Are Verbal Contracts Valid? A Comparative Analysis Between Common Law, Civil Law and the CISG

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Introduction

Comparative contract law is a fascinating field of scholarly discussion, as it explores numerous challenges pertaining to interpretation and application of various rules in competing jurisdictions. This article in particular addresses the validity of verbal contracts in common law, civil law and international commercial law.

Common Law

What is the Parol Evidence Rule and Why Does it Exist?

In the common law world, verbal contracts are subject to the Parol Evidence Rule, which is one of the oldest rules of evidence. Its effect is to prohibit testimony that is used to contradict, vary, add to or subtract from the terms of a valid written contractual document, which is intended by the parties to be their final agreement.¹ In practice, the type of testimony prohibited by the rule refers to verbal statements or agreements and conduct either prior to or subsequent to the conclusion of the written contract.

The leading justifications for the emergence of the rule include the legal uncertainty stemming from a person’s memory, which verbal agreements and statements rely upon, and the risk of falsehood, fraud or perjury.² Further justifications are advanced under two approaches. The ‘consent approach’ recognises that parties intend to make the writing a manifestation of their final agreement that is superior to any prior agreements.³ The ‘quality of evidence approach’ recognises that a written agreement that has been carefully drafted to reflect the parties’ intentions should be given higher consideration and more weight than any other agreements or understandings between the parties.⁴ This is to ensure that weaker evidence cannot alter or supersede the stronger written evidence.⁵

Application of the Parol Evidence Rule to Contract Interpretation


⁴ Ibid 238.

The parol evidence rule is a feature of contract interpretation, as it must be determined whether a piece of writing constitutes a partial or complete statement of the parties’ agreement. In the common law world, this determination is made in such a way that promotes certainty and predictability in performance of the contract. This determination seeks to ascertain the meaning of the language of the contract and therefore excludes evidence of pre-contractual negotiations used to interpret the contract. It is here where a divergence is seen between the common law and civilian theoretical approaches to contract formation and thus construction. The parol evidence rule was described by Justice Blackburn in the English case Smith v Hughes. He stated, ‘whatever a man’s real intention may be, if he so conducts himself that a reasonable man would believe he was assenting to the terms proposed by the other party, and that party enters into the contract on the basis of that belief, the man would be equally bound by the contract as if he had intended to agree to its terms.’

This classical theory of contract law is based on an understanding that a ‘contract is formed for a homogenous product concluded between two strangers who transact in a perfect spot market.’ This is important in the context of the parol evidence rule because if a contract’s terms are ambiguous or unclear, thus making subjective intent difficult to ascertain, then the general rule is that the parties’ objective intention will be ascertained by interpreting the language and actual wording of the contract and prohibiting the use of extrinsic material to aid that interpretation.

Many common law jurisdictions have, however, introduced numerous exceptions to the rule. For instance, in Australia, Judge Mason in the notable case Codelfa Construction Pty Ltd v State Rail Authority of NSW highlighted, "the true rule is that evidence of surrounding circumstances is admissible to assist in the interpretation of the contract if the language is ambiguous or susceptible to more than one meaning." Evidence of surrounding circumstances however is not admissible to contradict the language of the contract if it has a plain and clear meaning and so the subjective intentions of the parties are displaced by the contract itself. The rule is practically unknown in civilian law and it is debatable whether this principle should continue to operate given its growing inability to reflect contemporary international commercial realities.

**Parol Evidence in Civilian Law**

While the rule is universally recognised, it enjoys acceptance in its true form only in the common law tradition. While common law classifies parol evidence as a rule of substantive law, civilian law classifies any equivalent as a rule of evidence, which is mainly procedural rather than substantive. Civil or commercial codes usually contain the presumption that a written text is the parties’ final agreement and should be honoured on the basis of pacta sunt servanda and the principle of good faith.

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7 Ibid.
10 Ibid.
12 Codelfa Construction Pty Ltd v State Rail Authority of NSW (1982) 149 CLR, 352.
14 Ibid 259.
15 Ibid 258-259.
Civilian codes do allow for some restrictions on parol evidence in certain circumstances and this may also depend on the particular jurisdiction.

For instance, the French Civil Code prohibits parol evidence in the form of proof by witnesses if the object of a contract exceeds a certain amount of money.16 The Spanish Civil Code contains a similar provision in article 51.17 In Germany, principles of good faith and custom may be used to interpret contracts.18 Written agreements are presumed to be valid and accurate, however, parol evidence may be accepted to prove the parties’ intentions and interpret the contract.19

Interestingly, it is only the Italian Civil Code that incorporates a rule comparable to the common law parol evidence rule. It states that ‘proof by witnesses of prior or contemporary agreements of a written document are not permitted to establish stipulations which have been added or are contrary to the contents of a document.’20 Article 2724 however goes on to allow such evidence if the writing’s legitimacy is in doubt.21

As a general rule, however, civilian law is largely uniform in its acceptance of extrinsic evidence such as verbal agreements to prove parties’ intentions in contracting.22 The absence of formal requirements in everyday transactions is common in civil jurisdictions and if any terms are considered to be ambiguous, then they are to be construed in accordance with the parties’ subjective intentions and may take into account customs and usages.23

Parol Evidence and the CISG – Commercial Realities

This article has thus far discussed the parol evidence rule and its application in common and civilian legal traditions. The rule has, however, become susceptible to criticisms pertaining to its archaic nature and that its application no longer reflects contemporary commercial practice. Common law treats the contract as a final bargain concluded as a result of a string of negotiations.24 While such an approach may enjoy commercial expediency in a common law domestic setting, internationalised business and trade reflects a different reality.

Contracts negotiated between international parties have become recognised as ‘evolving instruments of bargain and exchange’ that can change and adapt to various contextual influences such as economics, rather than representing a rigid final product.25 A conflict therefore presents itself between contracting parties from different jurisdictions as to the rules of interpreting contracts and in particular, for the purposes of this article, whether parol evidence can be admitted to assist with contract interpretation.

In order to overcome the challenges posed by the application of inconsistent rules across the different legal traditions and States, the CISG26 was adopted to create a uniform international sales framework

16 Civil Code (France) art 1341.
17 Código Civil (Spain) art 51.
18 Bürgerliches Gesetzbuch (BGB) (Germany) arts 133, 157, 242.
20 Codice Civile (Italy) art 2722.
21 Ibid art 2724.
23 Alberto Luis Zuppi, ‘The Parol Evidence Rule: A Comparative Study of the Common Law, the Civil Law Tradition and Lex Mercatoria’ Vol 35 Georgia Journal of International and Comparative Law (2007) 263; Civil Code (France) art 1159; Codice Civile (Italy) art 1368; Código Civil (Spain) art 1287.
24 Ibid 320.
25 Ibid.
in order to facilitate international trade and commerce. With 91 contracting parties, the CISG accounts for a significant proportion of international commerce.

The CISG Advisory Council emphasized in their Opinion that the CISG does not incorporate the parol evidence rule. Article 11 of the CISG states that ‘a contract of sale need not be concluded in or evidenced by writing and is not subject to any other requirement as to form. It may be proved by any means, including witnesses.’ The commentary of the drafting Conference explained that this provision was incorporated due to the fact that an overwhelming number of ‘international sales agreements are concluded through modern means of communication, which may not always include writing.’ In an increasingly globalized world where commerce and communication have become largely electronic and subject to technological advancement, such as the emergence of e-commerce, it is conceivable why writing alone can no longer be deemed as a holistic or accurate expression of contracting parties’ intentions.

Consequently, article 8 of the CISG states that ‘in determining the [subjective] intent of a party, due consideration is to be given to all relevant circumstances of the case, including negotiations, practices and usages, and any subsequent conduct of the parties.’ In this manner, it appears that the CISG has followed the civil tradition in interpreting contracts according to parties’ subjective intent, which can be proven using extraneous and indeed parol evidence.

Concluding Remarks

This article has compared the treatment of parol evidence in contract interpretation within the common law and civilian traditions, as well as under the CISG. The common law’s heavy dependence upon the written agreement seeks to achieve objectives of legal certainty and predictability. These objectives, however, are achieved at the expense of the parties’ true intentions, which this article suggests is contrary to the well-established principle of freedom of contract, which is integral to the merchant world. Viewing contracts as a final and conclusive agreement incapable of being altered to reflect parties’ wishes, as expressed through verbal and other communications, runs contrary to the contemporary realities of international trade and commerce.

International contracts are increasingly treated as bargains and exchanges that are flexible in light of economic and other factors. Article 8 of the CISG seems to find a balance between common law

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considerations of certainty and predictability, and the civil law preference for ascertaining the true subjective intent behind a bargain by allowing all relevant evidence to be admitted.\textsuperscript{33}