Contract law

Part II

Short note

by Lecturer; Boru

Chapter One

Extinction of Obligations

Cumulative reading of Art.1806 & 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.

- ***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 mandatoy provisions of the law if it shall extinguish contractual obligation.*

- **Invalidation and cancellation of a contract**: Invalidation of a contract happens when there is defect in the formation of the contract (Defect in consent & Incapacity).Cancellation on the other hand is making a contract ineffective when there is non-performance, (One remedy of non-performance of the contract).

  What do you think the difference in grounds and effect of invalidation and cancellation of contracts?

The effect of invalidation is 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 damages/compensation 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.(Payment of compensation shall be made for parties to reinstate them, when ever invalidation of acts done in the performance of the contract is impossible or inconvenient, (Art.1817 sub.2)).

The **ground** for invalidation is defect in its formation while the ground for cancellation is non-performance. 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. However, the damages/compensation 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.

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. Article 1808 (1) of C.C is provided to this effect stating in its wording:

*"A contract which is affected by a defect in consent or by the incapacity of one party may only be invalidated at the request of that party" (*Article 1808 sub.1).it is because to protect the interest of the affected party. The other party who is not affected is considered to have full information or rationality behavior. Hence, there is no reason to help him by empowering him to invalidate the contract. Representatives of the party, that is potential to be adversely affected by the invalid contract might be in a position of enforcing the rights of the party.

Capacity and consent do not, however, render a contract ineffective. These grounds rather entitle one of the parties the power either to invalidate the contract or give it effect. An invalid contract can result in the extinction of contract eventhough it is not invalidated. the reaction of contracting parties to a contract is not necessarily invalidation. Contractants can also resort to other options like refusing performance without having the contract invalidated.

Article 1809 denotes that a party entitled to invalidate a contract can refuse performance at any time. The contracting party can extinguish the obligation by refusing performance of a contract. The presence of invalid contract does not necessarily mean that the contract will be invalidated and the obligation will be extinguished. Article 1811 indicates "the party whose consent was vitiated may waive his right to require invalidation where the cause which vitiated his consent disappeared."

The right to invalidate a contract is, however, limited by lapse of a certain period of time. Article 1810 connotes that a contract shall not be invalidated unless an action to this effect is brought within two years from disappearance of the ground for invalidation.except, unconscionable contract for which the starting point is the formation of the contract. If the ground for invalidation is a mistake, two years from the knowledge of the misperception , if the ground is duress, two years from the avoidance of the threat, and if the ground is incapacity from the time the incapable becomes capable are the points where counting starts.

The party who has the right to invalidation is imposed with certain obligation aimed at protecting certainty as to the fate of the contract. Article 1814 entitles a party whose contract can be invalidated to require if his contractant intends to confirm or cancel or invalidate a contract. When such inquiry is forwarded for the party with the right of invalidation or cancellation, he is duty bound to respond. If the party fails to respond, the contract is presumed to have been invalidated. Failure to respond gives the other party the right to make a contract ineffective.

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." *Where a contract is invalidated or cancelled, the parties shall as far as possible be reinstated in the position which would have been existed, had the contract not been made. Acts done in performance of the contract shall be of no effect" (Art.1815).*

When the reason of damage is non-performance perfect expectation damage is understood. Compensation that puts the victim in the place he would have been had the contract been performed.

Acts done in performance of a contract shall not be invalidated where the interest of third parties in good faith requires (Art.1816).

Impossibility of restoring to the previous position,serious disadvantage or inconvenience of invalidation to cause to one or both parties are z situations in which z acts done for z performance of z contract shall not invalidated/cancelled, but via compensation restitution effect performs.

❖ Termination of contract:

Termination of contract is making the contract ineffective starting from the time of termination of the contract. Termination does not have retrospective effect; rather it has prospective effect. Termination of contract can be bilateral,or judicial.

A) Bilateral termination: an end to a contractual obligation by the agreement of both parties. Agreement to terminate is, a contract as a contract can be to extinguish obligation of proprietary nature, (Art.1675).

B) **Unilateral termination***: It is made either* ***by the effect of agreement;*** *when it is provided in the contract. &* ***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:** *Court termination is the principle and termination by the parties is an exception as parties shall not be judges on their own case.*

Cases in which contract can be terminated by the court;

1) **Cessation of *Special relation between the parties,Art.1823*:** If the previous confidence, cooperation or community of view that helps the continuity of the contract ceases, the contractual relationship might not be worthy upholding. In this case an application may be made to the court for termination.
2) ***Gratuitous contracts:*** *The court may order the termination of a contract made for the exclusive advantage of one party where the other party for good causes so requires (Art. 1824).*

Similarities and differences between invalidation and cancellation on the one hand and termination on the other: The basic difference between z two categories is their effect. The ground of termination is not again 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. In relation to the effect of the two categories as stated above, invalidation and cancellation have **retrospective** effect(Article 1815) while the effect of termination is

prospective(Article 1819 Sub (2) & (3)**).** . Invalidation, cancellation and termination are the same in that they extinguish contractual obligations.

- **Remission of debt:** Along with termination, remission of debt is also one way of extinction of obligation. Remission of debt is voluntary release of debtor of his obligation by the creditor.

  "Where the creditor informs the debtor that he regards him as released, the obligation shall be extinguished unless the debtor forthwith informs the creditor that he refused his debt to be remitted "(Art.1825).

- **Novation (Art.1826):**

Novation is substitution of an existing obligation by new obligation in its nature or object. Mere difference without substantial change either in the object or in the nature does not amount to novation; rather it is **variation** in fact.

Assume for example that Mr. Kemal entered into a contract with Lelisa to deliver 100 kilos of sugar in Addis Ababa. Later they agree to change the place of delivery to be Mekelle. After sometime again both parties agree delivery of 100 kilos of sugar to be replaced by 50 kilos of coffee. The change of place is not novation. Change of sugar by coffee is, however, novation as the object of the contract has been substituted.

Novation is required to be intentional *" Novation shall not occur unless the parties show the unequivocal intention to extinguish the original obligation." ,(Article 1828).* Replacement of certain obligation with other obligation in the absence of intention to make novation does not have the effect of novation.

Absence of novation, Article 1829; Unless otherwise agreed, novation shall not occur where;

a) *a new document is prepared to support an existing debt; or*
b) *the debtor signs a promissory note or bill of exchange in respect of an existing debtor*
c) *New securities are provided to ensure payment of an existing debt.*

1827- Effect of novation

(1) Unless otherwise expressly provided, securities or privileges attaching to the original obligation shall not be transferred to the new obligation.

(2) Unless otherwise expressly provided interest due prior to novation may not be recovered there after.

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 in accordance with the aforementioned provision.

- **Set off:**

  It is among the grounds by which a contract is extinguished.

Article 1831- principle; where two persons owe debts to one another, set off shall occur and the obligation of both persons shall be extinguished in accordance with the provisions of the following Article.

Set-off can be made upon the fulfillment of certain conditions. These conditions have been put as positive and negative conditions.

Article 1832–positive condition

Set off shall not occur unless both debts are money debts or relate to a certain quantity of fungible things of the same species and both debts are liquidated and due.

The conditions that are provided in Article 1832 are.

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

(b) The debts shall be liquidated.

(c) The debts shall be due.

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. 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. However, there is exception to the requirement of "liquidation" of the debt. According to Article 1841 eventhough one of the debt is not liquidated, the court may decide that set-off has been made to the extent of the admitted amount.

The other condition is that the debt shall be due at the time set-off is required. 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.

1833 Negative conditions

Set –off shall occur regardless of the cause of either obligation except where

a. *the special nature of the obligation requires that the creditor be actually paid , as in the case of maintenance or wages necessary for the livelihood of the creditor and his family; or*
b. *the obligation is owing to state or municipality ; or*
c. *The obligation is to restore a thing of which the owner has been unjustly deprived ;or*
d. *The obligation is to return a thing deposited.*

❖ Merger:

is one z grounds of extinction of obligation.

Merger shall occur and the obligation shall be extinguished where the position of creditor and debtor are merged in the same person,(Art.1842).

Assume Haile borrowed 25,000 birr from his father ; however his father died before collecting the debt. whileAto Haile is the only successor of his father

Merger shall not affect the rights which third parties may have in respect of the obligation (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.

*Art.1844,**End of merger**;The obligation shall revive where merger comes to an end.*

An illustration in which obligation extinguished by merger could be revived is for instance, if company X lent company Y Birr 2,000,000 but if the two companies merged into one before company Y paid its debt (merged). However, if the two companies split back to their original position, merger is said to cease and the obligation will revive on the debtor.

- **Limitation of action:**

  The last way by which contractual obligation comes to an end is limitation of action. along with prescription and limitation of right.

  Period of limitation is one classification of prescription that includes libertive and acquisitive prescription. **Liberitive prescription** relieves the beneficiary from certain obligations after the lapse of certain period of time. **Acquisitive prescription** entitles the beneficiary with certain right after the expiry 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.

Art.1845,,Period of limitation; Unless provided by law, action for performance of a contract, action based on non-performance of a contract and action for invalidation of a contract shall be barred if not brought within ten years.

Discussing whether period of limitation bars right or action is on issue worth discussing:

The title of the section where the provision is found connotes that it limits action. 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.

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 as all the *rights* are subject to ten years limitation under Ethiopian Law of Contract. He has confirmed this position denoting that the right created by the contract disappears by limitation.

The controversial issue in light of period of limitation is the relationship between Article 1845 and Article 1810.

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.

***Art.1847- Annuities; In respect of annuities, the period of limitation shall run from the day when the first payment not made was due*.**

If the remaining last day for the effect of period of limitation is a holiday, the action shall be debarred on the next working day. According David, at the very beginning of the day 6:00Am.

Principally period of limitation is one way by which obligation extinguishes. Extinction of principal obligation might have different effect on the collateral obligations attached to it.

Interests and collateral claims shall be barred where the principal claim is barred, (Art.1849).

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 by z creditor.

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.

Serving notice to the debtor is enough to interrupt period of limitation.

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.

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 according to Article 1854 of the civil code.

The parties may not in advance waive limitation nor may they fix periods of limitation other than those fixed by law (Art.1855). It can, however, be waived after it has been due.

The court shall not have regard to the period of limitation unless pleaded,(Art.1856).

Chapter Two
Special Provisions Relating To Contracts

The most frequent areas where the parties do leave gaps or agree less clearly are stipulation as to time, earnest, liability, alternative obligation and condition. These areas are to be discussed under this chapter.

Provision as to time:

Contractants may more probably provide the time of performance within certain period of time without specifically stating the time. They may also provide the time in certain number of weeks, months, or

ambiguously on first, last, or middle of a month. The presence of different days in months in Gregorian calendar and the presence of thirteen months in Ethiopian calendar might continually and unexpectedly create gap as to time.

Article 1858, destined to cover time fixed in days, states that the debt to be due on the last day of such period without including the day of the conclusion of the contract.

For example, Mr. Aragaw promised in a contract made on 5/3/2000 to perform his obligation in 7 days from the formation of the contract. The last date for the performance of the contract is on 13/3/2000. In counting the days 5/3/2000, the reference time, is not counted. That's why the last date is not 12 but 13.

Time in contract can be fixed in weeks. Article 1859 reveal the calculation of the period fixed in weeks. If the time is fixed in weeks, the day of the last week that corresponds by its name to the day of the formation of the contract is the due date.

To illustrate, assume Samson concluded a contract to perform his obligation on Monday Sene 1/3/1998. He agreed to perform his obligation after three weeks from the making of the contract. The due date is then Monday 22/1998.

When the time is fixed in months; Art.1860 provides; the last date is the day of the last month which corresponds the day of the making of the contract in number not in name.
For example, the last date for someone, who entered into contract on June 1, 1998 promising to perform his obligation within four months, is Oct 1, 1998. Sameness shall be in date not in name.

Sometimes certain dates of a month in Gregorian calendar might not have corresponding number in other months. In such case Sub Article (2) of this provision stipulates the due date to be the last day of the last month. The due date of someone who concludes a contract on October 31 to perform his obligation in four months is February 29. Normally the corresponding number shall be 31. But there is no such number in February. For example, assume that a contract was made on Hamle 10 and stipulated that the obligation will be discharged within four months. The due date is Hidar 10 without considering

Pagumen. It must be born in mind that contract a contract concluded on any day of pagumen is considered that it has been made on Meskerem 1 in the Ethiopian calendar.

Art.1861.Monthly periods: Where the period expires at the beginning or at the end of a month, such period shall expire on the first or on the last day of such month. Where the period expires in the middle of a month such period shall expire on the fifteenth of such month.

Art. 1862.Holidays: Where the period expires on a day which is holiday at the place of payment, such period shall expire on the next working day.

Art.1863.Lapse of time.:Where an obligation is to be discharged within a specified period of time, the debtor shall discharge his obligations before the expiry of such period.

He shall fix the exact date on which he shall discharge his obligations unless the circumstances are such as to show that the said date is to be fixed by the creditor.

In such a period of time the debtor shall discharge his obligation before the expiry of the period even though the last date is a holiday.

If insolvency of the debtor is established or if the debtor reduces the value of securities, benefit of time cannot be invoked against the creditor.

The creditor may not demand performance before the expiry of the agreed period unless such period was fixed for his exclusive advantage,(Art.1867).

Conditional Contractual Obligations

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.

"A contract shall be deemed to be conditional where it relates to an obligation whose existence depends on the occurrence or non-occurrence of uncertain event."(Article 1869*).*

The determinant event shall be uncertain in its meaning.Professor David has defined it broadly to include uncertainty as occurrence or non-occurrence of certain event or even uncertainty as regards the time of its occurrence.

For example, Ato Behailu is not sure if his brother is alive or dead though his absence is declared. He sold his house on condition that his brother is dead. This is a conditional contract though the event may have already happened.

Condition determines the effect of contract in two ways. It either ends the effect of contract (*Condition subsequent*) or makes the contract effective upon its fulfillment (*condition precedent*). Consequently, a condition can be condition subsequent or condition precedent.

Article 1871, condition precedent; unless otherwise agreed, the contract shall be effective as from the day when the condition is fulfilled. (This condition is presumed in the absence of agreement otherwise.*)*

Art.1872, Condition subsequent :(1).A contract whose cancellation depends on the occurrence of an uncertain event shall be effective forthwith. (2).It shall cease to be effective where the event occurs.

Condition subsequent or resolutive condition is uncertain event upon the occurrence of which the cancellation of the contract is carried out. The contract ceases to exist upon the occurrence of the event. The effect of the contract starts immediately after the formation of the contract.

The effect of the condition subsequent is cancellation of the contract upon its fulfillment. A thing sold on condition subsequent shall be delivered immediately after the conclusion of the contract and handed back if the condition is fulfilled.

Saying the effect of condition subsequent is cancellation takes us to the conclusion that the cancellation will have the effect of reinstatement.It shall, however, be born in mind that it will not be preceded by perfect expectation damage as this cancellation is not owing to non-performance of contract.

In addition to that, condition subsequent shall clearly put it as condition subsequent. Unless there is agreement that shows the type of condition the presumption is condition precedent.

The parties themselves can sometimes influence the condition, which determines the contract. In such a case, the party who does not want the fulfillment of the condition may prevent its fulfillment. Considering such behaviors of contractants, Article 1870 provides a remedy.

Article 1870,good faith: A party may regard a condition as fulfilled where the other party has prevented its fulfillment in a manner contrary to good faith.

Eventhough the condition is not fulfilled, if its fulfillment 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.

The provision is equally applied to both condition precedent and condition subsequent. The requirements which are provided in this provision are prevention of the fulfillment of the condition and bad faith of the party that prevents its fulfillment.

Eg1.Abebe entered into a contract with Senait to sell his house if he is employed. Later if Abebe refuses the employment having got the chance, Senait can require performance of the contract proving that he did it in bad faith.

Eg2. Abebe bought a house, which will be given back on repayment of the price if he did not succeed his father. At the time of succession he renounced the succession. Senait can give back the house on the presumption of the fulfillment of the condition eventhough he did not succeed.

A buyer of an immovable under condition subsequent and seller of immovable under condition precedent are in actual control of the immovable. The act of these persons might affect the right of their respective contractants by preventing regular performance or restitution. Before the fulfillment of the condition, they are not allowed to carry out any acts beyond management like alienating, investing capital, denoting and so on.*Acts beyond management done by the party who exercises the right may be invalidated where the other party requires (Art.1875).*

Eventhough the parties in actual control of a thing before the fulfillment of a condition are allowed to exercise acts of management they shall be in good faith. The acts of management shall be made in good faith.

Art.1876,Fruits and profits:The party who exercises the right prior to the fulfillment of the condition shall, where the condition is fulfilled, retain the fruits and profits he received in good faith prior the fulfillment of the condition

A party whose right might be affected by the parties in actual control can take protective measures pursuant to Article 1877.*Protective measures: A party whose conditional rights are imperiled may take such protective measures as he could take, were his rights not conditional.*

for obligation subject to condition fulfillment which solely depends on the will of the debtor. Such obligation is not valid. If, for example, a debtor promised to do something if he wishes, if it pleases him, the obligation is not a valid obligation.

Art.1879.Condition depending on a party;(1) An obligation assumed subject to a condition the fulfillment of which depends solely on the party who assumes the obligation shall be of no effect.(2) An obligation shall be deemed to be assumed under sub-art. (1) where the promisor's liability for non-performance of the contract is excluded in the contract.

Alternative Obligations

Alternative obligation happens in a contract when the debtor is to discharge one among different obligations. Article 1880, in principle, depicts that the debtor is released by performing either of the obligations provided in the contract. Unless there is contrary agreement, it is the debtor who is entitled with preferring the obligation to be performed pursuant to Article 1881(1). This is not, however, without limit in that "where the party entitled to choose does not exercise his right on being required to do so such right shall pass to the other party pursuant to sub-art. (2) of the same provision."

Earnest

Earnest is considered testament for the conclusion of a contract. There are, however, different positions as to whether earnest entitles a party the right to terminate a contract unilaterally. When we see the position held by the Ethiopian law, termination of promise guaranteed by earnest unilaterally is possible upon certain limitations.

It can be clearly inferred from *Article 1885* a contract secured by earnest can be cancelled unilaterally by either party. The party that cancels the contract shall, however, pay the amount of earnest. The party that has given earnest can cancel losing the right to get back his payment. The party that has received earnest can on the other hand terminate the contract paying double of the earnest.

The earnest paid in advance is considered to be part of the performance when the contract is performed. *Unless otherwise agreed the party who has received earnest shall return it or deduct it from his claim where the contract is performed(Art.1884).*

Discuss: Do you think earnest shows conclusion of contract?

Provisions as to liability

Provision as to liability is one of the ways where such gap filling provisions can be set aside. In doing so, the parties can either extend or limit their liability subject to the legal limitation of unconscionable contract.

Freedom of contract to determine penalty for non-performance discourages reluctance to enter into a contract owing to fear of non- performance. They can fix penalty clause either in the main contract or in a separate document.

The underlying reason to provide a penalty clause is to be certain as to the remedies of non-performance.

Article 1710 shall, consequently, be applied to limit the extent of the amount of damage at the time of non- performance of contract. If the penalty is terribly maximum and backed up by condition that renders the party in unequal bargaining power, it is subjected to invalidation on the account of unconscionable contract pursuant to Article 1710 or to rectification pursuant to Article 1812.

The validity of penalty clause is assured in light with the validity requirements of general contract provisions.

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, (Art.1894).

Fixing of penalty does not imply the discretion of the debtor either to perform or pay penalty. It is rather upon the discretion of the creditor either to require performance or effect penalty unless they clearly deprive the creditor of such right by agreement. One of them cannot refuse to perform to pay penalty unlike earnest where one of them can cancel the contract paying either double of the received earnest or the amount of earnest itself.

Art.1890, Right of the creditor:(1) Unless otherwise agreed, the creditor may require the performance of a contract which includes a penalty.(2) He may not require both the enforcement of the contract and the penality unless the penalty was provided in respect of delay or the non-performance of collateral obligations.

Let us illustrate this: Messebo Cement Factory and Sur Construction entered into a contract whereby Sur Construction will pay 100,000penality in case of non- performance. If Sur Construction Company fails to discharge its obligation, Mesebo Cement Factory can require either forced performance or penalty, but not both. If the 100,000 penalty was provided for failure of performance in due time or for failure of providing pledge, Mesebo Cement Factory can require both forced performance and payment of penalty.

Art. 1893,variation of penalty:The agreed amount of penalty due for non-performance may not be reduced by the court unless partial performance has taken place.

Article 1891 provides that "penalty shall be due whenever the creditor is entitled to claim damages(compensation) by reason of non-performance of the contract."

Article 1892, sets aside the condition to get compensation to be applied to penalty. This provision shows that *there shall be penalty even in the absence of actual damage.*

Actual damage which is more than the penalty and less than the penalty cannot be required. However, exceptionally actual damage (its amount grater than z penality) instead of z penality can be required if the damage is caused intentionally or with gross negligence or grave fault of z debtor (Art.1892).

The validity of a penalty clause can be affected by the validity of the main contract. Not Vice Versa.

Agreement that set a aside gap filling provision is made 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 the gap filling provision dealing with non-performance of a contract, there is contractual liability in the absence of fault unless it is force majuer as you remember in your contract law I. However, contrary to this, parties can limit liability by agreement. They cannot, however, exclude liability of non-performance because of fault as it encourages deliberate breach of contract.

The parties may provide that they will not be liable where non-performance is caused by a fault of their employees or auxiliaries. Any such provision shall be of no effect where it is made to the prejudice of a party who is employee of the other party.(Art.1888)

Illustration: assume for example Sur Construction limits its liability emanating from the fault of its employees. When the employer is relived of such liability, the employee might be held liable for more than the liability he would be liable had the employer been not relieved, since both the employer and employee are jointly liable. Such liability might then negatively affect the employee. Such negative impact of limiting of liability is of no effect with regard to the employee pursuant to Article 1888 of the civil Code.

Providing a gap filling provision for incidents which contracting parties do not predict is among the purposes of the law of contract. Provisions as to time are among the laws, which fill the most repeatedly happening gap in contractual agreement. Accordingly, when the time is fixed in days, the day of the formation of the contract is not considered in assessing the time. Time fixed in weeks is determined with reference to the corresponding name of the last week unlike the period fixed in months, which is determined referring to the corresponding day of the last month by number.

In addition to provisions of time, provisions dealing with condition also play gap-filling role. When a contract depends on the occurrence and non-occurrence of uncertain even, it is said to be a conditional contract. Condition may be condition precedent if the contract will be effective upon the fulfillment of the condition. It can also be condition subsequent if the contract is cancelled upon the fulfillment of the condition being effective before the fulfillment of the condition. The presumption is in favor of condition precedent.

CHAPTER THREE

PLURALITY OF DEBTORS OR CREDITORS

Solidary Obligation (joint and several liability) in Case of Plurality of Debtors

under the Ethiopian Law

An obligation is said to be joint and several 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.

Thus, each debtor is held liable until the obligation is fully discharged. unless otherwise agreed or provided by law, co-debtors shall be jointly and severally liable,(Art.1896).

Z effect of joint & several obligations on Z relations b/n creditor(s) & co-debtors

All the effects, among debtors, 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.

joint & several liability of debtors produces the following effects.

A) **On Resjudicata:** the action of the creditor against one debtor does not amount to a waiver of the actions open against the others later (Article 1898). Conversely, the inadmissibility of the action against one debtor is no bar on the links to the other debtors. Personal objections may not be extended from one debtor to the other. 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,(Article 1898).

B) **On Default notice:** a notice given to one is deemed given to all, and interrupts limitation (Art.1899). The notice sent to one transfers risks for all debtors. Co-debtors represent each other in their collective relations with the creditor.

C) **On void and voidable contracts:** where the contract is void(Object or form related problems), any of the co-debtors can raise this defense against the creditor(s).this defense is **common defense** available to all. On the other hand, where the contract is voidable (defect in consent or incapacity) this may not be raised by all the co-debtors. It is only a debtor who has the right to invoke invalidation of such contract that may raise it as a defense. Accordingly, the defense is said to be a **personal defense**. Among the common defenses that are available to all the co-debtors are payment and limitation of actions.

D) **On Remission of debt:** 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,1902.Be that as it may, the creditor can make the remission to benefit only one of the co-debtors and reserve his right against the others. In this regard, the remission will benefit only that debtor and the creditor has a right to collect from the others less the amount he has remitted. But this will be the case where the creditor has expressly stated that the debt is remitted for the exclusive benefit of one debtor and that his right against the other debtors is reserved, (Sub 3 ofArt. 1902). Thus, if the creditor does not expressly reserve his rights, the remission may benefit all the co-debtors.

E) **On novation:** in case where the creditor agrees with one of the co-debtors to substitute a new obligation for the original one,(where novation occurs between one of the co-debtors and creditor), all the other co-debtors will be released from their obligation. As is the case of remission of debt, the creditor may limit the effect of the novation to only one of the co-debtors. In such a case 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,(Article 1902(3)).

F) **On set off:** Article 1904 clearly allows the co-debtor who is owed by the creditor to invoke set-off. The issue, however, is whether or not the other co-debtors can invoke set-off on behalf of the other co-debtor. The other co-debtors can plead set-off to the extent of the obligation of the debtor who is owed by the creditor.

G) **On Merger:** Article 1905 states that, 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. 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.

The Relation of the co-debtors among themselves (Art.1906-09)

- they are duty bound to promote the betterment of the condition of all of them. Accordingly, a debtor is required to abstain from doing anything which might aggravate the situation of the other co-debtors. where the debtor fails to raise a defense that is available to all co-debtors,

then such a debtor will be liable to the other co-debtors. Such is the case where one of the co-debtors fails to raise limitation as defense.

- the co-debtors will share the common debt after payment. After the performance of the obligation, the obligation becomes divisible among the co-debtors.
- **right of recourse:**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 as per-Article **1908**.However, where one of the debtor's shares cannot be recovered, Sub Article (2) provides that such unrecovered amount is to be repaid by the other co-debtors in proportion to their share.
- **Right of subrogation;** 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 pursuant to Article 1909 of the Civil Code. 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. In such cases, 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.

Joint Creditors

Regarding joint creditors, the law takes a presumption against solidarity or joint and several entitlements. Article 1910 of the Civil Code states exactly the reverse rule from Article 1896 of the Civil Code: joint creditors are not jointly entitled to claim payment. Article 1910 provides that unless otherwise agreed or provided by law, joint creditors shall not be jointly and severally entitled to claim payment. It means the law presumes that, where there is plurality of creditors, each co-creditor is only entitled to claim his share of the total claim and cannot claim the totality of the claim. This presumption, however, will not operate where there is an agreement otherwise.

There is also mutual representation among the co-creditor. Thus, the situation of joint creditors can be analyzed along the same lines as that of the joint debtors, i.e. in terms of unity of the debt. The unity of the debt is considered under Articles 1911 and 1912. Each creditor may require payment of the whole debt, the payment to one amounts to payment to all, and any interruption of limitation benefits all.

Translated on the side of the debtor, it allows the latter to pay the creditor of his choice, at least until proceedings have been instituted by another, who then takes precedence.

The plurality of links can be seen in Articles 1913 and 1914 of the Civil Code, where a remission of debt or a novation granted by one creditor only affects this creditor's share. In the same sense, in the event of a set-off, Article 1915 of the Civil Code states that the debtor may only oppose such a defense to the extent of the creditor's ultimate share in the claim.Although each creditor is considered as a representative of the other, solidary creditors do not have the right to dispose of the entire credit individually. there is a limitation on the power of each creditor to represent the other joint debtors.

Firstly, no one of the joint creditors can remit the entire debt without the consent of the others. The remission will be effective only as to the part of the joint creditor who effected the remission.

Secondly, similar to remission, 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 as per Article 1914 of the Civil Code.

Thirdly, in case where the debtor becomes creditor of one of the co-creditors, the debtor may invoke set off against the other co-creditors only to the extent of the share of such creditor pursuant to Article 1915 of the Civil Code.

Lastly, where one of the co-creditors has collected the entire amount of the debt from the debtor(s), there arises an obligation on such creditor to render an account to his co-creditors. He is held liable to the others for the share in the obligation corresponding to them.

Non Joint 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 either indivisible or divisible. Indivisible obligation is treated under Article 1917 of the Civil Code and divisible obligation is treated under Articles 1918 and 1919 of the Civil Code.

Indivisible obligations: Indivisibility is generally a characteristic of the object of the obligation. For instance, a car is indivisible if this is the object of the obligation. The same applies to a given obligation to perform a service. If there exists a plurality of debtors, the situation is **de facto** very close to a **joint obligation**. Hence the rule stated by Article 1917 is the applicability by analogy of the rules governing joint obligations. Article 1917 provides that the provisions regarding joint obligations shall apply by analogy to obligations which are indivisible owing to their nature. Indivisibility of an obligation has its own effects in case of plurality of debtors and creditors. In this regard, Article 1917 which is the only Article dealing with such obligation simply provides that the provisions dealing with joint obligations are to apply by analogy to obligations that are indivisible.

Divisible obligations: The other type of obligation treating the concurrence of two or more debtors and, or creditors is the concept of divisible obligations. Article 1918, which deals with plurality of debtors to a divisible obligation, according to such provision, an obligation is said to be divisible where it is neither joint nor indivisible. Thus, the principle underlying divisible obligations among several debtors is that the 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. If the obligation is not a joint one but a divisible obligation, Article 1918 states that each debtor may only be held for his own share.From this principle the following effects arise. Firstly, each debtor is bound to pay, only his respective portion of the debt. But there may be a situation where one of the debtors has acted as a surety and guaranteed the performance of the obligation by the principal debtor.

Secondly, acts interrupting the period of limitation directed against only one of the debtors cannot be asserted against the other debtors.

Thirdly, the risk of insolvency of one of the debtors is assumed by the creditor and not by the other debtors.

Fourthly, 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.

Fifthly, the default of one of the debtors is absolutely without effect as to others.

Sixthly, the remission of the debt made to one of them is without incidence on the others. 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.

The effect of a divisible obligation is that each link to the creditor is independent of the others. If one is void, it does not affect the others. If one is paid it does not affect the share of the others. A notice to one debtor does not concern the others. The interruption of limitation in respect of one debtor does not affect his co-debtors. Article 1918(3) of the Civil Code, moreover, states that the fact that the obligation is divisible does not affect the suretyship, which may have been granted by one debtor to the principal debtor.

CHAPTER FOUR

SURETYSHIP

(Art.1920-51)

Nature of Suretyship:

suretyship is defined as a contract in which a person binds himself for another already bound and agree with the creditor to satisfy the obligation if the debtor does not.

Suretyship involves a three party relationship of creditor, debtor and surety. The obligation of the surety presupposes and depends upon the existence of an obligation of a principal debtor.

The fundamental advantage of suretyship is to make transactions much easier by increasing the safety of the creditor entering such a secured transaction. The advantage of suretyship from the side of the debtor, on the other hand, is that he gains credibility and will be able to trade. Suretyship supports the creation of new businesses.The advantages of suretyship for the guarantor are not evident.

Eventhough the suretyship is an accessory obligation to that existing between the creditor and the debtor, the debtor is not a party to the suretyship. The suretyship does not have to be known by the principal debtor (Article 1921 of the Civil Code). He does not have to give his express consent to such suretyship, and it can even be concluded without his knowing.

"suretyship" is a contract by which a person engages himself to a creditor to satisfy an obligation undertaken by the debtor if the latter does no satisfy it. This person, called surety. a second debtor for the creditor.

There are also other institutions that seem to be similar but differ from suretyship such as warranty, teyass.

The Civil Code provisions dealing with suretyship, no form requirement is laid down for suretyship agreements. But as per Article 1725(b) suretyship agreements shall be made in a written form.

Pursuant to Article 1727, a contract which is required to be in written form needs satisfaction of three elements: **special document**(any paper but,not deal with matters other than the contract.), **signature of parties bound and attestation of two witnesses**.

George Krzeczunowicz: "A contract required to be in writing must be signed by all the parties bound, and only by them. Consequently, in unilateral contracts binding merely one party, only the latter has to sign; a mere contract of guarantee (Art. 1920) has to be signed only by the guarantor and the witness. ..." Since suretyship contract is a unilateral one and only the guarantor is bound by it, the obligation rests on the surety and not on the creditor. Accordingly, it is only the guarantor who is to sign the contract of guarantee.

a contract of suretyship must be express. The essential rule is that a suretyship may not be presumed, it has to be expressly given. The law does not admit tacit suretyship.

a suretyship must have limits, and a maximum amount must be indicated. the law requires that the contract of suretyship must specify the maximum amount of which the surety will be held liable for,Article 1922(3).The sanction,for failure to fulfil, is simply that the suretyship is void

the provisions of the Civil Code dealing with suretyship equally applies to guarantees for a person in the contract of employment

Would the surety be liable to pay interests and legal cost even beyond the maximum amount fixed in the suretyship agreement? Article 1930 of the Civil Code states that unless there is agreement

otherwise, the surety is held to pay interests when the debt guaranteed bears interest. But this extension of his obligation remains limited to the maximum amount he has given his suretyship for.

the scope of the suretyship may not exceed that of the principal obligation (Article 1924 CC). suretyship cannot exceed that which is due by the debtor. The guarantor is a second debtor, and the temptation must not be to punish him for the main debtor's default.The surety may undertake an obligation equal to or less, but not greater, than that of the principal debtor.

suretyship is an accessory.there are two obligations. The first is the principal and the second one is the obligation created by the contract of suretyship. The later cannot stand by itself and it exists only in relation to the former. Pursuant to sub-Article (1) of Art 1926 of the Civil Code the fact that the principal obligation is discharged results in the release of the surety. Similarly, where the principal obligation is void, there cannot be any guarantee with respect to such obligation, Article 1923.

On the other hand, where the principal obligation is affected by a defect relating to the mistake of incapacity on the part of the principal debtor, such obligation can be validly guaranteed where the surety on entering into the contract of suretyship was aware of such defect.

A suretyship contract is classified as a unilateral one. in bilateral contracts both parties assume obligation. The situation is different in unilateral contracts. Only one party is bound in such contracts. The surety assumes an obligation towards the creditor to discharge the debt of the principal debtor in case the debtor fails to discharge his obligation. The creditor assumes no obligation towards the surety.

the obligation secured may be a future obligation or a conditional one (Article 1925). Accordingly, it is not necessary that the debt to be secured be presently in existence. Just as one can promise future things, one can become surety for a future debt.

the scope of the suretyship may not be extended by the contracts concluded between the principal debtor and the creditor after the consent given for the suretyship. So the guarantor's conditions may not be worsened through a posterior agreement between the principal debtor and the creditor. The code does not prohibit, on the other hand, the agreement tending to reduce the extent of the guarantor's obligation, because it is obviously in his favor (Art. 1928 (1) of the C C)

Effects of Suretyship

Effects of Suretyship between the Creditor and the Surety: the surety may not be demanded to perform his obligation prior to the maturity of the debt. (See Art. 1932 of the Civil Code).Apart from this, where the principal parties the principal debtor and the creditor had agreed to a notice before the debt is due. Then such a notice has to be served to the surety too.

See Article 1929 of the Civil Code which deals with limitation of actions.

Simple suretyship and joint suretyship: ***Simple suretyship: (***Art. 1934 through 1937***).*** the obligation of the simple guarantor subsides to the principal debtor. He undertakes to discharge his obligation "should the debtor fail to discharge it." (See Article 1920).Similarly, Article 1934(1) of the Civil Code sets the principle of simple guarantee. The main condition to obtain payment from the guarantor is the non-execution of contract by the principal debtor. So it follows that the action of the creditor against the guarantor may only be initiated after the contractual term set for the execution of the principal debtor's obligation.

However, there are defenses available for the simple guarantor. The first defense derives from Article 1934 (2) of the Civil Code, the benefit of discussion. In the case of simple suretyship, the engagement of the surety is subsidiary; he images himself to pay only if the principal debtor does not. The idea is that he is not to pay simply because the main debtor arbitrarily refuses to do so.

The discussion is not automatic and has to be required by the guarantor when he is himself sued (Article 1935 (1) of the Civil Code). By availing himself of this benefit, the guarantor can compel the creditor to first seize the property of the debtor

Accordingly, in the words of Article 1936(1), the discussion is not automatic. The guarantor should raise and exercise his benefit "as soon as he is proceeded against." the guarantor has to advance the procedural costs for the discussion of the debtor's property. the burden of identifying the debtor's property that can be discussed and also covering the cost of discussion are borne by the guarantor.

Accordingly, the consequences of the defense of the benefit of discussion are the following. If the assets are sufficient for a total or part payment of the main debt, the guarantor benefits accordingly and is discharged in part or totally of his suretyship. If no money can be made from the debtor's assets, the guarantor has no option but to pay the main debt, pending his action against the principal debtor. But in the case of negligence of the creditor through failure to proceed upon the assets indicated by the guarantor (Article 1937 of the Civil Code) who has supplied sufficient money for costs, the loss of the

value of such assets through an insolvency of the principal debtor makes the creditor liable vis-a-vis the guarantor. Where the creditor by his failure to proceed against the debtor is suddenly faced with the insolvency of the debtor, then the surety will be liberated up to the value of the assets thus indicated.

*Is joinder of the principal debtor and the guarantor possible in our legal system?*Under our law, the substantive law does no stipulate joinder of the debtor and the guarantor. But the procedural law provides for the possibility of joining plurality of defendants in a variety of cases. In this respect, Article 36 of the Civil Procedure Code deals with joinder of defendants.Under this procedural provision, it is possible for the principal debtor and the guarantor to be joined in the same suit.

The practice in Ethiopia is that after judgment is passed against the co-defendants, the judgment is first executed against the principal debtor. This practice has no support of the law of suretyship. The Civil Code provisions are mute on this issue. You can, however, provide a solution by resorting to equity. It is equitable, in so far as it can be done, that a debt be paid by the real principal debtors who have benefited from it rather than by those who are bound others.

The second defense, next to benefit of discusson, available for the simple guarantor is the benefit of division which is raised in case of plurality of guarantors.

The third one, not special for simple guarantor, is the possibility to raise the principal debtor's defenses. Article 1942 (1) provides: the guarantor has the right and the duty of setting up all the defenses available to the debtor, unless excluded by the nature of his suretyship (by a contractual clause, for instance). in case of failure to raise sucuh defense The sanction is strict (Article 1942 (2)); the guarantor will be debarred of his remedy, in so far as it would have relieved him of payment. The sanction shall not apply where z guarantor can prove that he was ignorance of z defenses without his fault.

Joint Suretyship (Art.1933)

The surety (guarantor) may bind himself either by simple or joint guarantee. Under the former, you have seen that the guarantor's obligation is secondary because it arises if the principal debtor fails to discharge his obligation. In cases of joint guarantee, however, the obligation of the guarantor is primary and direct because the creditor is not required to demand payment from the principal debtor in order to bring an action against the guarantor.

In principle, pursuant to Article 1920 and 1934, every suretyship is presumed to be simple. There can be joint guarantee only where the person who becomes a surety expressly described himself as joint guarantor by using words implying the same. The intension of the guarantor to be bound jointly with the principal debtor has to be expressed clearly. Where the suretyship is joint, the creditor is entitled to proceed against the guarantor without demanding payment from the principal debtor. The direct effect of joint guarantee is the deprivation of the surety (the guarantor) of his benefit of discussion.

joint guarantee is a dangerous situation for the guarantor, who may then be required to pay for a debtor who still has some assets(since z guarantor can not raised benefit of discussion).

Effect of Suretyship between the Debtor and the Surety

This is the situation where the *guaran*tor has paid the debt in place of the debtor. When the surety pays the creditor, he is discharging the obligation of the principal debtor. The principle is that the guarantor, who has paid the creditor instead of the debtor, shall be indemnified by this debtor. Accordingly, the guarantor is entitled to be indemnified by the principal debtor.

In this regard, the fact that the guarantee may be given without the consent of the principal debtor does not relive the latter from indemnifying the surety what the latter paid to the creditor. In exercising his right of indemnification, the surety enjoys two rights of action, one which is personal to him arising from the contract of suretyship and the other which is the action of the creditor who has been paid and which the surety obtains by subrogation. The first is called chirographic action while the latter is the right of subrogation.The personal action of the surety arises from the contract of suretyship itself. The action is based on the theory of implied mandate. Accordingly, this recourse is open to the surety only against those debtors for whom he has become surety and not against the other debtors.

This personal action entitles the surety to claim the principal, interest, expenses and damages if any. Accordingly, in addition to interests, the surety is entitled to be indemnified for all damages he suffers as a result of the debtor's fault or negligence. In this respect, see Articles 1940 (2) and (3) and Article 1941 of the Civil Code.

What would happen if the surety guaranteed the obligation of one debtor alone who is bound with other co-debtors on joint obligation?

Protection of a Guarantor's Action against a Debtor

(Z ff will be discussed;Duties of a creditor,Securities obtained from principal debtor (Recourse before payment),& Loss of Right)

I) Duties of a creditor

The creditor who has been paid has a duty to ensure that, as far as possible, the guarantor enjoys an effective action against the debtor. Three situations are provided for:

1- Handing over of documents of title and performance of formalities to transfer available securities (Article 1945 of the Civil Code). A sanction in the form of a court injunction may be considered here if the creditor is negligent or late in passing over such documents.
2- 2- To make subrogation possible (Article 1946 of the Civil Code). The sanction of the creditor's action or omission is that he may not ask payment from the guarantor. So before paying, the guarantor has a right to check that the subrogation in the rights of the creditor is still possible.
3- 3- Debtor's bankruptcy (Article 1947 of the Civil Code). In this situation, the creditor has a double duty: i) to declare and prove the debt in the hands of the liquidator, so that the right to claim payment survives and can be transferred to the guarantor; and ii) to inform the guarantor of the bankruptcy as soon as he is aware of it.

II) Securities obtained from principal debtor (Recourse before payment): The surety who has paid to the creditor has a right of recourse against the debtor for indemnification. The surety who has not yet paid may also have recourse against the debtor. The guarantor, who is informed of a serious chance that the principal debtor is not going to pay, may take *protective measures* through securities demanded of the debtor, even before any payment is made to the creditor. Three situations are limitatively mentioned under Article 1948.

III) Loss of Right: The general principle is that upon payment the surety has a right of recourse against the debtor. However, there are two situations in which the surety loses his right against the debtor. The first exception is where the indemnity claim has lapsed. The guarantor has a duty to set up all available defenses of the debtor he reasonably knew of. If not, he is debarred from indemnification by the debtor.see Article 1942 of the CC. The second exception to the principle is the case where a second payment is made by the debtor (see Art.1943). According to this provision, the guarantor who pays has a duty to inform the debtor of such payment.

Plurality of Guarantors

The idea of a plurality of guarantors is that the risk of suretyship is spread over several persons.

Counter Guarantor:"The counter guarantor guarantees towards the guarantor the effectiveness of his indemnity claim against the principal debtor"(Article 1949).Therefore, the counter -guarantor has no relation with the creditor.

Secondary Guarantor (in French "suretyship certifier") :

Article 1950 - secondary - guarantor

1) A person may stand survey not only for the principal debtor but also for his guarantor.

2) The secondary guarantor shall be in the same position towards the guarantor as a simple guarantor is towards the principal debtor.

3) Merger between the principal debtor and the guarantor shall not extinguish the creditor's right of action against the secondary guarantor.

In respect of the secondary guarantor, both the principal debtor and his guarantor are considered as principal debtors. Accordingly, unless the creditor exhausts all his remedies against the principal debtor and the main guarantor, the secondary guarantor shall not be held liable.The secondary guarantor, in turn, if he happens to have paid may then be subrogated in the rights of the creditor against both the debtor and the main guarantor.

Plurality of Simple and/or Joint Guarantors: A common situation is where the creditor wishes to spread his risk over several persons acting as guarantors for the same debt and for the same debtor. Where the plurality of guarantors granted the security at the same time (Art. 1951(1)) of the Civil Code, each of them shall be liable for his own share as a simple guarantor, and as a secondary guarantor for the shares of the others.

Article 1951 of the Civil Code does not explicitly address the situation where each of the guarantors expressed the maximum amount of their obligation. In this respect, you may argue that Article 1918 (2) of the Civil Code will apply by analogy in which case one surety cannot stand as secondary for the debtors.

Where the plurality of guarantors granted the security at different times (Article 1951 (2) of the Civil Code), the chronological order determines the secondary character of the guarantors, and therefore the order of their respective contributions. Accordingly, if several persons become guarantors at different times, there shall be no benefit of division even if they are guarantors of the same debtor in respect of the same debt. The relationship of such sureties is governed under Article 1951(2) in which case the one who bound himself in the second place is considered as a secondary guarantor of the one who bound himself before him.

Apart from Article 1950, the situation of secondary guarantor is also governed under Article 1951. According to this Article, one is held liable as secondary guarantor for another in two events. These are: In cases of the insolvency of either one or more of the guarantors; and where the sureties entered in their undertaking by successive acts.

In considering the second situation, the provision of Article 1951(2) states that "where the guarantors entered into their undertakings by successive acts he who bound himself in the second place shall be held liable as secondary guarantor of the guarantor who bound himself before him."

Relationship between/among Co-sureties: When there are several sureties for the same debtor in respect of the same debt, the one who pays the creditor is entitled to contributions from the others. The basis of contribution is payment by surety of more than his share and also equity. Under our law, Article 1951 provides that guarantors who are either severally, or jointly and severally liable for the same debt and who stand as surety for the same debtor at the same time are entitled to proportionate contribution. This implies that persons who undertake as sureties in respect of different debts of the same debtor are not entitled to contribution from the other surety. Similarly, where a single debt is guaranteed by successive acts of two or more sureties, there is no right of contribution among such sureties. even where the surety has paid more than his share, he may not claim contribution until the debt is fully discharged coz he is still liable for the remainder. Accordingly, you may conclude that the surety has to discharge the totality of the debt so that he may claim contribution from the other co-sureties.

Grounds of Extinction of Suretyship:

- Payment
- Novation
- Remission

- set-off
- in case of principal obligation is void, However, in cases where the principal obligation is voidable, the contract of suretyship may or may not be invalidated.
- Merger: With regard to suretyship, there are three possible cases of merger; First, merger of debtor and creditor extinguishes the principal obligation and the accessory suretyship obligation also. Second, merger of surety and creditor extinguishes the obligation of suretyship, but not extinguish the principal debtor's obligation.Third, a merger of debtor and surety does not extinguish the principal obligation, but it brings an end to the contract of suretyship because a man cannot be his own surety.
- where the creditor has accepted a payment in the form of an immovable or any good, even if he is later dispossessed (Article 1927 of the Civil Code). The creditor, not the surety, bears the risks of the thing accepted in payment.
- where the creditor, without special permission given by the guarantor, has granted a delay to the debtor (Article 1928 (2) of the Civil Code). Accordingly, an extension of time for performance or payment, granted by the creditor to the debtor, is an alternation of the original obligation which is considered prejudicial to the surety.

CHAPTER FIVE

THIRD PARTIES IN RELATION TO CONTRACTS

In the civil law legal system, the basic principle, which is known as contracts produce effects as between the contracting parties is referred to as *"relative effect of contracts",* while it is called *"privity of contracts",* in the common law legal system. A contract may only affect its signatories, whether they benefit from it or have to implement obligations.

Similarly, this principle is incorporated under the Ethiopian law of contracts. Article 1675, The phrase "as between themselves" implies that a contract produces effect only among the contracting parties.

However, there may be exceptions in which case a contract may produce effect on third parties.

The first situation is that of *promises and stipulations concerning third parties*, whereby a party to the contract sets out that the contract will have effect on a third party. The second is where the right of a contractual party is assigned to a third party *(assignment of rights)*. The third unit addresses the reverse situation where a liability may be assigned to a third party *(Delegation & assignment of obligation)*. And finally, *heirs of the parties.*

But whatever the category of third parties concerned, Article 1952 states clearly that this part does not affect two categories of situations: Extra contractual liability and Agency.

Promises & Stipulations Concerning Third Parties

It is legally possible that persons may conclude a contract by reserving a right to substitute a third party in their place or by promising that a third party will commit a certain act or omit from performing an act. It is also possible to make contractual stipulations for the benefit of third parties.

The option to substitute a third party: Article 1953 of z CC opens the possibility for a contracting party including in a contract a clause enabling him to substitute another person for himself. Note: immediately that the identity of the third party to be substituted is not required at the time of the formation of the contract. Another remark is that such an option is open both to the creditor and to the debtor. It enables a person who does not have the adequate facilities or equipment to perform the contract to substitute himself a person better equipped. It makes it possible to contract secretly in the name of a person who does not what to be known to the other party until the contract is concluded. where the third party is substituted within the following three days from the formation of the contract, the contract will produce effect as between the third party substituted and the other party(1954 sub.1). However, if no substitution occur, the parties are bound by the terms of contract along ordinary rules, and specially, the contract is enforceable against each party.

The promise for third party: A person may stand promisor for a third party by promising his contractual partner that this third party will perform some contractual obligation or respect some omission, (Art.1955). Q. what is the effect of the contract in case the contract is or is not ratified by a third party? The answer is provided under Article 1956 of the CC; When the main contract is ratified by the third party the promisor is released; Regarding the scope of promise,the promissor promises the conclusion of the contract but does not guarantee its performance. The duty of the promissor is fulfilled from the moment the third party has ratified as he is not a guarantor for the performance of the obligation by the third party. where the third party refuses to ratify the projected main contract. Contrary to the situation

of substitution, the promissor is not held to implement the contract, simply because this is not the purpose of his obligation to the first partner. But such a failure will amount to the fact that the promise will not be held, and therefore that the promissor is liable to pay damages (Article 1956(3)). the obligation to pay damages resulting only from the non ratification and not from the non-performance. the obligation to pay damages resulting only from the non ratification and not from the non-performance.

Stipulation for the benefit of a third party: Art.1957 and following of the CivC open the possibility for two contracting parties to provide for a benefit to be granted to a third party. For instance, life insurance for the benefit of a third party. The relation seems to be triangular.

There are three persons: the stipulator- the creditor who can demand performance from the debtor; the promissor- the debtor; and the third party beneficiary for whom a benefit has been stipulated in the contract concluded between the stipulator and promissor.

Assignment of Rights and Subrogation

Assignment of Rights

The principle of assignment of rights is put under Article 1962 of the Civil Code. This provision states that a creditor may assign his right to a third party without the consent of the debtor, unless such assignment is forbidden by law or the contract or is barred by the very nature of the transaction(contracts made in consideration of the person, but seen here from the side of a creditor). Thus, an assignment is a contract concluded between the assignor and the assignee, whereby the former transfers his rights under the contract or part of it to the latter. consent of the debtor is not required for an assignment to be valid.

Types of Assignment: an assignment could be made for consideration or gratuitously. An onerous assignment is an assignment of a contractual right by the creditor which is made for consideration. In case of assignment of rights, warranty may or may not be required depending on the form of the assignment. *Where the assignment is made for consideration the assignor has to guarantee the existence of the right at the time of the assignment ,Article 1964 (1).*The assignor does not guarantee the solvency of the debtor.However, the situation is entirely different where the assignment is made gratuitously. In such cases the assignee should not expect any legal warranty (Article 1964 sub. 3 of the Civil Code).

The assignment is a transfer of the right to the performance of the contract. It entails naturally a transfer of the defenses open on the basis of this contract to the debtor. Art 1966 sub. 1, This provision allows the debtor to raise against the assignee those defenses he may have raised against the assignor.

when the debtor pays in good faith the original creditor before the request for performance is made by the assignee. In such a case the debtor shall be validly released if he was not informed of the assignment before he performs.

Subrogation

Subrogation is the situation where a right with all its accessories is transferred from one person to the other.In case of subrogation, there are three persons: subrogor (original creditor), subrogee (the new creditor who is subrogated on the right of the original creditor), and the debtor.

Thus, subrogation can be said is a situation where an obligation extinguished with regard to the original creditor by payment which he has received from a third person or from the debtor himself but with funds that a third person has furnished to that effect is regarded as subsisting in favor of this third person who is entitled to assert, to the extent of what he has paid, the rights and actions of the original creditor. Thus, subrogation accompanies payment.

Types of Subrogation: Generally, the sources of subrogation are two: conventional (contractual) or legal subrogation. Conventional or contractual subrogation is divided into two: subrogation by the creditor and the debtor.

> ***Subrogation by the creditor***: The most frequent form of contractual subrogation is where the creditor subrogates to his rights the third party who has paid him the debt (Article 1968 of the Civil Code). The third party is thus exactly transferred into the position of the creditor and is granted to refunded by the original debtor. the contract of subrogation must be express and must provide that the subrogation takes place at the time of payment.
>
> ***Subrogation by the debtor***: Art.1969 and 1970; In this case, subrogation is effected by agreement between a debtor and a third party who lends him money or fungibles for the purpose of paying the debtor's creditor. Then, the creditor's rights against the debtor are transferred to the third party, without the consent, or even against the will, of the original creditor.

Legal subrogation: In quite a number of cases, a person who pays another person's debt is accorded the benefit of subrogation by simple operation of the law, without the necessity of any agreement at all. In legal subrogation cases the law recognizes a special interest of the payer in the extinguishment of the other person's debt. Article 1971 provides three situations where there could be legal subrogation: 1) payment by a person bound with another or on behalf of others, i.e., subrogation as co-debtor or guarantor. 2) payment by a person who is owner of a property or who enjoys the rights of lien, mortgage or pledge, i.e., Subrogation as holder of sureties & 3) other cases of subrogation provided by law.

In essence, legal subrogation does not differ from the conventional type as both are based upon payment of the debt or obligation to the creditor and their effect is the same. Accordingly, a legal subrogee as well as a conventional subrogee is subject to any defenses which were available to the debtor against the original creditor.

Effect of subrogation and assignments: Effect of subrogation and assignments Articles 1973 and following of the Civil Code state the consequences common to assignments and subrogation. The assignment or subrogation to a right entails:

- the right to exercise the liens, securities and accessory rights attached to it, with an exception in respect of a pledge.
- The original creditor has a duty to cooperate to ensure as much as possible that the assignee or subrogated creditor has the best chances of being paid by the debtor.

Delegation (Art.1976-1982**) and Assignment of Obligations (**Art.1983-1985**):**

Unlike assignment of rights, what is delegated is obligation; Thus, in case of delegation, the debtor may delegate performance of his duties to a third person. On the other hand, rights arising out of a contract with its corresponding duties can be transferred to a third person by way of assignment of obligation, estate,.

Delegation of Obligations

Delegation is the act by which a person delegates the performance of his obligation to a third person. There are three persons in cases of delegation. These are: the delegator, the person whomakes the delegation; the delegatee, the creditor; and the delegate-debtor, the third party who is delegated and becomes a debtor.

Article 1976; the debtor of a contractual obligation may substitute himself another debtor to perform the obligation. In case of delegation of obligation, in principle, unlike assignment of rights, the debtor has to ask the creditor consent to accept a third person as his debtor, The change of debtor could be very detrimental to the creditor. But in cases where usage or the law itself allows such substitution of debtors without the consent of the creditor.Most often the delegator is the creditor of the delegate debtor. Generally, the economic importance of delegation is that it simplifies transactions. if the insolvency of the delegate debtor occurred after the delegation, the risk of insolvency is borne by the creditor. Unless otherwise agreed.

what is the effect of delegation on third parties - guarantors? Article 1982 of the Civil Code therefore decides that they shall not be liable, unless they consented to the delegation.

Assignment of Obligation: Articles 1983 to 1985 of the Civil Code consider special forms of delegation, which all rest on the same idea of an amalgamation of estates which include both assets and liabilities.

In the case of the assignment of an estate or an undertaking the acquirer (buyer) will be liable to the creditors for all the liabilities from the day he notified them of the assignment or published the transaction in the newspapers (Article 1983 (1) of the Civil Code). Note the imprecision here about the identity of the newspaper; "Herald or Tribune?"

HEIRS AND CREDITORS OF THE PARTIES

The last instance in which contract produces effect is upon heirs and creditors of the parties,(Articles 1986 and 1987).

Heirs of the Parties; They continue the person of the deceased, if they have accepted the succession. They will assume his contractual obligations, unless otherwise provided, or where the nature of the obligation prevents it (contracts *"intuitu personae")*

in respect of stipulations for third party beneficiaries (see Articles 1957 and following) the heirs of such a party are entitled to the performance of the obligation considered, if the deceased had already accepted the stipulation but dies before receiving the performance.

Creditors of the Parities

The principle: attachment of the debtor's assets ; Creditors are a special category of third parties in respect of the contracts made by their debtor. Article 1988 provided that; the entire assets of the debtor are open to be used as a security for the performance of his obligations. There is the maxim which says *"the property of a debtor is the common pledge of his creditors*". There is the maxim which says *"the property of a debtor is the common pledge of his creditors*". This means that a creditor has a general right to attach and have sold any asset belonging to the debtor in order to get paid. However,certain assets cannot be attached essentially the basic living commodities and tools of the debtor's trade (see Art.404 Civ.pro.C).

Agreements entered into by the debtor; The mere fact that someone is a debtor of another does not totally preclude him from entering into agreements regarding his property. Therefore, the principle is stated in Article 1989 (1) of the Civil Code that any other agreement entered into by the debtor can be set up against this other creditors.

Exceptions, in which Article 1989 will not apply:

- Article 1990 of the Civil Code which deals with preferred creditors. Preferred creditorship may arise from a contract (secured creditors) or from the law(eg. any claim of payment of worker and tax authority preferred creditors).
- Simulation; is defined by Article 1994 of the Civil Code as the case where the debtor enters a simulated contract with a third party, i.e. a contract which was not intended to be carried out. The simulated act is the apparent act, whilst the reality of the situation is in a hidden act, The parties did not intend to be bound by the apparent act or the simulated contract. As per Article 1991(2) of the Civil Code, it is the counter-deed or secret contract which alone is given effect.

  there are third parties against whom the secret agreement (real contract) will not be effective and others against whom the apparent act(simulation) is not admissible.For those third parties

against whom a secret agreement is not admissible, they should be able to rely on apparent acts as these are the only agreements known to them. That is why Article 1991(2) clearly states that counter deeds or the secret agreement shall bind contracting parties only. Thus, in all cases where the production of counter deed would entail unfavorable result as to those good faith third persons, the apparent act alone is observed. On the other hand, for those third persons against whom the apparent act is not effective, their right is put under Article 1994.

Rights of the creditors of the parties

i) ***Preservation measures,*** Article 1992

ii) ***Exercise of debtor's right or oblique action;*** The origin of the impoverishment is indifferent, provided the risk is there; it may be that the debtor is unaware of the risk, incompetent, absent or simply negligent. The law thus affords creditors a means of preserving the debtor's patrimony, a kind of supervision. The oblique action's chief purpose is to prevent the debtor from negligently allowing his valuable rights to extinguish. In cases of oblique actions, creditors do not act in their own name, directly, against the debtors of their debtor. The creditor must secure court authorization to take the oblique action(1993(3)).

iii) ***The Paulian action or Revocatory Action***;The Paulian or revocatory action is an action given to creditors to obtain the revocation of acts done by their debtor in fraud of their rights. The creditor will have to prove the fraud to his rights and thus obtain the annulment of the disputed agreement. Article 1995 of the Civil Code opens the right to what is called *"actio pauliana"*

An act is deemed to a fraud, in the meaning of Article 1996 of the Civil Code, when it was intentionally made by the debtor so as to become insolvent, or with the intention of becoming insolvent. For instance, the debtor sells his car to a friend for a very low price, and the friend, legally the owner, then lets him use it "free of charge" pretending it is a friendly loan.

Note here that the action is brought by the defrauded creditor in his own name and not as a representative of his debtor as in Article 1993.

Chapter Six

Proof of contracts

In civil cases such as in contracts the basic rule is that the burden of proof lies with the party that is seeking to assert the existence of the fact. An example of this would be if Mr.A seeks to rely on the fact that there was a contract for the sale of 1,000 quintals of cement against Muger Cement Factory to be due on March 21st 2008, but Muger Cement Factory denies this. In this case, it is Mr. A who has to establish the existence of the said contract of sale; otherwise, he will lose the case. For the Factory denial is enough except to defend itself against evidence of Mr. A when established.

The burden of proof also applies to negative assertions. In both cases, be it positive or negative assertion, burden normally lies upon the claimant who alleges some contention others. In most cases he will be a plaintiff. however, if the defendant admits the allegation of the plaintiff but raised counter-claim,the burden of proof as to texistence of facts raised as defense shifts to the defendant. This is what Sub-Article 2 of Art. 2001 affirms.

He who demands performance of an obligation shall prove its existence.He who alleges that an obligation is void, has been varied or is extinguished shall prove the facts causing such nullity, variation or extinction,(Art 2001).

evidences would be admissible be it written, oral, , presumptions, or admission of the party according to rules and prescribed forms(Art. 2002). However, Art. 2003 is an exception to the inclusive rule and provides: *Art. 2003. Contracts to be in writing; Where the law requires written form for the completion of a contract, such contract may not be proved by witnesses or presumptions unless it is established that the document evidencing the contract has been destroyed, stolen or lost,*

Written (documentary) Evidence and its probative value: Written evidence is normally used interchangeably with documentary evidence. Letters, contract, deeds, licenses, certificates, ticket, or other writings are documentary evidence.

Authentication of Documentary Evidence ; Authentication is a mechanism of ascertaining authorship of the document (who the author of a document is?) and genuineness of the document sought to be introduced. Unless a document is authenticated it may not be

admitted as proof.Examples of Modes of authentication: Admission authorship by the writer **,**Production of a person or persons who witnessed the writing or signature,Attesting witnesses.

Best evidence rule: *Authentication alone is not sufficient for the admission of documentary evidence as proof but must also be qualified by the best evidence rule, which states the contents of a document can only be proved by adducing the original document itself.* The best evidence rule is the common law rule of evidence which can be traced back at least to the 18th century. The general rule is that secondary evidence, such as a copy or facsimile, will not be admissible if an original document is available.The best evidence rule was predicated on the assumption that, if the original is not produced, there is a significant chance of error or fraud in relying on such a copy.The best evidence rule is also thought to be the basis for the rule precluding the admissibility of hearsay evidence, although the two rules are now quite distinct.

Secondary evidence : The contents of documents may be proved by secondary evidence where primary evidence could not be found. Secondary evidence is the second best alternative for proving the contents of a document

Presumption of payment

The code has given four instances in which presumption of payment should be taken.

A) **Handing over of evidencing documents**; When the creditor hands over to the debtor documents of title evidencing the existence of the debt (Art.2020 of the C.C) presumption of payment takes place.

B) **Creditor's entries** (2021 C.C); The civil code provides that entries in the contractual documents by the creditor, which tends to release the debtor from his/her obligation presumes payment.

C) Prior or Concomitant Debts (2022)

D) Period of time related presumptions(Arts.2023 and 2024**)**