The parol evidence rule and the CISG* — a comparative analysis

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Abstract

This paper will argue that globalisation of trade and hence the birth of international uniform laws has brought about changes in substantive law which need to be recognised by municipal systems. Specifically the parol evidence rule in common law will be put increasingly under pressure. It is argued that the sacred cows of common law namely the inadmissibility of evidence of a pre-contractual nature and hence the subjective intent of parties are outdated and change is required. As Lord Steyn in an address to the University of Sydney pointed out; the common law is possibly swimming against the tide. However changes are needed specially the inclusion and admissibility of subsequent conduct. The CISG has recognised that business people do not understand rules which exclude considerations on how the parties interpret their contracts.

This paper will highlight that contracts are based on bargain and exchange. The classical theory which suggests that contracts for a homogenous product, concluded between two strangers who transact in a perfect spot market is outdated and wrong.

As a result of the conflict between article 8 of the CISG and the parol evidence rule the outcome of litigation will yield possibly a different result as seen in recent US cases such as in MCC-Marble *Ceramic Center Inc v Ceramica Nuova D'Agostino, SPA.* However it is recognised that the common law has tools, such as rectification, which will bring about similar results as under the CISG. The time has come for the common law to slowly change and embrace international trends.

Introduction

The ascendancy of international commercial laws in the form of conventions and model laws has changed the contractual landscape significantly and can be viewed as a sea change in contract law. A knowledge of international contract law has become imperative considering that through ratification the CISG has become part of our domestic law. *Perry Eng P/L (Rec and Man appt'd) v Bernold AG*[1] in a general sense illustrates this problem well. The

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*United Nations Convention on Contracts for the International Sale of Goods.
[1]No SCGR-99-1063 [2001] SASC 15 (1 February 2001).

facts are simple. An Australian buyer sued the Swiss manufacturer in the South Australian Supreme Court for supplying defective goods. A clause in the contact, in brief, stipulated that the laws of South Australia governed the contract. However the judge noted:

> The statement of claim has been drawn up on the assumption that the South Australian Sale of Goods Act applies. This seems to me to be fatal to the plaintiff's ability to proceed to judgment [as the CISG applies].[2]

The simple fact is that domestic law cannot shield itself indefinitely from the influence of international trade laws. Principles in domestic law must be reviewed to remain in step with best practices.

Considering that the creation of international uniform laws is deeply political, it is not surprising that a compromise between the leading legal families had to be found. However, having reached compromises, the outcomes have shown to be workable and a significant international jurisprudence already exists. The importance of the CISG can be illustrated through its in effect having become the sales law of the EU, and having significantly influenced the new Chinese contract law.

This article will address only one issue, namely the parol evidence rule. As such, the intent of parties is central.[3] It is accepted that the common law demands an objective theory of contract. Therefore, in general terms, the law of contract is not concerned with the subjective intent of parties as objectively intent is not common to both parties.[4]

This view results from nineteenth century reforms when the influence of Continental writers and the subjective theory of contract was accordingly well established. However, by the end of the century the transition between the subjective and objective theories was well under way.[5]

The basis for the objective theory can be traced back to the ascendancy of the classical concept of contract law. Eisenberg points out that the classical theory operates under the premise that the contract is for a homogenous product concluded between two strangers who transact in a perfect spot market.[6] Given the background of classical contract theory, it is understandable that the parol evidence rule developed.

Today with internationalisation of trade and globalisation such a theory is untenable and 'what made the classical contract theory infinitely worse was

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[2] *Id* at 16.

[3] The common law problem of mistake as well as the introduction of the principle of good faith can only be understood in a comparative sense if the question of intent of the parties is examined. In that context, this article is an extension of another, published in the 4 (2002) *European Journal of Law Reform*.

[4] J Steyn 'Contract law: fulfilling the reasonable expectations of honest men' (1997) 113 *LQR* 433 434.

[5] JA McHugh *Air Great Lakes Pty Ltd v K S Easter (Holdings) Pty Ptd* (1985) 2 1985 *NSWLR* 309 335.

[6] M Eisenberg in J Beatson & D Friedman *Good faith and fault in contract law* (1995) 296.

that its tacit empirical premise was wholly incorrect'.[7] Needless to say, the CISG has recognised that many contracts are based on the concept of 'bargain and exchange'. It can be argued that the arguments regarding the need to review the subjective theory of contract interpretation are re-surfacing. In any case, it is doubtful whether the objective theory was ever in complete control. In *Taylor v Johnson*[8] the court noted that:

> [while] the sounds of conflict have not been completely stilled, the clear trend in decided cases and academic writing has been to leave the objective theory in command of the field.[9]

This article argues that a total rethink of the parol evidence rule is warranted. This is important for two reasons. First, subjective intent is anyway applied in certain circumstances within the common law, and secondly, domestic law cannot indefinitely ignore the increasing importance of international uniform laws. It is not in the interest of domestic law to create a dual system within its own laws, where depending on the place of business, different laws can apply. Such a problem can be minimised if domestic law takes note of international law and adjusts its own laws where possible. Also, an increasing number of academics are attacking the omission of subjective intent in the interpretation of contracts.[10] The parol evidence rule is simply incompatible with international developments and arguably with the needs of the business community.

This article will illustrate how the parol evidence rule is applied under the CISG by examining the leading jurisprudence. It will then explore what effect the intention of parties has in the courts' deliberation in interpreting the contractual obligations. It will be argued that the intent of parties is best served under the rules of the CISG. For that purpose the parol evidence rule of the common law will be compared with article 8 of the CISG.

The court ruling in *MCC-Marble*

MCC-Marble Ceramic Center Inc v Ceramica Nuova D'Agostino, SPA[11] *(MCC-Marble)* is the leading case on the intent of parties under the CISG. It has created enormous interest among scholars and jurists alike, and the decision:

> reveals a court striving to transcend its background in domestic U.S. law, energetic in pursuing an international perspective on the Convention's meaning, and informed, thoughtful and coherent in its grasp of CISG provisions and their meaning.[12]

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[7] *Id* at 297.

[8] (1983) 151 CLR 422.

[9] *Id* at 429.

[10] See D McLaughlan 'A contract contradiction' (1999) 30 *VUWLR*.

[11] 144 F 3d 1384 (11 cir (Fla) 1998) (http://www.cisg.law.pace.edu).

[12] HM Flechtner '*The UN Sales Convention (CISG) and MCC-Marble Ceramic Center Inc v Ceramica Nuova D'Agostino, SpA*: the eleventh circuit weighs in on interpretation, subjective intent, procedural limits to the conventions's scope, and the parol evidence rule' (1999) 18 *Journal of Law and Commerce* 259 260.

The interpretation of contracts, and the importance of the application of the intent of the parties, is regulated in article 8 of the CISG which states:

> (1) For the purposes of this Convention statements made by and other conduct of a party are to be interpreted according to his intent where the other party knew or could not have been unaware what the intent was.
> (2) If the preceding paragraph is not applicable, statements made by and other conduct of a party are to be interpreted according to the understanding that a reasonable person of the same kind as the other party would have had in the same circumstances.
> (3) In determining the intent of a party or the understanding a reasonable person would have had, due consideration is to be given to all relevant circumstances of the case including the negotiations, any practices which the parties have established between themselves, usages and any subsequent conduct of the parties.

The court recognised the implications and importance of article 8 by stating that:

> Contrary to the result of the objective approach which is familiar practice in United States courts[13], the CISG appears to permit a substantial inquiry into the parties' subjective intent, even if the parties did not engage in any objectively ascertainable means of registering this intent.[14]

The judge made it perfectly clear that article 8(3) 'trumps' the parole evidence rule. The clearest indication is expressed in the following statement:

> Moreover, article 8(3) of the CISG expressly directs courts to give due consideration ... to all relevant circumstances of the case including the negotiations ... to determine the intent of the parties. ... article 8(3) is a clear instruction to admit and consider parol evidence regarding the negotiations to the extent they reveal the parties' subjective intent.[15]

In brief, the president of *MCC-Marble* negotiated at a trade fair with D'Agostino. The negotiations took place in Italian with the help of a translator, as the American buyer did not speak Italian. The documentation, including the standard form clauses, were written in Italian. The buyer did not request a translation and signed the contract. The signing took place after the parties had agreed orally on price, quantity and other key terms. Under the signature in Italian was a clause stating that the buyer was aware and approved the clauses printed on the reverse side of the order form. In the months that followed, *MCC-Marble* submitted several orders using the Italian order form.

The court, predictably, dispensed with the question of signing a document containing terms in a foreign language by stating:

> We find it nothing short of astounding that an individual ... would sign a contract in a foreign language and expect not to be bound simply because he could not comprehend its terms. We find nothing in the CISG that might counsel this type of reckless behavior and nothing that signals any retreat from the position that parties who sign contracts will be bound by them regardless of whether they have read them or understood them.[16]

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[13] *MCC-Marble* n 11 above s 1387 n 8 and 1388 n 11.
[14] *Id* at 1387 to 88.
[15] *Id* at 1389.
[16] *Id* at 1387 to 88 n 9.

This opinion mirrors those in international jurisdiction as well as academic writing. It appears that the above views are settled law, not only in the CISG, but also in any other legal system.

The court noted and agreed with the magistrate judge's report that 'no interpretation of the contract's terms could support the buyer's position'.[17] In the common law this would have been the end of the matter as it was in the court of first instance. However, the circuit judge correctly pointed out that the CISG allows an inquiry into the parties' subjective intent even if the parties did not 'engage in any objectively ascertainable means of registering this intent'.[18] The whole purpose of article 8 in simple terms can be narrowed down to the above observations. It follows, therefore, that arguably domestic and international law differ in ascertaining the intent of the parties.

The *MCC-Marble* decision is also remarkable as the circuit judge recognised the importance of the CISG and its implementation by courts.

> One of the primary factors motivating the negotiation and adoption of the CISG was to provide parties to international contracts for the sale of goods with some degree of certainty as to the principles of law that would govern potential disputes and remove the previous doubt regarding which party's legal system might otherwise apply. Courts applying the CISG cannot, therefore upset the parties' reliance on the Convention by substituting familiar principles of domestic law when the Convention requires a different result. We may only achieve the directives of good faith and uniformity in contracts under the CISG by interpreting and applying the plain language of [its articles].[19]

The international legal methodology necessary to interpret the CISG has been recognised. In this regard it is significant that the court also consulted and cited treaties by scholars from outside the Anglo-American tradition.[20] It is also interesting to observe that the court stated in a footnote that it had searched for foreign case law. In so doing it also noted that:

> the parties have not cited us any persuasive authority from the courts of other States party to the CISG. Our own research uncovered a promising source for such a decision [on an internet site].[21]

It must be acknowledged that it is not easy for a court trained and indoctrinated by domestic law suddenly to embrace a new methodology not only in an interpretive sense but also in substantive law. The fact is that under article 8(1), a shared subjective intent is binding despite the fact that the parties signed documents which show a contrary intent. Furthermore, such subjective intent is not 'blocked by that ancient pillar of common law tradition, the parol evidence rule'.[22] However, it should also be noted that the parol evidence rule is merely a particular way in which the parties' intentions are binding. In view of the above it can be argued that the parol

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[17] *Id* at 1388.
[18] *Id* at 1387.
[19] *Id* at 1390.
[20] Flechtner n 12 above at 271.
[21] *MCC-Marble* n 11 above.
[22] Flechtner n 12 above at 273.

evidence rule has outlived its usefulness considering the possibilities offered by international conventions and model laws.

Intention of parties

Introduction

The first observation on the parol evidence rule is that it finds no uniform application amongst common law countries. The rule varies between Australia and the Unites States, and even within the United States it is not uniform. In the United States it has both statutory and varied common law manifestations, and is expressed in the Uniform Commercial Code article 2.[23]

In identifying the content of a written contract, the parol evidence rule determines which evidence is applicable in the circumstances. In the United States 'the Corbin approach instructed courts to look at all relevant evidence surrounding the agreement to decide whether the parties actually intended the writing to be complete and exclusive'.[24] The crucial point — it appears — is that the courts must determine whether the writing is a partial or a complete integration or statement of the contract. Common law courts in general solved this problem by taking a stance, which ostensibly promotes certainty and predictability in contract performance.

> The primary rule is to simply ascertain the meaning of the language of the contract and therefore ... evidence of the pre-contractual negotiations of the parties or their subsequent conduct cannot be used in aid of the construction of a written contract.[25]

Such a view ignores the fundamental reason for a contract as it looks only at the outcome of an action and ignores the motive. A contract is not merely an instrument, which can be interpreted by an impassive bystander ignoring each party's understanding of the statements or conduct of the other party.

A French case illustrates the difference between the common law approach, and the approach taken by the CISG. In *M Caiato Roger v La Societé Francaise de factoring international factor France*, the court looked at the prolonged dealings between the parties and found it impossible for the seller to deny knowledge that the goods were destined for the French market and hence had to comply with French marketing regulations.[26]

Arguably, in terms of the common law, the evidence of the conduct of the parties would have been inadmissible under the parol evidence rule, as the written contract did not include compliance with French marketing regulations. However, under the CISG the intention of parties is not a question of evidentiary rule, rather it is treated a one of the factual pieces of

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[23]DH Moore 'The United States parol evidence rule under the United Nations Convention on Contracts for the International Sale of Goods' (1997) III *International Trade and Business Law* 61.

[24]*Id* at 62.

[25]*Hideo Yoshimoto v Canterbury Golf International Limited* (2000) NZCA 350 (27 November 2000) 60.

[26]*Cour d'appel de Grenoble* 93/4126 (http://cisgw3.law.pace.edu/cases/950913f1.html) last update 24 October 2000.

information which are required to construct the contract as the parties intended it to be in the first place.

Subjective intent under the common law

The treatment of subjective intent is best summarised by McHugh JA who notes:

> Since the decision in *Prenn v Simmonds* [1971] 1 WLR 1381 ... a court's right to look at surrounding circumstances in construing a document ... is no longer open to dispute. No doubt the rule still remains that [evidence of the subjective intention] is not admissible to support particular interpretations of a contract.[27]

One could be forgiven for assuming that under the common law the subjective intent of parties has no place at all as it only introduces an area of uncertainty. However, this is not so. Lord Steyn admitted that a rule cannot be absolute and unqualified, as this would defeat the reasonable expectations of commercial men.[28] Admittedly a shift away from the black letter law approach has taken place, and but in *Investors Compensation Scheme Limited v West Bromwich Building Society*,[29] no shift in the treatment of subjective intent is detectable. Lord Hoffman in his influential principles has not embraced the introduction of subjective intent. Indeed in principle three he argues that:

> (3) The law excludes from the admissible background the previous negotiations of the parties and their declarations of subjective intent.[30]

Such an approach ignores the possibility that the parties may in previous negotiations have agreed on terminology, which is clear to them, but may be foreign to others. In such instances, despite the parties clear understanding, the law will contradict such subjective and clear intent and introduce its own 'foreign' construction to interpret the contract. Clark JA confirms this view when he notes:

> ... if a party seeks to rely on an antecedent oral agreement to support a contention that the word or phrase in the written agreement bore an agreed meaning which, as a matter of English, it was not capable of bearing. In that instance the oral agreement would contradict the written contract and the parol evidence rule would prevent its reception into evidence.[31]

Arguably, if the parol evidence rule is applied in the above manner it will 'defeat the reasonable expectations of commercial men'.

The real problem, besides the potential for artificial construction of a contract, is that in certain circumstances the principle of subjective intent is applied to interpret contracts. Lord Hoffman in his principle three noted that:

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[27]McHugh n 5 above at 334.

[28]Steyn n 4 above at 440.

[29](1998) 1 WLR 896.

[30]*Id* 912H913E.

[31]*Trawl Industries of Australia Pty Ltd v Effem Foods Pty Ltd* (1992) 27 NSWLR 326 362.

'[Declarations of subjective intent] are admissible only in an action for rectification.'[32]

Considering that subjective intent takes on a different meaning depending on whether contract formation or contract interpretation is the issue, there is a conflict with the policy of certainty and predictability. It does not make sense that subjective intent is admissible in one part of contract law but not in another. Admittedly, if one were to take a micro look at contract theory an argument could be advanced that certainty and predictbility are achieved in the parol evidence rule. However, in the 'big picture' approach, the argument of predictability and certainty is simply not defensible.

Formation of contract

In the formation of contract, *Smith v Hughes*[33] is often noted as advocating that objective or apparent consensus is sufficient.[34] Blackburn J stated

> If whatever a man's real intention may be, he so conducts himself that a reasonable man would believe that he was assenting to the terms proposed by the other party, and that other party upon that belief enters into the contract with him, the man thus conducting himself would be equally bound as if he had intended to agree to the other party's terms.[35]

Clearly a consensus *ad idem* or meeting of mind is an essential element in the formation of the contract. However, to ascertain what the parties consented to Blackburn J in his judgment not only referred to the objective intent, he also included a subjective element. Specifically his passage '... that other party upon that belief enters into the contract with him ... '[36] indicates that to show formation of a contract, a subjective understanding is essential. Simply put:

> A party who alleges the formation of a binding contract because a reasonable person in her position would have been entitled to infer a contractual offer can only succeed if, in addition, she subjectively understood that there was an offer.[37]

The importance of the above argument is that a distinction must be drawn between the presumed and actual intention of the parties. The most important consideration is that the actual or subjective intent of the parties is sought. If an informed bystander looking at the words concludes that there is a contract, but both parties are aware that they are play-acting, no contract has been concluded. This illustrates the problem of applying the objective theory: 'is it objectivity from the point of view of the promisor, the promisee or the detached bystander?'[38]

Only if no subjective intent can be established, should the objective or presumed intent be considered. Hope JA put it succinctly when he said:

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[32]*Investors Compensation Scheme* n 29 above at 912H–913E.

[33](1981) LR 6 QB 597.

[34]McLaughlan n 10 above at 175 176.

[35]*Smith v Hughes* n 33 above at 607.

[36]*Ibid.*

[37]McLaughlan n 10 above at 177 specifically n 7.

[38]McHugh n 5 above at 336.

> ... if the mutual actual intention was that there should be a concluded contract, it would be fraudulent to deny that intent.[39]

In essence it 'remains of social and commercial importance to enforce the actual intention of parties to make a contract as manifested by their conduct'.[40]

Interpretation of contracts

As soon as a binding contract is admitted the rules change. The evidence the parties relied upon to prove the contract, becomes inadmissible if there is a dispute as to the interpretation of the contract. Even liberal versions of interpretation stressing 'common-sense' and 'the importance of commercial men' merely reject the literal or plain meaning approach and not the parol evidence rule. As pointed out above, Lord Hoffman set out five rules for the application of the parol evidence rule. He basically reinforces that evidence of subjective intentions is inadmissible. However, in rule 3 he acknowledges that subjective intent '[is] admissible only in an action for rectification'.[41]

Rectification and the implication of terms have one thing in common. The problem is caused by the omission of a term which should have been included. It must be noted that the implication of terms in this context, is to be considered within the application of the parol evidence rule. Mason J noted this difference when he said that '[the] remarks were directed not to the implication of a term but to the application of the parol evidence rule ... '.[42] Furthermore Mason J explained the difference between rectification and the implication of a term as follows:

> Rectification ensures that the contract gives effect to the parties' actual intention; the implication of a term is designed to give effect to the parties' presumed intention.[43]

Such a distinction is very useful if based on an examination of the intent of the parties. If subjective intent can be established then rectification should automatically be used to give effect to the contract. However, if subjective intent is lacking, an implication of a term using objective criteria is the only way to give effect to a contract. But in essence the whole issue hinges on the approach by counsel, and not what evidence is available. In rectification evidence of subjective intent is admissible, but if counsel relies in the implication of a term, the parol evidence rule will bar the exact same evidence from being admitted or taken into consideration.

There is no debate that the presumed or objective intention leads to the implication of a term. The court in its capacity as the informed bystander can imply a term into a contract, which, objectively analysed, belongs in the

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[39]McHugh n 5 above at 309, 319.

[40]McHugh n 5 above at 338.

[41]Lord Hoffman n 29 above at 2.

[42]*Codelfa Construction Pty Ltd v State Rail Authority of NSW* [1982] 149 CLR at 347.

[43]*Id* at 346.

contract. Good faith, for example, is increasingly being recognised as such a term.

In sum it can be argued that as soon as subjective intent can be established, rectification should be sought. If subjective intent cannot be established, it ought to be seen whether objective intent can be elicited and a term can be implied into a contract. Mason J confirms this view when he states that:

> the prior oral argument of the parties being inadmissible in aid of construction, though admissible in an action for rectification.[44]

Logically speaking, it makes no sense that the same evidence is admitted if rectification or the formation of a contract is at issue, but is not admissible if the interpretation of the contract is in dispute. The observation by Lord Wilberforce is instructive when he notes that the alternative claim for rectification: 'let in a mass of evidence ... which would not be admissible on construction.'[45]

There is simply no consistency in the argument, or at best, the policy is not consistent. It smacks of the argument that there is a difference between being pregnant and being 'a little bit' pregnant. After all is the aim not to find out and to give meaning to the contract as it was intended by the parties?

The inconsistency argument is given weight when it is considered that extrinsic evidence 'is not even going to be admissible on the implication of a term'.[46] This ruling is rather confusing if another exception to the parol evidence rule, which was laid down in *the Karen Oltmann*,[47] is considered. Kerr J had to consider how meaning can be given to words which are capable of bearing more than one interpretation. He said:

> ... it is permissible for a Court to examine the extrinsic evidence relied upon to see whether the parties have in fact used the words in question in one sense only, so that they have in effect given their own dictionary meaning to the words as a result of their common intention.[48]

The problem with Kerr's view is that the court must make a decision whether words are capable of only one meaning. The argument reverts to the informed bystander who has to decide what the parties intended in the first place. A strong argument can be advanced to suggest that it would perhaps be simpler just to ask the parties what their subjective intent was, instead of second guessing its objective meaning. In any case, the exceptions do not advance the predictability and consistency argument which is frequently noted as the basis of contract theory.

McLaughlan also points out that the exception should not be limited to evidence of actual common intention. He advances the argument that where

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[44]*Id* at 337 352.

[45]*Prenn v Simmonds* (1971) 1 WLR 1381, 1383.

[46]*Lexcray Pty Ltd v Northern Territory of Australia* D1/2001 (3 May 2002), HCA.

[47]*Partenreederei MS Karen Oltmann v Scarsdale Shipping Co Ltd* (1976) 2 Lloyd's Rep 708.

[48]*Id* at 712.

the evidence establishes that one party intended a particular meaning, and the party reasonably believes the other party accepted that meaning, such evidence should be included. 'It would be a strange twist in the law if such an objectively determined agreement as to the meaning did not suffice.'[49] This is specifically so when one considers that in the formation of contract the above argument would not be contested.

Even in the landmark decision of the High Court,[50] Mason J found it important enough to admit the need for exceptions to the parol evidence rule. The fact that there should be exceptions is not surprising considering Lord Wilberforce's speech where he noted:

> When one speaks of the intention of the parties to the contract, one is speaking objectively — the parties cannot themselves give direct evidence of what their intention was — and what must be ascertained is what is to be taken as the intention which reasonable people would have had if placed in the situation of the parties.[51]

It is indeed strange to ignore primary evidence from the parties and base a judgment on secondary evidence. Whichever way the argument is presented, even an informed bystander is still only 'second guessing' what the actual or subjective intent of the parties was.

There is also a *naïveté* in the argument of the 'informed bystander'. As an example the words 'the goods must be in good repair' appears in a contract. The question is do they have to be repaired before shipment, or do they only have to be in good order, that is faults due to normal wear and tear are permissible? A person equally situated is now required to shed light on the proper interpretation of the contract as ostensibly now an objective intent is elicited. If this line of argument is extended, it can be argued that the only persons equally situated are the two contractual parties as they are the only reliable source of extrinsic evidence. However, the parol evidence rule would prohibit such evidence.

This is exactly where the problem lies, namely in determining primary evidence that is reliable evidence, which is obtainable from negotiations and the party's actions.

> There is no sensible reason why the interpretation process required to determine whether a contract was formed should differ so fundamentally from the process required to determine the meaning of that contract.[52]

A further problem with the objective approach is that it assumes that all relevant clauses are included into the contract, and by definition everything the parties rejected or on which they failed to find common ground, is not included in the contract. McLaughlan had this in mind when he posed the question: 'Why allow evidence of the fact that the parties have united in

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[49]McLaughlan n 10 above at 187.

[50]*Codelfa* n 42 above at 352.

[51]*Reardon Smith Line v Hansen-Tangen* (1976) 3 All ER 570 574.

[52]McLaughlan n 10 above at 182.

rejecting a particular meaning but disallow evidence of the fact that they have united in accepting a particular meaning?'[53]

It is also appears to be settled law that the reason for exclusion of previous negotiations as admissible evidence is not one of policy. Lord Wilberforce stated succinctly that the reason for exclusion is simply 'that such evidence is unhelpful'.[54] There is no doubt that caution must be exercised when admitting evidence of previous negations. It is an entirely different matter if there is a situation, which the parties did not anticipate, or where a party with the benefit of hindsight gives a different and unsubstantiated version of events. In such circumstances the subjective view must be rejected.

The argument that certainty in commercial transactions is of paramount importance must also be questioned in relation to the parol evidence rule. Arguably the most important element of certainty in commercial transaction is the ability of the business community to rely on the subjective or mutual intent of the contractual obligations, and for courts to enforce such intent. The certainty argument in relation to interpretative disputes is a weak one considering that judges cannot even agree whether a word has a plain meaning or not.[55]

The fact that language is often incapable of expressing meaning in a certain and uniform way, is well documented.[56] Therefore, to argue that a 'policy certainty' demands that evidence of a pre-contractual nature is not admissible, is fallacious. This is specially so as some evidence is found that courts will allow post-contractual conduct as an aid to determining the meaning of words in a written contract.[57]

In sum, it has been shown that the parol evidence rule is not a 'rule' in the true sense as too many exceptions and variations indicate that its abandonment is warranted. The argument is strengthened if consideration is given that many interpretation disputes are accompanied by alternative claims for rectification, misrepresentation or estoppel. In these cases, evidence of all the negotiations is admissible. However, the most compelling argument is that the parol evidence rule is out of step with international developments. Justice would not be well served if one class of litigants, namely foreigners, were to be treated differently from local litigants.

Intention of parties — jurisprudence of the CISG

In contrast to the common law the CISG exhibits what could arguably be termed, a simplified approach in ascertaining the intention of the parties and hence giving meaning to the contract. Not only the CISG, but also the UNIDROIT principles and the European Principles, have adopted the same

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[53]*Id* at 187.

[54]*Prenn v Simmonds* (1971) 1 WLR 1381, 1384.

[55]See, for example, *Investors Compensation v Bromwich Building Society* n 29 above.

[56]see for example D McLaughlan 'The plain meaning rule of contract interpretation' (1996) 2 *NZ Business LQ* 80.

[57]See for example *Attorney-General v Dreux Holdings Ltd* (1996) 7 TCLR 617.

approach in viewing the subjective intent as an important tool in understanding the purpose of the bargain which is expressed in a contractual arrangement. Arguably, both the common law and international instruments aim to give effect to a contract. However, their approach has diverged. The common law in essence views the written contract as the culmination of negotiations and hence the contract expresses the bargain of the parties. Such an approach is logical if placed within the classical contract theory. The CISG, on the other hand, has realised that a contract is an evolving instrument of bargain and exchange. Considering the cultural influences within internationalised trade, a strict adherence to a written contract is illusionary. Especially in Asian trade, a contract is an evolving instrument which can change according to economic situations.

The 'key stone' in the interpretation of a contract is the teasing out of the intention of the parties pursuant to article 8. The first question the courts would ask is, what is each party's understanding of the statements or conduct of the other party? The *Oberlandesgericht München* applied article 8(1) in such a way. The German buyer insisted that he could pay a reduced price as arranged in the contract. However, the court noted that by ordinary interpretation of the subjective intent, the parties had agreed to a discounted payment only if the buyer met certain terms. As he failed to do so, the full price became due.[58]

Not all intentions are expressly stated and silence can also amount to an expression of intent. Article 8(1), not only includes statements made, but also conduct by parties as constituting intent. A Swiss decision[59] illustrates this point. A German supplier filled an order for a Swiss buyer regarding a summer fabric collection. Because the buyer did not pay on time, the seller did not supply the winter collection. The purchaser, after part payment sent a letter to the seller setting out a payment schedule for the outstanding amount as well as delivery dates for the winter collection. The seller refrained from delivering and was sued for damages arising from the failure to deliver the winter collection pursuant to the written contract. The question was whether the seller's silence constituted an acceptance of the content of the letter. The court established the intention of the parties, and found that silence in this case did not constitute acceptance of the amendment of the contract. The other party, that is the Swiss buyer, must have been aware that through silence the seller did not accept the variations as proposed by the buyer. In other words, the buyer could not have been unaware of the true intention of the seller.[60]

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[58]7 U 2070/97 (http://cisgw3.law.pace.edu/cases/970709g1.html) last update 24 February 2000.

[59]*Obergericht Basel-Landschaft* 40-99160 (A15) (http://cisgw3.law.pace.edu/cases/991005s1.html) last update 19 July 19 2000.

[60]*Ibid.*

Formation of contract

Unlike the common law, the CISG does not distinguish between formation or interpretation of contracts in relation to the admissibility of extrinsic evidence. However, the CISG, unlike the common law, includes silence as an expression of the intent of parties. In *Ste Calzados Magnanni v SARL Shoes International*[61] the buyer placed an order for shoes but the seller denied ever having received such an order and furthermore relied on article 18(1) which states that silence 'does not in itself amount to acceptance'. Article 18 through its terminology does not indicate that silence as such is always insufficient. 'In itself' indicates that unless otherwise shown, silence does not constitute acceptance. The court therefore again looked at article 8 and found that the practice in previous years indicated that the seller always fulfilled the orders without formal acceptance. In addition, the seller was asked to manufacture samples and was left with the original material in his possession.[62] The court found that this fact alone should have prompted the seller to question the buyer on how an absence of an order should have been interpreted.

Silence as such, is a part of several articles, notably 18 and 14. Article 14(1) allows for indications of silent intentions (*stillschweigende Festsetzung*). Difficulty in discovering the subjective intent merely means that article 8(2) is the next step in a courts endeavour to ascertain the 'true intent' of the parties. In other words, in the absence of subjective intent, objective intent will also assist the court in establishing the contractual intent of the parties. The Austrian High Court[63] noted that price, quantity and character of goods can be ascertained by 'a reasonable person similarly situated' through a construction of the objective intent pursuant to article 8(2).[64] Silence, as expressing the intent of parties in relation to the offer and acceptance of a contract, is summarised by *Inta SA v MCS Officina Meccanica SpA*[65] where the judge noted:

> It is certain that in this framework the Convention provides that silence or inactivity in itself will not constitute acceptance, but in this case there were repeated acts that were taken to conclude the contract and, by the standards discussed above ... there was no disagreement with the clause and, even less, abuse of a dominant position by one party over the other.[66]

In sum there is a strong similarity between the common law and the CISG in the treatment of intent in relation to the formation of contracts. Both view subjective intent as of primary importance, and only in the absence of mutual

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[61]*Cour d'appel de Grenoble* 21 October 1999 (http://cisgw3.law.pace.edu/cases/991021f1.html) last update 12 July 2000.

[62]*Ibid.*

[63]*Oberster Gerichtshof* Austria.

[64]*Oberster Gerichtshof* 10.11.1994, 2 Ob 547/93 (http://www.jura.uni-freiburg.de/ipr1/cisg/urteile/text/117.htm).

[65]Argentina. *Camera Nacional de Apelaciones en lo Comercial* 14 October 1993 45.626 (http://cisgw3.law.pace.edu/cases/931014a1.html) last update 24 October 24 2000.

[66]*Ibid.*

consent will the court ascertain the objective intent of the parties. Arguably the CISG goes one step further by including silence in its deliberations. If there is a difference, it can be argued that the CISG advocates an holistic approach whereas the common law is more technical in nature in extracting the true intent of the parties.

Interpretation of contracts

At first glance it could be argued that the common law and the CISG are similar in their approach to the interpretation of contracts. Both view the words in the contract as the primary source of interpretation. The ICC Court of Arbitration as an example referring to article 8 argued:

> when parties have concluded a contract ... the agreement of the parties has to be analyzed in first instance by interpreting the wording of the contract itself. According to art. 8(3) ... usages of trade constitute guidelines only to establish what a reasonable person had to understand in view of the wording of the contract.[67]

It would indeed be strange if any system of law should not refer to the written contract in the first instance. More than likely the parties would have expressed their bargain in the contractual document. The question is whether the contract corresponds to the shared aspiration or subjective intent of the parties. If there is a discrepancy, the CISG will in all circumstances attempt to ascertain the true intent of the parties and will give effect to that intent. The common law, on the other hand, arguably places far too much reliance on the written contract and ignores the wishes of the parties in favour of perceived notions of certainty and predictability. There is a strong argument that the CISG has through article 8 managed to introduce a balance between certainty, predictability and the enforcement of the true intent of what the bargain between the parties ought to be.

The difference between the common law and the CISG becomes apparent when a contract needs to be interpreted: the CISG only asks whether there is evidence of subjective intent pursuant to article 8(1). That is, the other party either knew or could not have been unaware of the intent of the party. The common law, on the other hand, will dismiss subjective intent as extrinsic evidence and will only allow its reception into a contract in exceptional circumstances such as rectification, misrepresentation and estoppel. In other words, the common law introduces two variables into the interpretation of contracts. In essence the problem with the common law is, as Bingham LJ notes:

> English law has developed piecemeal solutions in response to demonstrated problems of unfairness.[68]

The CISG solves the problem of fairness of performance of contracts pursuant to article 8.

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[67]ICC Arbitration Case No 7645, March 1995 (2000) 11 *ICC International Court of Arbitration Bulletin* (ACAB) 36-37.

[68]*Interfoto Library Ltd v Stiletto Ltd* (1989) 1 QB 433 439.

The holistic approach of the CISG can be illustrated in an important area where the intention of the parties is not always easily ascertainable, namely in the inclusion of general terms and conditions into contracts. Schlechtriem points out that:

> [As the CISG lacks] provisions on the control on standard form contracts, I think the one tool that may come to grips with standard contracts is Art. 8(2). It enables the court to ignore fine print, which is contradictory, vague, or difficult to understand by using a 'reasonable person similarly situated' standard. And it is also possible that fine print in a language which under normal circumstances could not be expected to be understood by the other party will not determine the content of the contract.[69]

He alludes to two points namely, the treatment of standard form contracts, and the choice of a foreign language.

The mere fact that by mutual consent a foreign language has been chosen, does not in itself bring article 8(2) into play. It is settled law that there is an obligation on the other party to have the contract translated. If in doubt the principle of good faith would dictate that the party in question would ask for clarification from the other party, or gain understanding through expert translation. A party who agrees to contract in a particular language is bound generally not only by the standard form terms, but also by an expectation that the language is understood.[70]

Schlechtriem also argues that a term in a foreign language cannot necessarily be relied upon if the choice of communicating a term in a foreign language is unilateral.[71] Again the principle of good faith, as well as the reasonable person test of article 8(3), will determine this issue.

As far as the inclusion and treatment of standard terms and conditions is concerned, the matter appears to be settled. The *Oberlandesgericht Zweibrücken* confirmed the views held by Schlechtriem. It noted that the CISG does not provide specific requirements for the incorporation of standard form contracts. 'Whether such terms become part of the contract must be determined by the application of article 8.'[72] The court tested the subjective intent first and found that there were no negotiations which could have helped to establish the subjective intent. Recourse to article 8(3) also established that there was no customary practice therefore the objective intent could not be established. As far as the validity of the exemption clause was concerned the court relied on article 4 and decided the matter by recourse to national law.[73]

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[69]P Schlechtriem 'Uniform sales law — the experience with uniform sales law in the Federal Republic of Germany' 1991/92 *Jurisdik Tidskrift* 1 12.

[70]*Landgericht Kassel 1. Kammer für Handelssachen* 15.02.1996 11 O 4187/95 (http://www.jura.uni-freiburg.de/iprl/cisg/urteile/text/190.htm).

[71]Schlechtriem n 69 above at 20.

[72]8 U 46/97, (http://cisgw3.law.pace.edu/cases/980331g1.html) last update 17 July 2000.

[73]*Ibid.*

What then is the mandate of article 8? The Landgericht Heilbronn pointed to the fact that article 8 is not only concerned with communications. The question is what can a reasonable person in the same circumstances expect to have understood, and hence how would he interpret the communication?[74] The Landgericht Zwickau put it similarly by pointing out that in a communication between parties 'the wording was clear and unambiguous and furthermore the meaning given to the words corresponds with those a "reasonable person" would attribute to those words'.[75] Such intent is in line with the desire of the CISG to keep the contract afoot as long as there is a possibility of performance of the contractual obligations. This principle conforms to the attempts of uniform laws to overcome problems of distance, expense and time to have a contract terminated, where in fact a contract can be executed if the principle of good faith is applied.

Conclusion

Article 8 seeks to direct the courts or tribunals to consider the parties' actual intention. This is manifested in article 8(1) where it is stated 'statements made by and other conduct of a party are to be interpreted according to his intent'.[76] Failing this, the court will establish the objective intent of the parties pursuant to article 8(2) Such mandates do not pose any problems as seen from the above jurisprudence.

Article 8(3), however, does need further careful analysis. This article has recognised that to establish the intent of a party, certain tools or events must be used such as the negotiations, any practices the parties may have established, usage as well as subsequent conduct by the parties.[77] The aim of this article is to establish the state of mind or the belief of the parties in relation to the execution of their contractual obligations. An important point must be noted. The CISG and the common law are not 'poles apart'. The CISG does recognise that the contract is the crucial evidence which establishes the intent of the parties. However, if a contract needs interpreting, the common law and the CISG vary in techniques in relation to extrinsic evidence. Whereas under article 8(1) the CISG will admit subjective intent, the common law will not in all circumstances do so.

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[74]*Landgericht Heilbronn* 15.09.1997 3 KfH 653/93 (http://www.jura.uni-freiburg.de/iprl/cisg/urteile/text/562.htm).

[75]*Landgericht Zwickau 3. Kammer für Handelssachen* 19.03.1999 3HKO 67/98 (http://www.jura.uni-freiburg.de/iprl/cisg/urteile/text/519.htm).

[76]Article 8(1) CISG.

[77]Article 8(3) CSG.