Singapore Institute of Legal Education

Contemporary Legal Knowledge and Practice
Contract Law – Selected Principles

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1, 2	**0:00 – 4:08**	Hi everyone, welcome back to session 2. Agreement is the basis of contract, and all legal systems impose two requirements in determining where has been legally binding agreement: • First, parties must have manifested their assent to be bound – a requirement that follows from the premise that contractual liability is consensual; and • Second, the agreement through which they manifested their assent must be definite enough to be enforceable. You will all be familiar with contract formation under common law. Four elements need to be met for an agreement to be binding: an offer, an acceptance, consideration and intention to create legal relations. In determining whether an agreement has been made, what its terms are and whether it is intended to be legally binding, English law applies an objective test. Some of these concepts are slightly different under civil law. To form a contract, you must have consent, capacity and certainty of content. • **Consent:** civil codes with typically frame consent along, for example, "Only a sane individual can validly consent to a contract". • **Capacity:** typically relevant in the context of companies, the capacity of juridical persons is limited to acts useful for the achievement of their purpose as defined by their corporate documents and to acts which are accessory to them, in compliance with the rules applicable to each one of them. • **A lawful and certain content:** the contract cannot derogate from public order, either by its stipulations or by its purpose, whether or not the latter was known by all the parties.
3	**4:09 – 7:47**	Let's look at this through the lens of Indonesian law. The principles of contractual interpretation are found in the Indonesian Civil Code under the chapter "*Obligations arising from contracts or agreements*", specifically in Part 4, which contains the relevant provisions for interpretation of agreements, starting from articles 1342 to 1351. The starting point is **article 1342**, which tells you that if the contract is clear, you may not deviate from it using interpretation. There is some confusion here as some people may say that giving meaning to the words in a contract is already a form of interpretation. Article 1342 essentially applies the plain

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		meaning rule under common law – that is, *where the words, taken together and given their natural ordinary meaning, are coherent and are clear, then one should not assign a different meaning to those words by relying on the rules of interpretation found in this Part 4 of the Code*. The rules found in the following articles (**article 1343 onwards**) can only be used if the words in the clause or the contract are unclear or have several meanings when you read them. Additionally, there are 9 rules or canons of interpretation found in articles **1343 to 1351. These rules are designed to assist in discerning or finding meaning that will give effect to the intention of the parties.** Eminent jurist and foremost commentator on Indonesian contract law [*Jesa Triori*] reminds us that what you're looking for is the common intention or what has been mutually agreed and understood by the parties at the time the contract was entered into. Therefore, when the words in the clause or the contract are clear, article 1343 wants you to discern the intention of the parties at the time the contract was entered into. **Article 1344** requires that a party ensures that they adopt the interpretation that would allow the contract to be enforceable. Now turning to the next two provisions, **articles 1345 to 1346**, these provisions require you to interpret a contract in a manner that is aligned with the nature of the contract (that's 1345) and according to local custom or practice (now that's 1346). These provisions are meant to assist the intention of the parties because contracts are not entered in a vacuum. There is a body of knowledge behind every contract informed by its nature or usage. For example, is it a mortgage or loan agreement, or is it a production and sharing contract? In each case, it is helpful to understand what the custom and practice is for such a contract in that location. It may be that there is nothing special about the contract's nature or the local customary practice. And in that case, you move on to other rules or interpretation to help discern parties' intention.
4	**7:48 – 12:52**	Thai law gives us another example of how contracts are interpreted under civil law. Thai legal scholars and judges often seek guidance from two general rules: **section 171 and section 368 of the Civil and Commercial Code** (or "**CCC**"). **Section 171** of the CCC provides that in interpreting a declaration of intention, the true intention is to be sought, rather than the literal meaning of the words or expressions used. For example, in **Supreme Court Judgment No. 11107**, the court ruled that the true nature of a contract should be determined by the parties' intentions and actual terms, not just its name.

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		• In this case, 53 individuals entered a contract with the company, and the contracts were labelled as investment contracts. • However, the actual arrangement was a loan agreement as evidenced by the daily repayment schedule and the interest rate exceeding the legal limit. • The court found that despite being named as an investment contract, the true nature of the agreement was a loan under the Civil and Commercial Code. • Consequently, the rights and obligations should be governed by the laws applicable to loans, rather than investments. Next, **section 368** of the CCC provides that contacts shall be interpreted as required by good faith, taking customary practice into consideration. Customary practice can usually be seen in professional services, such as carriers, banking, legal, accounting, medical and agricultural services. • For example, **Supreme Court Judgment No. 1375** provides that "*although it did not state in the freight booking that the jute must be packed tightly, but in the customs of freight forwarding overseas, the consignor shall machine pack that jute that would be delivered tightly*". • The plaintiff was well aware of this custom, and thus such custom shall be deemed part of the contract between the plaintiff and the defendant. However, if the message is specified clearly in the contract, or the wording is specified clearly in the contract, interpretation by/though intention is no longer required. This principle is in accordance with **Supreme Court Judgment No. 2210.** • In this case, the party entered into a land lease agreement. The true intention of the party could be seen from such an agreement. • If the provision in the agreement is clear, there is no requirement to interpret the intention of the parties outside such an agreement. • No party may adduce the witness to supersede the written provision in the agreement. In summary, under Thai law, the court can see the true intentions of the parties under the law and section 171 and section 368 of the CCC. But if the wording in the contract or the agreement is clear, then there is no requirement to interpret the intention of the parties outside such an agreement.
5	**12:53 – 17:56**	Next, we will discuss filling the gaps with the statutory rules. If the true intentions of the parties cannot be discovered, or the true intentions of each party does not match, the contract is deemed to have gaps. This gap should be filled by applying relevant statutory rules and general document interpretation principles outlined in the CCC and other applicable laws.

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		These are prescribed under **section 10 to section 14 of the CC**C. Indeed, **section 10** provides that when any of the terms in a document may be interpreted in two meanings, the meaning which gives some effect shall be preferred over the other which does not. The principle set out in section is that: when interpreting the text of a document, and there are two possible interpretations or meanings, the preferred interpretation should be the one that gives effect. Next, **section 11** provides that in case of doubts, the interpretation shall be in favour of the party who incurs the obligation. This concept can be seen in the **Supreme Court Judgment No. 7257**. In this case, the court adjudged that as it did not clearly stipulate in the mortgage contract that the debt that should be covered under the contract includes the debt that the plaintiff provides a guarantee for other debtors. Therefore, the phrase (quote) "all types of debt and obligation" shall mean only the debt that the plaintiff as a primary debtor has against the defendant. Next **section 12**: in the case where an amount or money or quantity is expressed in a document both in characters and in figures, if there is inconsistency between them and the real intent cannot be ascertained, the expression in characters shall be governed. This concept can be seen in **Supreme Court Judgment No. 5827**, which provides that the defendant filled in an amount in the sheet, but the numbers and the letters were not consistent. The court therefore could not discover the true intention, so the amount in the written letter shall prevail in accordance with section 12. Next, **section 13:** if an amount of money or quantity is expressed in characters or in figures more than once in a document, but there is an inconsistency in them and the real intent cannot be ascertained, the lowest amount of money or quantity shall be governed. Next, the last example which is **section 14:** in the case where a document is made in several languages, whether in a single document or several documents, including the Thai language, if the contents in such several languages are different and the parties' intent as to which language is to prevail cannot be ascertained, the Thai language shall prevail. From these rules mentioned above, you will see that Thai law has inherent tension between the subjective and objective interpretations. Why? The general rule in Thai law is that an unexpressed intention cannot form a contract or part of a contract. Thai law does recognise both terms implied in fact and terms implied in law.

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6	**17:57 – 20:37**	Next, I will discuss the issue of pre-contract negotiations. Compare between common law position and civil law position. • First, common law position first: pre-contractual negotiations are part of the surrounding circumstances that are used to design, and hence interpret, the apparent (objectively determined) meaning of an agreement, unless the document is intended to be seen by third parties not privy to the negotiations. • Under common law, understand in general that various rules prohibit the admission of evidence of pre-contractual negotiations. • On the other hand, civil law systems are much more expansive when looking at pre-contractual negotiations. • The logic is that most contracts are subject to detailed negotiations in which the parties set out their position and will often explain their reasoning based on the commercial background. • Evidence of such discussion may sometimes be useful when seeking to interpret a contract at a later time. o However, please bear in mind that this is not conclusive, and it is still subject to interpretation under Thai law. When we look at pre-contractual negotiations, you are no longer interpreting the contract on the basis of what a reasonable objective person would have understood the contract to mean. Rather, you move *close to the subjective interpretation of either party during the negotiations to interpret the final common intention and agreement parties arrived at.* This is important to keep in mind as it may influence the way you construct and record your positions during negotiations, knowing that it can sometimes defy the interpretation of the contract, including in any potential dispute between the parties.
7	**20:38 – 27:18**	Next, we will discuss the doctrine of good faith. Firstly, under the CCC, **section 6** lays out a universal concept that it shall be presumed that each person acts in good faith. • As an example, **Supreme Court Judgment No. 9158** provides that - in this case, the plaintiff purchased a land from Mr S on 10 November 1989 and the title of the land had been registered and transferred to the plaintiff. • The defendant only argued that he possessed the land for more than 10 years, and the land therefore fell under his ownership by law under the concept of adverse possession.

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		• The court viewed that the plaintiff should benefit from section 6, that the purchase of land was done in good faith – that is, the payment had been met and the title had been registered. The plaintiff won this case. Further, as briefly mentioned earlier in slide 4, **section 368** explains the concept of good faith in contract that: contracts shall be interpreted as required by good faith, taking customary practice into consideration. **Section 368** of the CCC provides guidelines for interpretation to the effect that, in interpreting a contractual term, the common intention of the parties is to be ascertained, in accordance with good faith, in relation to good commercial practice without testing to the literal meaning of the statement. I note that the principle of good faith is an overriding one under civil law systems. It is applied not only to the interpretation of the contracts but also to the performance of obligations under the contracts. • It can be seen in **Supreme Court Judgment No. 478** which provides that the plaintiff had the right to use the path under the contract to sell the land. • The term (quote) "use the path" under the contract encompassed usual usage of path. • The actions of the defendant of narrowing the path down to one metre in order to obstruct the plaintiff from driving into the land thus prohibited the usual usage of the path and thus was considered breach of the contract. • The term of the contract allowed the plaintiff to use the path, but the action and the manner of use of the path was not prescribed by the contract. • Thus, it is debatable whether the plaintiff could only use the path on foot or could otherwise enter with a vehicle. When the true intention of the parties could not be revealed and no specific default rules are applicable, the interpretation of this term shall rest upon the principles of good faith and ordinary customs under section 368. And where no customs are known to exist, the term shall be construed as a person of ordinary prudence acting in good faith would. • The Supreme Court (in **Supreme Court Judgment No. 478**) then analysed that ordinary men in general would use any path with vehicles, such as cars. Therefore, the term of "use the path" must encompass the use of such with cars. • The action of the defendant limiting the use to be only by foot is thus a breach of the contract.

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		By contrast, under Thai law, good faith has near universal applicability. It governs the exercise of rights and performance of obligations. whether such rights or obligations derive from contract or tort, good faith has the power to override express contractual terms and impose an implied duty on a contracting party. The literal meaning of the word or expression is sometimes less relevant to the interpretation of the contract than the meaning of good faith and good commercial practice would suggest. **Section 171** and **368** of the CCC, which we already mentioned, guides us on the interpretation of the effect that in interpreting a contractual term, the common intention of the parties is to be ascertained in accordance with good faith, in relation to good commercial practice without clinging to the literal meaning of the statement. You see this on-screen now. I note that the principle of good faith is an overriding one under the civil law system. It applies not only to the interpretation of the contracts but also to the performance of obligations under the contracts.
8	**27:19 – 29:19**	Next, last one: I will discuss about the issue of liability of bad faith for torts. The concept of good faith also plays a part in torts under the CCC. **Section 421 of the CCC** provides that: the exercise of a right which will only injure another person shall be unlawful, or in other words, bad faith action. • For example, it can be seen in **Supreme Court Judgment 6599,** which is a renowned court case in Thailand where the Company T accounted that it would take the coupons valued 80 baht issued by the Company B and will double the value of the discount coupon to be 160 baht provided that the customer shall purchase the goods in Company T supermarket. • Company's T's operation is obviously to scramble for Company B's customers. • The Supreme Court held that the Company T's conduct was wrongful against Company B under 421 of the CCC. In summary, doctrine of good faith not only plays some significant part in the interpretation of the contracts, but also the Thai CCC mentions about good faith and bad faith under tort law as well.
9	**29:20 – 36:46**	Let me address in more depth the differences that exist as regards the allocation of damages under both systems. The approaches to determine compensatory damages necessary to achieve full reparation differs significantly across jurisdictions. Punitive damages do not exist in most civil law countries such as Germany, France, Switzerland, Poland, Italy, Japan, Korea and Taiwan. Punitive damages are also generally unavailable for a breach of contract in common law jurisdictions such as England.

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		• **Types of compensatory damages:** the various types of compensatory damages differ from jurisdiction to jurisdiction.
		
		• **Actual loss suffered and lost profits:** one distinction is between the actual suffered losses and the loss of expected profits. The distinction is regularly stipulated by law.
		
		  • **Section 252 of the German Civil Code**, for example, stipulates that the damage to be compensated includes lost profits.
		
		  • **Article 1231-2 of the French Civil Code** stipulates that damages generally include the damages actually incurred as well as lost profits.
		
		Under common law, compensatory damages may be available for direct harm resulting from a wrong (for example, the value of goods not delivered in breach of contract) and for consequential harm flowing from the same wrong (for example, lost profits).
		
		• **Direct damages** are often called general damages and are intended to compensate for the immediate consequences of a breach.
		
		• **Consequential damages**, on the other hand, are often referred to as special damages, and compensate for losses that may not be a direct consequence of a breach, but instead flow indirectly from the breaching conduct.
		
		• **Indirect losses** are only recoverable if it can be reasonably assumed that both parties contemplated them as a probable consequence of the breach of contract at the time the parties concluded the contract.
		
		• What qualifies as direct damages in one contract may be classified as indirect or consequential damages in another. Whether damages are classified as direct or consequential depends on the contract at issue, and the facts of the case.
		
		Remedies for breach of contract: under both common law and civil law a fundamental requirement for a contractual claim for damages is a breach of contract. However, the preferred remedy for a breach of contract in civil law jurisdictions is not monetary compensation, but rather specific performance.
		
		• In Germany, France and many legal systems influenced by the French Civil Code, specific performance is only denied if performance is not possible.

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		• By contrast, under common law, monetary compensation is the rule, and specific performance is only available where monetary damages are either inadequate or not available. **Breaches of contract** are often differentiated according to their nature, such as by their severity. In most civil law jurisdictions, a fundamental breach or similar material breach may be required for the termination of a contract but not for a claim for damages. • An exception may apply if the claim is for damages in lieu of performance, such as the party claims for damages instead of insisting on performance, as this is tantamount to a termination. • For example, in Germany, a non-material breach of contract doesn't entitle the non-breaching party to claim damages in lieu of performance. Only a material breach does. Under common law, compensatory damages are available for any breach of contract regardless of the cause or degree of materiality of the breach. **Amount of damages that can be allocated:** whether the injured party is entitled to full compensation might also depend on its own conduct – whether it is responsible for the cause of a damage, failed to mitigate the damage, or even gained any benefits from the other party's illegal conduct. Contributory negligence refers to the conduct of the injured party before or at the time when the damage occurred. **Mitigation of damages** refers to conduct after a party has become aware of the damage. French courts reject a general duty to mitigate damages in tort law. French courts have assumed that such a duty exists in contract law in exceptional cases. Some decisions have considered the creditor's fault as having contributed to the worsening of the harm, thereby limiting their compensation. The calculation of damages becomes particularly complex when the breaching party's actions or omissions have not only led to damage but have also potentially indirectly led to the benefit of the non-breaching party. The concept of **contributory negligence** also exists under common law. Moreover, the duty to mitigate the damage is enshrined in the mitigation of damages doctrine, according to which the injured party must take reasonable steps to reduce the damages. • If the non-breaching party avoids the potential loss resulting from the breach, then there is no recovery, because the claimant is entitled to damages only for the actual loss which is assessed by taking into account all the items within the notional profit and loss calculation for the whole transaction. • The injured party, however, may claim reimbursement of the cost incurred to mitigate the damage, even if its efforts to mitigate turned out to be unsuccessful.

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		Residual requirement to obtain damages: in civil law jurisdictions especially, it is a common requirement for the buyer to notify the seller of a breach of contract, or to request performance to give the seller a last chance to avoid a dispute by fulfilling its contractual obligations. In France, no claim for damages can be made until the other party is put in default by a formal protest, even if there was a fixed deadline for fulfilment.
10	**36:47 – 38:51**	Let's come back to the Turkish case study example that we looked at earlier this session. • After the alleged termination on 3 June 2015, the seller sold their shares to the third party on 1 Feb 2018, nearly three years after the original closing, for a significantly lower purchase price. • They tried to claim the delta – that is to seek to put itself in a position as if the contract and closing had been performed on 1 June 2015. • The claimants quantified their losses as the difference between the price it would have received under the SPA (the but-for scenario) and the price it received under the new transaction (the actual scenario). • Are they entitled to those damages? As a fundamental issue and as we saw earlier, we have to understand the treatment of damages under Turkish law. Where the termination was caused by default, the party in breach is liable for positive damages which are the difference between the current assets of the terminating party upon termination, and his assets if the contract had not been terminated and had instead been performed until its end – **article 126 of the Turkish Code of Obligations (TCO).** Negative damages are the difference between the current assets of the residing party and his assets if the contract had not been entered into at all – **article 125/3 of the TCO.** Here, the claimants were claiming for something else entirely – the difference between the original sale price, and the sale price identified through the third party at a later stage. This is neither positive nor negative damages granted under the Turkish Civil Code.
11	**38:52 – 40:42**	Similarly, civil law systems may also have strict rules on the election of damages. Article 112 of the TCO provides general compensation for breach. The Indonesian and Thai codes have similar provisions. However, the general provisions for compensation or damages will not apply if the codes provide for more specific breaches. In this case, article 125 of TCO was found to specifically address damages in the context of wrongful termination.

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		A further complication: to become entitled to remedies of positive damages instead of specific performance or any other type of damages, the Turkish Code, as many other civil codes, requires the claimants to confirm that they have renounced performance, that they have elected to claim positive or negative damages. On the claimants' case that the respondent's termination notice was invalid, Turkish law required the claimants to immediately elect and notify the respondents that they were electing to rescind the SPA. They did not do so, and the SPA would therefore have remained on foot. If a party fails to immediately make an election of its remedy under article 125 of TCO, it was to be deemed to have insisted on performance of the contract, with the result that the party can only claim damages for delay in performance. This is a great reminder of how civil law systems require us as lawyers to be very much more alive to the types of damages that may be claimed, and the form requirements for such elections.