

## **The Law Governing Contract Formation: *Solomon Lew v Kaikhushru Shiavax Nargolwala and others and another appeal* [2021] SGCA(I) 1**

### **I. Executive summary**

Cross-border contracts often raise questions as to which country's law should govern the contract. A three-stage test is usually used to determine the governing law. The first two stages determine, respectively, whether parties had expressly or impliedly chosen a governing law, and the third stage determines the governing law based on the law with the closest connection to the contract (if no express or implied choice had been made).<sup>1</sup>

However, this test assumes that a contract exists in the first place. If the very existence of a contract is disputed and each contracting party argues that a different law governs the issue of contract formation, does the three-stage test apply or is a different approach required?

In *Solomon Lew*, the Court of Appeal ("CA"), on appeal from the Singapore International Commercial Court ("SICC"),<sup>2</sup> handed down a landmark decision that set out the correct approach, *i.e.* the putative proper law approach.

### **II. Material facts**

The dispute concerned the sale of shares in Querencia Limited, which owned rights in relation to a villa in Phuket, Thailand ("**Villa 29**"). Querencia's shares were owned by Mr and Mrs Nargolwala. In 2015, the Nargolwalas put up Villa 29 for sale. Mr Solomon Lew wished to acquire Villa 29 and made offers through the resort's general manager, Mr Meury. Between September and November 2017, Mr Lew and Mr Meury, and Mr Meury and the Nargolwalas, corresponded with each other on the possible sale of Villa 29. Eventually, the Nargolwalas sold Villa 29 to Quo Vadis Investments Limited, a Hong Kong company controlled by Mr Christian Larpin. Therefore, Mr Lew sued the Nargolwalas, alleging (among other things) a breach of contract regarding an alleged sale of Villa 29 to him.

### **III. Issues**

#### **A. *Whether there was a binding contract between the Nargolwalas and Mr Lew***

Mr Lew had appealed against the SICC's finding that there was no binding oral agreement between the Nargolwalas and Mr Lew. Mr Lew had argued there was a binding contract because he had sent Mr Meury an offer on 11 October 2017 and Mr Meury had responded that the Nargolwalas had accepted the offer. This raised two sub-issues: (a) a contractual issue of whether an oral contract was formed on 11 October; and (b) an agency issue of whether Mr Meury was authorised to convey the Nargolwalas' acceptance of the offer.

Since the parties had not argued that Singapore law and Thai law differed on the first sub-issue, and were agreed that Singapore law governed the second sub-issue, the CA applied Singapore law to determine both sub-issues. Applying established principles, the CA found on the facts that there was no agency relationship (Mr Meury lacked both actual and implied authority to conclude an agreement on behalf of the Nargolwalas) and thus no agreement.

#### **B. *Costs and governing law issue***

The above finding meant that Mr Lew's appeal failed, without any need to consider Thai law for that purpose. However, the Nargolwalas had cross-appealed against the SICC's order of

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<sup>1</sup> *JIO Minerals FZC and others v Mineral Enterprises Ltd* [2011] 1 SLR 391 at [79].

<sup>2</sup> A division of the General Division of the High Court and part of the Supreme Court of Singapore, created to deal with transnational commercial disputes.

costs against them. The Nargolwalas had argued that Thai law applied because under Thai law, the oral agreement would have been unenforceable. Despite finding for the Nargolwalas on the existence of a contract, the SICC had ordered the Nargolwalas to bear Mr Lew's costs for the issue of whether Singapore or Thai law applied to determining the enforceability and validity of the alleged contract as the SICC had deemed it unreasonable for the Nargolwalas to argue for Thai law to apply. Consequently, to determine if the Nargolwalas' appeal against this aspect of the SICC judgment should succeed, the CA considered the approach to ascertaining the governing law of contract formation in order to determine whether it was indeed unreasonable for the Nargolwalas to have argued for Thai law to apply.

(1) *The approaches for determining the law governing contract formation*

The traditional approach for identifying the governing law of a contract, where it was undisputed that the contract exists, was well-established (“**3-Stage Approach**”): (1) the court would first consider if the contract expressly stated its governing law; (2) if the contract was silent on the governing law, the court would consider whether it could infer the governing law from parties' intentions; and (3) if the court was unable to do so, the court would then determine the contract's objective proper law, which was the law with the closest and most real connection with the contract. However, where there was a dispute over whether a contract had been formed in the first place, it was unclear what the approach to determining the governing law of contract formation was. The CA proceeded to analyse the various possible approaches.

The first approach considered was the “putative proper law” approach (“**PPL**”), which “assume[d] that a contract ha[d] been formed, and then determine[d] the proper law on that basis in order to determine whether the contract ha[d] been formed”.<sup>3</sup> The PPL applied a three-stage test analogous to the 3-Stage Approach. However, at each stage, what was considered was not the “contract”, but the negotiation or transaction which allegedly gave rise to the contract.

The second approach considered was the *lex fori* approach, where the governing law was simply the *lex fori* (i.e. the law of the forum, with the forum meaning the place where the legal action was commenced).

The third approach considered was suggested by Professor Yeo Tiong Min SC. Professor Yeo had argued that where parties had negotiated with reference to a legal system or had agreed on a law to apply to the issue of contract formation, that law would govern contract formation. Otherwise, the law with the closest connection with so much of the putative contract that was not disputed by parties should apply. However, where the entire contract was disputed, the court could only apply the *lex fori*.

The fourth approach considered was put forth by Professor Adrian Briggs QC. Professor Briggs had argued that the starting point was an application of the *lex fori* if the existence of the contract was denied. If the *lex fori* found that the basic components of contractual agreement are present,<sup>4</sup> there was then full and sufficient contractual agreement from which the proper law of the contract could be determined as any contract must have a proper law from its inception. This proper law would then supplant the *lex fori* and would govern all issues of

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<sup>3</sup> Professor Yeo Tiong Min SC, *Private International Law: Law Reform in Miscellaneous Matters* (unpublished), cited in *Pegaso Servicios Administrativos SA de CV and another v DP Offshore Engineering Pte Ltd and another* [2019] SGHC 47 at [73].

<sup>4</sup> In common law systems, under contract law, this refers to an accepted offer, consideration, an intention to create legal relations, and the absence of any factors nullifying consent.

validity. Professor Briggs relied on the *lex fori* rather than the legal system with the closest and most real connection with the contract because he viewed the proper law of the contract as a subjective idea, dependent on the choice of parties.

Finally, the fifth approach considered was that applied by the SICC. The SICC had applied the 3-Stage Approach, with slight variations to take into account that there was a fundamental dispute over the existence of the contract in the first place. However, the SICC had considered that where the court is unable to reach a clear conclusion that a particular law should be applied, the court should apply the *lex fori* as a matter of prudence.

(2) *The correct approach: the putative proper law approach*

In considering the correct approach, the CA observed that it was, by definition, not going to be possible to refer to any contractually binding selection of law to determine the issue of whether a binding and enforceable contract had been made. It was theoretically possible, but practically unlikely, that two negotiating parties agreed upon a particular law to govern this issue.

What was more likely was the situation where parties had agreed on some, but not all, of the suggested or the necessary terms, and those which had been agreed include what law would govern the contract. In some circumstances, it may be obvious what law should govern the contract (if and when any was made), even though nothing had been said about this. For instance, this could occur where the case involved a domestic contract made between domestic parties about a domestic subject matter. In other scenarios where there were significant cross-border elements in interchanges between parties, courts were accustomed in considering which legal system a factual complex or issue was most closely connected.

Given the above observations, the CA questioned the appropriateness of a rule which would automatically assign the determination of the issue of whether a binding and enforceable contract had been made to the *lex fori*. The *lex fori* approach would fail to attain uniform solutions, which was the chief purpose of private international law. Instead, the CA preferred the PPL as it gave effect to the parties' reasonable expectations with regard to the issue of whether they had made any contract. The law was precisely shaped to serve and give effect to the reasonable expectations of its users. It would be illogical to apply the *lex fori* regardless of whether the forum had anything to do with the parties or the subject matter, other than the fact that proceedings happened to be brought in it. Therefore, the court adopted the PPL, which it found to be similar to 3-Stage Approach, but with a focus on the circumstances of the transaction or relationship alleged to have given rise to a concluded contract.

In applying the PPL, the CA agreed with the SICC that the first stage would rarely be relevant since it was practically unlikely, though theoretically possible, that contracting parties had agreed on a governing law for the issue of contract formation. If parties had agreed on some of the necessary terms, it would be easy for the court to identify an implied choice of the law under the second stage to govern not only the contract when made, but also the issue of whether any contract had been made. There may also be circumstances where the court would have to undertake the exercise of identifying the system of law the circumstances and issue may objectively be said to be most closely connected with under the third stage (in the absence of any express or inferred choice of law by the parties), which the courts were familiar with doing. Each stage should be approached objectively.

However, the CA gave a caveat. The PPL may not apply in an extreme case where applying the PPL might give rise to grave injustice. For instance, one situation would be where there

were negotiations between Party A in England and Party B in State X, where the putative proper law was the law of State X under which silence in response to an offer amounted to consent. However, the CA observed that this was a small caveat that was rarely applicable and its effect would be that no contract at all came into existence under any law, not that the *lex fori* applied.

The CA rejected Professor Yeo's approach. While his approach began with propositions consistent with the PPL, it then carved out situations where the entire contract was disputed and applied the *lex fori* in such situations. However, the entire contract being disputed was not a reason to resort to the *lex fori*. Rather, the PPL provided a coherent framework to address such a dispute.

The CA also rejected Professor Briggs's approach as it was premised on the governing law as a subjective idea, dependent on the parties' choice, whether express or implicit. Rather, the law should give effect to reasonable expectations, objectively ascertained. Hence, it was appropriate for the court, in the absence of any express or implied choice, to identify the law which had objectively the closest connection to the relevant circumstances to resolve the issue.

Finally, the CA rejected the SICC's approach, which applied the *lex fori* as a fallback where the court could not reach a clear conclusion as to the governing law. When there was an allegation of a binding agreement, it would necessarily be between parties, in some context and language, and in relation to some purpose and/or place. There would be connecting factors to analyse and weigh. Even if the balance between factors was slight, courts did not, in practice, declare ties. Rather, the suggestion that the *lex fori* should apply where the court could not reach a "clear" conclusion as to the governing law would only lead to a lack of clarity and argument about how much doubt or clarity was required. Unlike what the SICC had suggested, the appropriate approach could not be as a matter of choice or discretion or even prudence. In addition, once again, the forum may not have any connection with the parties, and hence the *lex fori* would have no logical claim to determine the issue of whether any contract was made.

### (3) *Application of the correct approach*

Similar to the SICC, the CA did not find an express agreement between the parties as to the law governing contract formation.

With regard to the second stage, the CA disagreed with the SICC's finding that there was an implied choice of Singapore law because the Nargolwalas had insisted that Singapore lawyers should be instructed. The CA pointed out that the SICC had mainly relied on matters post-dating the making of the alleged oral agreement on 11 October 2017. For instance, the insistence that Singapore lawyers should be instructed was indicated only on 5 November 2017. At the date of the putative agreement (*i.e.* 11 October 2017), the offer sent by Mr Lew did not mention any law or lawyers, and it was this offer which had allegedly been accepted by the Nargolwalas. In fact, while Mr Lew had indicated that he had a Singapore lawyer to Mr Meury on 11 October, the Nargolwalas had nonetheless stated that it might be better for Mr Lew to instruct Mr Anurag Ramanat, a Thai lawyer, in Bangkok. Since the Thai lawyers' assistance would be relevant for substantive legal as well as technical issues, the reference to using Singapore lawyers did not appear as a conclusive indication of implied intent. Therefore, the CA questioned whether it was possible to derive any implied choice of law in this instance.

Moving to the third stage, the CA did not conclusively determine whether Singapore or Thai law was the governing law as it was unnecessary for the purposes of the appeals. The CA did observe (*in obiter*) that it was highly arguable that Thai law should have applied. Villa 29 was

in Thailand and so were Mr Lew and Mr Meury, between whom any agreement was said to have been made. While the shares were owned by a BVI company, any buyer would be more concerned about the Thai legal position regarding the title held by that company in respect of the construction, leasing and occupation of the villa when tying up the legal formalities to complete the oral agreement. The entire structure of the transaction could be said to be derived from Thai law as it was Thai law that prohibited foreign nationals from owning property in Thailand, and Mr Lew would need to check the Thai legal position to ensure that he indirectly “owned” Villa 29. The Nargolwalas’ residence in Singapore was of no real significance. The reference to Singapore lawyers during discussions was relevant but further references to Thai lawyers were also made. Therefore, it was eminently arguable that Thai law would govern the oral contract.

(4) *Decision on the costs issue*

The CA found that the SICC had erred by focusing on later developments and the Nargolwalas’ subjective state of mind to identify the law governing the existence and validity of any alleged earlier oral agreement. The CA held that the SICC’s view – that the Nargolwalas’ case advanced on Thai law was unreasonable and merely opportunistic – was unjustified. This was because it went to a point – the unenforceability under Thai law of any oral agreement – which the SICC actually accepted and which would, by itself, have been fatal to Mr Lew’s whole case. Thus, the CA saw no basis to depart from the general rule that costs should follow the event (*i.e.* the successful party in a suit should be awarded costs, even if they do not succeed on all issues). Therefore, the Nargolwalas’ appeal succeeded and they were awarded their costs, including those relating to the Thai law issue.

#### **IV. Lessons learnt and concluding thoughts**

The CA has definitively laid down the approach to determine the law governing contract formation and has resolved the uncertainties in this area of law, making it a landmark decision. This approach is principled as it gives effect to the expectations of contracting parties, which respects the notion of party autonomy underlying contract law. This approach is also practical as it mirrors the existing traditional approach to identifying the governing law of a contract. It will therefore be easy for courts and lawyers to adapt to this new development.

Practically, while the CA observed that it was theoretically possible but practically unlikely for contracting parties to agree upon a law governing contract formation, lawyers may wish to advise clients to agree on the law governing contract formation. This is to ensure that parties have autonomy over which law applies rather than leaving it up to the court and the PPL.

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