

❖ Effects of Contracts

- The legal consequence of a validly formed contract
- Principles of freedom of contracts and sanctity of contracts
- the widely accepted general principle is that one is free to enter into or refrain from entering into contracts. But once he has entered into it, it is enforceable under the law-*Pacta sunt servanda, a man's word is his bond, failure to keep a promise is worse than loosing a descendant (moral principle)*
- But contract is binding not only morally but also legally once the parties have show an unequivocal intention to be bind by the obligation they wish to undertake
- Pacta sunt servanda is not an absolute principle for the following reasons:
 - o Non-performance due to events beyond the parties' control (*forcemajuer*)
 - o contracting parties are bound not only in their words expressly stated in the contract but also to implied terms and incidental effects which of effective interpretation is to be left for the judges as in the sense of Article 1713 of the civil code
 - o Finally a contract shall be effective when the contracting parties are subjected to the imperative provisions of the law, while determining the object of the contract. Since mandatory provisions of the law cannot be set aside by the contracting parties; they limit the parties' freedom in contracting.

❖ Interpretation of Contracts

- The means to arrive at the true meaning of the contract.
- Contracts are law for the parties and are subject to interpretation
- When the provisions of a contract are not clear, interpretation is required to ascertain the terms of the contract.
- Article 1732 establishes the role of good faith in the interpretation of contracts. Good faith is referred to imply terms into a contract. In addition to that, reference should also be made to good faith in the interpretation of a contract: 'contracts shall be interpreted in accordance with good faith, having regard to the loyalty and confidence which should exist between the parties according to business practice'.

- Interpretation of contracts basically involves discovering the common intention of the parties. To that effect, the behavior of the parties before and after the contract is taken into account. On this point, Article 1734 provides ‘where the provisions of a contract are ambiguous, the common intention of the parties shall be sought’ and ‘the general conduct of the parties before and after the making of the contract shall be taken into consideration to this effect’. And it should not be the intention of one party but both.
- Example:

❖ **Question: What if interpretation is prohibited by legal provision? (Example Article 1922, 1828)?**

- Invalidation
- Declaration of nullity

❖ **Approaches:**

- Formation and interpretation are influenced by objective and subjective theories of contracts.

o **Objective:/English Courts**

- Gives emphasis to contractual assent that is “determined by analyzing external evidence”. So it is based on communication and not by cognition.
- Looking in to what the parties have said, done, expressed.
- Interpretation of vague and ambiguous terms are made by examining what the parties have said, wrote or did and not what they actually intended to say, write or do.
- So courts will apply an objective test to determine what meaning should be given to the vague terms.
- The basis is economic consideration and the main concern is security of commercial transactions.
- Great uncertainty will be created if men appeared to have agreed to certain terms could escape liability by claiming that he/she had no real intention to agree to them.
- The major consequence of this approach is the presence of Parole Evidence Rule. the written instrument is conclusive evidence. (Article 2005 of Eth. Civ. Code)

o **Subjective:/French Courts**

- Subjective assent has little to do with external perceptions, but rather is concerned with whether the parties each subjectively intend to make the contract
- Searching for the real/actual intentions of the parties. Correcting imprecise terms or incorrect figures where necessary.
- Concerned with the actual meeting of minds or literal intentions of the parties.
- External manifestations of assent are merely taken as evidence of the actual intent of the parties.
- It promotes freedom of contract: parties should only be bound when they clearly and subjectively intend to be bound by the contract.
- If the real intentions of the parties cannot be ascertained with sufficient precision, then Civil Law courts (French) declared the contract null.

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- ✓ Are the two theories mutually exclusive? Rules of equity in English Law allow some correction of contracts to give effect to the true intentions of the parties; while the difficulty of discovering real intention on the other hand leads a French Judge to give primary attention to the declaration of the parties.
- ✓ So the two approaches may not be mutually exclusive.
- ✓ Judges are not endowed with divine power to know what the parties really intend in entering to a contract. It is also difficult to know whether parties have changed the true intention they had after the making of the contract.
- ✓ Courts do not love an objective theory of contract or apply it in the process of interpretation merely because it is objective. They apply it only when they find in fact that one of the parties understood the words of an agreement in harmony with such interpretation and that the other party had a reason to know that he did"
- ❖ Ethiopian Law is a kind of compromise between the two
 - Two Guiding Principles under Ethiopian Law on Interpretation of Contracts:

- o Limitations on judicial interpretation, and
- o Common intentions of the parties
- **Literal Interpretation:**
 - o Article 1733 provides that when the provisions of a contract are clear, the court may not depart from them.
 - o The courts duty here is to determine the legal effect of the contract and not to interpret it.
 - o Inquiry into the actual intent of the parties is prohibited.
 - o The remedy for a person who claimed his intention is incorrectly stated is to require invalidation of the contract
 - o The court cannot make a contract under the guise of interpretation
 - o Justification:
 - Security of trade
 - Theory of declaration
 - o This is similar to the objective test that is used in Common Law.
- **Common Intention:**
 - o Once the term of the contract is found ambiguous the court is expected to interpret to find the true meaning.
 - o The main objective of interpretation is to discover the common intentions of the parties.
 - o This is in line with the subjective method of interpretation.
- **Interpretation in accordance with Good Faith:**
 - o Good faith should mean that no party to the contract intends to deceive the other party by intentionally making the provision of the contract vague, ambiguous, silent or contradictory.
 - o Had any party knew the problem, it would have been solved then and there
 - o No party wanted the problem of interpretation to arise but because of the above imperfections, interpretation becomes necessary.
 - o Article 1732 reaffirms the rule we discussed under Article 1713 together with the added guidelines of loyalty and trust in business relationships.

- o One will assume that the parties intended their relations governed by good faith, expected of a reasonable man
- o Good faith and usage are meant to fill gaps created by ambiguous words.
- o Usage is jurisdiction specific (Coffee growers in Sidamo n khat growers in Awaday)
- o Example: 1 kg. khat in Awaday and Bahir Dar
- **Interpretation in Accordance with General Terms**
 - o Example: Law Professor asked to teach economics
 - o Contract between American and Ethiopian for the sale of American's property. Later on the Ethiopian guy demands delivery of the American's property all over the world. Both parties in Ethiopia at the making of the contract and American guy has property in Ethiopia.
 - o You insured your Addis Ababa house on the basis of a declaration that "...you never had any fires before...". Later the insurer discovered that you had a fire accident on your house in Awassa ten years ago. So evidence of intention and insurance usage show that the term "...never had any fires" should be restricted to mean "in my insured house".
- **Interpretation in Accordance with the Context (Article 1736)**
 - o A stated '...i sold my furnitures such as chairs, wooden shelf, cupboard, and the *like* for 7000 birr to B. B later demands delivery of the bed, refrigerator, Television, Laundry machine, wooden buffet
 - o "A" has a small sanctuary whereby he used to protect certain species of animals; among them are bears, monkeys, apes etc. And an insurance company concluded a contract of insurance in that it will insure the liability A may incur by the zoo. In such cases, if there is a phrase which says "bear liability", does this mean the liability in respect of bears (those dangerous animals) or simply to say the synonym of to be responsible?

- **Positive Interpretation**

- o When there are two meanings for a certain word and one of them will make it effective and the other not, the court should give a meaning which will make the contract effective
- o This is relevant to secure the positive attitude of the society towards freedom of contract and contracts. If most contracts that come to the court are to be invalidated as result of negative interpretation, people may lose faith in the legal transactions,
- o It is in the general interest of the economy that contracts are implemented rather than open too many cases where they may be avoided
- o Policy wise also it is generally much better to try and bring contractual agreement to its end rather than try to reinstate the parties in their position they would have been had they not concluded a contract.
- o Eg. The principal (P) gives the Agent (A) a general authority regarding “*mans trade activity*”. Public Prosecutor says it is slave trade and human trafficking and the parties state that it is a business activity that any reasonable man can do. Which meaning should the court has to give?
- o But then, can the judge reconstruct or rebuild a clause which was badly drafted in order to give it a meaning? The answer is NO under Ethiopian Law. Articles, 1714(2), 1733 and 1763 of the civil code

- **Interpretation in favor of the Debtor**

- o *verba contra stipulatorem interpretenda sunt*
- o *It is only in case of doubt*
- o Rational behind for this rule:
 - The party who offers (stipulates obligations) makes more emphasis in securing his own interest
 - The element (terms) of the contract which led to doubt are inserted in the text of the contract are by the party who stipulates obligation

- **Partial Approach (Gratuitous Contracts)**

- o Gratuitous contracts shall be interpreted narrowly.

- o The benefactor is the only debtor of the obligation.

❖ *Rules of Interpretation Under Ethiopian Law: Summary*

- o **Discretionary:(1734-1737)**

- o The court may use any of them as it thinks fit.
 - Interpretation according to context
 - Interpretation in accordance with good faith and usage
 - Interpretation of general terms
 - Interpretation by reference to conduct
 - Positive interpretation

- o **Mandatory: 1738-1739)**

- o Are intended to be applied in the event no solution is found by the application of any of the other rules of interpretation.
 - Interpretation in favor of the debtor
 - Interpretation in favor of the adhering party