligee's good faith, though this may be mitigated by the silence and inaction of the obligor.

10. *Id*. (emphasis added).
11. *Id*.

This case offers a most interesting setting to revisit the interaction of good faith with contract performance and termination and its impact on court allocation of damages.

III. COMMENTARY

This commentary will first discuss the impact of the obligee's good faith in contract performance and its impact on the allocation of damages, assuming that the Supreme Court was legally justified in concluding that the contract had been terminated. Revisiting the issue of contract dissolution warrants further analysis of the obligee's duty of good faith.

A. The Duty of Good Faith in Contract Performance

Every contract imposes a duty for the contracting parties to act in good faith. Like most civil codes, the Louisiana Civil Code does not define good faith. Article 1759 states that, "[g]ood faith shall govern the conduct of the obligor and the obligee in whatever pertains to the obligation;" and article 1983 adds that "[c]ontracts must be performed in good faith."

The Louisiana Supreme Court assumes that Lamar has been acting in good faith all along the performance of its contract with Kacco, its subcontractor. A "pay-if-paid" provision in the contract afforded Lamar ten days to remit payment to its subcontractor after receipt of payment from the owner of the building project. However, the record shows that Lamar paid Kacco ahead of time when Kacco had accomplished forty-five percent of the work, since it had been made aware that Kacco's delay was due to Kacco's inability to provide manpower and pay for supplies. This portrays Lamar as a cooperative obligee, acting in a way that favors contract performance by the obligor, yet without ever renouncing its contractual right to full performance.

The term good faith has more than one definition.[12] Citing to French sources and to § 2.103(b) of the Uniform Commercial Code, the late Saúl Litvinoff noted that "it consists of honesty in a party's contractual behavior, or loyalty to, or collaboration with, the other party."[13] He then observed:

> The fact cannot be ignored, however, that as much difficulty may be encountered in defining honesty or loyalty as in defining good faith, which turns those definitional attempts into mere substitutions of words that fail to provide the clarity warrantedly expected from either a definition or an explanation.[14]

Yet, in the context of contract performance, the law attaches significant consequences to the existence or absence of good faith. Lamar's good faith as obligee is essential in its attempt to recover contract damages. Not that it needs to prove it (good faith is presumed throughout the civil law tradition),[15] but because on a show of the obligee's bad faith and by proving that this bad faith caused the obligor's failure to perform, Kacco, the obligor, may not owe damages. The first paragraph of article 2003 offers an all-or-nothing solution, stemming from pre-revision article 1934(4). This is a much more radical solution than simply reducing the amount of damages in proportion of the obligee's negligence, when it contributes to the obligor's failure to perform, as stated in the post-revision article 2003 paragraph 2.[16]

It, therefore, comes as no surprise that earlier jurisprudence based on the old article 1934(4) stated that bad faith in this context

---

12. Saúl Litvinoff, *Good Faith*, 71 TUL. L. REV. 1645 (1997).
13. *Id.* at 1663.
14. *Id.* at 1664.
15. Civil Code [Fr.], art. 2274 (formerly art. 2268, renumbered by Law no. 2008-561 of June 17, 2008, art. 2): "Good faith is always presumed, and he who alleges bad faith must prove it."
16. Comment (b) invites to compare with article 2323, dealing with comparative negligence in the title dealing with extra-contractual (tort) liability.

had to amount to a breach of contract by the obligee, making performance of the contract much more difficult for the obligor.[17] This interpretation fits the logic of reciprocity existing in synallagmatic contracts. However, it has the effect of stretching the meaning of bad faith to the extreme case of nonperformance of a contractual obligation.[18]

Though noting that nonperformance by Kacco was caused by the non-payment by Lamar, the district court did not apply the all-or-nothing bad faith provision, but the post-revision option of reducing damages in proportion of the obligee's negligence (article 2003 paragraph 2). Pointing out that the obligee's performance was due past the date of dissolution of the contract was sufficient motive for reversal.

This leads to a fundamental question, central to the resolution of our case: was the contract properly dissolved before the term of payment by the obligee?

B. The Duty of Good Faith in Contract Dissolution

The Supreme Court takes it for granted that the contract was *officially terminated* by the note sent by Lamar on February 5, at the expiration of the forty-eight-hour notice they had sent and was met by silence and inaction by Kacco.[19] This at least discards a common law reading of the case: whereas in common law the contract typically does not survive fundamental breach by one of the parties, in civil law the contract is a legal relationship that survives non-performance and can only be dissolved according to conditions set out by

17. The Supreme Court cites Board of Levee Commissioners of Orleans Levee District v. Hulse, 120 So. 589, 167 La. 896 (1929), also cited in LA. CIV. CODE art. 2003 (2017) comment (b), comment (a) indicating that this article does not change the law; *Lamar*, 89 So. 3d at 398.

18. Good faith has been defined as performance "in conformity with the intention of the parties and in the light of the purpose for which [agreements] have been formed." AUBRY & RAU, 4 DROIT CIVIL FRANÇAIS § 346 (6th ed., A.N. Yiannopoulos trans., West 1965).

19. *Lamar*, 89 So. 3d at 399.

the law. This is why it is so important to use the word "breach" sparingly, as it creates the mental picture of a destroyed and terminated contract.

According to the civil law tradition, dissolution of contract is typically judicial.[20] There is no indication, in our case, of a petition by Lamar that the contract be judicially resolved. We may, therefore, be in a situation where the obligee has a right, "according to the circumstances, to regard the contract as dissolved."[21]

The parties may have expressly agreed that the contract shall be dissolved for the failure to perform a particular obligation, as provided for in article 2017, which states that: "[i]n that case, the contract is deemed dissolved at the time it provides for or, in the absence of such a provision, at the time the obligee gives notice to the obligor that he avails himself of the dissolution clause."[22] The ruling of the Supreme Court is perfectly compatible with the existence of a dissolution clause that does not provide for a certain term and, therefore, leaves the obligor with a reasonable time for performance.[23]

In the absence of a dissolution clause, given the fact that there has been no judicial dissolution, we are left with two remaining possibilities: dissolution after notice to perform (article 2015) and dissolution without notice to perform (article 2016).

We understand from the facts of the case that Lamar lost patience and confidence in Kacco's ability to offer satisfactory and timely performance, and did not want to make payment without having assurances that there would be due performance. Hence, their issuing a two-day ultimatum that can be analyzed as an article 2015 "notice to perform within a certain time, with a warning that, unless performance is rendered within that time, the contract shall be deemed dissolved." This amounts to inserting unilaterally a term certain for performance together with an express dissolution clause,

20. LA. CIV. CODE art. 2013 (2017): "When the obligor fails to perform, the obligee has a right to the judicial resolution of the contract . . . ."
21. *Id*. at art. 2013 *in fine* (2017).
22. *Id*. at art. 2017 (2017).
23. *Id*. at art.1778 (2017).

whilst allowing additional time for performance in situations where there is obviously a delay.[24] This convenient way out allows a frustrated obligee to terminate the contract without judicial action, in the absence of an express dissolution clause.

Article 2015, however, does not seem to make room for a harsh ultimatum. As provided by article 2015, "[t]he time allowed for that purpose must be reasonable according to the circumstances." In the present case, Lamar granted a period of forty-eight hours. This may seem unreasonably short in a long-term contract taking weeks or months to perform. Had Lamar requested full performance in a period of two days, there is no way the additional time could be regarded as reasonable. However, Lamar did not call for full performance in two days. The obligee only wanted assurances that the contract could be performed, requesting Kacco, the obligor, to mobilize the work force needed for completion.

Given the tense situation and the threat of termination, it was very unwise for Kacco to remain passive and even more, totally silent. This brings us to the scenario envisioned in Civil Code article 2016, allowing for termination without notice, providing that "when it is evident that the obligor will not perform, the obligee may regard the contract as dissolved without any notice to the obligor."

We reach the point of the discussion where the duty of good faith appears as a two-way street. Knowing of Kacco's delays and cash-flow difficulties, Lamar had to give reasonable notice with sufficient time for performance. In a civil law jurisdiction, delay in performance does not *per se* warrant contract dissolution. One may question whether or not Lamar acted in a loyal or collaborative manner. The forty-eight-hour grace period expiring just four days before Lamar's contractual date of payment for the work that had been done looks like pushing for termination rather than giving a last chance

24. This parallels the grace period that may be granted by a court, in accordance with LA. CIV. CODE art. 2013 para. 2 (2017): "[i]n an action involving judicial dissolution, the obligor who failed to perform may be granted, according to the circumstances, an additional time to perform."

for performance; Lamar probably guessing that Kacco needed cash to secure full performance.

However, knowing that the situation was getting tense, total silence and passivity on the part of Kacco can be objectively understood, in a business sense, as an implied statement that they did not intend to complete performance. Had they prayed for an additional grace period of say, a few hours, just enough to secure payment, insisting on their willingness to perform, they may have deserved the generous award granted by the district court and upheld by the court of appeal. By its lack of response to the ultimatum and its subsequent lack of reliance on Civil Code dissolution rules when the case was argued before the Supreme Court, Kacco did not show good faith or bad faith, but simply lacked faith in its ability to save a bargain or avert a loss.