

When An Agreement Is Binding Or Subject To Contract

Introduction

In the course of negotiations, parties may come to an oral agreement, which may or may not envisage the execution of subsequent documentation. However, when are such agreements binding on the parties, and when does the requirement for documentation constitute a “subject to contract” clause? This was the issue faced by the Court of Appeal in *OCBC Capital Investment Asia Ltd v Wong Hua Choon* [2012] SGCA 54.

The case involved an oral agreement between the Appellant and Respondent which required the parties to execute a supplemental agreement “to effect necessary changes”. However, the Respondent later refused to sign the documentation, claiming that he was not legally obliged to as the agreement was “subject to contract”.

The Court of Appeal held that a binding agreement had in fact been reached. On an assessment of the documentary evidence and witness testimony, it was found that the parties did intend to be immediately bound, and did not intend to defer legal relations until formal execution of a written contract.

The Appellant was successfully represented by Lee Eng Beng S.C., Jonathan Lee, and Derek On of Rajah & Tann LLP.

Brief Facts

- (1) The Appellant was an investment holding company, and the Respondent was its customer. The Respondent was the CEO and shareholder of a company, which is listed in Malaysia (“**the Company**”).
- (2) In 2007, the Appellant and Respondent entered into a Risk Participation Agreement. Under the terms of this agreement, the Appellant agreed to purchase a number of the Company’s shares, and the Respondent agreed to pay the difference between the sale price and floor price of the shares if sold. The parties agreed that the Appellant was entitled to enforce this agreement until early in August 2009.

- (3) Due to the global financial crisis, the market price of the Company's shares fell drastically below the floor price. In February 2009, the Appellant indicated that it intended to sell its shares in the Company. At the Respondent's behest, the parties entered into negotiations to find a mutually beneficial solution before the deadline of the Risk Participation Agreement.
- (4) On 23 June 2009, the parties had a meeting in which they settled on the terms contained in a term sheet.
 - a. It essentially provided for the sale of the Appellant's shares in the Company to the Respondent in five tranches.
 - b. Importantly, it also contained a provision ("**the Documentation Term**") that stated "Documentation: A Supplemental Agreement to be executed to effect necessary changes."
- (5) Following the meeting, the Respondent did not observe the Appellant's requests to sign the formal documentation. He asked for time to consult his lawyers, and then ignored the Appellant's requests for updates.
- (6) Finally, on 28 August 2009, the Respondent indicated in a meeting that he would not sign the documentation (including the Supplemental Agreement) as he was not legally obliged to do so.

Holding of the High Court

The Appellant subsequently initiated its claim against the Respondent. It alleged that a legally binding oral contract had arisen as a result of the 23 June 2009 meeting, and that the Respondent had been in repudiatory breach by refusing to execute the formal documentation and perform his contractual obligations.

However, the High Court Judge held against the Appellant, finding that there was no binding oral contract. It found that the Documentation Term constituted a "subject to contract" clause, and that the conduct of the parties was consistent with the understanding that legal relations had been deferred until the execution of the Supplemental Agreement.

Holding of the Court of Appeal

The Court of Appeal overturned the High Court's decision, holding that the objective evidence pointed towards the existence of a binding oral contract between the parties. The Supplemental Agreement did not have to be signed before the contract came into force.

General law

Although the existence of a "subject to contract" clause generally creates a strong inference that the parties did not intend to be bound until they execute a written contract, this is not the be all and end all of determining whether there is a binding contract. Even if a "subject to contract" clause exists, and certain terms remain to be negotiated, it is possible for parties to already be subject to a binding contract.

The Court will look at the circumstances surrounding the negotiations between the parties, including their intentions, in determining whether there is a binding agreement in force. The critical inquiry lies in determining from the objective evidence whether the parties intended to be immediately bound to perform on the agreed terms or to defer legal relations until formal execution of the written contract.

Application to the facts

First, the Court found that the Documentation Term was not a "subject to contract" clause. The term required a Supplemental Agreement to effect the "necessary changes", implying that there was already an underlying agreement regarding the new arrangement on the Company's shares, and that the Supplemental Agreement was merely to give effect to those changes.

The Court thus had to consider what those changes were, and whether the failure to execute the Supplemental Agreement somehow invalidated the underlying agreement. In doing so, it highlighted that it would rely more heavily on documentary evidence, rather than the oral testimony that the High Court placed greater emphasis on. This is because documentary evidence tends to be more reliable and objective, and should thus be the first port of call.

On an analysis of the objective evidence, the Court found that the parties had intended to enter into binding legal relations in their agreement at their meeting of 23 June 2009.

- (i) E-mail correspondence before the 23 June meeting suggested that the parties were eager to reach a final resolution of matters between them, which thus required a binding agreement.
- (ii) The Respondent's own testimony acknowledged that he was wholly in agreement with the terms set out in the term sheet at the 23 June meeting.
- (iii) Further, correspondence after the 23 June meeting indicated that both parties were of the view that a binding oral contract had been entered into.
- (iv) The Respondent had asserted that there were unresolved issues in an e-mail of 11 August 2009. However, the Court found this to be a legal ploy rather than evidence that the parties intended to be bound only on the execution of a written contract.

The Court agreed with the Appellant that it was more than likely that the parties intended for the Supplemental Agreement to be a mere formality. The circumstances related to the modification of an existing contract rather than the initial establishment of contractual relations. The parties were already familiar with the underlying obligations and the difficulties which they were trying to resolve. It was thus unsurprising that they would enter into a binding oral contract at the 23 June 2009 meeting.

Concluding Words

In its decision, the Court of Appeal provided valuable guidance as to when a binding agreement is reached between the parties. Whether or not a binding contract has been reached depends on the true intention of the parties, as indicated by the objective evidence of the case. If an agreement has been entered into, parties cannot avoid being bound by its terms merely by slapping a label of "subject to contract" on one of the provisions, or by requiring the execution of subsequent documentation.

It is not uncommon for binding oral agreement to be reached in the course of commercial negotiations. Parties seeking to defer the formation of a contract should thus make it clear in the terms that there is no agreement until the execution of a written contract, and that such execution is a condition precedent of the contract. This is so as to avoid any subsequent uncertainty as to whether they are actually legally bound by the terms discussed.

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