BOOK II

Chapter One

Extinction of Obligations

Extinction of obligation connotes the stoppage of already existing obligation. According to Article 1806 of the civil code (C.C), there are different grounds which cause extinction of obligation. Cumulative reading of Articles 1806 and 1807 of the C.C takes performance, invalidation, cancellation, termination, novation, set off, period of limitation of a contract, and merger as grounds of extinction of obligation.

1.1. Performance of contract

Performance of obligation is not only an effect of contract but also a ground of extinction of obligation. Performance of the contract shall however be made according to the terms of the contract and mandatory provisions of the law if it shall extinguish contractual obligation. It shall be performed according to the agreement without discrepancy if it shall bring the contractual obligation to an end. Extinction of obligation by performance of a contract needs performance of a contract in a legally required conformity.

1.2. Invalidation and cancellation of a contract

Invalidation of contract is one means by which contractual obligations are extinguished. Invalidation of a contract happens when there is defect in the formation of the contract. If a party that is incapable concludes a contract or if one of the parties concludes the contract without having the legally required consent, the contract is subjected to rescission.

Invalidation means making an effective contract ineffective when it has a problem in its formation. Invalidation is related with the problem in the formation of the contract. Invalidation comes into question when one of the parties wants to be free from the contractual obligation owing to a problem in the formation of the contract.

Therefore the mere presence of willingness of one party to have a contract invalidated is not enough. In addition to that, the legally provided grounds shall also be fulfilled. Lack of capacity and lack of sustainable consent are among the grounds that render a contract invalid.

The nature of invalidation of a contract is reflected in its effect. Now that invalidation of contract takes us to the conclusion that the contract is not properly formed, the effect of contract is said to

be restitution. The contracting parties are put to the place where they were before the formation of the contract.

Sometimes compensation might be ordered when a contract is invalidated. This might lead us to the conclusion that the effect of invalidation and cancellation is the same in compensation. However, the damage following from an invalidation of a contract shall aim at putting the contracting parties in a place they would have been had the contract not been formed.

Cancellation on the other hand is making an effective contract ineffective when there is non-performance. Cancellation of a contract is one effect of contract in that the contract is formed within the legally provided requirements. When one of the contracting parties fails to perform a contract the other party might cancel the contract as one remedy of non-performance of the contract. There might be again other grounds of cancellation like the condition which results in cancellation.

The other basic difference between invalidation and cancellation is their ground. The ground for invalidation is defect in its formation while the ground for cancellation is non-performance. This does not, however, mean that the only difference is in their ground. They are also different in their effect. Even though the effect of both invalidation and cancellation is restitution, cancellation additionally entitles the party a compensation that rewards the benefit of contract.

Unless the invalid contract is invalidated, the contract is upheld and becomes effective. Even though the contract might not be performed, the remedies of non-performance will be due. Under Ethiopian law of contract anybody that wants it to be invalidated cannot invalidate a defective contract. It shall be the party who is affected by the invalid contract that can invalidate the contract.

Extinction of contractual obligation does not however mean that there is not any obligation left to be carried out by the obligation. If one of the parties or both have discharged their obligations, invalidation or cancellation will create obligation of effecting restitution. See art.1815.

According to article 1815 (1), the parties are required to be put in their original position before the formation of the contract. The parties are expected to be with their original properties before the contract. After the formation of the contract the parties are put in different position because of the newly created obligation. All or part of the obligations might have been performed. If invalidation or cancellation happens the parties are put in their previous position in that the performed obligations are reinstated.

Any party who has performed can invalidate the performance. Someone who has given something to discharge his obligation can reclaim the thing given.

A question as to whether cancellation and invalidation are the same, excepting a titular difference, may be raised if the effect of both is reinstatement under the law of contract of Ethiopia. Although cancellation might be followed by compensation, invalidation can also be followed by compensation according to Article 1817 (2), as it shows that payment of compensation shall be made for parties to reinstate them.

However, difference still exists in their effect as **cancellation paves the way for compensation that puts the victim in the place he would have been had the contract been performed.** Article 1790 (1) shows that damage shall be made good for injury of non-performance of contract. When the reason of damage is non-performance perfect expectation damage is understood. The possibility of forced performance and damage together strengthens the inclusion of perfect expectation damage.

Invalidation is, on the other hand, followed by compensation that puts the victim in his original position. Such effect also exists in Ethiopian law of contract pursuant to Article 1817 which shows that the compensation shall be aimed at reinstating the party in his original position. Even though this provision is equally applicable to cancellation, cancellation can also be followed by additional damage pursuant to Article 1790.

The reinstatement effect of invalidation and cancellation is not made without limitation in a way it hinders security of transaction. These include:-

Article 1816:Rights of third parties in good faith.

Article 1817: Impossibility of restoring to the previous position, serious disadvantage or inconvenience

1.3. Termination of contract

Termination of contract is making the contract ineffective starting from the time of termination of the contract. Termination of contract can be either, bilateral (by the agreement of both the contracting parties), unilateral by one party, or judicial (by court order).

A) **Bilateral termination(**1819)

Bilateral termination refers to putting an end to a contractual obligation by the agreement of both parties. Agreement to terminate is, actually, a contract as a contract can be to extinguish obligation of proprietary nature (see art.1675). Termination of contract by agreement can be made in two ways. The parties may affect termination pursuant to their contract provided that they have inserted such termination clause in their contract or agreed later. The termination clause may also entitle one of the parties the power of termination unilaterally. It may also put a condition upon the fulfillment of which the contract is terminated. Even though the parties might not agree in the contract about termination and its condition, they can also agree later to terminate the contract. Termination of contract by consent of the parties provided under Article 1919(1) includes all that are discussed above.

B) Unilateral termination

Unilateral termination is made either by the effect of agreement when such unilateral termination clause is provided in their contract and when a condition which entitles unilateral termination is fulfilled. Unilateral termination can also be made by giving notice in advance. The time of notice might be either fixed by law, by custom, or reasonably by the contractants

C) Judicial Termination (see articles 1823 and 1824)

Termination can also be made when one of the parties requires to that effect in case where there exist Special relation between the parties and case of Gratuitous contracts . Court termination is the principle and termination by the parties is an exception as parties shall not be judges on their own case.

Effect

Termination does not have retrospective effect; rather it has prospective effect. This means, extinction of contractual obligation by termination of contract works only in the forwarding direction from the time the contract is terminated regardless of its type.

1.3.2 Similarities and differences between invalidation and cancellation on the one hand and termination on the other.

A. Cause

The ground of termination is not attributable to defect in the formation of a contract or non-performance on one of the parties. Termination can be made by agreement, unilaterally by one party or by court order. However, the grounds of invalidation and cancellation are defect in consent and non-performance in accordance to the terms of the contract respectively.

B. Effect

Invalidation and cancellation have retrospective effect while the effect of termination is prospective. Article 1819 Sub (2) and (3) are obvious in indicating the prospective nature of termination. Quite the reverse, Article 1815 is testament for retrospective effect of invalidation and cancellation. Restitution is effect of invalidation and cancellation unlike termination.

Similarity

Invalidation, cancellation and termination are the same in that they extinguish contractual obligations.

1.4. Remission of debt (1825)

Remission of debt is voluntary release of debtor of his obligation by the creditor. But mere willingness of the creditor to release the debtor by remission is not enough to make the remission effective and result in extinguishing of obligation. The willingness of the debtor to that effect is also required. However the provision does not put express acceptance of the remission as a mandatory requirement. The debtor shall object when he is informed of the remission if he wants the remission not to be made. Unless such protest is made the law seems to presume silence as acceptance in the case of an offer to effect remission of debt to the debtor.

1.5. Novation (Art.1826)

Novation is substitution of an existing obligation by new obligation in its nature or object. The new obligation shall be different from the substituted obligation either by its object or nature. Mere difference without substantial change either in the object or in the nature does not amount to novation; rather it is variation in fact. When original obligation is different from the substituted obligation in its cause it is also considered to be novation.

Novation is required to be intentional so that it can have the desired consequence in accordance with Article 1828.Hence replacement of certain obligation with other obligation in the absence of

intention to make novation does not have the effect of novation. Intention of the parties could be shown in different ways.

Acts like Preparing a new document to support an existing debt, signing a promissory note or bill of exchange in respect of an existing debt does not show novation and nor does providing securities to ensure a debt show ovation.(See art. 1829).The article seems to be illustrative not exhaustive.

Novation in its effect does not extinguish only the principal obligating but also the accessory ones. Accessory obligations in pledge, mortgage and personal guaranty are extinguished as the principal obligation extinguishes by novation.But it must be born in mind that if the guarantor agrees to that effect, his accessory obligation is upheld.

As novation creates new obligation, the effect of period of limitation is different as to the new obligation from the previous obligation. There might be even difference in the duration of the period of limitation. A new period of limitation starts to run and the defense on the lapse of period of limitation based on the original contract does not work.

1.6. Set off

Set off refers to a situation where two parties in which one is a debtor in respect of one obligation while a creditor with respect of another obligation to other party may extinguish the obligation. Set-off can be made only upon the fulfillment of certain conditions although the contractants owe debt to one another. These conditions have been put as positive and negative conditions respectively under Articles 1832 and 1833.

The conditions that are provided in Article 1832 are.

(a) The debts shall be money debt or fungible things of the same species.

Set-off is not possible if someone owes in item and the other owes in money. Nor is set-off possible when the debts are items unless the items are fungible things.

(b) The debts shall be liquidated.

The money debt or fungible things shall also be liquidated ones in that the parties should be certain about the debt. The parties shall not have a dispute as to the amount of the debt. If the

amount claimed by the creditor and the amount accepted by the creditor is not equal, the debt requires further liquidation. In such disagreement the debt is not liquidated and hence not subjected to set-off.

Exceptions to this rule

A. Although the debt is required to be liquidated court can make set-off when it is required to do so to the extent of the admitted amount as exception to the requirement of "liquidation" of the debt. (See art 1841).
B. The other exception is when the debt can be liquidated without delay. A debt whose amount is contested by the parties or which is not fully liquidated can be delayed so that set-off is made with regard to the whole debt. The court may suspend judgment against the debtor whose debt is liquidated until the other debt is liquidated if the debt can be liquidated without delay.

(c) The debts shall be due.

The other condition is that the debt shall be due at the time set-off is required. The time when both obligations are required to be performed shall be at the same time. This requirement protects the debtor who can be beneficiary of time limit.

An exception to this requirement has been provided under Article 1834 dealing with period of grace. Granting of period of grace does not bar set-off although the time in which payment shall be made is protracted by the court order of period of grace. A debtor who is given period of grace shall not be protected against set-off like other beneficiaries of time limitation.

Although the debts are liquidated and due, there are also other requirements which shall be additionally fulfilled. Additional negative conditions have been provided under Article 1833.

In general set-off cannot be made in the absence of intention to do so. Article 1838 provides that if the debtor fails to inform the creditor his intention to effect set-off, set-off does not occur. Knowing intention can be difficult as there is no proof of mental element of the parties. Circumstances from which the mental element of the parties can be inferred should be considered. Set-off cannot be made upon the proposition of the court. The court is strictly prohibited from making set-off unless it is raised.

Parties do have freedom of contract about set-off with regarded to obligation they assumed reciprocally. Parties may wave their legally permitted right to require set-off. Article 1839 to this effect has provided that the debtor may in advance waive his right to make set- off. Freedom to wave set off encourages further transaction between parties who have unsettled obligation.

Freedom of the parties is not only to waive their right to set off but also to extend set-off beyond the legally possible ones and set aside certain conditions. Article 1840 permits occurrence of set-off even though it is not provided by law if the parties agree. Legally it is money debts or tangible things, which are subject of set off. However, parties can specify conditions of set-off, otherwise setting aside the legally provided conditions.

The effect of set-off is then extinction of obligation. Although set-off extinguishes obligation, its extinction effect is limited to the lesser amount regarding debts subject of set-off.

This might cast doubt if the right to refuse part payment might not be applied in the case of set-off in light with the extinction effect of set-off to the extent of the smaller debt because if set-off is effective to the lesser amount, the one who is entitled to a greater amount might not refuse set-off although part of his claim is to be extinguished. He can, however, refuse part payment.

Set-off and payments are not the same although both are grounds of extinction of obligation. Set-off is not mode of payment. This can be exemplified by the validity of set-off made with an incapable person and invalid nature of payment made to incapable person unless it is proved that the incapable benefited.

Contracting parties are not allowed to set-off their debts if it is going to affect the rights of third parties. Extinction of obligation by set-off "*shall not affect rights which third parties have on one of the debts*." Extinction of obligation has effect only between the parties who make set-off.

Appropriation of payment in the case of set-off has been provided in Article 1835 of the civil code in its wording as: "Where several debts liable to set-off are owing from the same person, the set- off shall be made in accordance with the provisions of chapter 2 of this Title relating to appropriation of payments" (Art. 1752-1754 of the C.C).

When set-off is made with a person who has claims related to costs, interests and principal debt, set-off extinguishes first the cost, then the interest and finally the principal debt pursuant to

Article 1752. When set-off is made against a creditor who has several claims, the debtor who wants to effect set-off may specify the debt which is extinguished by set-off. However, if the debtor, who effects set-off, does not exercise his right of specifying the subject of set-off, the person who has several claims may specify the subject of set-off among his several claims according to Article 1753.

When both parties do not specify the subject of set-off among the several claims, the law fills the gap as provided under Article 1754. Accordingly, the debt which is due or where none of them is due, the debt which shall first become due shall be subject of set-off. When there are several debts which become due at the same time, the debt which is of greater advantage to the debtor shall be extinguished by set-off. As far as debts which are of the same advantage to the creditor are concerned, such several debts shall be extinguished proportionally.

1.7. Merger

Merger happens when the position of creditor and debtor becomes one and the same. There are different reasons for merger between debtor and creditor. Successions, formation of partnership are among the juridical acts which result in merger. Merger makes the debtor and creditor the same person.

Extinction of obligation on the account of merger has certain limitations in its effect of extinction of obligation. The limitation is when it affects the right of third parties. Merger shall not be made to the prejudice of the interest of third parties, which have a right on the debt.(see art 1843).

The protection of the right of the third party gets its strong support from the privity principle provided in the definitional provision of Article 1675, 1731 (1) and 1952 (1). Third parties may have a right on the credit which is subjected for extinction by merger. The right of third parties shall be protected to avoid the externality effect of merger. When third parties who have usufruct right or pledge on the credit, such right is not subject of extinction though the main obligation on which such right depends could be extinguished by merger.

Merger has certain peculiar characteristics, as obligation extinguished by merger might revive in certain circumstances.

1.8. Limitation of action

Under the Ethiopian law of contract limitation of action has been put as one way of extinction of obligation. Making period of limitation a means of extinction of obligation creates security of business transaction eroding uncertainty among contractants. Period of limitation also avoids bafflement which might be created owing to loss of evidence when time lapses. Its deterrence impact on dormant contractants is also considerable purpose of extinction of obligation by period of limitation after which the party will not be compelled by the undertaking in the contract. The problem related with loss of evidence after the lapse of a considerable of period of time is also avoided by period of limitation or prescription.Prescription can be either acquisitive or liberative. Acquisitive prescription entitles the beneficiary with certain right after the expiry of certain period of time.Liberitive prescription relieves the beneficiary from certain obligations after the lapse of certain period of time.In liberative prescription there can be limitation of right and limitation of action.Limitation of right absolutely extinguishes the right of the other party while limitation of action extinguishes the right to bring action i.e. court action. The Ethiopian law of contract under Article 1845 provides the principle of period of limitation.

According to this provision “action for performance” refers to bringing a court action to effect performance, “action based on non-performance of a contract” refers to bringing court action aimed at remedies of non-performance like damage, cancellation and even forced performance and “action for invalidation of a contract” refers to bringing court suit to have a contract invalidated. All these actions shall be barred unless brought forward within ten years.

Discussing whether period of limitation bars right or action is an issue worth discussing. In dealing with this, the title of the section where the provision is found connotes that it limits action. In addition to that the French version equivalent to this provision (Article 2262) limits all actions. There are also provisions that show the possibility of existence of certain rights even after the lapse of the prescribed time. Article 1850, showing that limitation does not bar the right exercised on pledge even when period of limitation bars the principal obligation, exemplifies such provision.

On the other hand, it is argued whether this provision limits all rights out of the contract albeit the indication of its title. Professor Rene David has put this position in his commentary as: “The Ethiopian code preferred the formula found in the Italian civil code which provides that all the

rights are subject to ten years limitation." He has confirmed this position denoting that the right created by the contract disappears by limitation; it can be asserted in anyway.

The other controversial issue in light of period of limitation is the relationship between Article 1845 and Article 1810. The time when period of limitation starts to count has been put under Article 1846 of the Civil Code as:

Art.1846__ beginning of period of limitation

The period of limitation shall run from the day when the obligation is due or the right under the contract could be exercised.

Period of limitation for action based on non-performance does not for example begin to run from the time of the formation of the contract unless performance shall be made immediately. If the time of performance of the contract is after one year from the formation of the contract, period of limitation runs one year from the formation of the contract as the obligation is due after one year.

Haziness, which can be created by way of assessing a year whether in weeks, days or hours, has been dealt with under Article 1848. Accordingly, the period of limitation shall run from the day when the obligation is due or the right under the contract could be exercised and is effective, excluding the day on which period of limitation begins to run. The action is barred upon the expiry of the last day without having been used.

Art.1849__Collateral claims.

Interests and collateral claims shall be barred where the principal claim is barred.

According to this provision, as a rule interests and collateral claims are barred when the principal obligation is debarred by period of limitation. This seems justified, for the collateral claims depends on the principal claim which is being barred by period of limitation.

When the collateral claim is a pledge, however, the pledgee may exercise his right on the pledged property pursuant to Article 1850 which says: *"A creditor whose claim is secured by a pledge may exercise the rights arising out of pledge notwithstanding that the claim is barred"*

There are two ways by which period of limitation is interrupted. These are recognition of the debt by the debtor and bringing of action or providing default notice to effect payment. These two ways have been stated in Article 1851 sub (a) and (b).

Art.1851__Interruption.
The period of limitation shall be interrupted where:
(a) the debtor admits the claim, in particular by paying interest or installments or by producing a pledge or guarantees; or
(b) the creditor brings an action for the debtor to discharge his obligations.

When the debtor recognizes the presence of debt by paying interest, installments, providing pledge or mortgage, the period of limitation is interrupted. When the creditor brings an action to effect performance, period of limitation is again interrupted. A court action interrupts period of limitation if it is communicated to the debtor. If the debtor is communicated, it is not necessary that the action be brought to a competent court. Serving notice to the debtor is enough to interrupt period of limitation. It must be born in mind that these ways by which period of limitation is interrupted are illustrations which might again include other ways like novation.

Interruption of period of limitation is of great importance for the creditor, as his right is not debarred. This effect of interruption of period of limitation has been indicated under Article 1852 as follows:

Art.1852.__effect of interruption.
(1) A new period of limitation shall beginto run upon each interruption
(2) Such period shall be ten years where the debt has been admitted in writing or established by a judgment.

According to this provision, a new period of limitation runs when there is interruption. A new ten years period starts to run. Assume for example Ato Abraham did not require performance for 9 years against his debtor. If Ato Abraham did ask performance or put the debtor in default, a new period of limitation starts to run. Then Ato Abraham can require performance again within ten

years after 9 years. He can then require performance within 19 years from the formation of the contract.

The court has discretion whether certain claim shall be barred by period of limitation or not when there is special relationship between the parties. Article 1853 empowers the court with the power of setting aside a plea of period of limitation if it is convinced that the creditor failed to exercise his right because of obedience or fear he feet of the debtor with whom he has special relationship.

Art.1853 __ Special relationship between the parties.

(1) The court may set aside a plea based on limitation where it is of opinion that the creditor failed to exercise his rights in due time on the account of obedience he owed to or fear he felt of the debtor to whom he is bound by family relationship or subordination.

(2) In such a case, third parties who guaranteed the payment of the debt shall however be released.

Chapter Two

Special Provisions Relating To Contracts

Limitation of action

1. **Meaning**

Period of limitation is also referred as statutes of limitations or period of prescription. It a period of time after which either right itself or the right to bring court action is barred.

2. **Types of period of limitation**

   Period of limitation could be either:-

   A. Acquisitive limitation or liberative limitation

   - Acquisitive prescription entitles the **beneficiary** with certain right after the expiry of certain period of time.

   - Liberitive prescription relieves the beneficiary from certain obligations after the lapse of certain period of time.

   B. Limitation which bar right or actions

There can be limitation of right and limitation of action. Limitation of right absolutely extinguishes the right of the other party and hence the right cannot be enforced in any manner while limitation of action extinguishes the right to bring court action but the right holder can assert it as counter claim or may invoke self help remedies if there are any.

There are different opinions on whether the civil code provisions dealing with period of limitation limit right or action or both. But from the following facts we can conclude that Ethiopian laws accept limitations of action as far as contractual obligations are concerned.

- Article 1845 is entitled limitation of action.
- Article 1850 recognizes the possibility of exercising a right on any available pledge even if the right of action is barred.
- Article 1809 provides that a party who was incapable or gave defective consent may refuse to perform even if his right of action to invalidate the contract is barred.

According to article 1845

® Action for performance refers to bringing a court action to effect performance whether it is forced or substitute performance.

® Action based on non-performance of a contract refers to bringing court action aimed at remedies of non-performance like damage and cancellation.

® Action for invalidation of a contract refers to bringing court suit to have a defective contract invalidated.

All these actions shall be barred if not claimed within ten years unless either longer or shorter period is provided by law.

As far as relation between article 1808 and 1845 is concerned the former can be taken as an exception while the later is a general rule. Therefore the action for invalidation could be invoked as long as the action to invalidate these acts is not barred by the limitation that extinguishes all actions.

3. Purpose of period of limitations

The main purpose of period of limitation is to protect the defendant. There are two reasons for this:-

a. To ensure certainty and predictability in transactions.

b. Whenever person is sued after long period of time he might have lost evidence necessary to disprove the claim.

4. **Beginning of period of limitation**

- **General rule:-**The period of limitation shall run from the day when the obligation is due or the right under the contract could be exercised.
- **Conditional rights:-**Conditional right cannot be exercised till the condition is fulfilled and it is then when period of limitation starts
- **Annuity:-**Annuity is a fixed amount of money payable to someone yearly or at other regular intervals. In annuities the due date of the payments is different. One payment is paid first and the following will be paid next. The Civil Code makes the time of the first payment a reference for counting period of limitation in respect of annuities.

  According to Article1847, all the rights are barred starting from the time when the first payment which was not made is due.

5. **Effect of period of limitation on principal and collateral obligations (1849 and 1850).** In principle interests and collateral claims are also barred when the principal obligation is debarred by period of limitation. This seems justified, for the collateral claims depends on the principal claim which is being barred by period of limitation. When the collateral claim is a pledge, however, the pledgee (creditor) may exercise his right on the pledged property even after principal obligation is barred.
6. **Interruption of period of limitation(**See 1851(a and b)

   There are **two** ways by which period of limitation is interrupted. These are:- **Recognition by debtor:-**Recognition of the debt by the debtor in any manner possible interrupts period limitation.From the wording of the article it can be understood that these ways by which debtor could admit debt are illustrations which might again include other ways.

   Action of the creditor:-Bringing of court action or providing default notice to effect payment interrupt period of limitation. A court action interrupts period of limitation if it is communicated to the debtor. If the debtor is communicated, it is not necessary that the action be brought to a competent court.
7. **Effect of interruption(1852,1853)**

A new ten years period starts to run when there is interruption.

8. **Special cases**

Special relation between parties:-The court has discretion whether certain claim shall be barred by period of limitation or not when there is special relationship between the parties.

Good faith:-Although the value of good faith has paramount importance in law of contract, bad faith of the parties is rarely considered in enforcing period of limitation. The beneficiary of period of limitation can raise period of limitation contrary to good faith.

Agreement of parties: - Period of limitation is a mandatory way of extinction of obligation and is not subjected to the agreement of the parties. They can never waive it in advance by agreement, nor can they fix period of limitation other than that fixed by law. It can, however, be waived after it has been due. (1855,1856).

Section two

Conditional contracts

1.1. What is conditional contract?

Condition is a provision making the effect of a legal instrument contingent upon uncertain events. So contract is said to be conditional if the existence of the obligations is determined by occurrence or non-occurrence of uncertain event. (See art.1869).

Uncertainty implies occurrence or non-occurrence of certain event or even uncertainty as regards the time of its occurrence.

Contract shall not be subjected to Unlawful, immoral or impossible conditions. If the condition is Unlawful, immoral or impossible it is regulated by applying provisions relating to the impossible, unlawful or immoral object of a contract, starting Art.1715-1716. Their consequence depends on the relationship of the condition and contract. If there is strong relationship the contract will be invalidated.

1.2. The effect of conditions

Providing a condition upon the fulfillment of which the effect of contract depends is one way by which contractants exercise their freedom of contract. Accordingly, contracting parties can make their contract conditional as a whole or one of its terms.

Condition determines the effect of contract in two ways. It either ends the effect of contract or makes the contract effective upon its fulfillment.

1.3. Type of conditions

There are two types of conditions.

A. Condition precedent (suspensive condition)(1871)

- The contract starts producing effect upon the fulfillment of the contract.

B. Condition subsequent (resolutive condition)(1872)

- The parties must clearly state that condition is condition subsequent.
- The contract starts producing effect immediately upon its formation and ceases to exist upon the fulfillment of the condition.
- The effect of the condition subsequent is cancellation of the contract
- Cancellation will have the effect of reinstatement (See art.1815).
- But there is no perfect expectation of damage as this cancellation is not owing to non-performance of contract.

1.4. Presumption in favor of condition precedent

- The parties must clearly state whether they are making their agreement on condition **precedent or condition subsequent**. If there is ambiguity whether the condition is condition precedent or condition subsequent the law presume that it is condition precedent.

1.5. Duty to refrain from acts which hinder fulfillment of the condition(1870)

- Parties must be in good faith so that the condition fulfilled as agreed.
- If the fulfillment of the condition is **hindered** by one of the parties and his act of hindrance emanates from **bad faith,** the condition can be presumed to have been fulfilled.
- Then the other party may require the right he would have acquired had the condition been fulfilled.
- The presumption is equally applicable to both condition precedent and condition subsequent.

1.6. Duty to refrain from acts which hinder performance (1873)

- This article is not clear whether it is referring to acts of the parties which hinder the fulfillment of the condition there by hindering performance or acts which directly hinder performance of the contract.
- But since the acts of the parties which interfere with the fulfillment of the condition has already been addressed under article 1870 this article should be referring to acts of the party which hinder performance of the contract after the condition fulfilled.
- So parties must refrain from acts like destroying, damaging or alienating the object of the contract to which condition is attached. Since these acts clearly prevent the normal performance of the contract.
- The article applies to both condition precedent and condition subsequent since it is equally important to prevent acts which hinder **performance** of the contract under condition precedent and acts which hinder **restitution** under condition subsequent.

1.7. Acts of management (1874) cum (Article 2204 and 2205)

- Parties are not absolutely excluded from any act with regard to the object of the contract subject to condition.
- Accordingly the holder has the right to take necessary measures to protect damage and depreciation and administer the thing.
- The acts of management shall be made in good faith. Acts of management made in bad faith are subjected to invalidation.
- If acts beyond management are performed, they are subject to invalidation by the other party.(1875)

1.8. Fruits and profits collected in good faith

- The party which exercises the right on the subject of the contract before the fulfillment of the condition is entitled to profits and fruits which he received in good faith before the fulfillment of the condition.

1.9. Protective measures by would be owner

- The actual holder of the good may do acts which affect the right of the other party before the fulfillment of the condition. In such cases the other party could take protective measure to prevent the occurrence of any actions which might imperil his right.

1.10. Liability for non performance

Conditional contract where:-

- The fulfillment of condition solely depends on the will of the debtor or
- The liability of the debtor for non-performance of the contract is excluded is not valid.

Section two

Alternative obligations

Alternative obligation happens in a contract when the debtor is to discharge one among different obligations.

2.1. The right to choose obligation to perform

- Unless there is contrary agreement, it is the debtor who is entitled to choose what to perform.
- If the debtor failed to exercise his right to choose after he received default notice to choose the obligation which shall be performed then the creditor can choose what to be performed for him.
- If the creditor failed to exercise such right the right is reserved to the debtor.

2.2. Obligation become impossible

- If one of the obligations becomes impossible then the debtor should perform the other obligation.
- If impossibility is owing to a fault of the party that is not entitled to choose, damage is required to be paid to the party that is entitled to choose.

Section Three

Earnest

3.1. Meaning

Earnest is something of value given by a buyer to a seller to bind bargain.

3.2. Effect of earnest

Unless otherwise agreed

- Earnest is considered as part of performance of the main obligation.
- When the contract is performed, the party to whom earnest is paid shall return it to the other party or deduct it from his claim.

- It entitles both parties the right to cancel the contract upon either forfeiture of the amount of the earnest paid or paying double amount of earnest.
- Note:-Cancellation is the right given to party who is victim of non performance. But under earnest cancellation is exercised by party refusing performance.

Section four

Provisions as to liability

Parties can either extend or limit their liability subject to the legal limitation. But Contractual sanctions which are not specific enough are seen with suspicion. Consequently, such contractual sanctions are subjected to court verifications.

4.1. Agreement to Extend liability

- Force majeure is a defence for a claim based on non performance under article 1791(2).
- But the parties can agree to extend their liability even in the presence of force majeure and may fix the amount of damages which will be due (1886 cum 1889).

4.2. Agreement to limit liability

- Parties may agree not only to extend but also to limit liability due to non-performance.
- Article 1887 to this effect says" *the parties may limit their liability under the contract and provide that they will not be liable unless they commit a fault.*"
- In principle the absence of fault is cannot be raised as a defense to pay compensation for non performance. But parties may agree that they will not be liable to pay compensation unless they commit fault.
- They cannot, however, exclude liability of non-performance because of fault as it encourages deliberate breach of contract.
- Parties can however specifically exclude liability owing to the fault of their employees or auxiliaries as long as it is not to the prejudice of a party who is employee of the other party.

4.3. Validity of penalty clause

- Parties can fix penalty clause either in the main contract or in a separate document.
- If the penalty for non performance is terribly high and backed up by condition that renders the party in unequal bargaining power, it could be invalidated on the account of

unconscionable contract pursuant to Article 1710 or to rectification pursuant to Article 1812.

- A penalty clause which is made owing to mistake, fraud, duress and undue influence or which is illegal is also subjected to invalidation provided that the grounds which foster invalidation are fulfilled.

4.4. Effect of invalidation of either the main contract or the penalty clause (see art.1894)

- A penalty shall be of no effect where the contract in which it is prescribed is invalidated.
- A contract shall remain in force notwithstanding that the penalty is not valid. According to this provision invalidation of the contract is a precondition for the penalty clause to be of no effect.
- But what if the party who has a right to invalidate the contract simply opted to refuse performance rather than requiring invalidation? Will the penalty clause still lose effect?

4.5. Right of the creditor to choose either performance or penalty

- Fixing of penalty does not imply the discretion of the debtor either to perform or pay penalty.
- It is rather the discretion of the creditor either to require performance or effect penalty for non performance unless the parties clearly deprived the creditor of such right by agreement.
- The creditor cannot require both enforcement of the contract and the penalty unless penalty was provided in respect of delay or the non-performance of a collateral obligation.
- According to article 1890 is there any prohibition on parties' right to provide penalty along with forced performance? Actually, unless there are business inexperience, necessity, senility and other instances that render the other party in a position of unequal bargaining power, and the contract become unconscionable contract, the contract is valid and they can agree as they think fit.

4.6. When do penalty clause enforced?(1891 cum 1801)

As a principle the following conditions must be fulfilled to enforce penalty clause:-

- There shall be non performance.
- There shall be actual damage as a result of non performance.

- A person who could not have damage as a remedy of non- performance cannot be entitled to payment of penalty.
- The creditor must put the debtor in default unless the contract is of nature which does not require default notice. Default notice is not required to require remedies for non performance if:-
    - ® A debtor assumed negative obligation (obligation not to do).
    - ® The assumed obligation is required to be performed only within a fixed period of time and that period expired.
    - ® The debtor declared to the creditor in writing that he would not perform the obligation
    - ® There is express agreement that the creditor can require remedies of non-performance without giving default notice.

4.7. Exception to principle of "actual damage". (See article 1892).

- There shall be penalty even in the absence of actual damage.
- Actual damage instead of penalty can be required if the damage is caused intentionally or with gross negligence or grave fault.

4.8. Role of courts on penalty

- The underlying reason to provide a penalty clause is to be certain as to the remedies of non-performance. Consequently, the role of the courts in varying the penalty is limited to protect the required certainty of the parties. So court can vary the penalty clause only if there is partial performance.

CHAPTER THREE

Plurality of Debtors or Creditors

3.1. Civil and common law approach

Obligations in which there is either more than one debtor or creditor are called ***Solidary obligations*** in Civil law and ***joint and several obligations*** in common law legal system.

In common law legal system there are three categories of obligations

A. Joint promise/obligation/
B. Several promise/obligation/

C. Joint and several.

(For details on these types of obligations please refer to discussion on types of obligations on law of contract I)

Solidary obligations are divided into two

- Those which are contracted in favor of several creditors(active solidarity) and
- Those which are contracted by several debtors (passive solidarity).

In both Solidary obligation and joint and several obligations each solidary debtor binds himself for the whole obligation with the result that performance by one debtor discharges the other debtors.

3.2. Solidary obligations under Ethiopian Law: Case of plurality of debtors (1896-1909))

- An obligation is said to be joint and several (solidary obligation) among the debtors when each debtor is considered in his relation with the creditor as debtor of the entire performance (as if he were the only debtor) or where both debtors are jointly liable for the whole debt.
- Each solidary debtor or both solidary debtors, in so far as the creditor or creditors are concerned, is/are the debtor (s) of the entire amount individually (severally) or jointly. (see article 1896 & 1897).
- Hence Creditor of a solidary obligation has an advantage in that he may obtain payment from any solidary debtor.
- Each debtor is held liable until the obligation is fully discharged. The same debt may be required, be it divisible or indivisible, from only one of the co-debtors.
- The creditor has the discretion to select the most solvent debtor and ask everything from such debtor.
- This implies that failing an express provision to the contrary, the very fact that there are two or more debtors makes them jointly and severally liable to perform the obligation.

3.3. Sources of Solidary obligation (Joint and Several Obligations)

There are two sources of joint and several obligations

A. **Contract:-**Joint and several obligations is an automatic by-product where a contract involves several debtors.

B. Law:-The law itself might impose a joint and several obligations in various cases. For instance in the case of the debts contracted by spouses, for persons jointly held to pay maintenance (Article 819) etc.

3.4. The effect of joint and several obligations on the relations between creditor(s) and co-debtors

- All the effects derive from the principle that each of the co-debtors, taken separately, is bound towards the creditor so completely and absolutely as if he was the only debtor.
- This representation, which serves primarily the interests of the creditor towards the several co-debtors, serves likewise the interest of the debtors against the creditor.

This mandate has different effects on relation between the creditor and co debtors on Resjudicata,Default notice, void and voidable contracts, remission of debt, Novation,set off and Merger.

A. On Resjudicata(1898)

- An action brought against one of the co-debtors shall be no bar to an action which may be brought against the others so long as the debt has not been fully discharged. The creditor has the liberty to pursue successively all his debtors as long as the obligation is not fully discharged.
- So the action of the creditor against one debtor does not amount to a waiver of the actions open against the others later.
- Conversely, the in admissibility of the action against one debtor is no bar on the links to the other debtors.
- He may prosecute different debtors before different courts if necessary.
- But the creditor who has instituted a court action against one joint debtor is precluded from proceeding against the same person. This is implied from the phrase "other debtors".

B. Default notice(1899)

- Creditor who has a right to demand performance from co-debtors is required to put the debtors in default to claim rights arising from the non performance of the debtors unless it is unnecessary according to Article 1775 of the Civil Code.
- Accordingly since co-debtors represent each other in their collective relations with the creditor a default notice putting one of the co-debtors in default implies that such notice

is deemed to have also been given to the other co-debtors.The notice sent to one transfers risks for all debtors.

A) Void and voidable contracts(1900)

- Sub-Article one refer to void contracts while the second sub Article relates to contracts which are voidable.
- Accordingly defenses which based on (1900(1) constitute ***common defense*** while defenses based on (1900(2) constitute ***personal defense***.

  Please try to distinguish what constitute common defense and personal defense!

B) Payment and limitation of action(1901)

- Where there has been a total or partial payment or where the claim of the creditor is barred by limitation, each debtor may invoke this as a defense according to Article 1901.
- If payment is made by one, being the same debt, all are released in respect of the creditor. In case of particular payment by one of the co-debtors, however, the obligation will be reduced to the extent of the payment made by the co-debtor.
- Total payment and limitation of actions bar the total obligation.
- Payment and limitation of actions are common defenses that are available to all the co-debtors.

C) Remission of debt(1902)

Remission of debt may be absolute or relative in accordance with Article 1902 of the Civil Code. In this regard,

- If the creditor remits the debt to all co-debtors the obligation is extinguished and all co-debtors are released.
- Where the creditor remits the debt to one of the co-debtors, then all the co-debtors will benefit from such remission as they are released from the obligation to the extent of the remitted debt.
- If creditor has *expressly* stated that the debt is remitted for the exclusive benefit of one debtor the remission will benefit only that debtor and the creditor has a right to collect from the others less the amount he has remitted(1902)(3).
- So there is rebuttable presumption that debt remitted will release all co debtors unless expressly stated.

D) Novation

In case where the creditor agrees with one of the co-debtors to substitute a new obligation for the original one, then provisions of Article 1902 will *mutatis mutandis* apply.

- Accordingly where novation occurs between one of the co-debtors and creditor, all the other co-debtors will be released from their obligation.
- The creditor may limit the effect of the novation to only one of the co-debtors. He can do this by expressly specifying that the novation will only apply to the share of that co-debtor.
- Where this occurs in accordance with Article 1902(3), the remaining co-debtors will remain liable to the creditor but their liability will be reduced to the extent of the share of the co-debtor who has agreed with the creditor.

E) On set off *(1904)(read both versions together)*

Co-debtor who is owed by the creditor to invoke set-off and the other co-debtors can plead set-off to the extent of the obligation of the debtor who is owed by the creditor.

F) Merger(1905)

- Merger between the creditor and one co-debtor does not release the co-debtors unless the debt should have ultimately rested with the beneficiary of the merger.
- If there is merger, on the debt between one co-debtor and creditor, the portion of the common debt that relates to one of the co-debtors will no longer exist.
- Accordingly, the new creditor, the co-debtors will no longer exist. Thus, the new creditor, the co-debtor whose debt is merged with the previous creditor, may demand payment from the remaining co-debtors less the amount that relates to his share.

3.5. **The Relation of the co-debtors inter se(1906 and 1909)**

Firstly,

- Where several debtors are bound jointly and severally for the performance of one and the same obligation, they are duty bound to promote ***the betterment of the condition of*** **all** of them by abstaining from doing anything which might aggravate the situation of the other co-debtors and raising any defense that is available to all co-debtors.

Secondly,

- The fact that each debtor is held liable for the performance of the whole obligation in his relation with the creditor does not prevent the common debt from being divided.
- Accordingly in the absence of contrary stipulation by law or agreement the co-debtors will equally share the common debt after payment. This presumption may, however, be rebutted.

Thirdly,

- In so far as each debtor is liable to contribute to the extent of his part in the common debt, a debtor who has paid in excess of his share will be entitled to a right of recourse against the remaining co-debtors for the excess amount in proportion of their share.
- Where one of the debtors is insolvent, the risk is assumed by the others who pay his share, again in proportion of their own (Article 1908(2)).

Lastly,

- A debtor who has paid in excess of his share will be entitled to a right of recourse against the other co-debtors who have not yet paid their shares. Such action is what is called the legal right of ***subrogation*** as a result of which such paying debtor will be placed in the position of the creditor to the extent of the amount paid by him to the latter.
- The creditor is legally required to hand over any document and make available all information to the paying debtor to enable the latter to claim from his co-debtors. If the creditor fails to discharge this legal duty, he is subject to the payment of damage arising from his failure.

Defenses open to joint debtors

Common defenses	**Personal defenses extended to all**	**Purely personal objections**	**Debt finally rest with other debtor**
• Total or partial payment • Absolute nullity • Remission of debt to all co-	• Remission of debt to one debtor 1902 (1) • Novation 1903(1)	• Incapacity • Vice of consent • Condition • Specific remission 1902 (2) • Specific	• Remission of debt 1902 (3) • Set-off 1904 • Merger 1905

debtors • Limitation • Liability 1906 (2)		Novation 1903 (2) • Set-off 1904 • Merger 1905	

Chapter Three

Part II

2.1. Joint creditors

When more than two persons are making a contract, the co-debtors are presumed by the law, unless otherwise agreed, to be jointly and severally liable (Article 1896). On the other hand, co-creditors are presumed to be simple joint creditors (Article 1910).

According article 1910

- Each co-creditor is only entitled to claim his share of the total claim and cannot claim the totality of the claim.
- But either law or agreement may allow co creditors to claim totality of the claim.

There are different opinions on the relationship between article 1910 and 1911.The persuasive argument is that article 1911 is a guideline to be followed where either the law or agreement provided that co-creditors are jointly and severally entitled to claim total payment.

So according to article 1911

- Creditors are jointly and severally entitled to claim payment.
- The debtor can choose any one of the co creditors and pay the whole debt.
- But when there is any judicial or extra judicial demand of payment by one of the creditors, such creditor should be paid first.
- In such cases the debtor may not plead the benefit of division of the payment. Accordingly, the debtor may pay the entire debt to any of the creditors and such payment extinguishes the obligation of the debtor.

Any act interrupting the period of limitation as regards one of the joint creditors interrupts it for the benefit of all the joint creditors (see art.1912 cum with 1851 of C.C).

There is a mutual representation among the co-creditors. So if one of the co-creditors gives default notice for the debtor; the effect of such notice is to benefit all the creditors.

There are *limitations* on the power of each creditor to represent the other joint debtors. Accordingly:-

- One of the co-creditors cannot remit the whole debt on behalf of other creditors.the remission will be effective only as to the part of the joint creditor who effected the remission (Art. 1913)
- A joint creditor does not have the mandate to enter into a novation agreement with regard to the entire credit.Any novation agreement made by a joint creditor will have effect only with respect to the share of that creditor (Art.1914).
- However, where the other joint creditors have consented to the novation, it may have effect as regards such consenting creditors.
- The debtor may invoke set off against the other co-creditors only to the extent of the share of such creditor (1915).
- A joint creditor who is paid more than his share must then distribute the surplus between his co-creditors, in proportion of their respective shares.
- In the absence of contrary stipulation by law or agreement between co creditors the principle is that of equality of shares (1916).

2.2. Obligations other than joint obligation

The mere existence of plurality of debtors or creditors is not sufficient to conclude the obligation to be of joint and several obligations. There may be situations where there is plurality of debtors and/or creditors regarding an obligation that is not joint and several one. The Obligation may be divisible or indivisible.

A. Indivisible obligation

An obligation is said to be indivisible where it is impossible to divide or separate because of its nature. But nothing prevents the parties from stipulating that a given performance will be

indivisible even if it is divisible by nature. Indivisibility is either absolute or relative. Thus, where the obligation is indivisible; it cannot be executed in part, but must be performed altogether. So if there exist a plurality of debtors whose obligation is to perform indivisible obligation, the situation is de facto very close to a joint obligation and provisions governing joint obligation shall apply by analogy.

I. where there are several debtors

- The co-debtors must necessarily execute the obligation at one time.It follows that each one of the co-debtors can be sued for the total debt or obligation.
- Where the obligation is fully discharged by one of the co-debtors, the obligation is validly discharged. Accordingly, the creditor has no right of recourse against the other co-debtors.
- Actions effected against one of the co-debtors preserve fully the rights of the creditor against all.(See Art.1899 cum 1917 C.C).

In general, the provisions dealing with jointly and severally liable co-debtors are applicable for those co-debtors whose obligations are indivisible by its own nature (see Art. 1896 through 1909 cum 1917).

II. Where there are plurality of creditors (see 1910-1916 cum 1917)

- Each creditor may demand performance of the obligation in full and may validly discharge the debtor.
- However, each creditor may not be entitled for remission of entire debt or make novation agreement over the total debt.
- If this happens, the debtor remains bound to the other creditors, deductions being made of the part of the one who dealt with him.
- Nevertheless, interruption caused by one of the creditors, and suspension of prescription established in favour of one of them, benefits all others.
- If one of the creditors received the payment, he is required to reimburse the extra amount he received.

B. Divisible obligations

I. Where there are plurality of debtors(see art.1918)

An obligation is said to be divisible where it is neither joint nor indivisible (where it could be performed by individual debtor dividing into parts).

So if the obligation is divisible:-

- Debt is to be divided into as many fractions as there are debtors.
- Unlike the case of joint obligations, there is no representation among the co-debtors.
- Debtor may only be held for his own share as may be prescribed by law or by agreement.
- If one of the debtors has acted as a surety and guaranteed the performance of the obligation by the principal debtor. Such debtor will be held liable for his own share in the debt as well as for that of the debtor whose performance he guaranteed.
- Acts interrupting the period of limitation directed against only one of the debtors cannot be asserted against the other debtors.
- The risk of insolvency of one of the debtors is assumed by the creditor and not by the other debtors.
- Where the divisible obligation is accompanied by a penalty clause, the penalty is incurred by the debtor who breaches the obligation and only for the portion of the principal obligation for which he is bound.
- The default of one of the debtors is absolutely without effect as to others.
- A remission of debt made by a creditor to a co-debtor will only have effect with regard to the share of such debtor. The remission does not profit nor burden them, because their obligation is divisible.
- Lastly, a novation agreement made between a creditor and a co-debtor will release only such co-debtor, but no effect with respect to the other co-debtors.
- Each debtor of a divisible obligation will only be liable for his own share, which of course is not necessarily equal to that of the others.

III. Where there are plurality creditors(see art. 1919)

In respect of creditors, the divisible nature of the obligation means that each creditor may only claim his share of the obligation or such other shares as may be determined by contract or by law.

The basic principle underlying divisible obligations among several creditors is that the portion of the various creditors in a divisible obligation are to be considered as being as many distinct credits as there are creditors. Based on this principle, the following principles arise.

- Each creditor may claim only his respective portion of the debt that is determined based on the contract.
- Acts interrupting a period of limitation proceeding from only one of the creditors do not benefit the other creditors.
- Moreover, remission of debt, novation, set-off applies only to the creditor who is making them.