

**Contracts**  
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**Contract Terms**

**I. Construing and Interpreting Contracts**

A. **Purpose:** A court's primary concern is to ascertain and give effect to the parties' mutual intent at the time of contracting.

1. **Construction vs. Interpretation**

- a. Courts **interpret** to "ascertain ... meaning." R2 § 200.
- b. Courts **construe** to "determin[e] the legal effect of words or other conduct." R2 § 200 cmt. c.

2. **Objective vs. Subjective Intent:** Courts must give effect to the objective intent of the parties as it is expressed or apparent in their agreement, as opposed to the subjective intent of parties who failed to fully capture their intent when they formed the contract in question.

- ◆ Test is what a reasonable person in the position of the contracting parties understand the parties' intent to be. Recall *Lucy v. Zehmer*.

3. **Exceptions:**

- a. **R2 § 201(1):** If **both parties attach the same meaning** to a term or to the agreement, that meaning should prevail even if not objectively reasonable.
- b. **R2 § 201(2):** If one party attaches a particular meaning to a term or to the agreement, not knowing or having reason to know that the other party attached a different meaning, and the other party knows or had reason to know of the first party's meaning, the first party's meaning will prevail.

4. **No Contract:** While the law favors finding a contract, if each party attaches a different reasonable meaning to the contract, without knowing or having reason to know that the other party attaches a different meaning. There may be no contract. (Recall *Raffles v. Wichelhaus*.) R2 § 201(3).

B. **Key Concept: Integration**

1. If the parties to a written contract intend it to serve as a final and complete expression of their agreement, then the contract is integrated. An **integrated** agreement is “a writing or writings constituting a final expression of one or more terms of the agreement.”
2. **Written Contracts May Be Fully or Partially Integrated**
  - a. A **fully integrated** contract is one that is a final and complete expression of all the terms agreed upon between (or among) the parties.
  - b. A **partially integrated** contract is one that is a final and complete expression of all the terms contained in that agreement, but not a final and complete expression of all the terms agreed upon between [or among] the parties.
3. **Whether, and the Extent to Which, a Written Contract is Integrated is an Issue of Law**
  - a. **The Issue:** A writing cannot prove its own completeness.
  - b. Thus, while the court must determine whether the agreement is integrated before any parol evidence (other than that specified in UCC § 2-202(a), if Article 2 governs the contract) may be admitted for the trier of fact’s consideration, the trial court is free to rely on that parol evidence in reaching its threshold determination that the agreement is fully integrated, partially integrated, or not integrated.
    - ◆ Distinguish between a trial court **considering** evidence for the purpose of deciding a question of law and **admitting** evidence for the purpose of resolving a disputed question of fact.
  - c. **Extent of Negotiations:** Did the parties negotiate the term in question prior to signing the writing? If so, the party who signed the writing containing the term she now wants to dispute is going to fight an uphill battle.
  - d. **The Significance of “Merger” or “Integration” Clauses**
    - i. **Rule of Thumb:** To manifest their intention of creating a completely integrated agreement, parties often include a clause stating that there are no promises or agreements between the parties except those found in the writing.

- ii. **But, on the Other Thumb...:** The mere fact that a written contract contains a merger or integration provision does not guarantee full integration.
- 3. **Finding Lack of Integration:** For a court to determine that a written agreement is not fully integrated, it must decide that, as a matter of law,
  - a. the writing is facially incomplete and requires extrinsic evidence to clarify, explain, or give meaning to its terms, or
  - b. when viewed in light of the circumstances surrounding its execution, the writing does not appear to completely embody the terms relating to the subject matter of the writing.

C. **Key Concept: Ambiguity**

- 1. **“Ambiguity” Defined:** An agreement is **ambiguous** if its terms are **reasonably susceptible to more than one meaning**, taking into consideration circumstances present when the parties formed their agreement.
- 2. **What is Not Ambiguous?**
  - a. **General Rule:** If a written instrument “is so worded that it can be given a certain or definite legal meaning or interpretation, then it is not ambiguous and must be construed as a matter of law.”
  - b. An instrument is not ambiguous simply because
    - i. the parties offer conflicting interpretations of the same contract or contractual provision,
    - ii. it requires a careful reading,
    - iii. a fair reading of it does not comport with the desires of one party, or
    - iv. it contains obscure language, or language of doubtful meaning.
- 3. **Whether a Written Contract is Ambiguous is an Issue of Law**
  - a. **Threshold Issue of Law:** Whether a written agreement is ambiguous is a question of law for the court.
  - b. As with integration, while the court must determine whether the agreement is ambiguous before any parol evidence (other than that

specified in UCC § 2-202(a), if Article 2 governs the contract) may be admitted for the trier of fact's consideration, the trial court is free to rely on that parol evidence in reaching its threshold determination that the agreement is or is not ambiguous.

4. **Resolving Ambiguity**

- a. **Issue of Fact:** If the court finds that an agreement is ambiguous, then it is up to the trier of fact to resolve the ambiguity.
- b. If document is ambiguous, the judge should instruct the jury on the permissible means for resolving ambiguities and any relevant presumptions.
- c. The jury can then consider all admissible evidence to resolve the ambiguity.

D. **Primary Rules of Construction and Interpretation**

1. **Account for Surrounding Circumstances:** When construing and interpreting a contract, a court should take into account the circumstances surrounding the formation of the contract. In so doing, the court should place itself, as near as possible, in the exact situation of the parties when they executed the instrument, so as to determine their intentions, the objects to be accomplished, obligations created, time of performance, duration, mutuality, and other essential features.
  - a. Unless the parties clearly manifest a contrary intent, "surrounding circumstances" may include any prior course of dealing between the parties, as well as any operative usages of trade.
  - b. Courts should also construe all contracts in light of any applicable state or federal law or constitutional provision in effect when the parties formed their agreement.
2. **Afford Words and Phrases Their "Plain Meaning":** A court should give each word and phrase in a written agreement its plain, ordinary, commonplace meaning, unless doing so would cause a result that is contrary to the parties' clearly manifested intent or to law or public policy.
3. **Construe the Contract as a Whole:** A court should look at the instrument as a whole and determine the provision's meaning in the context of the entire agreement.
  - a. A court should avoid ascertaining the meaning of a contract by resort to solitary or fragmentary parts of the instrument. The language used in a single clause or sentence is not to control as

against the evident purpose and intention of the contracting parties as shown by the whole document.

- b. If a contract consists of more than one document, or if a contract incorporates another document by reference, then all documents comprising the contract or transaction should be read together to give full effect to the intent of the parties.

4. **Afford Each Provision Meaning and Purpose:** The law generally presumes that parties who go to the effort to consummate a written contract intend for each word and provision of the contract to have meaning and purpose. Therefore,

- a. a court should construe a contract, if possible, so that no word or provision is rendered “repugnant, senseless, ineffective, meaningless, or incapable of being carried out in the overall context of the transaction consistently with all of the other provisions” of the contract; or, put another way,
- b. a court should, if possible, give effect “to all words, clauses and provisions of the instrument, if they are not inconsistent with each other or with the general intent of the whole instrument when taken as an entirety, unless the court is satisfied that no particular effect was intended to be given a particular word or phrase.”
- c. A court should not construe a word or provision to be nullified or stricken by some other word or provision unless such a result is fairly inescapable.

5. **Require a Fair and Reasonable Construction:** A court should give the words of an instrument a reasonable construction, where that is possible, rather than an unreasonable one, and should avoid constructions that give words a meaning they will not bear. A court should avoid a construction leading to an absurd, harsh, or unreasonable result – including one that would result in forfeiture – unless the terms are express and lend themselves to no other reasonable interpretation.

6. **Avoid Illegality:** If a contract or term is susceptible to two reasonable constructions, one of which comports with statutory law, regulation, common law, or public policy and one of which does not, the court should construe the contract or term in such a way as to make it legal.

7. **Avoid Implied Terms**

- a. Implied terms are permitted when necessary to effectuate the intent of the parties as evidenced by the agreement as a whole. Examples of this type of case include implying that
  - i. a contract which sets no time for performance must be performed within a “reasonable” time, considering the condition and circumstances of the parties, and may not be terminated without reasonable notice to the party whose performance is subject to the “reasonable time” requirement;
  - ii. “in the absence of some provision in the contract authorizing termination or cancellation, every contract is presumed irrevocable”; and
  - iii. “[w]here a contract is performable on the occurrence of a future event, there is an implied agreement that neither party will place any obstacle in the way of the happening of such event, and where a party is himself the cause of the failure he cannot rely on such condition to defeat his liability.”
- b. Implied terms may also arise by operation of law, such as the implied warranty of habitability, the implied duty of good faith and fair dealing, and the implied warranties of title, merchantability, and fitness for a particular purpose set forth in the UCC.

8. **Consider the Parties’ Own “Practical Construction”:** Courts should consider the interpretation placed upon the instrument by the parties (and their successors) in seeking the intent of the parties.

E. **Secondary Rules of Construction and Interpretation:** In addition to, or sometimes in conjunction with, the primary rules, courts also rely from time to time on a number of “secondary” rules. These secondary rules are easier both to define and to apply than the foregoing, more general principles. However, a court should apply the following secondary rules only if two or more provisions of a contract, or two or more reasonable readings of the provisions of a contract, remain uncertain after the court has applied the foregoing primary rules.

1. ***Contra Proferentem* (Construe Against the Drafting Party):** Ambiguous contract terms are construed most strongly against the party responsible for drafting them.

2. ***Noscitur a Sociis (Take Words in Their Immediate Context):*** The meaning of a word may be affected by its immediate context. Therefore, a court should construe a word in the context of the terms immediately preceding and following it.
  3. ***Ejusdem Generis (Limit Generalities to Things of the Same Genre as Those Specified):*** When an enumeration of specific things is accompanied by some more general word or phrase, then the general word or phrase will usually be construed to refer only to things of the same general nature or class as those specifically enumerated.
  4. ***Expressio Unius est Exclusio Alterius (Exclude Similar Things Not Specified):*** When an enumeration of specific things is *not* followed by some more general word or phrase, then things of the same kind or species as those specifically enumerated are deemed to be excluded.
  5. **Favor Specific Terms Over General Terms:** If a general provision and a specific provision in the same contract conflict or are inconsistent, the specific provision controls or qualifies the meaning of the general provision, unless the parties clearly manifest a contrary intent.
  6. **Favor Specifically Negotiated Terms Over Boilerplate:** If a negotiated provision controls or qualifies the meaning of an inconsistent non-negotiated provision in the same contract, unless the parties clearly manifest a contrary intent.
  7. **Favor Words Over Numbers or Symbols**  
When there is a variance between unambiguous written words and numbers or symbols, the written words control.
  8. **Favor Handwriting to Typing and Typing to Printing:** Except where the parties clearly manifest a contrary intent, handwritten contract provisions are favored when they conflict with or alter typewritten or printed provisions, and typewritten provisions are favored when they conflict with or alter printed provisions.
- F. **The Common Law Parol Evidence Rule:** A fully integrated, unambiguous written agreement discharges all prior or contemporaneous oral agreements and all prior written agreements between the parties regarding the same transaction as the fully integrated, unambiguous written agreement.
1. The parol evidence rule is a rule of substantive law. Nonetheless, it has **evidentiary consequences**. A court should not admit evidence regarding
    - a. prior or contemporaneous oral agreements or prior written agreements,

- b. offered to alter, add to, or contradict
  - c. the terms of a fully integrated,
  - d. unambiguous,
  - e. written agreement.
2. Thus, subject to one or more exception(s) discussed below, and unless the contract is governed by UCC Article 2,
- a. if the writing is both **fully integrated and unambiguous**, then parol evidence is inadmissible;
  - b. if the writing is **fully integrated but not unambiguous**, then parol evidence is admissible to explain the terms of the contract, but not to alter or contradict any unambiguous term;
  - c. if the writing is **not fully integrated but is unambiguous**, then parol evidence is admissible to explain or supplements the terms of the contract, but not to alter or contradict any unambiguous, integrated term;
  - d. if the writing is **not fully integrated and not unambiguous**, then parol evidence is admissible for any purpose except to alter or contradict an unambiguous, integrated term;
  - e. if the writing is **unintegrated and not unambiguous**, then parol evidence is admissible for any purpose.

3. **Types of Extrinsic Evidence**

- a. **Interpretive Evidence:** Extrinsic evidence offered to **prove the intent of the contracting parties** at the time they executed the written agreement. Such evidence is generally “exempt” from the parol evidence rule; and, therefore, the trier of fact is free to consider it.
- b. **Suppletive Evidence:** Extrinsic evidence offered to **add to, subtract from, or otherwise modify** the terms of the written agreement. Such evidence is subject to the parol evidence rule; and, therefore, the trier of fact may not consider it until the trial court first finds that the written agreement is not fully integrated, is not unambiguous, or both.

4. **Subsequent Agreements:** The parol evidence rule bars neither evidence regarding nor enforcement of agreements made by the parties after they executed the written agreement that is subject to the parol evidence rule.
5. **The Parol Evidence Rule and Statutes of Frauds:** A statute of frauds (or an agreement between the parties that all agreements must be in writing) may bar the enforcement of a subsequent oral agreement, but should not bar its admissibility into evidence.

G. **The Article 2 Parol Evidence Rule:** Terms set forth in

1. a **writing** that
  - a. the parties **intended**
  - b. to be a **final expression** of their agreement
  - c. with respect to **such terms as are included** therein
2. may not be **contradicted** by evidence of any prior agreement or of a contemporaneous oral agreement,
3. but may be **explained** or **supplemented**
  - a. by evidence of a relevant **course of dealing, usage of trade, or course of performance**, § 1-303,
  - b. to the extent not clearly negated or varied by the terms of the written agreement, any relevant **UCC gap fillers**, and
  - c. *if the written agreement of the parties is not fully integrated*, by evidence of **consistent additional terms**. § 2-202.
4. **UCC Hierarchy** [*See* §§ 1-303(e) & 2-202]:
  - a. **Express Terms** trump
  - b. **Course of Performance** trumps
  - c. **Course of Dealing** trumps
  - d. **Usage of Trade** trumps
  - e. **Terms Implied as a Matter of Law** trump
  - f. **Consistent Additional Terms**.

5. **Discarded Presumptions:** The UCC specifically **discards** the following common law presumptions:

- a. a written agreement is presumed to be fully integrated, § 2-202 cmt. 1(a);
- b. the parties intended that the terms of their agreement be given their “plain” meaning, rather than some other meaning that might be discovered by looking outside the four corners of the document to the circumstances surrounding the contract’s formation, § 2-202 cmt. 1(b); and
- c. a contract must be ambiguous before the court may admit evidence of, *inter alia*, course of performance, course of dealing, or usage of trade, § 2-202 cmt. 1(c).

6. **Evidentiary Consequences of Integration**

- a. If the writing is **fully integrated**, then § 2-202 will only permit the court to admit evidence of course of performance, course of dealing, and trade usages in order to explain or supplement the terms of the writing itself.
- b. If the writing is **partially integrated**, then § 2-202 will also allow the court to admit evidence of consistent additional terms.
- c. **“Additional” vs. “Inconsistent” Terms:** Even in those instances where § 2-202 permits the court to admit evidence of prior or contemporaneous terms or agreements, it may only do so if the evidence reflects terms that are **additional** to – as distinct from **inconsistent** with – the integrated terms of the written contract.
- d. **“Prior or Contemporaneous” vs. Subsequent:** § 2-202 only bars consideration of prior or contemporaneous agreements; it does not bar the consideration of subsequent agreements, even if they modify the terms of the integrated writing.
- e. Evidence of **trade usage, course of dealing, and course of performance** may be considered, even if the writing is fully integrated, as long as the express terms of the writing do not “carefully negate” a particular trade usage, course of dealing, and course of performance.

## H. Exceptions

1. **Fraud:** Parol evidence is admissible to show that one party has been fraudulently induced into a contract.
2. **Negligent Misrepresentation:** Parol evidence is admissible to show that one party has been induced into a contract by negligent misrepresentation.
3. **Duress or Undue Influence:** Parol evidence is admissible to show that one party has been induced into a contract by threats to her physical or, in limited circumstances, economic well-being.
4. **Mutual Mistake:** Parol evidence is admissible to show that one or both parties were induced into a contract by a material mistake of fact.
5. **Illegal Provisions or Agreements:** Parol evidence is admissible to prove that a contract provision is illegal or that the contract was illegally formed.
6. **Non-Existent, or “Sham,” Contract:** Parol evidence is always competent to show the non-existence of a contract. Parol evidence is admissible to show that despite the existence of a written instrument purporting on its face to be a contract, the parties never intended it to be such or that the purported contract is a “sham” agreement. Parol evidence is used to protect the parties’ intent.
7. **Evidence Pertinent to Consideration**
  - a. **Lack of Consideration:** Parol evidence is admissible to prove that there was never any consideration to justify enforcing the contract.
  - b. **Failure of Consideration:** Parol evidence is admissible to prove that the consideration contemplated by the parties failed before the contract was fully performed.
  - c. **True Consideration:** Parol evidence is admissible to prove that what the parties actually agreed to exchange differs from what is recited in the written agreement.
8. **Scrivener’s Error:** Parol evidence is admissible to prove a typographical error or handwriting error – due either to a mistake or a failure to accurately transcribe.
9. **Lost or Destroyed Contract:** If the writing has disappeared, parol evidence is admissible to show what was in the writing.
10. **Material Alteration:** Parol evidence is admissible to prove that a writing was altered, without mutual consent, after it was executed.

11. **Condition Precedent:** Parol evidence is admissible to prove that a party's obligation under the contract was conditioned on some occurrence or non-occurrence and that the occurrence or non-occurrence never transpired.
12. **Subsequent Acts or Agreements:** The parol evidence rule draws a line in the sand when the contract is signed and trumps any prior agreements. However, it does not prevent subsequent acts or agreements, nor does it prevent a party from offering evidence of subsequent acts or agreements.

## I. **Parol Evidence Under the CISG**

1. **No Parol Evidence Rule:** Article 11 provides that “[a] contract of sale need not be concluded in or evidenced by writing” and “may be proved by any means, including witnesses.”
2. **Interpretive Guidance**
  - a. **Subjective Intent:** Like § 201(2) of the *Restatement (Second) of Contracts*, the CISG gives effect to the subjective intent of one party to the contract if the other party knew or should have known the first party's intent. CISG art. 8(1).
    - ◆ Unlike § 201(2), the CISG does not explicitly require that, in order to bind party X to party Y's subjective intent, party Y must be actually and constructively unaware of party X's intent. However, it seems fair to imply that requirement in Article 8(1).
  - b. **Objective Intent:** If neither party knew or should have known the other party's subjective intent (or if both parties knew or should have known the others' intent and also know their own intent to be different), statements made by and other conduct of a party are to be interpreted using a “reasonable person” test. CISG art. 8(2).
3. **Relevant Circumstances:** Article 8(3) provides that, in determining contractual intent, courts should give “due consideration” to all relevant circumstances of the case including
  - a. the **negotiations**,
  - b. any **practices which the parties have established** between themselves,
  - c. **usages** and
  - d. **subsequent conduct** of the parties.

## II. Implied Terms

A. **The Basic Idea:** The agreement that the parties have reached or the writing they have executed does not necessarily contain all terms relevant to the contract; therefore, the law will imply certain terms to make the contract “complete.”

1. **Terms Implied by Law:** Legal consequences of the parties’ decision to contract with one another (*e.g.*, good faith, UCC “gap fillers”).
2. **Terms Implied by Fact:** Natural consequences of the parties’ words, acts, and relationship (*e.g.*, “best efforts”).
3. **Freedom of Contract:** Parties can avoid most implied terms by specifically waiving or disclaiming them in the agreement (often explicitly providing some express alternative to the implied term), but there are exceptions, such as the duty of good faith. One cannot contract out of the duty of good faith.
  - a. **Severability Clause:** A clause that expresses the parties’ intent to be bound by all enforceable parts of the agreement, notwithstanding a later adjudication that some part of the agreement is not enforceable.
  - b. **Savings Clause:** A clause that says, in essence, “If we screwed up, please make whatever adjustments are necessary.”

### B. Good Faith

1. **Common Law:** “Every contract imposes upon each party a duty of good faith and fair dealing in its **performance** and **enforcement**.” R2 § 205.
  - ◆ R2 § 205 cmt. a refers to the UCC’s definitions and emphasizes faithfulness to an agreed common purpose and the other party’s justified expectations.
2. **UCC Approaches**
  - a. UCC § 1-304: Every contract requires the parties to **perform** and **enforce** it in good faith.
  - b. UCC § 1-201(b)(20): “Good faith” means “honesty in fact and the observance of reasonable commercial standards of fair dealing.”
    - ◆ *But see, e.g.*, UTAH CODE ANN. § 70A-1a-201(2)(t) (West Supp. 2008) (requiring only “honesty in fact”).

- c. A court may ascertain reasonable commercial standards of fair dealing (objective) by considering course of dealing, course of performance, and trade usage.

**C. Reasonable/Best Efforts**

1. **Generally:** A party granted an exclusive right to benefit another impliedly promises to use “reasonable efforts” on the other’s behalf.
2. **UCC § 2-306(2):** “A lawful agreement by either the seller or the buyer for exclusive dealing in the kind of goods concerned imposes *unless otherwise agreed* an obligation by the seller to use best efforts to supply the goods [or] by buyer to use best efforts to promote their sale.”

**D. “Satisfaction” Contract:** A contract that requires one party to perform to the other’s satisfaction. Courts generally apply one of two tests:

1. **Objective satisfaction:** Did the defendant perform to a reasonable person’s satisfaction (who was in the plaintiff’s position)?
  - a. This test echoes the “reasonable” or “best” efforts test.
  - b. Courts generally apply this test where the issue is functionality rather than aesthetics or personal sensibilities.
2. **Subjective satisfaction:** Did the defendant perform to the plaintiff’s personal satisfaction?
  - a. The plaintiff’s duty of good faith in performing and enforcing the contract tempers her ability to refuse to be satisfied for anything other than genuine reasons.
  - b. Courts generally apply this test where the issue is aesthetics or personal sensibilities rather than functionality.
  - c. A party wanting the right to be subjectively dissatisfied should make that clear at the outset.

**E. The “Bottom Line”:** Inherent in a contract where there is an ability to exercise some form of discretionary power, a duty exists to act in good faith and maintain the notion of fair dealing. And, while the parties cannot abrogate their duty of good faith by the terms of their agreement, they may expressly permit certain conduct that might otherwise violate the duty.