



University of St.Gallen



University of St.Gallen (HSG)

Contracts II

Prof. Dr. M. Müller-Chen, February 12, 2024

*“From insight
to impact”* 



A. The Pre-Contractual Phase



Obligations during Negotiations

- Must act in good faith
- Must not mislead or trick the counterparty
- In principle no obligation to form the contract!

Violation of these obligations can lead to liability for damage (**culpa in contrahendo**) if breaching party is at fault

Example: A negotiates with its competitor B just to get access to sales numbers; they have no intention of actually forming a contract.



Structuring the Pre-contractual Phase

Contract			
Non-disclosure agreement	Letter of intent	Memorandum of understanding	Heads of agreement

In case something goes wrong – you will need documents!



B. Formation of Contracts



Expressions of Intent

Art. 1

¹ The conclusion of a contract requires a mutual expression of intent by the parties.

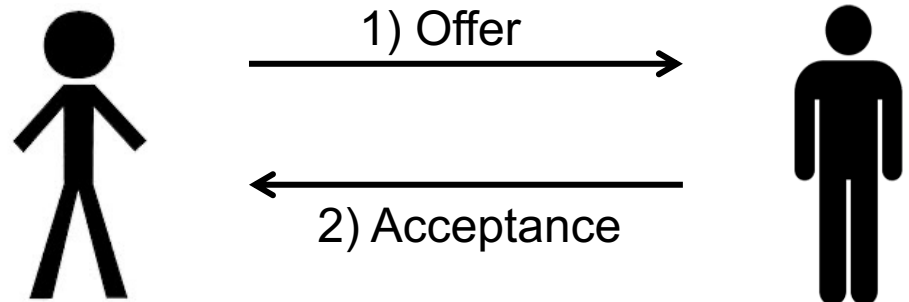
² The expression of intent may be express or implied.

«expression of intent»

- The will to act, (legally) bind oneself and to declare one's intent

«communication of intent»

- Explicitly
- Implicitly





Offer

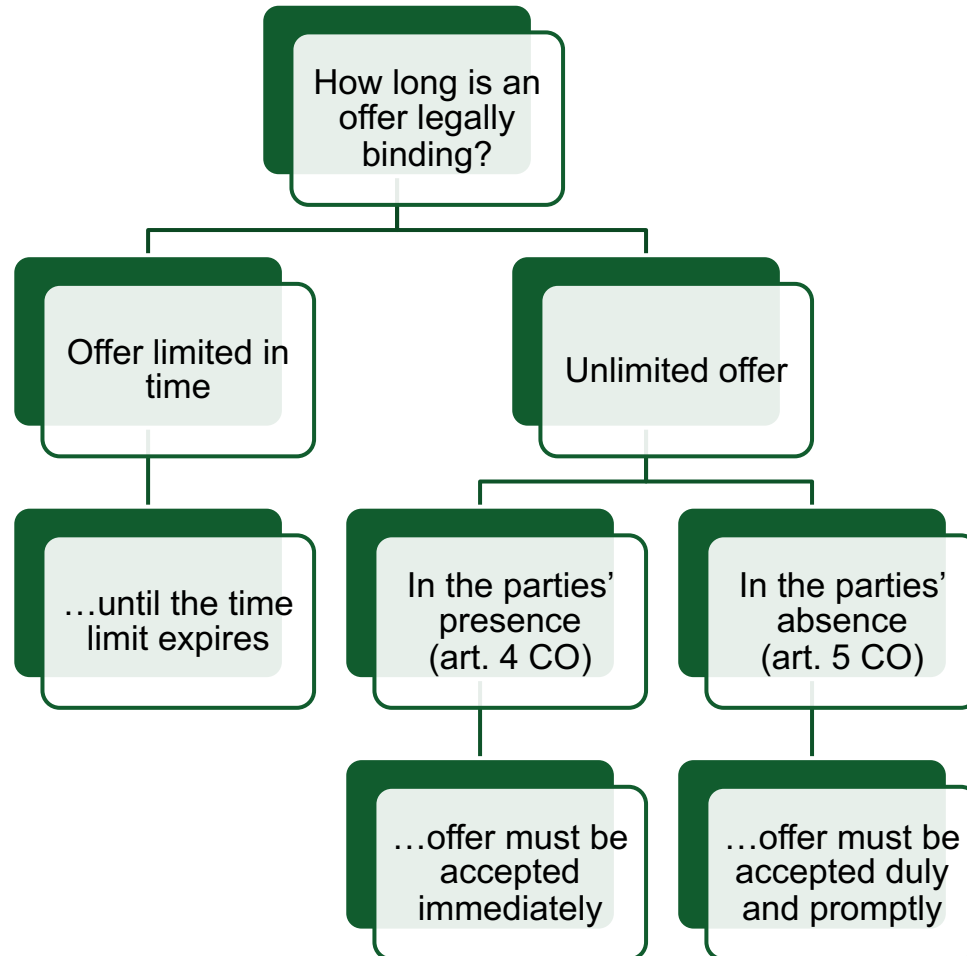
= the first expression of intent

- It must contain all the **essential characteristics** of the future contract that allow to determine:
 - Parties & type of contract
 - Performance and counter-performance
- An offer is **binding** (see slide 8 as to how long), i.e., in general **unchangeable** and **irrevocable** (exceptions see slide 12)
- An offer must be directed towards the formation of a contract



Offer

Example: Bill offers to pay 1000 CHF for your car. You accept this offer two months later. Was a contract formed?





Offer

The binding effect of an offer can be excluded by:

Declaration

- Art. 7 para. 1 CO
- Clauses such as «without obligation», «while stock lasts» etc.

Law

- Art. 6 and 7 para. 2 CO
- Sending of unsolicited goods, of price lists, catalogues etc.

Nature of the specific circumstances

- Clearance sale
- Offering goods to the general public



Acceptance

«saying yes to the offer»

- Identical to the offer's content in relation to the (objectively or subjectively) *essential* characteristics of the future contract.
- Differences about objectively and subjectively *non-essential* terms do not hinder the formation of the contract (art. 2 CO).
- Explicitly or implicitly, but in general not by remaining silent / doing nothing (art. 6 CO)

Example I: Darcy offers to buy Emma's car for 10'000 CHF. Emma says she accepts his offer to buy her car for 10'500 CHF. Was a contract formed?



.....

Example II: Darcy offers to buy Emma's car for 10'000 CHF in cash. Emma agrees, but would like him to transfer the money to her bank account instead. Was a contract formed?



.....



Offer and acceptance must be received by other party («mailbox theory»)

- The expression of intent must have entered the recipient's domain
- It is sufficient that the recipient *could have taken notice*
- Decisive: Recipient can independently access the place of receipt (e.g. mailbox, reception desk, e-mail server, mobile phone etc.)
- Ignoring the expression of intent does not preclude reception:

Example: Audrey refuses to accept her mail because she is afraid that the postman may deliver a bill she doesn't want to pay.



Withdrawal of Offer and Acceptance

Only possible if (art. 9 CO):

- the withdrawal reaches the recipient before or at the same time as the offer or acceptance itself, or
- where it arrives subsequently, if it is communicated to the recipient before he becomes aware of the offer or acceptance

Example: Martha writes a letter to Vinissa Ltd. accepting their offer of 100 CHF for two bottles of wine. She posts the letter on Wednesday, and it arrives on Thursday at 1 p.m. Was this acceptance withdrawn on time if:

- a) she calls Vinissa Ltd. on Thursday morning and withdraws her acceptance?
- b) she leaves a message on their answering machine on Wednesday night but the cleaning lady accidentally deletes the message on Thursday morning?
- c) She calls on Thursday 4 p.m. before somebody at Vinissa read the letter?



- a)
- b)
- c)



Formation of a Contract in a Nutshell

A contract has been formed timewise when the offeror receives the acceptance.

The parties have to be in agreement, i.e. offer and acceptance have to be congruent contentwise.

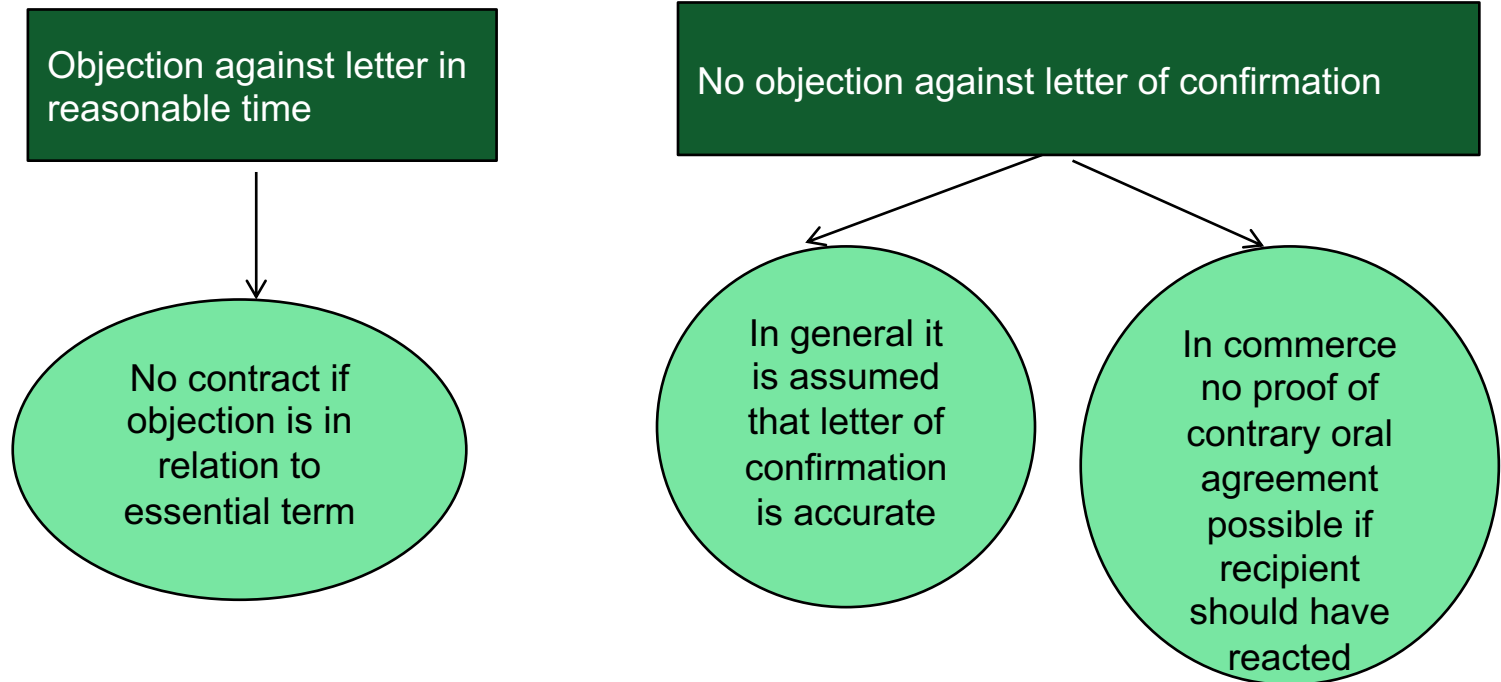
If there is no consensus, the parties are in dissent. No contract has been formed.

- **Open dissent:** The parties know that they disagree.
- **Hidden dissent:** The parties falsely assume that they are in agreement.



Commercial Letter of Confirmation

- It is a written acknowledgement of an oral agreement;
- It serves as evidence of the contract.
- If there is a discrepancy between agreement and letter of confirmation:





Quiz – Question 1

Andrew's fruit delivery business isn't going so well. To increase revenue, he chooses to send crates of fruit directly to new customers together with a short letter introducing his business and an invoice without prior solicitation.

Benjamin, one of the recipients of such a crate, refuses payment but eats the fruit and sends the crate back to Andrew. Andrew demands performance of payment.

Is Benjamin required to pay?



Quiz – Question 2

Sunny offers to sell Bobby **flour** for his bakery. Bobby, who likes to decorate his shop with lots of flowers, and is constantly busy, thinks Sunny wants to sell **flowers** and puts in an order. Initially confused, Sunny assumes that Bobby wants flour.

Has a contract been formed?



Quiz – Question 3

Charlie sends Nora an email, asking if she'd like to buy his last cake. Nora only sees the email after she returns from holiday two days later and quickly rushes to send her acceptance. In the meantime, Charlie ate the cake.

Was a contract formed?



Quiz – Question 4

Marco wants to buy a new deck chair. In the store he signs an order form but leaves the “method of payment” section blank, as he forgot to bring his wallet and can’t remember any of his credit card or bank account numbers.

Eager to make the sale, the sales rep nevertheless processes his order; the chair is subsequently delivered.

Marco breaks the deck chair after half a day. The store refuses to exchange or repair the chair; Marco is angry and refuses to pay. He argues that no contract was formed since he never filled out the “method of payment”.

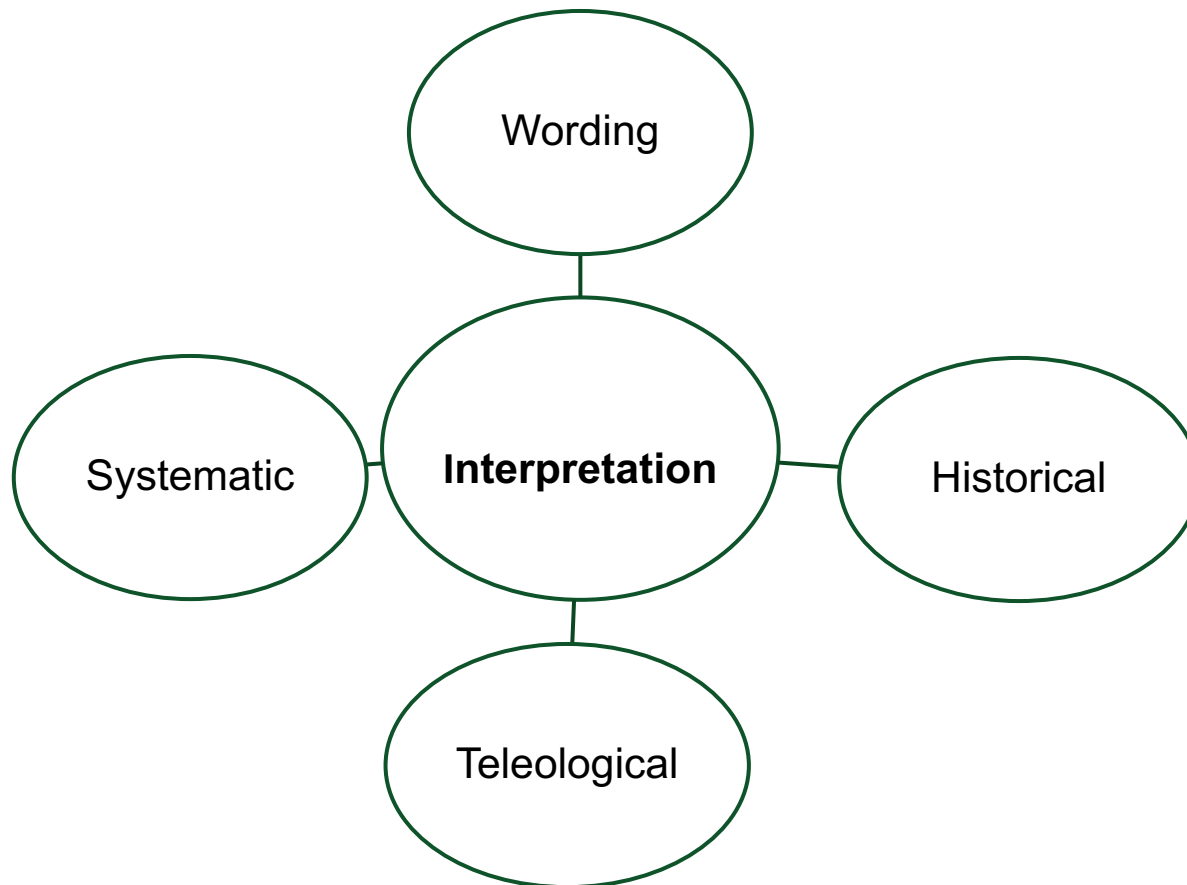
Does Marco have to pay?



C. Interpreting and Supplementing Contracts



Principles of Interpretation



- Contracts can be supplemented if there is a gap.



D. Validity of Contracts



Form of the Contract

- Principle of freedom of form, however either the law (art. 11 CO) or the parties (art. 16 CO) may require a certain form.
- Types of form requirements found in the law:
 - Simple written form (art. 13-15 CO): declaration in written form and signature of the party that commits itself. This can be done by hand or with an authenticated electronic signature combined with an authenticated time stamp (art. 14 para. 2bis CO)

Example: an apprenticeship contract (art. 344a CO)

- Qualified written form = simple written form + extra element

Example: handwritten will (art. 505 para. 1 CC)

- Public deed (done by a notary public)

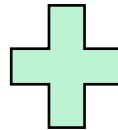
Example: sales contract of immovable property (art. 216 CO)



Scope of the Form Requirement

Objectively essential
terms

E.G. Sale of land: Parties, land,
price



Subjectively essential
terms

... If they influence the ratio of the
performance and counter-
performance (e.g. commission of
the realtor)



Parties Require a Form

- Parties agree upon a form -> art. 16 CO contains two important presumptions:
 - (1) Contract is only valid when it complies with the form
 - (2) Presumption of simple written form
- Form free revocation of agreement to use form is ok (unless contract states otherwise)



Infringement of Form

- Legal consequence of an infringement of form requirements:
 - ✓ Nullity (art. 11 para. 2 CO)
 - ✓ Exception: Abuse of right (art. 2 para. 2 CC)
- Example for «abuse of right»:
 - ✓ A wants to buy B's house for 1 Mio. CHF. They agree that only 800'000 CHF should be notarized, and the remaining balance is to be paid in cash.
 - Is this contract valid?
 - What are the legal consequences if A later refuses to pay the balance of 200'000?



Content of a Contract

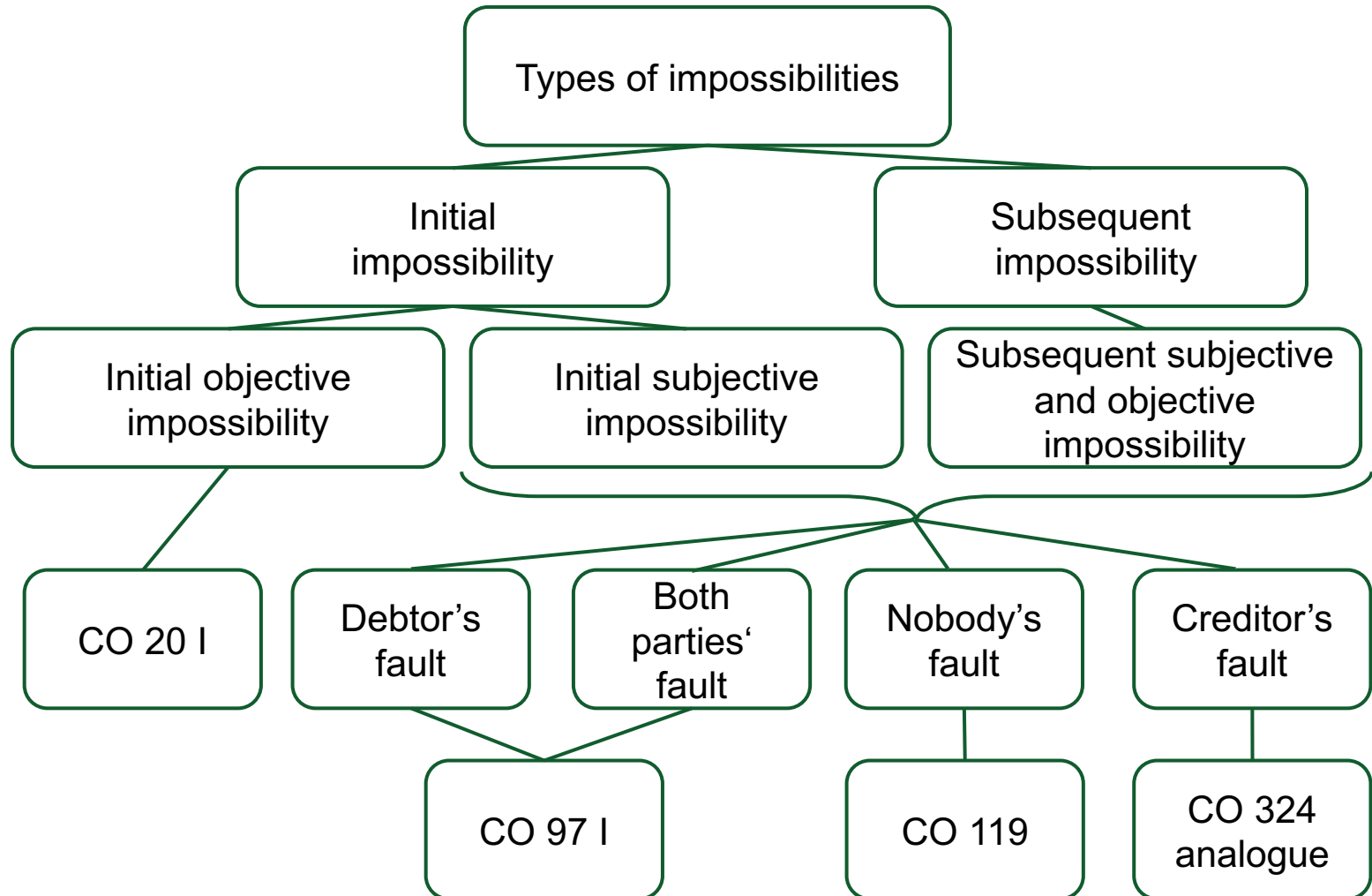
«Anything good in life is either illegal, immoral or fattening»

(Attributed to a certain Frank Rand of St. Louis)

- «The terms of a contract may be freely determined within the limits of the law» (art. 19 para. 1 CO).
- However, a contract is null and void if «its terms are impossible, unlawful or immoral» (art. 20 para. 1 CO);



Impossibility in Particular





E. Errors and Fraud



Types of Errors and Fraud (art. 23-31 CO)

An error can influence:

Formation of a will

Declaration
of intent

Error

Fraud
(art. 28 CO)

Duress
(art. 29 CO)

Error in
declaration (art.
24 para. 1 seq.
1-3 CO)

Motive error
(art. 24 para. 2
CO)

Fundamental
error (art. 24
para. 1 seq. 4
CO)



Simple Motive Error

- Somebody is making an error about the motive to do something
- Generally, not considered material (art. 24 para. 2 CO)

Example: Jack wants to propose to Jill. He goes to a jewellery store and buys a ring. That same day, Jill leaves him for another man.





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Fundamental Error (art. 24 para. 1 sec. 4 CO)

Requirements:

1. Subjective materiality
2. Objective materiality
3. Recognizability for the counterparty

Example: Pete buys a Picasso for 3,000,000 CHF.

Four months later, the painting turns out to be a fake.





Error in Declaration

- Must be objectively and subjectively material
- Is assumed to be material in the cases of art. 24 para. 1 sec. 1-3 CO)
 - Maggie wants to lease a car, instead she ends up buying it (art. 24 para. 1 sec. 1 CO)
 - Steven wants to buy *UBS* shares. He accidentally buys *UPS* shares (art. 24 para. 1 sec. 2 CO)
 - Andrew is seriously ill. He wants to be treated by Nora Sanchez, a famous cardiologist. He accidentally goes to Noemie Sanchez, an obscure healer (art. 24 para. 1 sec. 2 CO)
 - A jeweller accidentally sells a ring for CHF 1'380 instead of CHF 13'800 (art. 24 para. 1 sec. 3 CO)



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Willful Deception

Requirements:

1. Act of deception
2. Intention to deceive
3. Causal link to the error



Example: Mitchell is trying to sell his car (with a mileage of 100'000 km). He knows Cam is looking for a car with less than 50'000 km, so he manipulates the odometer until it shows 40'000 km. Cam buys the car and later finds out that the mileage is not correct.



Assertion of Fraud and Error (art. 31 CO)

Right to contest	• <i>Only</i> person who erred or was deceived
Declaration of contestation	• Explicitly, implicitly • Recommended: In writing • Contract is being transformed • Irrevocable
Contestation period	• One year (relative forfeiture period, art. 31 para. 1 CO) • Begins to run with discovery of error or fraud • Absolute period: ten years after formation of the contract (art. 67 para. 1 CO)
No contestation, in case of ...	• Ratification (art. 31 para. 1 CO) • Pure calculation error (Art. 24 Abs. 3 OR)



Consequences of Contestation

- Contract is unilaterally nonbinding and terminated with retroactive effect
- Exception: Contracts with continuous obligations -> effects are limited to the future
- Restitution of the contractual performances:
 - Things: according to art. 641 para. 2 CC
 - Claims: according to art. 62 para. 1 CO
- Art. 26 CO: possible liability for damages of the party that acted in error



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F. Agency



Agency Relationships

- Art. 32-40 CO regulate the rights and obligations arising from a contract made by an *agent* in the name of another person (the «*principal*»).
- They define the conditions under which the principal must accept the actions of his representative as being attributable to him.
- They also contain rules to protect the third party relying in good faith on the agent's authority to act in the principal's name.
- In practice, the law of agency is of great importance in commercial dealings – a company needs agents to act in its place.
- The governing bodies of companies are not agents, their authority is much broader and – in principle – only limited by the objects of the company (e.g., art. 718a CO).



Types of Agency

- **Direct agency**
 - The agent acts in the name of and on behalf of the principal (art. 32 para. 1 CO).
 - The agent does not act in the name of the principal, but «the other party must have inferred the agency relationship from the circumstances or did not care with whom the contract was made» (art. 32 para. 2 CO).
 - All the rights and obligations from the contract immediately and directly arise with the principal, not the agent.
- **Indirect agency**
 - The agent acts in his own name, but on behalf of the principal, i.e., on the account of the principal.
 - In that case the contract is formed between the agent and the third party; the rights and obligations must be transferred to the principal (art. 32 para. 3 CO).



Requirements for Direct Agency

- Agency must be permissible
- Agent must have capacity of judgment (art. 16 CC)
- Acting in the principal's name
- Acting on behalf (on the account) of the principal
- Authority to act for the principal
 - Power of attorney is form free
 - Scope is determined by the principal (art. 33 para. 2 CO); If the power of attorney is communicated to the third party, the scope is determined according to the communication of the principal to the third party (art. 33 para.3 CO)
 - Procuration is a commercial power of attorney (art. 458 et seq. CO) with its own set of rules.



Quiz – Question 5

Chris is too lazy to go outside and thus gives his 18-year-old daughter Nancy a slip of paper empowering her to purchase cigarettes in his name. In which of the following scenarios is Chris validly represented by Nancy?

1. Chris decides to stop smoking the moment Nancy has left for the store, Nancy buys the cigarettes anyways;
2. Nancy buys a car in Chris' name;
3. Nancy is severely mentally disabled.

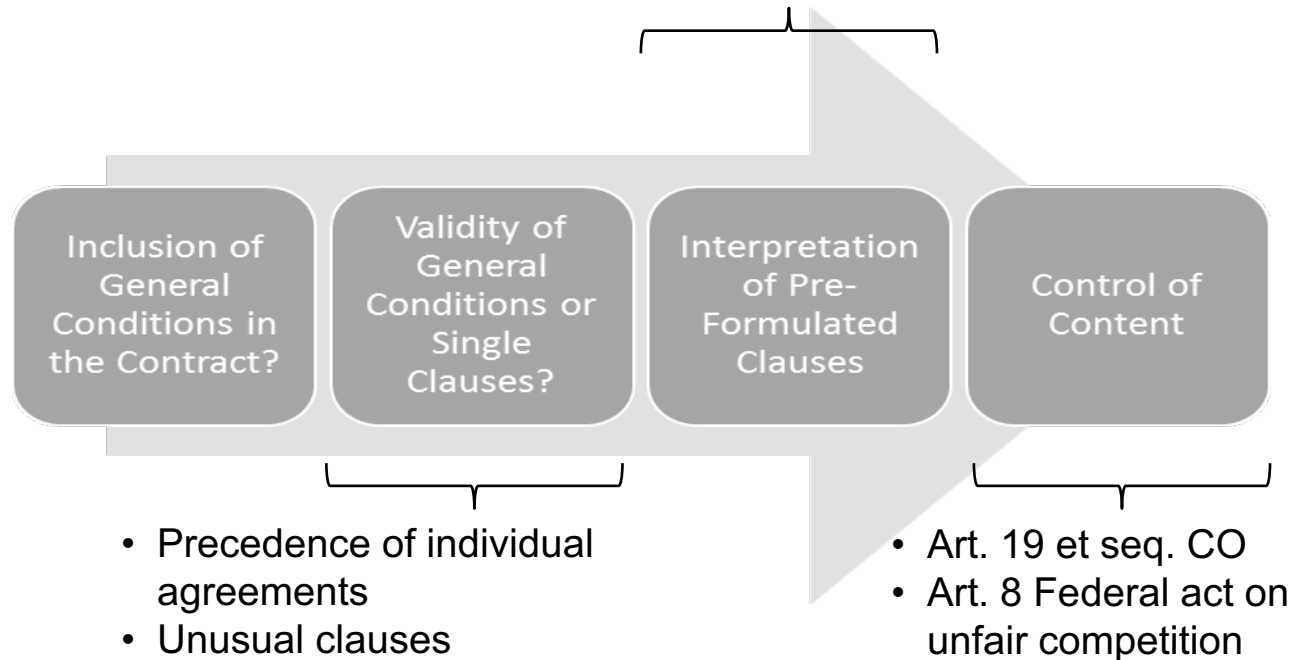


G. General Terms and Conditions



= Standard, one-sided, pre-formulated contractual clause(s), intended for the use in a multitude of contracts

- Usual rules to be applied
- General language
- Ambiguity rule





Battle of the Forms

Often both parties use their own general terms and conditions when forming a contract.

What happens if these terms contradict each other?

- a. If they are objectively or subjectively essential: No contract.
- b. If they are non-essential clauses:
 1. Theory of the final word: the chronologically last general terms and conditions are applicable
 2. Theory of the remaining validity: both GTC become part of the contract as long as they are in accordance with each other. Parts that contradict one another will be struck out and supplemented by the court according to optional law or the hypothetical will of the parties.

University of St.Gallen (HSG)
Law School
Bodanstrasse 3
CH-9000 St.Gallen
Switzerland

Prof. Dr. Markus Müller-Chen
Professor for Private and Commercial Law as
well as Comparative Law

+41 71 224 30 09
markus.mueller-chen@unisg.ch
www.ls.unisg.ch

