

Project contracts

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PMG323

Lecture 2



Chapter

01

Rules of Interpretation



Illegality

A contract must not require one or both parties to do something prohibited by law. If it does, all or part of the contract will be unenforceable, depending on the facts. A contract to traffic in endangered species, for example, would be unenforceable between the parties, allowing either party to back out.

The same would be true of a contract to commit murder, fraud, or even a “tortious act” on a third party, including trespass, misrepresentation, defamation or contractual interference. Interestingly, amounts paid toward the performance of an illegal contract generally cannot be recovered in a civil lawsuit.

Against Public Policy

Even absent a specific rule or statute, a contract or a specific provision in a contract may be found by a court to be “against public policy.”

Depending on the circumstances, a court may invalidate all or part of the agreement or refuse to provide a remedy for breach of the agreement. Courts vary in how they define what is “against public policy,”

Against Public Policy

“An agreement is against public policy if it is injurious to the interests of the public, contravenes some established interest of society, violates some public statute, is against good morals, tends to interfere with the public welfare or safety, or is at war with the interests of society or in conflict with the morals of the time.

Chapter

01

The Parol Evidence Rule



What is it?

The parol evidence rule is a legal evidence rule that applies to written contracts. Written contracts are complete and final agreements outlining obligations between parties and enforceable by law. Specifically, the parol evidence definition is the evidence pertaining to an agreement that isn't included in the written contract.

What is it?

Parol evidence is, in simplest terms, evidence regarding discussions about what a contractual agreement should contain before entering into the contract. In other words, if you hire someone to paint your house, and in the process of negotiating the contract you also mention that you would like them to caulk around your windows, but the contract you subsequently enter into does not include anything about caulking, those discussions are parol evidence.

What is it?

The problem with parol evidence is that it is generally inadmissible at trial. So, if you were to sue that painter on a breach of contract theory, you would not be able to submit evidence that you had discussed having the caulking done if that provision did not make its way into the final contract. Why? The courts believe that parties must know and understand agreements they enter into, and will not hold parties liable for things that are omitted. Maybe it was left out because of a concern about the additional cost of performing the caulking work, maybe it was just an honest oversight. But, whatever the reason, it was not in the final contract, so it cannot be the cause of a breach of the contract. As such, it is not relevant, and is therefore inadmissible.

What is it?

The parol evidence rule provides that, where parties have a signed agreement, it is not generally permissible to adduce extrinsic evidence to:

- *show what the parties' intention was in entering that agreement*
- *contradict, vary or add to the terms of the written agreement—this extends to implied terms*
- *earlier drafts of the agreement between the parties*
- *preliminary agreements*

Expectations to the Parol Evidence Rule

In a perfect world, all contracts would be drafted with precision and foresight, clearly and comprehensively describing the parties' intentions and accounting for the unexpected. Reality being what it is, not every contract meets this standard. As a result, courts have created a number of important exceptions to the prohibition against evidence "outside of the four corners" of a contract, i.e., not found within the contract language itself.

The following exceptions to the Parol Evidence Rule are often important in contract litigation. As with other concepts of contract law, understanding them in advance can aid in preventative drafting to avoid disputes down the road.

Expectations to the Parol Evidence Rule

Ambiguity

Even where a contract recites that it contains the complete understanding of the parties and disclaims the existence of any other written or oral agreements or understandings, the Parol Evidence Rule will allow a party to introduce evidence outside of the contract to resolve an “ambiguity.”

Expectations to the Parol Evidence Rule

Ambiguity

An ambiguity is a term to which reasonable persons might assign different, to the extent possible, contracts should be drafted to avoid ambiguities by assigning clear definitions to important terms, precisely describing the obligations of each party and carefully avoiding grammatical and word choice errors.

In practice, contracts are rarely free from all ambiguity, and, in any dispute, ambiguities are often among the first points of attack of any good lawyer.

Expectations to the Parol Evidence Rule

Interpretation

Parol evidence may also be permitted by a court to “interpret” a contract in order to determine the parties’ actual intent, but it will be permitted only to explain missing terms, not to contradict terms clearly provided for in the contract. The “Rules of Interpretation” discussion below goes into more detail on when and how courts decide whether parol evidence, also called “extrinsic” evidence, should be considered to better understand the parties’ intent.

Expectations to the Parol Evidence Rule

Mistake

Parol evidence can also be introduced to show the absence of mutual assent necessary for the creation of a contract in the first place. To qualify under the exception and to invalidate a contract, a mistake must be “held by both parties” – i.e., both parties were mistaken about a fact material to the formation of the contract.

Expectations to the Parol Evidence Rule

Mistake

A common example cited in text books is where party A agrees to pay party B a certain amount to drill a well to supply fresh water. After drilling at the place identified by A, B encounters impenetrable rock 20 feet down. Since both parties were mistaken about the feasibility of drilling the well, a court might nullify the contract on grounds of mistake.

Expectations to the Parol Evidence Rule

Mistake

A mistake in business judgment or mistake of fact by one party, however, will not nullify a contract. For example, if one party gets a great deal on a rare coin because the other party did not know its value, he or she cannot later seek to invalidate the transaction. That is not what is meant by the term mistake in contract law. flag warranting guidance from counsel.

Expectations to the Parol Evidence Rule

Fraud, Duress

Like mistake, proof that a party entered into a contract under duress or in circumstances involving fraud by the other party is permitted as an exception to the Parol Evidence Rule in order to show the absence of voluntary mutual assent.

Expectations to the Parol Evidence Rule

Fraud, Duress

As one somewhat familiar example, a party stuck in a resort timeshare contract that has not turned out to be what the timeshare company represented might be able to invalidate the contract based on any documented fraudulent statements about things such as the likelihood of price appreciation, whether the timeshare contract was freely transferable, or even the degree to which the time share purchaser would enjoy booking priority over non–purchasing vacationers.

Expectations to the Parol Evidence Rule

Fraud, Duress

Similarly, an elderly person pressured into a timeshare contract following hours of high pressure sales tactics, including actions that made it difficult for the person to leave the sales presentation, might have a case for breaking the agreement due to claims of duress.

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Rules of Interpretation



Intent of the Parties

Most contract disputes involve questions of interpretation. Disputes can arise from different views of the same language or different ideas on how to deal with unanticipated gaps in the contract language. The goal of contract law is to determine what the parties intended at the time they entered into the agreement. This is done first and foremost by examining the contract language, and then, as necessary, the factual context.

Intent of the Parties

Drafting to minimize issues of interpretation is often challenging for non-lawyers. This is because of the inherent subtleties of written language and the non-lawyer's inexperience in dealing with contract disputes, litigation, judges, juries and other aspects of law that are learned only by lawyering.

Intent of the Parties

With that caveat, here are some generally accepted rules of interpretation:

Plain Meaning. Words are given their plain and normal meaning, except where the usage of a particular word has varied that meaning.

Technical Words. Technical words, or words customary to a particular industry, will be given their technical or special meanings when used in that context.

Intent of the Parties

Words will be given the meaning that seems to best reflect the intentions of the parties.

Consistency with General Purposes. Every part of a contract will be read in a manner that is consistent with its general purposes.

Surrounding Circumstances. As described above under the Parol Evidence Rule, the circumstances surrounding a contract's negotiation may sometimes be shown to aid in its interpretation.

Intent of the Parties

Words will be given the meaning that seems to best reflect the intentions of the parties.

Narrow or Restricted Meanings. Specific uses of a term or phrase in a contract may impose the same narrow or restricted meaning upon more general uses of the same term or phrase in a contract.

Lists. Depending on the context and specific language used, detailed lists of similar items can be read to exclude items that are not similar. Conversely, a general list can be read to include more than those listed.

Intent of the Parties

Words will be given the meaning that seems to best reflect the intentions of the parties.

Reasonableness. Where possible, a contract will be interpreted to render it reasonable rather than unreasonable.

Non-Drafting Party Bias. Given competing meanings, a court will generally favor the one urged by the non-drafting party.

Intent of the Parties

Courts use these rules to standardize how language will be interpreted in the event of a dispute. The goal is always to determine and give effect to the “intent of the parties.”

First and foremost then, parties to an agreement should attempt to summarize their intentions. As discussed below in Chapter Five, Common Contract Terms, the intent of the parties can be explained in the “recitals” or “whereas” clauses at the top of the agreement.

Intent of the Parties

Other drafting tips for clarifying the intent of the parties:

Avoid words, clauses, or sentences that may have more than one meaning. This includes being sensitive to the different outcomes that the use of “and” can have when “or” is the better choice and visa versa.

Place adverbs, adjectives, and other modifiers with precision and use appropriate grammatical techniques and punctuation to achieve clarity.

Intent of the Parties

Other drafting tips for clarifying the intent of the parties:

Lastly, use terms consistently. Contract drafting is not the same as creative writing – avoid using a variety of terms to express the same meanings and using variety of terms to express many meanings. Contracts need to be clear, not interesting.

Chapter

01

Implied Covenant of Good Faith and Fair Dealing



Here are some examples where the covenant might be successfully invoked:

Intentionally withholding critical information from the other party.

Intentionally performing poorly in order to extract concessions from the other party, particularly if done by a party in a much more powerful position.

Failing to provide reasonable cooperation necessary for the other party's performance or otherwise interfering with or thwarting the other party's performance.

Here are some examples where the covenant might be successfully invoked:

Seeking to terminate an agreement based on false or highly exaggerated claims of breach by the other party.

Willful conduct intended to cause commercial harm to the other party.

Chapter

01

Letter of intent & Oral contracts



Definition

“Letters of Intent,” or “LOIs,” are often used by parties during an exploratory phase of discussions. They express mutual intentions to move forward toward a contractual arrangement, but are, by their terms, nonbinding.

Here is a typical LOI introductory paragraph:

This letter of intent is for discussion purposes only and this letter of intent is not intended to be a binding agreement between the parties regarding the subject matter hereof. A binding agreement will not occur unless and until the parties have agreed upon the terms of the transaction and such terms are included in the appropriate definitive agreement that has been negotiated, approved, executed and delivered by each party hereto.

Importance

When done correctly, an LOI describes a mutual undertaking the parties are considering and further states that, in the event the parties are unable to negotiate an acceptable written contract, neither party is bound to take any further action. An LOI should include nothing that contradicts this except that each party might explicitly agree to protect and not misuse the other party's confidential information and one party might even agree to pay the other's pre-approved expenses.

Misuse of LOIs

The misuse of LOIs can be a problem in organizations lacking policy and procedural checks and balances to regulate the impatience or naiveté of individual team members. Be quietly alert for the possibility that talk of an LOI is a red flag for a potentially troubled commercial relationship.

Misuse of LOIs

An LOI is used as a morale booster to portray a deal as all-but-certain;

Whether or not spelled out in the LOI, work begins on some aspect(s) of the project;

Signing of the LOI distracts attention from timely finalizing a real agreement;

Work on the project evolves beyond the LOI's terms and problems are encountered; and

One of the parties decides to terminate the project and disappointments and uncertainties abound.

LOI best practices

Because of the tendency to misunderstand and misuse LOIs, they should be discouraged if those managing the process are inexperienced. Where business dynamics make avoidance of an LOI impossible

The following conditions should be observed:

The LOI should be drafted narrowly and precisely, with the help of a lawyer if possible.

The LOI should be drafted narrowly and precisely, with the help of a lawyer if possible.

Performance by either party should be forbidden except, where critical, within very limited and explicitly described boundaries and with costs clearly allocated.

The LOI should be quickly followed by a comprehensive agreement that the parties can sign as soon as they have decided how to go forward.

Oral agreements

Somewhat akin to LOIs, oral agreements between parties that are performable within a year and not for the purchase of real estate are generally valid and enforceable.

Despite their technical validity, it is best to avoid oral agreements. First, they are subject to obvious problems of proof. In the event of any type of dispute, how will the injured party present his or her case? Further, even the most casual arrangements can pose hidden or unforeseeable risks of non performance, inflated charges, and a range of potentially serious liabilities.

Oral agreements

Similarly, a simple agreement with a company to provide cleaning services for your offices can and should include indemnification provisions as well as specific warranties and representations around licenses, worker background checks, insurance, and protection of confidential information.

In summary, it is difficult to draw a line of materiality or significance below which oral agreements make sense, particularly since most responsible business persons have some form of standard agreement to offer as a starting point. In fact, resistance by any business person to a signed, written agreement should be a red flag prompting questions about insurance certificates, appropriate bonds or licenses, tax ID numbers, and other documentation.



Thank You