Contract Formation

Contract formation is a long and thorough process that requires due attention from both parties. The most important stage in the "life" of any contract is its "birth." Every detail of a future deal should be discussed and agreed upon by both partners-to-be in order to avoid possible conflicts that may occur in the future. International contracts are more complex than any agreement between parties from the same country, as legal, cultural and lingual differences should be accounted for during the contract formation.

Contract formation

Contracts are a legally binding form of social agreement, thus, the stages of contract formation are universal and are applicable to every legal system. Although, in some countries this process has some traditional elements, the process always includes three essential elements of contract formation: offer, consideration and acceptance. A contract is formed when the parties have agreed on the essential terms of the contract.

Offer

Negotiations begin at the moment one party makes a proposal to another party. Such proposal is called an offer and the person who makes it is the offeror.[1] The initiator of an offer is usually the party that provides services or items (seller, supplier, the contractor).

In order to be valid an offer must meet certain conditions. First, the offer should contain all the essential terms of the future agreement so the offeree will understand what the offer is about.[2] If the proposal does not contain all essential terms, it is not an offer, but only an invitation to an offer, which has no obligations meant by it. Second, offer

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[1] An Introduction to American Law', McAlinn, Rosen & Stern, Carolina Academic Press, 2d.Edition, 2010, Chapter 4,Page 94

[2] Id, Chapter 6, Page 172

must be addressed to a specific person. Therefore, advertisements and price lists are not offers, but only show an intention to make an offer in the future.

Acceptance

After an offer is made a person to whom it was addressed, an offeree has to accept or decline such offer. The offeree's decision on the proposal is called an acceptance. Only the person to whom the offer was addressed can accept an offer. If the acceptance of an offer comes from a different person, it is a new offer, which the original offeror can choose to accept.[3]

Counter-offer and acceptance by silence

Acceptance must be complete and unconditional. If the party agrees in general with the proposal, but wants to make some adjustments to the conditions of the contract, then the offeree's answer is not an acceptance; it is a new offer, which is called the counter-offer.

If the contract offer has a deadline for the offeree's reply, the contract is formed if a positive response is provided within the specified period. If the period of reply was not specified, the contract is concluded if an acceptor enters into this agreement immediately or within the usual time for such response. Acceptance, which is received after the specified term of reply, is a new offer.[4]

If a the offeree, within the deadline for reply, committed action in accordance with the terms of the contract specified in the offer (shipped goods, provided services, performed the work, paid the appropriate amount of money, etc.), which indicates its desire to enter an agreement, such action is considered an acceptance of the offer, unless otherwise is

[3] Contract Formation: Law and Practice', Furmston & Tolhur, Oxford University Press, 2010,Chapter 4, Page 83
[4] An Introduction to American Law, Chapter 6, Page 172

specified in the offer or the law.[5] As it was indicated in *Weichert Co. Realtors v. Ryan, 128 N.J. 427, 437 (1992)*, when the agreement on the terms of the contract was not reached, but the offeree began performance and the offeror accepted his performance, the court held that a contract was formed.

Consideration

Consideration is an element of every contract. In broad terms, consideration may be referred to as a bargain between parties. A contract is only valid when there is a real exchange of some goods or services, or any material or nonmaterial objects that have value. Agreement that is not meant to exchange any goods at all is void. Consideration is about the exchange of items of value not the fairness of such exchange.[6]

Nevertheless, consideration may be regarded not only as a bargain. The "benefit-detriment theory" supported in *Hamer v. Sidway, 124 N.Y. 538, 27 N.E. 256 (1891)*, states that forbearance of legal rights on promises of future benefit made by other parties can constitute valid consideration.

Legal capacity and enforceability

Most social agreements are not legally binding. This fact leads to two other stages of contract formation, which are the checking of the legal capacity of both parties and the legal enforceability of the contract. It is necessary to check legal capacity of parties and legal enforceability of the contract during the whole process of contract formation and its performance.

The contract should be clear to both parties and to any other person that may be involved in its performance, e.g. the court that will hear the case should be able to

[5] Id, Chapter 6, Page 177
[6] Id, Chapter 6, Page 182

understand and interpret the terms of the contract in order to provide a decision. During the formation of an international contract it is essential to remember that legal or any other terminology might be interpreted differently in the countries of parties. Both the offeror and offeree should make sure that they are on the same page, meaning that all the terms and conditions of the contract are clear for them and they understand the terms in the same way[7]. Moreover, by agreeing to enter into the contract, both parties should understand what they are required to do and what are the probable consequences of a breach of the contract. As the court held in *Hadley v. Baxendale, 9 Exch. 341, 156 Eng. Rep. 145 (1854)*, the party should be liable for the injures caused to non-breaching party in the amount that ordinarily follows such breach even if it was not directly specified in the contract.

In order to reach an agreement and to make sure that parties interpret the contract in the same way, negotiations take place. The Seventh Circuit's decision in *Venture Assoc. Corp. v. Zenith Data Sys. Corp., 987 F.2d 429, 433 (1993),* affirms that parties should negotiate in a good faith, meaning that the terms of an offer that were under negotiation should not change drastically. During the negotiations, as it was already stated above, parties should reach a mutual understanding of all the terms of the contract and not only to understand, but also discuss them. As the court held in *Frigaliment Importing Co. v. B.N.S. International Sales Corp., 190 F.Supp. 116 (S.D.N.Y. 1960)* the parties to a contract should actually say the same thing and not only to think that they mean the same thing.

[7] Contract Formation: Law and Practice', Chapter 1, Page 19

Choice of law

In order to avoid possible problems connected with the different understanding of the terms by the contracting parties, all terms and conditions should be interpreted within the scope of legal provisions. However, legal provisions may differ from country to country. Therefore, international contracts have a unique stage called "choice of law." Parties must agree material and procedural law of which country they should use to interpret the terms and conditions of their agreement and what procedures should be followed in the case of a dispute between them. In case the parties do not choose the law to be used, they will have to address laws of their countries to identify which law is applicable in their case. Although, every country has its own provisions on the law that is applicable to certain types of international contracts, the situation in which laws of those countries have different provisions is possible. Thus, it may be impossible to decide which law is the right one without the mutual consent of the parties.

In the end one thing is clear, international contract formation is a process that includes such elements as offer, acceptance, consideration, legal capacity and enforceability, choice of law and others. Needless to say that both parties to a contract have to negotiate every detail of the future agreement before concluding it, in order to avoid possible breaches in the future.

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