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STable of Contents

Contents

Page

Table of Contents..... ii

Chapter One: Nature, Classification and Function of Law.....5

1.1. Introduction 5

1.2. Nature of law 5

1.3. Features of Law 5

1.4. Functions of law 6

1.5. Classification of Laws 7

1.6. Sources of law 10

1.7. Self-test exercises 11

1.8. Progress Questions 11

Chapter Two: The Law of persons 13

2.1. Introduction 13

2.2. Definition of person.....13

2.3. Attributes of legal personality 13

2.4. Personality of physical persons 14

2.4.1. Capacity of physical person.....14

2.4.2. Incapacity.....15

2.5. End of personality.....16

2.6. Self-test exercises 17

2.7. Progress Questions 17

Chapter Three: Law of Contracts Introduction.....18

3.1. Introduction 18

3.2. Definition of contract.....18

3.3. Capacity of contracting parties.....19

3.4. Defective consent 1-Mistake 23

3.5. Void and illegal contracts 27

3.6. Effect of contracts.....29

3.6.1. Performance of contractual obligation.....29

3.7. Variation of contracts.....30

3.8 Non-performance of contractual obligation....31
3.9. Remedies for non-performance contractual obligation....31
3.10. Self-test exercises....32
3.11. Progress Questions....32
Chapter Four: The Law of Sales....34
4.1. Introduction....34
4.2. Formation of contract of sale....34
4.3. Subject matter of the contract of sale....36
4.4. Obligation of the parties to the contract of sale....36
4.4.1. Obligation of the seller....37
4.5. Consequence of transfer of ownership....40
4.6. Warranty against defect....42
4.7. Obligation of the buyer....44
4.8. Self-test exercises....45
4.9. Progress Questions....45
Chapter Five: The Law of Agency....47
5.1. Introduction....47
5.2. Sources of authority of an agent....47
5.2.1. Authority by operation of law....49
5.2.2. Contractual agency....50
5.2.3. Authority of an agent....50
5.3. Effects of Agency....52
5.4. Termination of agency....53
5.5. Self test exercises....55
5.6. Progress Questions....55
Chapter Six: Introduction to the law of Traders and business organization....57
6.1. The law of traders....57
6.1.1. Who are traders....57
6.1.2. The right to operate business activity in Ethiopia....57
6.1.3. Obligations of traders....58
6.2. Business and unfair competition....58
6.3. Introduction to the law of business organization....58

6.4. General features of business in Ethiopia.....63
6.5. Dissolution of Business organization.....66
6.6. Self-test exercises.....67
6.7. Progress Questions.....67
Chapter Seven: Introduction to Law of Insurance.....68
7.1. Background and functions of insurance.....68
7.1. 1. Contractual requirement.....69
7.1.2. Parties to the contract of insurance.....70
7.1.3. The subject matter of insurance.....71
7.2. Insurable interest.....71
7.2.1. Rights and Duties of the parties in the contract of insurance.....71
7.2.1.1. Duties of the insurer.....71
7.2.1.2. Duties of the insured.....72
7.3. Classification of contract of insurance.....72
7.4. Insurance of object.....72
7.4.1. The concept of proximate cause.....72
7.4.2. Making claim for compensation.....72
7.4.3. Subrogation.....72
7.4.4. Insurance of liability.....73
7.4.5. Insurance of persons.....73
7.5. Self-test exercises.....73
7.6. Progress Questions.....74
Chapter Eight: Negotiable instruments.....75
8.1. Negotiable instruments.....75
8.2. Characteristics of a bill of exchange.....75
8.3. Technicalities of Acceptance.....78
8.3.1. Qualified Acceptance.....79
8.4. The nature of a cheque.....82
8.5. Self-test exercises.....84
8.6. Progress Questions.....84
Appendix.....85

Chapter One
Nature, Classification and Function of Law

1.1.Introduction

Dear learners, in the very beginning of this course, it is quite compulsory for you to have understanding and basics of business law since neglect/ignorance of law has no excuse.In this unit, we will deal with introductory aspects of what is law, features law and how issues related to law are came in to existence.

Learning objectives:

At the end of this unit, you will be able to:-

- Explain the definition of law
- Discuss features and functions of law
- Classify law among different categories

1.2.Nature of law

Definition

The word "*law*" is difficult to define, particularly as it is used in many different ways. It contains, however, the concepts of orderliness, universality and objectivity. It is concerned with behavior and not with causes, and either contains an element of inevitability, e.g. scientific laws, such as the laws of gravity, or of sanction, e.g. divine laws. Some philosophers have postulated the existence of **natural law** by which they mean the Law of God which regulates the actions of mankind. This concept is often known as the **principles of natural justice**.

In the narrower concept of law, there must be a set of rules which can be applied objectively with someone to enforce them. There have been many attempts to put these into a workable definition, some more successful than others. One of the better is that of **Salmond.**

"Law consists of any principle which is recognized and enforced by the courts in the administration of justice". Another, which is possibly superior to that of Salmond, sinceit has a slightly wider application, is that of **James**: *"A body of rules for the guidance of human conduct, which are imposed upon and enforced among the members of a given state"*.

1.3.Features of Law

The following are features that make law different from some mores and other forms of social control.

i-Law is obligatory

It is repeatedly stated that laws are enacted for public good. To attain the desire goal the law has to be obeyed by everyone. Unless specially made to or for observance of special category of people, the law binds every one. It points out how we behave. And it is because of this fact that one feature of law is being it obligatory.

ii- **Law has to be made by competent authority** (the parliament)

An organ making law shall be empowered with legislative power. As stated in the article 55 of the present constitution, the house of peoples‟ representatives makes laws governing the Ethiopian people. Each of the state has also their law making organ. Laws that are in acted by the state organ bind only the people within the jurisdiction of the same state. Law making function may also be exercised through delegation. As a result executive organs sometimes make laws. In Ethiopia, at present regulations and other enactments subordinate to the proclamations are being made by executive organs through delegations. The parliament may not have time to deal with subordinate rules applicable to every office or authorities. Law making power is shared through the process known as delegation.

iii-**Every law is backed by sanction or has organized enforcement machinery**.

Sanction motivates enforcement of laws. Sanction is punishments or fine that the law imposes if subjects or low fail to obey the law. If you trespass someone's boundary, you know that legal action would be taken against you and you would be punished. If you fail to pay tax or committed forgery, you may be sued and subjected to fine or imprisonment. In fear of these remedies of non-observance of law you ought to be abided by the rules of law. This is especially true for individuals who are not governed by moral considerations.

-A law is established in performance.

In most instances, laws are enacted for undefined period of time. The Ethiopian civil code for instance, was enacted in 1960 and still works. Law may be modified to suit changing situations and may be altered whenever necessary. Law may also enact to regulate temporary situations.

Do you know about a state of emergency? Discuss with your colleagues.

When a country faces a sudden social disorder or war, the highest organ of government may declare state of emergency. You may consider this temporary and special order. In most instances, laws are permanent subjected to modifications.

In addition to the above basic features of law, the other features that should be taken in to considerations are:-

- The law has to be applicable to the people in the same situations
- The law has to be specific
- There shall be law enforcement institution

1.4.Functions of law

You may hear that every individual are equal before law. Do you agree or disagree? Togive you illustrative fact think **life without law, people without law, nation without law, Globe without law**

Now, it might not necessary to tell you about the function of law.

The primary function of law is maintaining peace and stability. The law attains this by a

number of specific functions. These are:-

- **Dispute resolution**- By limiting the extent to which one exercise his/her right, the law acts as a fence bysetting boundaries to give resolution of dispute between the parties. Also by putting legal sanctions avoids chaos.
- **Protection of property**
- **Preservation of state**

1.5.Classification of Laws

Different scholars classify law from different perspectives. The following are specific classifications of law based on the different nature**.**

- **Imperative Law**

These are rules of action imposed on men by authority, e.g. by the state.

- **Physical or Scientific Law**

These are rules which formulate the uniformities of nature, e.g. the law of gravitation. You can distinguish them from man-made laws, in the sense that they merely state observations on a state of affairs that already exists.

- **Natural or Moral Law**

These are rules formulating the principles of natural justice. This conception of law is derived from Greek philosophy and Roman law, and has found more favor with Continental jurists than in English jurisprudence. It overlaps to some extent with physical or scientific law. In the English language, law and justice are two separate words, showing that we recognize them to be two separate things – a distinction that is not made in most other languages.

- **Conventional Law**

These are rules agreed upon by persons for the regulation of their conduct towards each other. Agreements entered into by, for example, the parties to a contract or members of a company (who agree to be bound by the rules of its Articles of Association) are enforceable under the law of the land. Other agreed systems of rules, e.g. the rules of a football club or the laws of chess, may not be enforceable by law.

Customary Law-these are rules of action embodied in custom.

- **International Law**

These are rules which govern sovereign states in their relations with each other.

- **Civil Law**

This is the law of the state, as applied in the state's courts of justice.

- ***Criminal and Civil Liability***

In essence, it can be said that a **crime** is a wrong **against the state**, while a **civil wrong** is one against an individual**.**

You should note the following major distinctions:

- **State Action and Private Action**

In the case of a crime, whilst under certain circumstances an individual may prosecute, the prosecution will normally be brought by the state. In a civil wrong, such as breach of contract, the injured party may bring an action against (or "sue") the party liable, andmay recover damages or other forms of satisfaction.

- Redress and Punishment

The purpose of a civil action is to redress a wrong, whereas the aim of a criminal prosecution is to punish the wrongdoer, to prevent him from repeating his crime and to discourage others from committing similar crimes.

- Indictment and Writ

Criminal proceedings are initiated by indictment or summary procedure, whereas civil proceedings are commenced by action resulting from the issue of a writ. A fundamental difference thus exists between **criminal law** (dealing with crimes) and **civil law** (dealing with civil wrongs) and each branch is, in general, administered by different courts on different principles.

Criminal law is concerned with offences against the state, i.e. crimes such as murder, housebreaking, and theft. The more serious criminal cases are dealt with by a judge and jury; less serious offences (the overwhelming majority) are dealt with by magistrates. The two parties are the **prosecution** and the **accused**.

Civil law is concerned with private litigation, e.g. breaches of contract, disputes concerning property. The complainant issues a statement of claim, setting out the facts healleges against the defendant and asking for damages or other remedy. The defendant puts in his defense to the allegations of the complainant. The case is then tried by a judge and jury, or by a judge sitting alone, without a jury.

Today, there is normally no jury in civil cases, unless one of the parties makes special application that a jury should be summoned. If there is a jury, it decides the facts of the case and the judge decides the law. The judge then, if the jury has found for the complainant, will make the appropriate order, and usually awards the complainant his costs. It is the jury, however, which fixes the amount of the damages. If the case goes in favor of the defendant, the judge will normally award the defendant his costs to be paidby the complainant. Should the judge be sitting alone without a jury, he decides both fact and law, the amount of damages, and deals with all matters.

The Set of Rules

Law, then, must consist of a set of rules which are known or readily discoverable by those who must obey them. It is, of course, a maxim of English law that "ignorance of thelaw is no defense". However, this does not mean that each citizen is expected to know all the rules

which are in force which is clearly impossible – but that knowledge of them is available, since they are all published. The citizen, therefore, must have a general idea of the principles upon which English law is built, e.g. rights of property, person, contract, and he must be prepared to consult an expert in law for finer points, when necessary. A permitted defense of ignorance of the law would, clearly, make the administration of justice impossible.

Objectivity

"No man can read the thoughts of another" is a principle of wide application in law. Clearly, no authority can impose sanctions upon the thoughts of its subjects, although in some societies in the past this has been attempted. The law will recognize motives butonly as far as they are apparent and can be imputed from the actions following them. In other words, it is with actions, and not with thoughts and feelings, that law is concerned.

Enforcement

It is essential, if law is to operate efficiently, that it should operate only within an area controlled by an effective government. This may vary for different laws, since there may be different authorities operating within the same area, e.g. state law and federal law inthe United States of America, and bylaws of local authorities in England – but, nevertheless, the principle of territorial limits is preserved. If a government loses control of an area of its territory in that portion its law will not prevail. It is the duty of the government of the area concerned to make its laws effective by establishing judicial machinery for the investigation of alleged breaches of the law and for the enforcement of the law by sanctions, i.e. penalties or rewards designed to influence the human will to conform to the law.

Impartiality

Although it is not an essential component of law, in most civilized countries it is regarded as fundamental that the rules of law should apply to all citizens alike. This principle of impartiality is one of the principles of natural justice which has influenced English law in particular.

The Rule of Law

The rule of law is an essential doctrine of the constitution. It is not a written code of rules but a general principle implicit in the common law which the courts will apply, unless some statute can be quoted modifying its application. It has the following important aspects:

(a) No person can be punished except for a definite breach of the law, established in the ordinary law courts of the land.

(b) No person is above the law and everyone must bear the legal consequences of his own acts, i.e. there is equality before the law.

1.6.Sources of law

Unwritten Law

- Common Law

The common law which was originally based on the merging of the various local customary, laws especially in England as a result of the decisions of the royal judges. In fact, in the law report of Henry IV in the 15th century it is said:
"The common law of the realm is the common custom of the realm".

It is therefore unwritten, since it depends originally upon a judge's interpretation of the customs of the realm. When we come to discuss the importance of case law in the English judicial system, we shall show that the decisions of judges are, in fact, binding, but this does not invalidate the fact that the basis of common law, which has also absorbed mercantile law and some canon law, is essentially unwritten, although cases heard in the courts appear in written law reports. The reports only relate the unwritten law. You should note, at this point, that the expression "common law" has come to be used in four distinct senses, as follows:
- Historically, as above, to denote the body of law common to all England that arose to supplant the previous local systems of law.
- As opposed to equity (see below).

- As opposed to statute law, also considered below.

Thus, in this sense, it is sometimes said that a certain rule of common law was modified by an Act of Parliament.
- To mean the whole body of English law, including equity and statute law, as distinguished from any foreign system of law. Thus, we frequently speak of "*the common-law countries*", meaning England, the USA and those Commonwealth countries which have adopted English law, especially when we wish to contrast them with European countries, such as France and Germany, the legal systems of which have been strongly influenced by Roman law. Just as the Romans had their "*jus civil*" as the basis of their law, so English common law lies at the foundation of the English legal system. The law of torts is almost wholly based upon the common law, as is a good deal of English contract law. The common law has played its part in the development of the complicated system of English land law, and has covered departments of public law like constitutional law.

- Equity

Like common law, equity is also based on judicial decision, and not upon written rules. It originally stemmed from the Chancellor's interpretation of what was fair and just according to his conscience and, while in time it became rigid, it was originally flexible. Its basis is, again, unwritten.

Written Law

We have not yet discussed statute law, because it was a later development than common law and equity. It is true that, from Norman times onwards, decisions of the King-in-Council had the effect of law, but the promulgation of new laws was very rarely carried out, and **Magna Carat (1215)** is usually regarded as the first published statute.

A statute is a written law passed by the approved legislative process of the state, i.e. nowadays by the Queen-in-Parliament, and it supersedes any other forms of law. Thus, statute law can override both the common law and equity, since it is enacted by the sovereign power and is therefore superior to custom and judicial decision. Here, an important distinction must be made between "**the** law" and "**a** law". The former is the whole body of law, as defined at the beginning of this study unit, while "**a** law" is a written statute or an order made on the authority of a written statute. Thus, "**a** law" refers only to statute law. You need to understand this distinction clearly, since it sometimes serves as a basis for examination questions.

Unit Summery

In this chapter, we have gone through definition, function, classification and source of law. Law could be defined as *a body of rules for the guidance of human conduct, which are imposed upon and enforced among the members of a given state. Of course there is no universally accepted definition for the term law.*

Law has its own distinct feature. The basic features of law are:

- Law is obligatory
- Law has to be made by competent authority (the parliament) and every law isbacked by sanction or has organized enforcement machinery

Law serves the society in different manner. The basic functions of law are:-

- Dispute resolution
- Protection of property
- Preservation of state

Law could be classified to different categories based on its nature or features. We have for example customary law, criminal law, international law etc. The team/central idea of the different division varies based on the classifications.

1.7.Self-test exercises

1-Write at least four features of law.
2-What are the primary functions of law?
3-Discuss about rule of law
4- What does State of emergency mean?

1.8.**Progress Questions**

Multiple choices

Instruction: **Choose the letter which carries the best option**

1, All of the followings are **features of Law except _____.**

A, law has to be made by competent authority B, law is obligatory C, law is not obligatory D, every law is backed by sanction

2, _____ are rules agreed upon by persons for the regulation of their conduct towards each other's.

A, conventional laws B, international laws C, civil laws D, all

3, criminal and civil liability can be said that a **crime** is a wrong against the state, while a **civil** wrong is one against an individual.

A, True B, False C, both

4. The _____ is an essential doctrine of the constitution.

A, sources of law B, the rule of Law C, unwritten Law D, common Law

5, crimes such as murder, housebreaking, and theft are concerned under ___ Law.

A, civil B, conventional C, scientific D, criminal

Chapter Two
The Law of persons

2.1. Introduction

Dear learners, in this part you are going to see what a person is from legal perspective of having, exercising different facts. You may familiar with the term person to mean individual. Do all individuals are persons? We shall see it together by referring to our articles of civil right.

Learning objectives

After completing this unit, you will be able to:-

- Define the term person
- Distinguish legal and artificial person
- Compare and contrast personality of physical and legal person
- Discuss attributes of legal personality
- Identify moments of acquisition of personality of physical persons
- Explore legal safeguards the law makes available to incapable person

2.2. Definition of person

By the term person, ordinarily we refer to physical person or individual. In this case we all are physical persons or natural persons. In addition to physical person, the law personifies some entities such as organizations, associations etc. After all the formalities are satisfied organizations are legal by law. So, unless otherwise determined by the context, the term person means both human beings (physical person) and legal persons created by individuals (artificial person). This means, for all legal proposes, legal person are supposed equal to the physical persons. Physical person can do whatever human beings can perform.

Legal (juristic person) do have their own names and separate legal existence. Juristic person enjoy effects of personality by the help of physical persons that act through a representative capacity. Thus the term person embraces legal and physical person.

2.3. Attributes of legal personality

Personality distinguishes people and legal persons from other things. Animal and other things or organizations having no legal existence cannot be responsible for what they do. Some of the consequences of being a person are:-

i- Capacity to sue or to sued

To sue means to bring legal action demanding legal remedy. For instance if an animal say a dog bites you, you cannot sue a dog because it lacks legal personality. On the other hand if an organization performs badly on you, you can sue the company and on the other hand if you do some evil to one organization, the organization can sue you. This is because of the presence of capacity to sue and to be sued.

ii- Capacity to own property

iii- Capacity to enter in to contractual relationships

Contractual relations are relations in whom a person promises to do, to give, or not to doa given task to the other.

2.4. Personality of physical persons

Acquisition of personality

Art 1. Of the civil code, deals with the moment at which a person acquires personality. It states; human persons are subject of rights from birth to death. Personality of physical person's begins on birth and ends when they die. As stated in the article 2 of the civil code, birth by itself is not sufficient to confer the personality. In order to be considered as a person, the child shall be born alive and viable.

The exact time at which the child is said to be born is very important as he/she acquires legal existence from that moment. A child may be born after full 9^{th} month or below that. In this regard, it is not the time that takes the child in the mother womb that matters, but birth. On the other hand, birth alone, however is not sufficient. The new born child shall be born alive and be viable. The child may be born dead or die immediately. In this case the child is not viable. If the child before his separation from his/her mother's wombat or during birth dies, the law regards, it is not viable.

The child shall have the capacity to live. This is to say, the child should be viable. Viability is the capacity to live; if the child lives 48 hours after his/her birth, he/she may be taken as viable in accordance with Art. 4 of the civil code, if the child lives 48 hours and dies after that, he/she acquires personality. Exceptionally, where a child dies by external factors before living for 48 hours, she/he may be taken as viable .If a newly born child dies because of mishandling of a nurse afterhis/her birth, the death is caused by external factor. We may consider this kind of death asa death of person. Art.2 of the civil code provides "a child to be considered as born and viewed as a person, the following requirements shall be met.

1-His/her interest shall demand this benefit.

2-He/she may enjoy the benefit if born alive and viable.

A conceived baby to be supposed as a born one, if his interest so requires this state. How could the conceived baby's interest require the baby to be assumed born? Sometimes it may happen that unborn baby may have interest. Assume unborn baby lost his/her wealthy father in a car accident, what could seem secession? This time, we say the baby has interest and succeed his/her father even though not born.

2.4.1. Capacity of physical person

Capacity of a person is presumed. That is to say, everyone is considered by law as ifhaving capacity to enter in to any juridical act. Juridical act are acts producing legal effect. Therefore unless the law declares certain categories of persons in capable of exercising acts

recognized by law, we may assume capacity (Art.193 and 194 of the civil code). If a person is declared in capable, he/she cannot be bound by juridical acts he/she enters in to beyond the legal power guaranteed by law. Under this section we will see incapacity and related issues next.

2.4.2. Incapacity

Art.193 and 194 of the civil code focuses on this issue and accordingly incapacity is of two types, General incapacity and special incapacity. General incapacity is based on age, mental conditions of persons and consequence of criminal convictions. Special incapacityis based on citizenship. For instance certain fields of reserves in Ethiopia is for Ethiopian nationals only but not for foreigners.

General incapacity

A-minors

Art. 215 of the revised federal family code define persons regarded as a minor. It states "a minor is a person of either sex who has not attained the full age of eighteen years" These physical persons under the age of 18 are minors. According to the law, minors are not capable of engaging in commercial or other juridical acts, the acts of transactions are very important for human existence. To make use of such activities, minors should use minds of capable persons. In matters relating to economic interest, minors may be represented by tutors. According to Art.219 of the revised family code, where the parents of the child's are alive, both of them are taken as guardians or tutors. Where there is disagreement, the court determines the tutor or guardian and also according to Art.227 of the revised family code, where there is no relative, again the court determines.

Minority ends when the person joins the age of majority (becomes 18 years old) or emancipates. The other is marriage. There is an option to get married at the age of 16 by the permission of the ministry of justice. Art.311 states" where a minor is married in accordance with article 7(2) of this code; he shall be emancipated by the sole fact of such marriage". A minor may be emancipated by court order as stated in the Art.312 of the revised family code by the application of his guardian/tutor to the court at the age of fourteen.

B-person under juridical interdictions

The court interdicts the person by the initiation of some other people. The person to be interdicted may apply for the interdiction. This may be merely ideal as the person to be interdicted in most cases may not be able to understand the condition he/she is. In most cases, the application thus may be lodged by some relatives. The court examining the condition in which the person is, may declare interdiction. From the moment of interdiction, the person happens to be incapable to enter in to commercial transactions or other acts producing legal effects. As incapable person may not be able to understand what his/her advantage and disadvantage is, the hair of the incapable person may demand invalidation. Art 373(1) of the civil code states," acts performed by an interdicted persons in excess of his powers, may be impugned in the same circumstances as if they had been performed by

a minor." For purpose of invalidating acts of a minor, you may use analogy of the invalidation of contracts of minor.

As stated in the Art 341 of the civil code," a person shall be deemed by a low to be notoriously insane where by reason of his mental condition; he is an inmate of a hospital or an institution for insane persons or a nursing home, for the time for which he remains an insane". The person may also be under special protection where for his example his family or other people keep over him a watch required by his mental condition and where his liberty of moving is restricted, the court may declare invalidation.

Similarly infirm person (persons with physical deformity) may be considered as incapable. There are persons that may not be take care of themselves, administer their property because of their physical condition. According to Art 347 of the civil code, if a person has entered in to contract during the lucid period, the contract may not be invalidated unless the person or his representatives proves that the consent of the personis not free.

C .Legal interdiction

Legal interdiction is a process in which a certain civil rights of the criminals may be withdrawn because of criminal sentence passed on the criminals. The court examining the behaviors of the criminal, if assumed important, may declare interdicted on certain matters. A criminal may interdicted for instance not to enter in to some contractual agreement, if he/she do so, his/her acts may be invalidated by the request of public prosecutor according to Art.387 of the civil code.

2.5. End of personality

According to Art.1 of the civil code, physical personality starts at birth and ends on death.A dead baby cannot be taken as a person. A person to be taken as dead, the death shall be ascertained by medical testimony. A person may also lose personality, if he declared absent. As stated in the article 154 of the civil code, "where a person has disappeared andhas given no news of him for two years, any interested party may apply to the court to declare his absence". If the where about of a person is not known, the court for all legal purpose assumes the person dead and declares his absence. From this time on wards, the property of the person may devolve up on the heirs.

Summery

Dear students, in this chapter we have studies about personality. This could be seen from two perspectives. That is legal personality and Physical personality. Under legal personality it is better to distinguish majors from artificial persons (organizations). Personality distinguishes people and legal persons from other things. Persons have legal rights and obligations. If you are a person, you have the ability to sue or to be sued, Capacity to own property, Capacity to enter in to contractual relationships. Every human could not do this. That is there is incapacity of individuals because of being minor(incapacity because of age), person under juridical interdictions and due to Legal interdiction.

2.6. Self-test exercises

1-What are the difference b/n physical person and legal person?2-What are the attributes of legal personality?

3-What makes general incapacity from special incapacity?

2.7. Progress Questions

True or False

Write true if the statement is correct or false if the statement is wrong.

1. By the term person, ordinarily we refer to physical person or individual, in this case we all are physical persons or natural persons.
2. To sue or to bring legal action demanding legal remedy is consequences of being an animal.
3. If you are a person, you have the ability to sue or to be sued.
4, General incapacity is based on wealth or wealth conditions of persons and consequence of criminal convictions.
5, physical person means the law personifies some entities such as organizations, associations etc.
6, Some Animals having no legal existence can be responsible for what they do.

Chapter Three

Law of ContractsIntroduction

3.1. Introduction

Dear students, in this part we will see some basic concepts of contract. You may signed a contract with someone to get performed some activity; but that contract may be valid or invalid before law. What distinguishes a valid contract from non-valid? The chapter will broaden your thinking on such and related concepts.

Learning objectives:

At the end of this unit, you will be able:-

- Realize the importance of law of contract
- Explain elements of valid contract
- Discuss procedures of acquiring consent
- Distinguish effects of defect in consent and capacity of contracting parties
- Explain effects of vices of consent
- Discuss the effect of failure to comply with the formality requirement in contract
- Explain important rules of the civil code regulating performance of contract
- Identify exceptional situations in which a contract may be varied
- Analyze remedies of non-performance of contract

3.2. Definition of contract

The whole essence of business life is the making of contracts – contracts to perform work; contracts to buy and sell; contracts to make something; or to employ someone; orto use something. We must, therefore, know what a contract **is**, and **when we have one**. A contract is an **agreement** between **two or more people**. Every contract is an agreement but not every agreement is a contract. Two people agree about something to bedone. They are called "the parties".

First, the subject of their agreement may be such that neither of them has the remotest intention that any legal consequences should flow from it. For example, you invite someone to dinner and he says "*Yes, I would love to come*". You have an agreement. However, if he just does not turn up, neither of you would expect to hurry round to court and sue for the cost of the wasted food! So, the first essential of a contract is that the parties should intend their agreement to have **legal consequences**. In the second place, the agreement reached may have certain aspects about it which make it such that the law will not enforce it. In other words, although it isa contract, it is not a **valid** contract.

Article 1675 of the civil code provides **"a contract is an agreement whereby two or more persons as between themselves create**

, vary or extinguish obligation of a proprietary nature." This definition shows what the nature of valid contract should embrace.

Essential Elements of a Valid Contract

In order that an agreement can be a valid contract which the law recognizes and will enforce, it must contain certain essential features. We shall be discussing them all in much greater detail later, but at this stage you should know what they are.

(a) There must be agreement between the parties, or a **meeting of minds**. This is called "consensus ad idem".

(b) Usually, there must be "**consideration**" present – that is, something of **value** must be given in exchange for a promise.

(c) There must be an intention to **create legal relations**.

(d) The parties must have **legal capacity** to contract.

(e) There must be no circumstances surrounding the contract which make it

Unenforceable, void

(I.e. as if it had never existed), **voidable**, or **illegal**

Formation of Contract

Article 1678 of the civil code states: -No valid contract exists unless:

a-the parties are capable of contracting and give their consent sustainable at lawb-the object of the contract is sufficiently defined and is possible and lawful

c-the contract is made in the form by the law; if any

If the requirement of this article is met, the article binds the contacting parties (art1731). Therefore, a valid formed contract has to be respected by all contracting parties.

3.3. Capacity of contracting parties

Contracting parties must be capable enough that means incapability by one party creates impact to legality of a given contract. There will be legal interference to protect the incapable persons. As minor's faculty of understanding is not yet developed or the facultyof understanding of insane or persons under juridical interdiction is collapsed, these people may easily be cheated. There economic and other interest may easily be drawn by some deceitful people. People under legal interdiction have no physical or mental deficiency but the law supposed them incapable as punishment for their undesired behaviors.

The incapable if enters in to contract, beyond his or her legal power, may demand the invalidation of the contract. If not, a tutor or heir can demand invalidation of the contract. If the contract is invalidated, the incapable person will be free from contractual obligations. If the contract is invalidated, things or money given under the guise of the contract shall be returned back.

Communication of Offer and acceptance

In order to be effective, an offer (offer or) must be communicated to the offered or, at least, he must know about it. This is not quite as obvious as it sounds, because, if a person does something in ignorance of the offer, he can neither reap the benefit nor be bound by any obligations.

Art 1681- Form of an offer and acceptance

1- Offer or acceptance should be made orally or in writing or by signs normally in use or by conduct such that in the circumstances of the case, there is no drought as to the parties agreement.

2- The party who makes an offer may stipulate a special form of acceptance. b-Duty to accept

In certain exceptional cases, the law dictates a contracting party to accept the offer. As there is no option to refuse acceptance, mere receiving of an offer creates contractual engagement between the offer or and offered. Article 1683 of the civil code provides:

1- No acceptance shall be required where a party is bound by law or by concession granted by the authorities to enter in to a contract on terms stipulated in advance.

2- In such a case, the contract shall be completed up on receipt of the offer.

A party may also bound to accept an offer if bound by a concession granted by authorities. This is different from law. Authorities may permit certain persons to enter in to contracts without the need to communicate an acceptance. With order given by public authorities therefore an under taking may be compelled to accept an offer without communicating acceptance. In such a case too mere communication of an offer brings contractual relationship.

Pre-existing business relationships

Where contracting parties are already in the contractual relationship and if one of the contracting parties makes an offer in relation to the contract already existing, the offer may be accepted by silence. As that of cases of duty to accept if an offer is made on the basis of pre-existing business, communication of acceptance is not a requirement. Art.1684 of the civil code regulates the process of formation a contract where there is pre-existing business relationship.

Art.1684

1- An offer to continue or vary an existing contract or to enter in to subsidiary or complementary contract may be accepted by silence.

2- Such shall be the case where the offer is made in special document in forming regardedas accepted if no reply is given within a reasonable period of time.

An offer to be accepted by silence has to satisfy any of the following requirements.

i- It may be continuing the existing contract. If an existing contract is going to an end, any one of the parties may propose for, continuation of the contractual relationship.

A contracting party may demand extension of the contract. If one subscribes a newsletter for a year, before laps of the time, he/she has subscribed him/her to continue the subscription for the coming year. If the publisher after accepting the prescription keeps silent, the silence may be taken as acceptance.

ii- If you make an offer to vary the existing contract, the offer for variation may be accepted by silence.

iii- The offer may be related to a complementary of subsidiary contract.

Complementary contracts are contracts that complement an earlier contract. Subsidiary contracts on the other hand, are contracts supplementing and dependent on the earlier contract.

iv- The offer related to any one of the aforementioned cases to be accompanied by a written document.

General terms of business

The concept of general terms of business has its own legal recognition. Art. 1686 of the civil code express instances in which general terms of business may regulate the relationship of parties in Ethiopia. See the following facts.

-Ethiopian airlines have no time to negotiate with you.

-When you open a bank account, you follow what the bank employee directs you or follow instruction on papers.

-Different laundries have ground rules at the back of their receipt paper, not to lose your paper when you turn back and the like. These are the general rules, pre-determined obligations of business given to customers to obey and this governs business transactions. Art.1686 of the civil code a general term to have a binding effect, the following requirements shall be met.

a- where the offered knows and accepts the obligatory terms or

b-where the terms are prescribed or approved by public authorities

Art; 1685-invoices

Particulars entered by a party in an invoice shall not bind the other party unless they conform to a prior agreement or have been expressively accepted by the other party. Any variation in terms enshrined in the invoice cannot bind unless the new term is accepted by the purchaser.

It is clear that contracts may be formed orally, in writing or in any sign, if the contract was concluded before preparation of the invoice; the invoice merely supports the earlier contract.

Declaration of intention Art; 1687-declaration of intention

No person shall be deemed to make an offer where:

A-he declares his intention to give, to do or not to do something but does not make his intention known to the beneficiary of the declaration or

B-he sends to another or posts up in a public place tariffs, price lists or catalogues or displays goods for sale to the public

As the sub article (a) shows, the declaration of intention, not to have binding effect, shall not be communicated to the person that may benefit from it, the declaration may be taken as offer.

If I told to you, I will buy your sisters car by birr 250, 000, and told the same thing to your sister, both does not mean the same. In my speech with you, I am expressing my intention and in my talk with the owner (your sister), I have declared my intention.

Sale by auction

Auction is a declaration of intention where person competing to win the auction are referred as bidders. The bidders may make offer but there is no obligation to accept it.

Art.1688-sale by auction

1- who so ever offers a thing for sale by auction, shall be deemed to make a declaration of intention and an offer

2- In such a case, the contract shall be completed only where the thing is knocked down upon the last bid being made.

Discuss with your colleague Suppose, you have lost your son and declare publicly declare to give a reward to anyone who brings your child, how could you promise seen? Is it an offer or declaration of in tension?

See article 1690 of the civil code. As stated in the article:-

1- Whoso ever offers to another to enter in to contract and fixes a time limit for acceptance shall be bound by his offer until the time limit fixed expires.

2- He shall not be bound where his offer is rejected before the expiry of the time limit fixed.

- In the above example therefore, your promise is taken as an offer and deliveringthe child is an acceptance of the offer.

Withdrawal of offer and acceptance

After a person has sent an offer, he may change his mind and wish to avoid effects of the offer or acceptance. Article 1693 of the civil code regulates the process of offer and acceptance. The article states:-

1- An offer shall be deemed not to have been made where the offered knows that it is withdrawn before he knows or at the time when he knows of the offer.

2- The provision of sub-article (1) applies where acceptance is withdrawn.

The process of making withdrawal is also applicable for withdrawing an acceptance. If an offer or knows the acceptance on or before he/she knows or should know both of the

offer or acceptance simultaneously.

3.4. Defective consent1-Mistake

The subject of "mistakes" in contracts, and how they affect the validity or otherwise of the bargain one of the most illogical areas of contract law. Many of the cases turn on fine distinctions. As a generalization, if you make a mistake in entering into a contract, that is your bad luck – you must suffer the consequences. However, there are certain types of mistake which the law recognizes as affecting the agreement. In some instances, common law will declare that a mistake has served to nullify the consent, and so made the contract void "abs initio", or as if it had never been made. In others, equity will step in to allow the contract to be rectified or rescinded, or to act as a defense to a request for an order of "specific performance" of the contract (you will remember that specific performance is a court order compelling the guilty party to execute the contract accordingto its terms).

At common law, there are two basic types of mistake which may serve to render the contract void. These are **common mistake** (where both parties have made the error), and **unilateral mistake** (where only one of them has made error).

To be defective the mistake must be:-

-fundamental

-the mistaken decisive

Art.1669-mistake as to the nature or object of the contract

The contract may be invalidated on the ground of mistake where:a-the mistake relates to the nature of the contract

b-the mistaken party has under taken to make a performance substantially greater orreceive a consideration substantially smaller than he intended.

Common Mistake

Where the mistake is shared by both parties, it may mean that there is no true agreementor "Consensus ad idem" There is agreement of a sort but it is based on a false assumption, hence, common law may declare the contract void on the grounds that the agreement is not atrue consensus. There are only a few circumstances where this will apply.

(a) Mistake as to Some Fact Which Lies at the Basis of the Contract

If both parties assume some fact to be true, and that fact is a root condition of the contract, and it is either false or non-existent, then the contract is nullified.

(b) Mistake as to the Existence of the Subject-matter of the Contract

This, usually, occurs in contracts for the sale of goods. If both parties think they are contracting for a certain thing, and unknown to both it does not actually exist, then the contract is void.

(c) Mistake as to Title

This is an uncommon type of mistake but it does occur not least in examination questions!

The principle is that, if a man makes a contract in the belief that the subject-matter

belongs to the other party whereas in reality it is his own property, the contract will be void..

(d) Mistake as to the Quality of the Subject-matter

This category of mistake probably raises the greatest number of problems for the courts. An ordinary error as to quality will not avoid the contract, although it may well give rise to an action for damages. In order to qualify as a mistake which will serve to avoid the contract?

- It must be common to both parties, and

It must be such that the quality makes the thing contracted for an essentially **different thing** from that which it was thought to be.

(e) False and Fundamental Assumption

This is the last category of common mistake. "*Whenever it is to be inferred from the terms of the contract or its surrounding circumstances that the consensus has been reached upon the basis of a particular contractual assumption, and that assumption is not true, the contract is avoided"*.

Unilateral Mistake

As we mentioned earlier, this occurs when only **one** party is mistaken. It is fundamental that no contract can validly be formed if offer and acceptance do not correspond. So, if one party makes an offer which is accepted in a radically different sense by the other, there is no valid agreement.

However, contracts are construed **objectively** – so, the test is not what the intention of the one mistaken party was but, rather, what would a hypothetical reasonable man have understood from the words used? Cases can occur when there is so much ambiguity, whether actual or latent, that no reasonable agreement could be reached. Once again, these fall into various categories.

Mutual Mistake

If, even after applying the objective test, the parties are genuinely at cross-purposes as to the subject matter, or as to the terms of offer or acceptance, the contract will be void.

(a) Mistake as to the Terms of the Contract

A mistake as to the terms of a contract will serve to avoid the contract only if the mistake is **known** to the other party. In this case there is, probably, an element of bad faith, if not of actual fraud. The normal "objective" test can, therefore, be replaced by subjective intention. It must, however, be an error as to the **terms**, not as to the quality or substance. These latter constitute **motive**, and an error in motive will not avoid a contract.

(b) Mistake as to Person

The next category of mistake is where one party is mistaken as to the person with whom he has contracted. It is in this area where most confusion arises, and in which the courts have drawn fine distinctions. When solving examination questions on this subject, there are two vital questions which you must ask yourself:

"*Does the identity of the person with whom the contract is being made matter*?" In other

words, is it the intention to contract with that particular person, and **no other**? And, if the answer is "yes", then: "*Is the mistake as to his identity, not as to his attributes*" (e.g. solvency; character; socialstanding; etc.)?
If the answer to both these questions is "yes", then, in all probability, the contract will be avoided if a mistake has been made.

2-Fraud

In the case of fraud, in addition to the requirements of mistake, the law demands practice of some kind that may be conducted by contracting party or third party with intention of persuading another contracting party to enter in to deceitful contract.Art.1704 of the civil code declares the effect of fraud.
Art.1704-Froud

1-A contract may be invalidated on the ground of fraud where a party resorts to deceitful practices so that the other party would not have entered in to the contract, had he not be deceived.
2-A contracting party who has been deceived by a third party shall be bound by the contract unless the other contracting knew or should have been known of the fraud on themaking of the contract and look advantage thereof.

3-Duress

If a person is coerced into making a contract by fear for the physical wellbeing of himselfor his immediate family, or for the safety of the goods, or – on rare occasions – for his economic profits, this is called "duress". The coercion may be either actual or threatened. The so-called "contract" is void.

Duress to the Person

This consists of actual or threatened violence to the person, or imprisonment. It can be either in respect of a party to the contract or in respect of his immediate family. The degree of threat necessary varies with the physical or mental state of the person threatened. In other words, the test is a **subjective** one. If the person was in a state of fear, whether reasonably so or not, then this will suffice to permit him to avoid a contract he was coerced into making as a result of the threats of or actual physical violence or imprisonment. Imprisonment, in this sense, does not necessarily mean being thrown into goal. It also means loss of liberty, e.g. by being locked in a room.

Duress of Goods

This is actual or threatened unlawful detention of goods. This type of duress does not, at common law, entitle a party to avoid a contract entered into as a result of the duress but,in equity, it entitles him to recover any money paid in order to secure the release of the goods.

Economic Duress

The threat of loss of profits if a contract is not made is called "economic duress". It has only fairly recently been recognized by the law as a possible cause for avoiding a contract, and the law on economic duress is not yet fully developed.

The proposition is that, if a person is induced to enter into a contract by fear of loss if he does not agree to the contract, this may constitute actionable duress. However, the degreeof coercion must be substantial.

Article 1706-Duree

1-a contract may be invalidated one the ground of the ground of duress where the act of duress led a person to believe that he, one of his ascendants or descendants or his spouse were threatened with a serious and imminent danger to the life, person, honor or property.2-Duress must be such as to impress a reasonable person

3-the nature of duress shall be determined having regard to the age, sex and position of the parties

Art.1707-Duress by third party

1-A contract may be invalidated on the ground of duress not withstanding that duress was exercised by a person other than the party who benefited by the contract

2-The party who invokes duress to avoid the effect of a contract shall make good the damage arising out of the invalidation of the contract where duress was exercised by a third party and the other contracting party did not and should not have known thereof.

3-Undue influence

Undue influence is said to exist where one person has a special relationship with another and, as a result of this relationship, that other is induced to enter into a contract to his disadvantage. A contract is voidable at the option of the innocent party if it was entered into as a result of undue influence.

Examples of where such a confidential relationship is likely to exist are:

- Parent and child

- Guardian and ward

- Solicitor and client

- Doctor and patient

- Religious adviser and the person to whom advice is given

Strangely enough, it is not automatically presumed between husband and wife, althoughit can be shown to exist. Nor is the above list exhaustive. Any situation where trust and confidence is imposed by reason of the relationship can be one where undue influencecan apply. These persons are subjected to:

-threat to exercise their legal right

-reverential fear

-unconscionable contractsArt.1709-reverential fear

1-fear of an ascendant or a superior shall be no ground for invalidating a contract whereno duress where exercised

2- The provision of sub-article 1 shall not apply where the contract was made with the

person inspiring the fear and such person derived an excessive advantage from the contract.

Generally speaking for the contract to be free from defect what should be taken in to consideration and as an element of the contract are: object, form time ,and place of formation of the contract.

3.5. Void and illegal contracts – A general perspective

For one reason or another, the state may either refuse to assist a person in enforcing certain contractual rights or it will declare a contract to be null and void. Contracts fallinginto these categories are, in some way, tainted. However, the reasons why they are tainted, and why the state takes or denies the actions it does, cover a very wide range of situations. A contract to commit murder may have all the ingredients of a perfectly valid contract. However, quite obviously, the state is not going to enforce it. Can you imagine the furor there would be if a judge made an order of "specific performance", compelling aman to carry out his contract to strangle someone's mother-in-law, according to its terms?At the other end of the scale, a contract may either be only mildly naughty or it may have no moral taint whatsoever but merely be contrary to some state regulation. A contract to fiddle your income tax might fall into the former category, and one to sell goods without having obtained a statutory license into the latter.

I-Objects Illegal by Statute

Statute may declare certain types of contract void ability – that is, the contract itself is illegal and incapable of creating any rights. Certain gaming and wagering contracts fall into this category.

Gaming and Wagering

The subject of gaming and wagering is extremely complex. However, a short summary is called for. A wagering contract is one where there must be two parties or sides who both stand to win or lose on an uncertain event. Buying a sweepstake ticket, entering a coupon for the pools, or betting on the "tote" at a racecourse, are not wagering contracts. In all of these, only **one** of the parties stands to win or lose. Another essential of a wagering contract is that the parties have no interest in the contract, other than that created by the bet. This lets out of the category such transactions as insurance contracts and Stock Exchange bargains, both of which bear a superficial resemblance to wagering.

II-Objects Illegal at Common Law

Public policy decrees that the courts will not assist parties who have made certain typesof contract. The contract is not illegal to make but its object is illegal. Public policy is an imprecise concept, and it changes as time goes by. There are, however, broad categories.

(a) Agreements to Commit a Crime, a Tort, or to Perpetrate a Fraud

Plainly, a contract the object of which is to commit a criminal offence cannot be enforced. However, if an illegal act is committed during the performance of an otherwise perfectly lawful contract, it will not necessarily render the whole contract unlawful.

b) Agreements Injuring the State in Relation to Other States

These can either be contracts with an enemy in time of war, or they can be contracts which are hostile to a friendly state.

(c) Agreements which Tend to Harm the Public Service

Any agreement which tends to harm the public service is contrary to public policy. Examples are:

- Contracts for the sale of public offices;

- The assignment of salaries from public offices;

- Contracts for a person to use his influence to secure for another a title, a public or government office, or similar.

(d) Agreements to Pervert the Course of Justice

Contracts under this heading usually comprise agreements not to disclose crimes, or not to prosecute for criminal offences. They are unenforceable but, in addition, by virtue of the

(e) Agreements Tending to Abuse the Legal Process

These largely comprise the acts of "maintenance" and "Champerty".

Maintenance is the supporting (usually financially) of litigation in which the person maintaining has no legitimate interest.

Champerty is where a person assists in litigation in exchange for a share in any proceeds gained from it – e.g. a solicitor representing a client for a percentage of the damages awarded to his client.

(f) Agreements Contrary to Good Morals

Contracts which are for immoral purposes will not be enforced.

(g) Contracts in Restraint of Marriage which Affect the Due Discharge of Parental Duty

It is against public policy to restrain the freedom of marriage or to promote for a fee the marriage between one person and another.

Likewise, agreements for a fee to promote a separation or divorce are unenforceable, or those to transfer rights and duties in respect of a child from its parents.

(h) Agreements which Oust the Jurisdiction of the Courts

(j) Agreements in Undue Restraint of Trade

These also form a most important category of contracts which are contrary to public policy but also one which contains fine distinctions. The problem is that, prima facie, any agreement is void if the purpose of it is to restrict the liberty of a person in the future to carry on trade with persons who are not parties to the contract – that is to say, to restrain trade. But, at the same time, a person has every right to protect his interests and his business from unfair competition. There is an obvious clash between these two propositions. So, the principle is that a person may restrict the right of another to trade, only so far and to the extent that is necessary and reasonable to protect his legitimate interests.

Unconscionable contracts

Sub article (1) of the Art.1710 of the civil code defines the general rule of unconscionable as stated below.

"A contract may not be invalidated on the sole ground that its terms are substantially more favorable to one party than to the other party"

Unconscionable contract tainted by simplicity of mind, senility or manifest business inexperience may render a contract to be invalidated. This is simple on the ground of incapacity than simplicity of mind as per Article 1710 of the civil code. So it is necessary to show unconscionably rather than simplicity.

3.6. Effect of contracts

A validly formed contract is assumed as a law for contracting parties. That is, it governs the relationship between the parties. Article 731 of the civil code declares the effect of contract.

1-The provision of a contract law; fully formed shall be binding on the parties as though they were law.

2-The content of the contract shall be determined by the parties subject to the mandatory provisions of the law.

3-The provision of this title shall apply to all contracts where such provisions are of a mandatory nature or their application has not been set aside by the parties.

Contractual terms or obligations may be interpreted in accordance to the rules set from Art.1732-1739 of the civil code. Techniques of interpretation may be employed where words or phrases stated in the contract are doubtful. Where words in the contract are clear no need for interpretation.

3.6.1-Performance of contractual obligation

Performance is doing a promise obligation. If you agree to sell your house for birr 500,000 and hand over your cash according to your contract, you should handover the house to the buyer. So the contract itself answers the following questions related to performance.

Performance by whom and Performance to whom

Art.1743-payment to unqualified person

a- payment to a person unqualified to receive on behalf of the creditor shall not be valid unless the creditor confirms it or such payment has benefited him
b- payment shall be valid where it is made in good faith to a person who appears without doubt to be the creditor

Since the subject matter of contract is related to business transaction (good and services), the contracting parties have to perform their contract lawfully. If one of the contracting party demands performance, the other contracting party may refuse performance if any of the following condition is satisfied.

-Where the time of the performance is extended by agreement, until the agreed time lapse, the debtor cannot be forced to discharge the obligation.

-where the party declaring payment is insolvent, a contracting party may refuse to discharge his/her obligation

-Where a contracting party in clear terms informs a contracting party that he would not

perform a contractual obligation, the other party can refuse performance

3.7. Variation of contracts

In principle a contract lawfully formed has to be maintained irrespective of change of market price or economic situation in which the contract is based on. A court cannot modify terms of the contract to make it suitable to the changed situation. Exceptionally however, contractual obligation may be varied. For example

-where the contracting parties agree for variation they can do it at any time i.e. where the contracting parties all agree to change their respective obligation, there is no limitation

-where the contract contains an arbitration clause for issues related to variation, the arbitrators in accordance with power vested on them can vary the terms of the contract(Art.1765 of the civil code)

-where there is special relationship between the contracting parties the court may vary terms of the contract

-contracts with the government or public administration may be varied where the economic basis of the contract was changed because of act or contribution of official decision of public authorities or government

-terms of the contract may be varied where part of the obligation become impossible

3.8. Non-performance of contractual obligation

We have already said a contract binds the relationship between the parties. This requires performing in accordance to their agreement lawfully. In case if there are situation for nonperformance, Art.1772 of the civil code states: „"A party may only invoke nonperformance of the contract by the other in default by requiring him by notice to carry out his obligations under the contract"

In certain circumstances, the law dispenses the requirement of giving notice. See the following points of Art.1775 of the civil code.

a- Where the obligation required from the contracting party is not to do and the party breaches his duty by doing, the creditor of the assumed obligation may not notify the party at fault.

c- where the date of performance is compulsory and the debtor failed to discharge his obligation on due date there is no need for default notice

d- where the debater has declared in writing that he would not perform his contractual obligation, the creditor need not give default notice

d- Contracting parties using freedom of contract may avoid the requirement of giving default notice. If the contract discloses this, there is no need to give default notice (Art.1775 (d)) of the civil code.

3.9. Remedies for non-performance contractual obligation

Art.1771 of the civil code reveals three remedies for non-performance. These are: -1-forced or specific performance

2-cancellation3-damages

Where a party fails to respect terms of his contract, the creditor (the person demanding performance) may ask any one of the remedies stated.

Cancellation

This could be by:-

i- Judicial cancellation- the court order cancellation depending on the criteria's of art.1785 of the civil code. This based on fundamentality of breach and the requirement of good faith(the interest of the parties)

ii- unilateral cancellation- this may be possible due to:-

-freedom of contracting parties to cancel their contract

-expiry date of contractual obligation

-where performance of obligation is impossible

-where a debater declares in writing that he/she would not discharge an obligation he/she owes an other

Damages/compensation

This is monitory reparation for the economic loss that may happen because of non-performance. If a debater fails to perform contractual obligations because of unexpected events, he/she may not be forced to pay damages. The unavoidable and unforeseen circumstances are called force majeure.

Art-1792 –Force Majeure

1- Force Majeure results from an occurrence which the debtor could normally not foresee and which prevents him absolutely from performing his obligations.
2- 2-Force Majeure shall not exist where he could normally have seen foreseen by the debtor or when it renders more onerous the performance by the debtor of his obligations.

An event to be force majeure, the following requirements shall be met.

-the event has to be unforeseen

-the event has to prevent performance absolutely.

The following could be seen example of force majeure

-Accidental death of a debater who has agreed to perform contractual obligation personally

-Enactment of new legislation

-destruction of the subject matter of contract (for instance if to sell donkey, death of the donkey, if sell of house fire on house etc.)

-war making performance fully impossible

Dear students with regard to damages to the different subject matter of contract the calculation varies accordingly. To broaden your understanding you can ask and discuss with professionals on the sector and with this we came to the end of this unit.

Summery

In this unit, we have seen about contract law. Contract could be of different contracts to perform work; contracts to buy and sell; contracts to make something; or to employ someone; or to use something. Whatever the contract is it should be lawful and then it serves as a law between the contracting parties. Of course, all contracts are not neither fully defective, nor fully perfect. This demands correction based of freedom of the contracting parties or by their good will for their good will. Contract impulses obligation of performance and not to perform the contract brings to be applied what the law said for non-performance of contractual obligation usually damages. Of course, there are cases related to force majeure where unforeseen happened and to ask damages for non-performance is impossible.

3.10. Self-test exercises

1-what are the essential elements that need to be satisfied to form a contract?2-Differentiate offer and declaration of intention.

3-Explain exception to the rule, "silence does not amount to acceptance" 4-What does performance of obligation mean?

5-What are the three remedies the law provides for non-performance of contractual obligation?

6-What is the difference between normal and greater damages?

7-Is there any requirement for an event to consider as force majeure? Discuss

3.11. Progress Questions

Multiple choices

Choose the best appropriate answer form given alternatives

1, _____ occurs when only one party is mistaken**.**

A, mistake as to title B, unilateral mistake C, common mistake D, mutual mistake

2, ___ is a declaration of intention where person competing to win the auction are referred as bidders.

A, sale by auction B, general terms of business C, pre-exists business relationships D, all 3, 3, 3, when two people agree about something to be done. They are called_____.

A, the companies B, the individuals C, the parties D, none

4, Identify the essential elements of a valid contract.

A, consideration B, legal capacity C, meeting of minds D, all

5. After a person has sent an offer, he may change his mind and wish to avoid effects of the offer or acceptance, this means _____.

A, capacity B, withdrawal of offer and acceptance C, declaration of intention D, none

6, what are the remedies for non-performance contractual obligation?

A, damages B, cancellation C, forced or specific performance D, all

Chapter Four

The Law of Sales

4.1. Introduction

Dear students, various special types of contract have additional rules superimposed on the general ones, which are applicable only to those particular contracts, namely:

- For the sale of goods

- Of agency

- Of installment

-Of insurances

- Of carriage of people and goods by sea, land and air and so on. In this unit we will deal with law related to sales.

Learning objectives:-

- Distinguish the essential elements of contract of sale

- Distinguish obligation of seller

- Disposes cases involving issues of obligation of seller

- Explain each of obligation of buyer

4.2. Formation of contract of sale

Contract of sale of goods is a contract by which the seller transfers or agrees to transfer the property in goods to the buyer for a money consideration, called the price. In order to form a contract binding all the contracting parties have to be competent enough to enterin to legally enforceable acts. If for instance a minor is party to sales of contract, the contract is subjected to invalidation. On the other hand for capable contracting parties, the parties should give their consent and this has to be suitable by law. That is, it should be free from vitiating factors. These are defined by the articles from 1696 – 1710 of the civil code. For instance if you have purchased an item by mistake because of fraud or someone has coerced or forced you, you may demand invalidation of the contract.

In addition, the contracting parties owe each other shall be defined possible and lawful. In this regard Article 1678 of the civil code uses the expression “object of contract” to mean obligation of the contracting parties and hence a contract is combination of obligation of the contracting parties. It encompasses a promise one makes to the other. So a person who that desire to enter in to contract has to have the ability to charge the promise. Onthe other hand if you promise a thing there is not exist, there is no contract. Similarly, where contract of sale contrary to any law enacted by the Ethiopian legislature or accepted morality .That is this type of agreement does not lead to legal effect. Immoralityalso has identical effect. For example sells of kids. As a rule, sales law does not demand parties to follow a given

instruction. For instance if a buyer and seller agree to buy or sale that is enough. But if a law prescribes a given formality, it requires the parties to go through that formality.
The property that is sold could be tangible i.e. movable and non-movable properties and intangible assets like good will. For movable properties articles from 2266 to 2367 of the civil code are applicable. For intangible assets, it is important to regulate by the commercial codes.

Sale of certain things that are attached to movable properties is also taken as a movable property. A person may sell a standing tree. As the tree cut down and detached from the land, it converted to this category. Things that are attached to building, if they could be detached without losing its value, may be sold separately. Future things may also be sold. This thing is produced in the future. In the case of future things the law demands, the main materials necessary for production delivered by the producer or the manufacturer. And this is sale of future material. On the other hand, if the materials are supplied by the purchaser, this is this is contract of work.

The other essential element for the formation of sale contract is the price at which the thing is to be sold. The price shall either be agreed or procedures enabling determination of the price shall be determined. The obligation of the buyer is said to be fixed in the contract of sale. If the price is not fixed in the contract, the buyer's obligation would be obscure. This makes the contract of sale of no effect. Therefore unless the price is fixed or a procedure enabling the determination is agreed, a sales contract cannot be formed. To determine the price, the buyer and the seller may agree or may not agree. If not agreed, they may refer to third party to determine the price for example in purchase of a car they may refer to a mechanic and if the mechanic is unable to determine or refuses to determine, there would be no contract by referring to Article 2271 of the civil code.

If the price is not fixed at the formation of the contract and merely procedures are set, the contract is conditional. Conditional contract are not pure and simple but depend up on fulfillment of conditions. If the condition subsequently fails there will be no contract. Determination of price is a condition necessary. Until the price is sharply determined , there is contract but it is temporary, If determination of contract to neutral third until the price is fixed, there is contract. The existence of the contract is not however final, its life depends on the third party desire and ability to determine the price. There are other procedures enabling determination of the price. A buyer and a seller for example refer the determination of market price or prices usually determined by the seller. If the price at which the things is to be sold depends on the market, the buyer and seller may refer the determination to a given market.
In fear of price fluctuation, a buyer and a seller may agree to the effect that the sales price to be the market price. For instance see the coffee market which fluctuates from time to time. So, the price is arranged by the market specially the global market.
Article 2307 of the civil code, states"" where the sell relates to a thing which the sellers

normally sell, the parties shall be deemed to have concluded the sale at price normally charged by the seller having regarded to time when and place where delivery is to take place." Assume a seller sells a given item at a certain price. The price is the same in most cases. This is the price normally charged by the seller.

4.3. Subject matter of the contract of sale

It is fairly obvious that the contract must be in respect of "goods". But what are "goods"? Globally different scholars of law define goods from the spirit of the following concept in the following definition.

"*Goods include all personal chattels other than things in action and money; and in particular „goods" includes emblements, industrial growing crops, and things attached toor forming part of the land which are agreed to be severed before sale or under the contract of sale*".

"Things (or choses) in action" are intangible rights that cannot physically be handled – such as patents, copyrights, shares, securities, etc. – and "emblements" are products created by annual industry, or the profits of a crop which has been sown. Wheat is emblements,but grass is not.

So, in other words, "goods" covers not only those things which are **normally associated** with the word, but also agricultural produce, cut timber and so forth. In particular:

(a) **Motor cars** are in all respects "goods".

(b) **Ships and aircraft** are covered by the definition, but they are subject to special rules, and certain aspects of the law of sale of goods cannot apply to them.

(c) **Coins** – current coins of the realm are money, and therefore not goods. But collectors" pieces, even those which are current legal tender but which have a market value in excessof their face value, may be "goods" (***Moss v. Hancock (1899)***).

(d) **Water, oil, gases** – these are capable of being bought and sold as goods, so come within the definition. For example, when you buy a cylinder of CO2 for a soda stream, you are certainly buying "goods" other than just the metal cylinder.

(e) **Electricity** – there is some doubt about this. It is probably best to say that electricity is not "goods", but other forms of power may be.

In ***Bentley Bros v. Metcalfe & Co. (1906)*** a landlord hired a machine to his tenant. He also supplied the mechanical power by means of a shaft to drive it.

HELD: The power to drive the machine was consumed in the process, therefore it was bought and not hired.

(f) **Domestic animals** – these are "goods", but wild animals are not.

(g) **Buildings** – whilst attached to the land on which they stand, they are not goods; but if they are demolished and sold, the constituent parts then become goods.

4.4. Obligation of the parties to the contract of sale

It is repeatedly pointed out that the contract of sale is a special contract that comprises obligations of the buyer and seller. When you purchase a given item, you promise to pay money. The seller on his own part promises to deliver a given item. A promise one makesto

the other is his/her obligation.

4.4.1. Obligation of the seller

Some of the obligation of a seller has to discharge are stated in Article 2273 of the civil code. These are:

A- delivery of the thing sold

Delivery is handling the thing sold to the buyer. The buyer has to use the thing purchased. Use of the thing is possible only if the thing sold is delivered. There are various ways of effecting delivery.

- **Modes of delivery**

Delivery could be actual, for example if the owner of the camel who sold the camel actually handover the camel to the buyer, it is referred as actual delivery. Delivery can also effect constructively. This is to refer the thing will not actually delivered to the buyer but after happening of certain acts the law regards the thing delivered. For instance if you buy TV and the TV is at the shop of the seller, the seller cannot further resale the material and also you cannot use the TV because it at the sellers hand.

- **The thing to be delivered**

Article 1745 of the general contract refers that the buyer cannot be compelled to take lesser or greater thing. This is to refer the seller has to deliver the agreed thing. And in this instance delivery of any other thing is considered as breach of contract.

Similarly the seller has the thing he/she promised to sell. If you are a buyer and willing to take the partial delivery, you can do so. But sometimes it may happen that part of a thing may contest. This is to refer the seller may deny the fact that he /she agreed to sell a portion of the things. In such a case, you may take the uncontested thing and continue litigation for the defined one by referring to the concept of Article 1746 of the civil code.

The rule of full delivery, exceptionally, is not strictly applicable to fungible things. These are things that may be changed one another. If you are agreed to purchase a given donkey and the seller delivers you another donkey, you can refuse to take delivery of the given donkey even if the donkey is similar with the one you promised to purchase. The reason for this is the donkeys are even similar; they are different in some regards. The quality, power and strength and age may not identical.

If the quality of fungible things is the same, the seller can deliver any of the similar things. With regard to fungible things, a slight difference may not entitle the buyer to refuse acceptance of the delivery. From the concepts of article 1748 if the buyer agrees to buy 100 kg of coffee, he/she cannot refuse to take 100kg of coffee. The difference isimmaterial.

What about Gold? Discuss with your colleagues

The place at which the thing sold is to be delivered May or may not be agreed in the contract. The buyer and the seller are free to stipulate any place that pleases them. In the absence of agreement the law fills the gap.Article2279 and 2280 spell out the place at which the thing sold is to be delivered. If the place where the thing delivered was not known at the time of the formation of the contract, in the absence of agreement, the thing will be delivered at the seller's business place. If the seller does not have specific business place or where it is doubtful, the buyer may demand delivery at the seller's residence, it is the place where the seller normally resides at the time of conclusion of the contract of sale. When the place where the thing sold stipulates is known at the formation of the contract, the buyer may take delivery from that place. If the place where the thing at the time of the formation of the contract is changed before it is delivered, the buyer has no obligation to take delivery from the changed.

B-Transfer of ownership

Ownership of a thing may be transferred from one person to another in two ways. As in stated in the article 1184 of the civil code, ownership of a thing may be transferred by operation of law and by the virtue of the contract.

i-Good faith acquisition Art.1161

1-Who so ever in good faith enters for consideration in to a contract to acquire the ownership of a corporeal chattel shall become the owner there of by the virtue his good faith when he takes the possession of such chattel.

2-His rights not affected by the fact that the person with whom he contracted had no valid title.

Art. 1163-time when good faith must exist

1- Good faith must exist at the time of the entry in to possession

2- Discovery by the possessor that he acquired the thing from a person who was not entitled to transfer the ownership there shall be of no effect where such discovery occurs after he entered in to possession

Article 1161-principle

1-Whosoever in good faith enters for consideration into contract to acquire the ownershipof a corporeal chattel shall become the owner there of by virtue of his good faith when hetakes possession of such chattel.

2-His rights shall not be affected by the fact that the person with whom he contracted hadno valid title.

For the person to be an owner of a property because of good faith, the following requirements shall be met.

a-The acquirer has to be in good faith

a- There shall be contract of consideration between the non-owner dealer the good faith

acquirer

c-The contract shall to be acquire ownership of a movable property

d-a person to acquire ownership by good faith, shall take possession of the property. ii-Transfer of ownership by virtue of contract

Whenever a valid sales contract is entered between an owner or a representative of an owner and a purchaser, on delivery of the subject matter of sale (the movable property) ownership is transferred to the purchaser. In a very exceptional cases, in addition to delivery, the law demands writing or registration. If you sell a car, delivery of the car and its documents alone does not transfer ownership. The sale shall be in writing and shall be registered. The other cases the law demands is the seller shall transfer peaceful procession. Art.2281 of the civil code states "the seller shall take the necessary steps for transferring to the buyer unassailable rights over a thing. "Unassailable right means undistributed right. This means the buyer has to enjoy the property he/she has purchased without interference of anyone. If anyone claims ownership of the thing purchased, the seller will be responsible.

Warranty against dispossession, therefore, is a guarantee the law confers on the buyers. If the person claims to take property purchased, the seller is responsible as the law expects him/her to sell a property free from any kind of claim. The seller has to deliver a peaceful right. Disturbance may be classified in to two.

1-diterbance in fact2-diterbance in law

Disturbance in fact is a simple material disturbance. When someone took forcefully a book you have purchased, the seller is responsible as the law expects him/her to sell a property free from any kind of claim.

Disturbance in law is peaceful disturbance. In this case, the third party peacefully claims to disposes the buyer. The third party peacefully brings action against the buyer for dispossession. The seller is responsible for peaceful disturbance. Article 2282 of the civil code states "the seller shall warrant the buyer the buyer against any total or partial dispossession which he might suffer in consequence of the third party exercising a right he enjoyed at the time of the contract." If the entire property or part of it is taken by a third party, the seller is responsible to the extent of the dispossession.

Whenever an action for dispossession is instituted against the buyer, he/she shall make call on the guarantee. This means the buyer has to call the seller to defend the case. Art.2285(1) of the civil code states "where the buyer is sued for dispossession, he shall join the seller as a party to the proceedings instituted against him." If the seller is calledin due time, she/he has to defend the case and avoid dispossession or compensate the buyer.

There are certain situations in which the buyer may not enjoy warranty against dispossession. The following are instances in which warranty against dispossession not available.

a- Where the buyer, at the time of entering in to the contract of sale was knowledgeable as to the defective title of the seller and the buyer is not protected by the warranty against

dispossession.

Art.2283(1) of the civil code states, "where at the time of the contract, the buyer knows that he risks dispossession, the seller does not warrant the thing unless he has extremely undertaken to do so." If the buyer for example before or at the time of the formation of contract had information that the seller is not entitled to sell the property, the law does not protect the buyer by the shield of the warranty against dispossession. Awareness of defective title of the seller cannot bar or bloc the buyer's right against dispossession where the seller gave an express warranty or where the thing is encumbered with pledge.

-Expression of warranty- a seller with defective title may express warrant a hesitate buyer for warranty against dispossession.

-Where the thing sold is pledged the buyer of the pledged thing cannot be deprived to enjoy the protection of warranty against dispossession.

Art. 2283(2) of the civil code provides, ""Warranty shall, however, be due where dispossession is due to the falling of the pledge made by the seller.""

b- Exclusion of the pledge against dispassion

The implied warranty may be avoided by a contrary agreement. The implied warranty is designed to protect the buyer. The buyer, however, may waive his/her right and agree to purchase a thing without the protection of the warranty against dispossession.

The buyer and seller are always free to relive the seller from all obligations that may emanate from dispossession. The obligation to refund the purchase price may also be excluded by such express agreement. The seller, however, may not benefit from the exclusionary provision if he/she has cancelled important information if known the buyer would not agree to the exclusionary provision.

If the seller has cancelled threats of dispossession for instance if committed fraud. Sub article 3 of art.2284 of the civil code declares, "A provision exclusion or restricting the warranty shall be of no effect where the seller has intentionally cancelled that a third party had a right on the thing or dispossession is due to the act of seller" Similarly if the seller has contributed or caused the dispossession, he/she cannot make use of the limitation or exclusion of the warranty against dispassion.

On the other hand, in accordance with Art.2286 of the civil code, if the buyer is absolutely sure that the third party claimant is an owner and dispossession is inevitable, he/she may surrender the property and demand compensation and purchase price from theseller.

4.5. **Consequence of transfer of ownership**

The effect of passing the property in goods to the buyer is to transfer to him the title and full legal interest in the goods, subject only to any rights in the goods retained by the seller or by any third parties. It is a condition of the contract that any such retained rights are first disclosed to the buyer. Before the property has passed, the seller can dispose of the goods to a third party, albeit in breach of contract with the buyer, and the third party will thereby acquire a good title to them. The reason is that the title is still vested in the seller until the property passes; hence he (or she) is at liberty to pass that title to someone other than the buyer. The disappointed buyer is, of course, entitled to damages for breach of contract, but not to the

goods themselves.

The **exact point in time** when the property **passes** is most important in the event that either buyer or seller goes bankrupt (or, in the case of a company, into liquidation or receivership). In the event of the seller becoming insolvent whilst, still in possession of the goods: If the property **has passed** to the buyer, he can, on tendering the price, demandthe goods themselves from the liquidator or trustee in bankruptcy. If the property has not passed, the entire buyer can do is to seek damages for breach of contract. If the seller is hopelessly insolvent, this right may be worthless. The general rule of transfer of ownership has certain exceptions. The exceptions are stated in Art.1758 (2) of the civil code and re-mentioned in art.2325.

Art.2325-Delay of the buyer

1-The risk shall also transfer to the buyer from the day he is late in paying price.

2-Where the sale relates to fungible things, the delay of the buyer shall not transfer the risk to him unless the thing clearly designated for the performance of the contract, has been especially allocated to the buyer and the seller has sent notice to the buyer to that effect.

3-Where tangible things are of such nature that the seller cannot set aside part of them until the buyer takes delivery, it shall be sufficient for the seller to have performed all the acts necessary to enable the buyer to take immediate delivery.

Sub article 1 of Art.2325 incorporates the first exception. The buyer may bear risk even where he/she is not an owner. In Art.1758 of the civil code, where a buyer is late in taking delivery, though ownership is with the seller, risk transfer to the buyer. Therefore itis important to read art 2325(1) with article 1758(2) of the civil code.

If you buy from Ato Balchas store 10 quintals of teff and by chance all Materials in the store is stolen, do you legally request your property? Discuss with your colleagues

In the case of international sale of goods, risk and ownership may not necessarily go together. Risk in the case of international sale transfers after the thing sold is delivered to the carrier or loaded on the board of ship. The moment of the transfer of risk depends up on agreement of the buyer and the seller. They may refer to the terms set out by international chamber of commerce.

Do you remember CIF and FOB from your marketing course?

If the term agreed by the parties is CIF (cost insurance freight) risk transfer to the buyer from the moment which the thing is put at the shore of the sea, the buyer bears the risk even before the sold thing is loaded. He/she will give the document specifying delivery of a thing which is referred as bill of lading. The shipper after receiving the goods for delivery gives the document that serves as receipt and that disclose the true nature of the property received for delivery. The seller after having payment or otherwise sends the bill of lading to the buyer. So then the buyers possess now ownership. Of course the risk transferred before the buyer get ownership.

Fob on the other hand means free on board .In this term the seller has the obligation to cover all costs until the sold thing is loaded. So the risks transfer after completion of effective loads by the seller. After effective loading the risk transferred to the buyer. For any sudden risk or accident that may happen before the goods are loaded, the seller is responsible.

The other widely used term is container trade term. In this case, the seller delivers the thing sold to the shipper in the in land at the container trade station. The container trade station may stipulate in the cities like Addis Ababa. From the moment the thing is delivered to the container station, the risk transfers to the buyer. The shipper at the container station prepares a received bill of lading and gives to the seller. The seller sends the bill of lading to the buyer. From the moment of receiving the bill of the bill of lading the buyer acquires ownership over the goods delivered to the carrier. Article 2226-2328 and art.2397-2402 of the civil code are meant to regulate legal issues relating to the sea transport.

Sub 1 of art.2326 of the civil codes states," where the sale relates to the thing under voyage, the risks shall be transferred to the buyer from the day when delivery has taken place by the thing having been handed over the carrier." The provision is in line with the rules of transfer of ownership in the case of CIF and container trade terms.
The other exception to the general rule of transfer of risk is where the ownership of the thing sold is reserved on the seller. In rural areas where a rich farmer sells cattle to a poor farmer, the farmer reserves the ownership of the cattle until the price is paid. The cattle will be delivered to the buyer but until he/she pays the price, the seller retains ownership of the thing.

This rule may be applicable in all cases of the sale. As stated in Art.2388, of the civil code where ownership is reserved on the seller, the risk transfer to the buyer. Note that, the buyer is not the owner but bears the risk that may happen on the property sold subjected to payment of purchase price.

Discuss with your colleagues

You have sold a car to Obbo/Ato Girma with 500,000 birr and appointed him on the tenth day of the sale. But, before the tenth day a sudden earth quake has happened and lost the car. Then what might happen legally? Could Obbo Girma get his money back? Why or why not?

4.6. Warranty against defect

The seller should not only deliver a peaceful possession but a useful possession. The thing delivered shall benefit the buyer. This obligation of the seller refers to the quality of the

thing sold. The thing sold should process a quality desired by the buyer. A quality expected from the thing sold may be expressed in different ways. The thing sold should possess any one or more of the following qualities.

-Quality for normal use

-Quality for particular use and

-A described quality

A quality normally expected from a given item may not necessarily be the same in all places. The required quality varies with the variation of service given by the item. A horse may serve for plugging or for carrying goods and people for hunting. A society using the horse for plugging land may regard quality of plugging as a normal quality. The normal quality, therefore, may vary with the variation of use expected from a given thing. Quality of a particular purpose may not necessary be identical to that of the normalquality.

Discuss with your colleagues If you order someone to prepare a cake for your wedding lock and if prepared for you a birth day cake, what is your response?

In the case of prescribed quality, the thing delivered should possess a prescribed quality. The buyer may list down certain qualities the thing has to possess such as color, size, weight, appearance etc.

Requirements that should be fulfilled to enjoy the effect of warranty against defects

-Ascertaining Quality of the thing delivered

Art.2291-Examination of the thing by the buyer

i- As soon as the buyer has the opportunity, he shall without examining the thing.

ii- Unless otherwise agreed, such examination shall be made as provided by the usages of the place of examination.

iii- Where the buyer intends to avail himself of the results of the examination, he shall in due time invite the seller or his representative to attain such examination, unless the thing is likely to perish.

The obligation to invite the seller may be dispensed if the thing to be examined demands immediate examination that may not be sufficient enough for attendance of the seller. The examination process may not be identical in all cases and in all places. It depends up on business usage.

-Notification

The other important procedure that has to be met to avail effects of the warranty against defect is notification. The buyer has to notify the seller that the thing delivered does not confirm the contract or that it is defective. Notifying the seller may serve as a default

notice. The seller should know the intention of the buyer to remedy the defect. The buyer has to inform the seller that how the defect may be avoided. This means the buyer has to indicate the nature of the defect and solutions the buyer proposes to be avoided.

Art.2292-notification of defects

1-Where examination discloses non-conformity with the contract or a defect in the thing, the buyer shall without delay give a notice there of to the seller.

2-In notifying the defect, the buyer shall indicate the nature in accordance with the custom and good faith.

Art.2293- Absence of notifications

1-Where the buyer has notified the seller as provided in Art.2293, he may no longer avail himself of the non-conformity or defects unless the seller admitted their existence.

2-Where defect is subsequently discovered which could not be discovered by normal process of examination, the buyer may avail himself of such defect where he notifies the seller as soon as he discovered it.

3-The seller who has intentionally misled the buyer may not avail himself of the fact that the notification of defects has not been sufficiently precise or made in due time.

Failure to notify the seller may not always bar the buyer to enjoy effects of the warranty. If the seller admits existence of defect or where the seller committed fraud on the thing sold he/she may not refuse to remedy the defect merely on the ground of failure to notify the defect.

Notification may not necessarily be immediate in all cases. Where express guarantee is given, the buyer may notify the seller at any time before lapse of the stated time.

-to benefit the implied warranty the buyer has to be innocent (should not be knowledgeable as to the defective nature of the thing purchased) – as indicated inArt.2296 of the civil code unlike the case of the warranty against disposition, buyer's awareness of defective nature of the thing sold cannot be remedied by an express agreement.

-The buyer has to examine the thing prudently- sometimes the buyer may overlook the thing because it is new and normal, this may not avail effects the warranty against defect.

-Action for warranty should be instituted within one year- the one year period starts from the date of notification. This is called period of limitation. If he/she keeps silent for a long period of time, the law assumes as if he/she waived the right and the bar right to institute action. Art. 2298 of the civil code prescribes one year to bring action for consequence of warranty against defects or non-conformity.

4.7. Obligation of the buyer Art. 2303-General provisions:

1-The buyer shall pay the price and take delivery of a thing

2-He shall be bound by any other obligation imposed upon him by the contract of sale

As you see from Art.2303 of the civil code, the two important obligations of the buyer are:

- Obligation to pay the price at which the thing is sold

- Obligation to take delivery
- Any other obligation stated in the contract of sale

Chapter summery

In this part, we have learned contract of sale which is a special type of contract. To have valid contract of sale, all the essential elements of contract shall be satisfied. There shall be express agreement to the nature of the thing to be sold and the price to be paid. The other obligation of the seller and the buyer, if not expressly agreed may be filled by law. There are also implied terms of contract of sale. This means the law imposes implied obligation. Whatever the case, it is important for you to understand all issues related to obligation of the seller as well as buyer as far as you are business students. Hence contract of sale should have legal ground that is the subject matter of contract of sale between the parties should be legally possible to be free from legal liability or validity of the contract of sale.

4.8. Self-test exercises

1- What are the modes of delivery of the subject matter of contract of sale?

2- What legal consequence would follow if a person delivers a non-conformingthing?

3- What is the place of delivery of the subject matter of contract where the contractis silent

4- Discuss the two method of acquiring ownership.

5- “the seller has to deliver unassailable right over the thing sold” , Explain the statement

6- What is warranty against dispossession?

7- What are the procedural requirements of exercising warranty againstdispossession?

8- Distance instances in which warranty against dispossession may not be enjoyed?

9- Explain an instance in which exclusionary provision avoiding or limiting warranty against dispossession may not effective.

10- What do you mean by warranty against defects?

11- Elaborate different ways of defining quality expected from the subject matter ofsale.

12- What do you mean by examination and what are the procedural requirements for effective examination?

13- Discuss situation in which warranty against defects may not exercise.

4.9. Progress Questions

True or False

Write true if the statement is correct or false if the statement is wrong.

1. To have valid contract of sale, all the essential elements of contract shall be satisfied.

2. Pay the price and take delivery of a thing is obligation of the buyer.
3, A quality normally expected from a given item may necessarily be the same in all places.
4, Ownership of a thing may be transferred from one person to another only in one way.
5, Delivery is handling the thing sold to the buyer.
6, Contract of sale of goods is a contract by which the seller transfers or agrees to transfer the property in goods to the buyer for a money consideration called the price.
7. If the price is not fixed at the formation of the contract and merely procedures are set, the contract is not conditional.

Chapter Five

The Law of Agency

5.1. Introduction

Dear students, this unit deals issues related to law of Agency. Since a principal or one man by himself could not reach every place of his business, an agent becomes the important stake holder for an individual. But this requires its own rules and procedures. This again makes this chapter an important unit that we shall deal with.

Learning Objectives

At the end of this unit, you will be able to:-

- Discuss sources of authority of an agent
- Explain kinds of authority of an agent
- Mention duties of the agent and principal
- Discuss the reasons for termination of agency

5.2. Sources of authority of an agent

A person to represent the other person shall have authority. The source of authority may be law or an agreement (Article 2179 of the civil code). Under the normal rule of privacy of contract, if one person contracts with another, a third party can derive no benefit, nor incur any obligations, under that contract. However, if one person authorizes another to do an act on his behalf, that other becomes the **agent** of the first. The act of the agent, then, under the maxim quoted above, becomes the act of the first person who, therefore, "steps into the shoes" of the agent, and becomes liable for the act (and able to enjoy its benefits) **as if he himself had done it in the first place**.

The agent has no personal liability; he "drops out" of the transaction. In commercial matters, the relationship of agency usually arises as a result of a contract between **two** people, for one (the agent) to affect a contract on behalf of the other. However, this is by no means the only way in which the relationship cannot arise, nor is the affecting of a contract the only duty an agent can perform. The fundamental principle is that, by the agreement of both parties, the agent is enabled directly to affect the legal relations of another person. Except in the case of "agency of necessity" about which we shall talk later in this study unit nobody can have an agency relationship forced upon neither him, nor it arise other than by **agreement** (express or implied).

Definitions of related terms

There are a number of definitions on which, even at this early stage, you should be clear.

We shall be discussing them in greater detail later but, in outline, the essential ones are as follows:

Principal-the "principal" is the person who agrees, expressly or by implication that another shall do an act for and on his behalf, and that he shall be **legally bound** by that act. (Note re spelling: it should be a principle to spell "principal" correctly.)

Agent-the agent is the person who acts on behalf of his principal, and **binds** his principal **in law**.

Authority-the authority of an agent is the act(s) and thing(s) which he is permitted or is authorized to do by his principal, and which will bind the principal. There are several different types of authority some express, some implied – but, in general (subject to exceptions), the principal will be bound by anact only if that act is **within the authority** of the agent to do on the Principal's behalf.

Other Types of Relationship

There are certain basic relationships which arise out of a contract whereby one person commits an act
(Or acts) for another but which are not (or not wholly) agency relationships.

- **Master and Servant** (covers most employer/employee situations)

This is not primarily a matter of agency. A servant is under the contract and direction of the master and the master is vicariously liable for the acts of the servant. However, vicarious liability arises by virtue of the **relationship**, not by reason of the servant's acting as an agent and the relevant liability is generally in **tort**, particularly negligence. If a servant makes a contract on behalf of his employer, then he does so as agent for the employer.

However, the liability of the employer is much wider than if it were a strictly agency relationship, and it extends to torts (e.g. negligence) committed by the servant in the course of his employment. There is inevitably an overlap between the two relationships, that of agency and that of master and servant, but essentially an employee acts by virtue of a contract of employment, and it is only when he has occasion to contract on behalf of his employer that he assumes the mantle of an agent for that matter only. Some employees cannot be said to be servants because they are not sufficiently under the control of their employers, but even most doctors working in hospitals are now regarded as "servants".

- **Independent Contractor**

This is not an agency relationship. Again, the concept arises principally in negligence. An independent contractor carries out duties or work or services for another by virtue of a contract. However, the "employer" of an independent contractor is not liable for the acts of the contractor (except in rare instances). If the contractor makes a contract with a third party in connection with his employment, he is solely liable in respect of it. The "employer" is not liable either vicariously or under the law of agency.

- **Partnership**

"Every partner is an agent of the firm and his other partners for the purpose of the business of the partnership." That is to say, a partner can bind the firm by an act done in the course of the business of the partnership. The "firm" is not a legal entity in England (unlike in some other jurisdictions) but each partner is **jointly liable** for all the debts of the partnership. Their liability for debts incurred by their other partners arises by virtue of the agency, not vicariously. However, the relationship of partners with each other extends far wider than that of principal and agent.

5.2.1. Authority by operation of law

Agents of minors

Minors are persons below the full age of 18 years. The minors are not permitted to engage in acts beyond their power. They cannot act by themselves but by their representatives/guardians or tutors. The father and mother of a minor child are assembled by law are agents of the minors. If the child is an orphan, the tutor may be appointed by a court.

b- representation of persons under interdiction

Interdiction is of two types. That is Juridical and legal. Juridical interdiction is an interdiction passed by the court. A person may be incapable or unable to act his/her task because of mental disorder or other reason, this time interested parties may apply to the court to represent the person.

A person may be interdicted by law. If a person is convicted by crime offence because of the dangerous behavior of a person, a court may limit his/her civil rights and deprive not to engage in certain acts. In such a case, necessities of life of the interdicted person may be dealt by an agent or tutor.

c- agency of necessity

Sometimes a person may represent the other even without having the formal authorization to represent him or her. This is true when unexpected damage happens on belonging of any one, you may represent the person to safeguard the economic interest of a person. But you are not contractually authorized to represent the person.

Article 2257-2265 of the civil code provides rules regulating agency of necessity. The code calls this kind of agency "unauthorized agency".

Art-2257- scope is of application.

Unauthorized agency occurs where a person who has no authority to do so undertakes with full knowledge of the facts to manage another person person's affairs without having been appointed to agent.

Where a person who has no contractual authority to represent another person acts on behalf of another with full understanding, the system of agency is called agency of necessity .As the law confers authority in this case, we cannot say the agent has no authority. The agent is not contractually authorized rather legally authorized to make the representation. The expression is "agency of necessity" is more expressive than unauthorized agency.

In order to make representation under agency of necessity, the following requirements shall meet.

-A sudden situation shall happen. Unexpected situation causing damage on economic interest of a person shall happen.
-unless represented by a necessity agent, the economic interest of the person represented shall be affected.
-there shall be no means of communicating the matter to the principal.

The necessity agent shall manage the affairs of the principal in good faith and in accordance with the requirement of good faith.
d- curator

A person may be does not manage his/her business because of different reasons like illness or absence. Here to appoint an agent by the court may be quite important and hence a curator is an agent the same to other cases but the difference lays his/her authority is appointed by the court and limits the power of the curator is determined by the court.

5.2.2-Contractual agency

Contractual agency is an agency that arises from contract. This is the usual method of creating agency relationship. The principal communicates his/her offer to appoint someone and if the agent accepts the offer, the contractual relationship is created between the agent and the principal. As contractual agency is special contract, it has to specify all the requirements necessary for the formation of valid contract.
Art.1678 –Elements of contract

No valid contract shall exist unless:

a) the parties are capable of contracting and give their consent suitable

b) the object of the contract is sufficiently defined

c) the contract is made in the form subscribed by law, if any

To form a contract binding both of the agent and the principal, the parties to the contract of the agency shall give consent. This means both the principal and the agent should agree to engage in to a contract of agency. The consent of the parties to the contract of agency shall not be vitiated by the factors affecting consent. Art.1696 – 1710 of the civil code provide factors that may vitiate consent of contracting parties.

Unless the law demands the contract of agency to be in writing, it need not to be in writing or registered. Art.2200 of the civil code states the contract of agency even may be formed by implication. The power of attorney however, shall always be in writing.

5.2.3-Authority of an agent

Authority of an agent may be expressed or implicit. The power of agency is said to be explicit where it is given in writing or communicated. A person may be authorized by implication. This means he/she may be instructed to represent a principal by conduct. Art.

2205 of the civil code lists down activities that may be performed by an agent conferred with special authority. A special agent may sell, donate or exchange a property. Activities that may be operated by agent authorized to execute are mentioned in Art.2205 of the civil code and they are called acts of disposition. Generally, there are a number of different types of authority, derived from differentsources, which an agent may possess. It is necessary to study these in some detail – but first, let us define them.

Definition of Terms

- Actual Authority

This is the actual authority given by the principal to the agent. It may be **express** or implied – that is, given by express words, or implied from conduct or the circumstances of the case.

- Apparent Authority, or Ostensible Authority

These are two terms for the same thing. In this study unit, we shall always refer to "apparent" authority – but remember that, if you see the term "ostensible" authority used elsewhere, it is the same thing. Apparent authority is the authority the agent has **as it appears to others**.

An agent can plainly appear to have a certain authority which he does not actually possess.

- Incidental Authority

The authority given to an agent will normally be in respect of his primary tasks. However, it is implied that he also has authority to do all such things as are **necessarily incidental** to the performance of the duties given by his actual authority.

- Usual Authority

Agents in particular trades or professions usually carry out certain set duties (e.g. insurance brokers, stockbrokers, solicitors). Hence, if a person in one of these trades or professions is employed in respect of that business as an agent, then he is presumed to have the authority to do whatever is usually done by agents in that particular business.

- Customary Authority

This is similar to usual authority but it is applied to the customs or usages of a particular **place**, as opposed to a particular business.

- Presumed Authority

Certain relationships inevitably involve one person acting as agent for another (e.g. husband and wife). In such cases, the agent is presumed to have a certain authority.

-Actual Authority

(a) Express Actual Authority

The capacity of an agent to act is the same as the capacity of his **principal**. Subject to exceptions already mentioned, anything the principal can lawfully do can be done for him ban agent. Hence, the express actual authority of an agent can be co-extensive with the powers of the principal. Express actual authority can be conferred by deed, in writing, or

orally. Authority by deed is, usually, called "a power of attorney" – and, as such, it is a formal document and construed more strictly than other types of express authority. Authority granted by virtue of a power of attorney is only such as is actually given by the **wording** of the power, by necessary implication, and it is necessarily incidental for effective execution. Strict tenets of construction should be used.

(b) Implied Actual Authority

Implied actual authority is whatever authority is necessary or incidental to the effective Carrying out of the agency in the usual way. It, therefore, includes "incidental", "usual" and "customary" authority. However, it is more – it is also the authority necessary to give **business efficiency** to the agency contract. This does not mean that an agent has discretion to contravene the express instructions of his principal if he considers them ill-advised or impractical – it does mean that additional ancillary powers will be implied if they are not expressly given. For instance, consider the following points.- An agent who has express authority to receive payment or **money** has, *prima facie*, implied authority to receive it other than in cash (e.g. by cheque).

- A managing agent has implied authority to do all those things necessary or usual **effectively** to manage.

- A professional agent has implied authority to do all those things which are usual in the profession or trade – but this does not extend to **unusual** things.
- Every agent has implied authority to act in accordance with the customs or usages of the trade or market in which he operates, and with the usual and prevailing commercial customs.

.Apparent Authority (or Ostensible Authority) (Sometimes Called Agency by Estoppel)
This type of authority occurs either where the principal has led third parties to believe that his agent has a particular authority (called "holding out"), or where the agent has assumed a certain authority to the principal`s knowledge, or when it comes to his knowledge and the principal takes no steps to correct the error or inform the third party of the fact that his agent does not possess such authority. If this situation develops without correction, so that the third party reasonably assumes the agent has the relevant authority, then the principal will be bound to the same extent as if the agent were properlyauthorized.

5.3. Effects of Agency

Art. 2189- Complete agency

1-Contracts made by an agent in the name of another within the scope of his power shall be deemed to have been made directly by the principal.
2-The principal may avail himself of any defect in the consent of the agent at the time of the making of the contract
3-Any fraud committed by the agent may be set up against the principal by the third party who entered in to contract with the agent
Art.2195-Liability of the principal

The principal shall be jointly liable with the agent where:

1-he/she informed the third party of the existence of the power of agency of but failed to inform him of the partial or total revocation of such power
2-he failed to ask the agent to return the document evidencing the power of attorney and failed to seek a juridical decision to the effect that such documents was revoked or
3-he caused in any other manner, in particular by his statement behavior or failure to act a third party to believe that the person with whom he was dealing was authorized to act on behalf of the principal

Duties of an agent

a- duty to follow the instruction of the principal

b- duty of care and diligence
c- duty to remit sums and make reportd-duty to avoid conflict of interest
d- - Duty not to delegate

This does not include the exception raised in the article 2215 of the civil code. These are activities that are depends on:
-the nature of activity- urgency, perish ability and the like

-consent of the principal-by agreement with the principal (formally as well as informally)

-emergency situation

In such situations the agent may delegate a sub agent and if problem happens theprincipal is also liable and the agent is liable for the improper selection of the sub agent. **Duties of the principal**
-duty to remunerate

-cover the costs of the agent for performing his/her task

-release the agent from liability due to his/her act while performing the activities

5.4. Termination of agency

The principal is always free to fire the agent at any time. An agent who is appointed by contract may be appointed under numerous circumstances and conditions. The appointment may be for a specific task (e.g. to sell a house), or for a limited time (e.g. for one year only) or it may be indefinite. Consequently, the agency contract may terminate under equally diverse circumstances. As between principal and agent, the termination of the contract serves to **revoke the agent's authority**. However, as between agent and third party this may not necessarily be the case. The agent's actual authority will be revoked – but, if the third party is unaware of the revocation, then the agent's apparent authority may subsist. But more of this anon, the seven circumstances under which an agent's **actual** authority is revoked are set out below.

(a) Agreement

Like any other contract, an agency can be terminated by agreement between principal and agent. This is self-evident.

(b) Completion

If the agency is for a specific task, the authority of the agent automatically ends when that task is **completed**. For example, a broker was employed to sell goods for the principal. It was held that, immediately the sale was completed, his authority ceased, so he could not subsequently alter the terms of the contract by agreement with the purchaser without new authority from the principal. Likewise for example, an estate agent was commissioned either to sell or to lease a house. He succeeded in letting it but then later negotiated the sale of it. It was held that, having let it, his job was done, and he had no authority to sell. He was not entitled to commission on the sale.

(c) Expiration

If the agency is for a specific period of time, it is determined when that time has **expired**. Equally, if it can be reasonably inferred from the circumstances that the agency was for a limited (although not specific) time then it will lapse after a **reasonable** time.

(d) Specified Event

It may have been agreed, or be inferred, that the agency will cease if a certain event occurs. Then, it will terminate if and when that event **does occur**.

(e) Frustration

The frustration of the contract of agency will serve to terminate the authority of the agent. This is likely to occur if the subject-matter of the agency is destroyed (e.g. if an estate agent is commissioned to sell a house and, before sale, it is burnt down). Or if something happens which makes either the agency or its objects illegal or impossible (e.g. an agent in a foreign country becoming an alien enemy owing to outbreak of war between the Ethiopia and that country).

(f) Death/Winding-up

The authority of an agent, is, normally, terminated by the **death** or **insanity** of either the principal or the agent, or the **bankruptcy** of either. In the case where either is a limited company, the **winding-up** of the company has the same effect.

(g) Revocation

Lastly, if either the principal or the agent **revokes** the agency or **renounces** it (whether or not the act of so doing is in breach of the contract) the agent's authority will be revoked. If it is done in breach of contract, then the innocent party – be the principal or agent – will have the right to seek damages for breach of contract. However, this will not affect the fact that the authority of the agent is terminated. In certain circumstances, the innocent party may also be able to get an order of specific performance from the court, compelling the guilty party to carry out the contract in accordance with its terms. Or if relevant an injunction prevents the guilty party from revoking the agency. However, neither of these equitable remedies will be granted if the relationship between principal and agent is a

personal one that is, if the character, skill, experience, etc. of the agent is an **essential element** of the relationship.

Irrevocable Agency

An agency contract may be irrevocable, either by agreement or by implication, as a resultof the Circumstances. This, however, is not straightforward. The mere fact that the partieshave agreed that the agency shall be irrevocable does not, of itself, make it so. There is nothing to prevent one party renouncing in breach of the contract, notwithstanding that hehas agreed not to. Something more is necessary to render the contract legally irrevocable.

Unit summery

These days, when every one of us occupied with different simultaneous activity it is difficult to act in every corner simultaneously and this necessitated the importance of an agent to act on behalf of the principal. By Principal we refer to the person who agrees, expressly or by implication, that another shall do an act for and on his behalf, and that he shall be legally bound by that act and an agent is the person who acts on behalf of his principal, and **binds** his principal **in law**. An agent gets authority to act on the agent's behalf. The authority of an agent is the act(s) and thing(s) which he is permitted or is authorized to do by his principal, and which will bind the principal. How this goes from the perspective of legal ground and liability of a principal due to act of agent has been thefocus of this chapter. So it is compulsory for every one of us to appoint the right agent due to legal consequences of improper act by the agent brings liability to the principal.

5.5- Self test exercises

1-Differentiate a curator and a necessity agent.

2-What is the most important difference between a contractual agency and agent acting within the scope of the power entrusted on him/her.

3-Discuss the effect of agency where the agent acts within the scope of the powerentrusted on him/her.

4-Explain effects of the repudiation and ratification of unauthorized representation.

5-Differenciate special and general agency

6-What are the requirements for representing a person because of unexpected event.7-What are the instances in which sub agency may be repainted?

8-Differentiate renunciation and revocation.

5.6. Progress Questions

Multiple choices

Choose the best appropriate answer form given alternatives

1. In the sources of authority of an agent, a person to represent the other person shall have _____.

A, obligation B, authority C, both D, none

2, _____ is the person who acts on behalf of his principal, and binds his principal in law.

A, buyer B, seller C, owner D, Agent

3, Minors are persons below the full age of ____ years.

A, 12, B, 20 C, 16 D, 14 E, none

4, Contractual agency is an agency that arises from _____.

A, contract, B, law C, family relationship D, couple E, all

5, All of the followings are Duties of an agent except _____.

A, Duty not to delegate B, a- duty to follow the instruction of the principal C, Duty to delegate D, duty of care

6. If the agency is for a specific task, the authority of the agent automatically ends when that task is completed called _____.

A, expiration B, specified event C, frustration D, agreement E, none

Chapter Six

Introduction to the law of Traders and business organization

Dear learners, we have seen previously in unit four about law of sales. The most important agent of sales or business transaction is traders. This unit deals with law of traders and related business organization to carry on business.

Learning objectives:

At the end of this unit, you will be able to:-

- Define who are traders
- Discuss the restriction in operating business activity
- Explain the obligations of traders
- Define unfair competition
- Differentiate the form of different business organization

6.1. The law of traders

6.1.1-Who are traders

Traders are persons that operate any one or more of the activities stated in article 5 of the commercial code professionally and for gain. Article 5 of the commercial code enumerates about 21 activities. If a person carries out any of these activities professionally and for gain, he/she is taken as trader.

All persons who carry different activities for nonprofit are not considered as traders. Such as:-

-individuals who operate agriculture, cattle breading, maintaining pasture land, fisheries

-Hand craft men

But individuals who add value for instance a farmer who fattens ox, or sheep for profit could be considered as a trader.

6.1.2. The right to operate business activity in Ethiopia

Everyone is free to engage in any kind of activity at any place with in the territory of Ethiopia. (Art.41 of the constitution) Freedom to operate business is not absolutely free. There are some restrictions; the following are the restriction imposed by the law.

a- Incapable person who are incapable under the civil code may not carry on any business activity bythemselves.
b- Married person- this is not in all instances as seen in the general nature of trade. Couldyou sale your house without the will of your spouse?

c-foreigners- require residential permit before dealing in business activity.

d-associations- Associations are basically established for nonprofit motives and therefore cannot operate trade based on article 25 of the commercial code.

6.1.3-Obligations of traders

The law imposes on the persons called traders the following obligations. a-the obligation to keep books and accounts
b-the obligation to be registered

c-the obligation to obtain business license

6.2-Business and unfair competition

The term business as implied by Art.124 of the commercial code, it is an intangible property that emerges out because of the activity of traders. The main component part of business is good will.

As it is a property, in which side of the balance sheet, you register good will? Discuss with your colleague

"Good will" is a difficult word to define as it is intangible. It has money value even if not seen.
Goodwill is considered as a probable and possible relationship of customers and a trader. If a trader make good relationship with customers and people who are willing or have good out look to wards a given trader, we say money value of the goodwill is so great. Art130 of the commercial code illustrates the term goodwill as follows. The goodwill results from the creation and operation of a business and is the value which may vary according to the probable or possible relations between a trader and a third parties who may require from him/her good and services. So the goodwill is important value of the trader. It cannot be used by third parties without the permission of the trader. If a person uses goodwill of another person without authorization, that may be taken as usurpation of property of another person. It is illegal and **termed as unfair competition.** Unfair competition, as defined in proclamation No.329/2003, is any act misleading customers.

6.3-Introduction to the law of business organization

There are various ways of operating business activity. A person may operate an activity of trade individually or in group with similar people. Business activity may also be conducted by public enterprises and cooperatives. Each scheme of operating business has its own advantages and disadvantages.
In a trade operated for business organization he/she can choose any one or more of the business organizations. Business organizations are organizations that may be formed to operate commercial activity. The commercial code recognizes 6 kinds of business organizations. Art.212 of the commercial code declares business organizations that may be formed in Ethiopia. These are:-
-Ordinary partnership

-General partnership

-Limited partnership

- Share companies

-Private limited company

Article 210 of the commercial code attempts to define the term "business organization"". It states a business organization is any association arising out of partnership agreement. The word "association" used here not to equate business organizations to non-profit making entities that may be set up in accordance to the rules of the civil code. The code used the word association here to mean grouping of people. A business organization is therefore, is a grouping of business persons that comes out of the partnership agreement. Article 211 of the commercial code defines the partnership agreement. It states, "apartnership agreement is a contract where by two or more persons who intend to join together and to cooperate. Undertake to bring together contributions for the purpose of carrying out activities of an economic nature and of participating in the profit and loss arises thereof, if any."

General view about partnerships

In your introduction to business or marketing courses, you may see different types of forming business. One of them is partnership. We will see it from the general perspectives.
A partnership is based on a contract between its members and, since it can be created informally and dissolved informally, it differs completely from a corporation. You will remember that a corporation must be created either by charter or by statute and, once formed; it has a continuous legal personality. Partnership, on the other hand, can be formed by means of a deed, i.e. an agreement under seal signed by the persons who agreeto become partners, or by means of a simple agreement in writing, or even by an agreement made orally or simply implied from the actions of the persons concerned.

Differences between Partnership and Corporation

We can now note the following important differences between a partnership and a corporation:
- A partnership has no legal personality; a corporation has a legal personality of its own.

- All partners share in the management, unless it is agreed otherwise. The management ofa corporation is left to a selected body (directors, council, committee etc.).
- Each partner, except a "limited partner", is liable for **all** the debts of the partnership personally, to the full extent of his private estate.

Limited Partnerships

- No more than 20 persons (or 10, in a banking business) may usually associate in a partnership.
- Each partner has implied authority to contract on behalf of the others in the ordinary

scope of the partnership business, and he thereby binds all the other partners, even if they are unaware of what he has done. A corporation acts through appointed agents, and an ordinary member has no power to bind the corporation.

Differences between Partnership and Company

The characteristic of legal entity is one of the main distinctions between a limited company and a partnership, which is not a distinct person in law but simply the partners acting together.

Partnerships Limited Companies

The consent of the other partners is required before one partner can dispose of any of his interest. Shares are freely transferable (subject to the Articles).Each partner is an agent for the firm to make contracts. A shareholder is not an agent for the company. The liability of each partner for the firm's debts is unlimited, except in the case of a limited partnership. The liability of each member is limited by shares or guarantee. Partners may make what agreements they like *inter se*,(between themselves).There are some arrangements between members of a company which are prohibited, e.g. purchase by the company of a member's shares. Partners may undertake any business. The business undertaken is restricted by the Memorandum of Association.

The Articles of Partnership

As a general rule, the partnership comes into being by means of an agreement in writing, the document being known as the **Articles of Partnership**. This document, which will be signed by all the partners, contains all the conditions etc. under which the partners intend to carry out their business. The Articles of Partnership usually include clauses dealing with the nature of the business, its capital and property and the respective capitalsof each partner, the method of sharing profits and losses and the rules as to interest on capital and drawings. Provision is also often made for the method of determining the value of goodwill on retirement or death, and of computing the amount payable to an outgoing or deceased partner. The partners are bound by the Articles and, if any point is not dealt with in the articles.

For a long time there was considerable acrimony between two of the partners, which eventually came to a head when one assaulted the other. It was held that his expulsion was justified, since his assault was an act of disloyalty and constituted conduct which was clearly contrary to the good faith required of partners.

Registration – the Firm Name

A partnership is not subject to registration, unless it is a limited partnership. Legally, the firm's name is merely a convenient way of alluding to existing partners. An authority to lend to a firm does not authorize a loan to that firm when the partners have changed, but copyright can be registered in a firm's name. The firm's name will be protected. Partners can sue and be sued in a firm's name, although they must appear in person.

Rights and Duties between Partners

The relations of partners to one another are governed by the Articles of Partnership. In the absence of express provision, the following rules apply

- All partners are entitled to share equally in the capital and profits.

- No partner is entitled to interest on capital before the ascertainment of profits.

- No partner is entitled to remuneration for acting in the partnership, even if the partners have acted unequally.

- Every partner may participate in the management of the business.

- No new partner may be introduced without the consent of all existing partners.
- Differences arising as to ordinary matters connected with the partnership may bedecided by a majority of the partners, but changes in the nature of the partnership business require the consent of all.
- A majority of partners cannot expel one of their numbers.

- Each partner is entitled to be indemnified by the partnership for liabilities incurred in the ordinary and proper business of the firm or in doing anything necessary for the preservation of the firm's business or property.
- Partners making advances of capital beyond the amount of capital which they have agreed to contribute are entitled to interest at the rate of 5%.

- The partnership books are to be kept at the place of business of the firm, and each partner must have access to them.
- Every partner is under a duty to his fellow partners:

(i) To tender true account and full information of all things affecting the partnership.

(ii) To account to the firm for any benefit derived by him from transactions concerning the partnership or from his use of partnership property.
(iii) Not to compete with the firm.

In ***Bentley v. Craven (1853),*** one of the partners in a sugar-refining firm carried on a separate business as a sugar merchant with the consent of the other partners. He arrangedfor the sale to the firm of a consignment of sugar, making a profit which he did not disclose to his co-partners. It was held that he was under an obligation to share the profit with his partners.

Relationship of Partners to Third Parties

As third parties are not permitted to inspect the Articles of Partnership, the court does not presume that third parties know the contents of the Articles. No matter what the Articles of Partnership may state with regard to the relation of partners to one another, an act performed by a partner in the ordinary course of business will bind the firm and all the other partners. This is known as **joint and** several liabilities**.**

A distinction is sometimes drawn between the **express** (or actual) and **implied** (or ostensible) **authority** of a partner. Express or actual authority is that conferred upon a

partner by the terms of the Articles of Partnership. Implied or ostensible authority is vested in a partner by virtue of his status as a partner, and is determined entirely by what is necessary for the usual scope of the firm's business. Whether the act of a partner is necessary for the usual scope of the business is a question of fact to be determined by the nature of the firm's business and by the practice of the persons engaged in it. It is usual for partnership articles to contain a clause imposing some agreed limitations on the authority of certain or all partners, e.g. forbidding junior partners to negotiate loans on behalf of the firm, but remember that such express restrictions have no effect on outsiders dealing with the firm,unless the outsider knows, or should know, of the restriction.

Termination of Partnership

A partnership can come to an end and, in certain circumstances, must be terminated. As a general rule, the Articles of Partnership contain the regulations regarding the termination of the partnership. Thus, a partnership may terminate at the end of the time fixed in the Articles or on the completion of the purpose for which the partnership was formed, by one party giving notice to the remaining partners of his intention to terminate the partnership, or by the common consent of all partners.

A partnership is automatically terminated on the bankruptcy or death of any partner, or if any event occurs which makes the business of the partnership illegal. In addition, the court may decree the dissolution of the partnership in such circumstances as willful breach of the partnership agreement by one partner, or action by one partner which is prejudicial to the continuation of the firm's business. In addition, if it can be shown that the firm's business can be carried on only at a loss, or any circumstances arise which render it fair and equitable that the partnership be dissolved, the court may also act by dissolving the partnership.

Bankruptcy of Partnership

Since the liability of a general partner extends to the whole of the debts of the partnership, or he is liable jointly with the other partners, a creditor in the bankruptcy of a partnership can pursue one of two courses.

- In the first place, he can proceed against the partners jointly, i.e. in the name of the firm. If he obtains judgment against the firm, the debt must be satisfied out of the assets of the firm; if, however, the assets of the firm are insufficient, then the creditor can look to the private assets of the partners in order to satisfy his debt.

In the second place, the creditor can proceed against any individual partner. If he obtains judgment against a certain partner and this judgment cannot be satisfied out of the private property of that partner, then the creditor cannot proceed against the remaining partners. The, creditor must pursue one course or the other. If he pursues the second course described above, the partner against whom the judgment is obtained will be liable to pay the full amount. He has a right to call upon the other partners, however, to contribute the shares that they should bear.

Liability of New and Retiring Partners

Pay particular attention to the following points dealing with the liability of partners.

(a) Incoming Partner

Unless a new partner makes a special agreement to the effect that he will take over the liability in respect of the firm's debts at the time of his joining the firm, he cannot be held liable on such debts. In the absence of such an agreement, the new partner can be held liable only in respect of debts incurred **after** he became a partner in the firm.

(b) Retiring Partner

A retiring partner can be held liable only in respect of debts incurred before his retirement, provided due notice of retirement is given.

Rights of Partners on Dissolution

The rights of partners on dissolution are usually contained in the Articles of Partnership. Where they are not provided for in this way, the following are the more important provisions which apply:

- The assets or property of the firm must be applied in paying off the creditors of the firm.

- The assets remaining are to be applied in paying to the partners the amounts which are due to them as partners.

- The assets of the partnership, together with any amounts contributed by partners to make up a deficiency, are to be distributed as follows:

(i) In paying off all creditors of the firm who are not partners.

(ii) In paying rate ably to the partners the amounts due to them in respect of capital.

(iii) If any surplus remains, it is to be shared among the partners in the proportions in which they share profits.

6.4. General features of business in Ethiopia

A business organization is an organization that is formed for the purpose of operating profit making activity and business persons for different reasons may prefer to work together and form business organization. Art.210 defined business organization as any association arising out of a partnership agreement as we put also in section 6.3 above.

Now, in addition to the general view of business organizations, we shall see the form of organizations the law defines one by one.

A-Partnership

The Ethiopian commercial code recognizes three kind of partnership.

i- Ordinary partnership

Art.227-270 of the commercial code contains rules regulating ordinary partnership. Rules meant to regulate ordinary partnership are very flexible and given wider options to partners. An ordinary partnership may set up to operate activities mentioned in article 6,8 or other activities that do not make their doer a trader.

Art.227-definition

-`A partnership is an ordinary partnership within the meaning of this title where it does not have characteristics which make it a business organization covered by another title of this code.

As other kinds of partnership, partners of ordinary partnership are jointly and severally liable to the creditors of the partnership where the partnerships assets are not sufficient enough to meet demands of the creditors. Partners of an ordinary partnership's asset by agreement may avoid a joint and several liability obligations (Art 255(2)) of the commercial code. The exclusionary provisions cannot guard partners unless the provisionis known to their third party.

ii-General partnership

Art 280 – 295 of the commercial code contains rules regulating general partnerships. Some of the provisions governing ordinary partnership are also applicable to general partnership.

All partners may be appointed as managers of the partnership. Creditors of the general partnership may not demand from the individual partners before exhausting all possible remedy against the partnership assets. (Art.294 of the common code) Thus, while the partnership is solvent, creditors cannot free the partners unless they have got fictitious dividend.

Art 280(1) of the commercial code defines the nature of general partnership. A General partnership consists of partners who are personally, jointly, severally and fully liable as between themselves and to the partnership for the partnership firm's undertakings. Any provision to the contrary in the partnership agreement shall be of no effect with regard to third parties.

A joint and several liability of partners may avoided by agreement. However, exclusionary provision of joint and several liabilities may only be effective among the contracting parties. The provision may be enforceable against co-partners but produces no effect against third parties.

The last provision of Art.280 of the commercial code states," Any provision to the contrary in the partnership agreement shall be of no effect with regard to third parties.

iii-Limited partnership

Art.296 to 303 of the commercial code regulates limited partnership. As pointed out in the article 303 of the commercial code, some of the provisions of the ordinary partnership and general partnership are also applicable to the limited partnership.

Art.296-Nature of limited partnership

A limited partnership comprises two types of partners; general partners who are fully liable personally, jointly and severally and limited partners who are liable to the extent of their

contribution.

Art 3 of Art. 301of the commercial code provides:

Limited partners may not act as managers even under power of attorney. A limited partner who contravenes this rule shall be fully, jointly and severely liable in respect of some or all the firm's undertakings.

B-joint venture

Art. 270 to 279 of the commercial code regulate the process of operating business activity by the instrumentality of joint venture. A joint venture is a business organization that may be formed to operate any kind of activity. It is a secret business organization since it is not disclosed to third parties. The organization is known only to the ventures. Hence joint venture cannot get separate legal assistance; the agreement between the ventures should be in writing. The parties know the manager of the joint venture and he/she is liable for all faults and liabilities that may emerge because of the business. The power of the manager and liability of other partners will be determined in their mutual agreement.

C. Companies

Today, most business in Ethiopia aspires to operate in the form of company. Our commercial code recognizes two kind of companies; Share Company and private limited company. Art.304 -509 of the commercial code sets out rules regulating Share Company. Art.510-543 contains special rules governing private limited companies.

Similarities between Share Company and private limited company

a- Liability of all members is limited to the extent of initial contribution

Art. 304 –definition of Share Company

1- A share company is a company whose capital is fixed in advance and divided into shares and whose liabilities are only met by assets of the company

2- Members shall be liable only to the extent of their share holdings

Art. 510-Definition, Nature

-A private limited company is a company whose members are liable only to the extent of their contributions.

Therefore, members of a share company and private limited company cannot be forced to pay company debt if they have paid contribution they owe to the company. That is to say, individual members cannot be forced to pay company debts from their own personal properties.

b-The partnership agreement forming both Share Company and private limited company expressed in the memorandum and articles of association.

c-Both share company and private limited company is always commercial business organizations.

As expressed in the commercial code of Art.10, share companies and private limited companies are always commercial business organization.

Distinctions between Share Company and private limited company

a- Maximum and minimum number of members that may form both of the companies is not identical

b- The minimum amount of capital of both the companies is not identical

c- A share company can issue different kinds of shares but a share of a private limited company are always registered

d- Shares of a share company may be offered for public subscription

e- While a share company can issue debentures a private limited company is not permitted to issue transferable securities

f- Certain fields of activities are reserved only to share company

g- Personality of members in private limited company is important whereas, personality of members of share companies is not important

6.5. Dissolution of Business organization

From the very beginning of its establishment, a business organization will have legal personality. Now organizations are treated as human beings for legal propose. Legal persons are called juristic or artificial persons in general. On the other hand article 223 of the commercial code deals with legal publicity to have legal personality for business organization.

Art.223-Effect of publicity

A business organization shall not have legal existence or personality until all the provisions of this code relating to publicity have been compiled with and registration is published.

After acquiring legal personality, the organization has the right to:-

-own property of its own and in turn capacity to sue or to be sued

-Sue or sued

-enjoy other consequences of legal personality

But the above points are not guarantee does not mean business organization is existed for ever. Different contingencies may take them away. Causes dissolving business organizations are stated in Art.217, 218, 258,495,279, and 542 of the commercial code. Art.217 and 218 of the commercial code are the general provisions applicable to the dissolution of all forms of business organizations. Business organization may be dissolved by agreement of the persons who formed them, by operation of law and by court. Art.217 of the commercial code provides instances in which a business organization may be dissolved by agreements of person who formed them, by operation of law. The court can declare a business organization to be dissolved.

Before a business organization is virtually dissolved, business at hand have to be

completed, doubts to be paid, and properties have to be facilitated in a way possible for distribution among the persons who formed the business organization. This process is called liquidation or winding up. The liquidation process is conducted by liquidators. After an agreement for dissolution of a business organization is reached or decided for dissolution, management organs of the business organization (managers in the case of partnership and joint venture and directors in the case of companies) have to make inventor with the liquidators and hand over documents and properties to the liquidators. The liquidators have to finish the business at hand. They cannot start new business while the business organization is at liquidation. The liquidators after paying all business debts have to distribute the remaining property among persons (member or partners) who formed the business organization.

6.6. Self-test exercises

1-What is the basic difference between partnership and joint venture with regard to personality?
2-Partnership agreement refers to what?

3-Could business organization be formed without entering in to a partnership agreement? 4-Discuss the most important difference between association and business organization. 5-Compare and contrast a share company and private limited company.
6-What does commercial business and non-commercial business organization mean? 7-Discuss the statement "joint venture is a secret business organization

6.7. Progress Questions

True or False

Write true if the statement is correct or false if the statement is wrong.

1. All persons who carry different activities for nonprofit are, considered as traders.
2. Everyone is free to engage in any kind of activity at any place with in the territory of Ethiopia.
3, Goodwill is considered as a probable and possible relationship of customers and a trader.
4. A partnership is not automatically terminated on the bankruptcy or death of any partner.
5. A business organization is an organization that is formed for the purpose of operating non-profit.
6, A joint and several liability of partners may avoided by agreement.

Chapter Seven

Introduction to Law of Insurance

Dear learners, this again another important section you have to award with due to the fact that insurance goes with business transaction. You are familiar with "Idir" that sets to pay a little during a registered/unregistered relative's death, depends up on the contractual agreement of the member of the "idir." So you may incur cost for a long period of time without any payment. There should be death of relatives in the given family and the payment in most cases does not balance with what the person contributes. In the same way in modern business practice, you may buy insurance to decrease or to transfer risk to the third party usually insurance agencies on described contractual issues signed between you and the organization. The insurance may be paid if there is any loss due to certain facts. Unless those things exist, you incur insurance expense rather than payment. You pay for the described potential black days on the issues signed between you and insurance company.

Learning objectives

At the end of this unit, you will be able to:-

- Explain functions of insurance institutions
- Discuss the process of forming insurance contract
- Distinguish person that may insure property
- Examine requirements of insurance policy
- Discuss rights and duties of the insurance policy

7.1. Background and functions of insurance

Historically most scholars believe that, first insurance was emerged in Babylon (Iraq) at about 3000 B.C. The merchants‟ of the time pooled or combined their money to protectto protect themselves from losses of cargo by thieves and pirates. King Hammurabi, the ruler of Babylon at that time dictated the traders to repay merchants who finances trading voyage in cases thieves' stolen goods in the transit in which case debt will be cancelled. In early times, the concept of insurance was used by Phoenencials also (Lebanon). At that time, money was loaned to merchants to finance voyage. Merchants offer their ship as collateral for such loan. When the trip succeeded, the merchants would pay the trips original loan plus the interest; the equivalent in their context.

The societies of Greece and Rome developed some of the realist form of life insurance. Greek and Roman citizens formed insurance like organizations in which members paid contribution that may be used for burial of members who died. Sometimes, these societies also paid for decreased members families. Many modern form of insurance developed in England between 16-18th centuries. The first known insurance was written in London in

1500s. In the 700s marine traders started pooling their risk against damage to goods they transport by ship. Seafarers and people wishing to back their experiment in formally to make insurance arrangement sometimes at pub called Lipoid's in London; this then transferred to London's of London. It is this arrangement that opened door to modern insurance.

It is difficult for an individual to shoulder a risk but if the risk is distributed over a certain individuals, it losses weight. Different people that are exposed to the same peril may organize themselves as that of "idir" and distribute peril among all. In England, mutual assurance company protected the interest of members by distributing perils through periodical payments. Later on such business is taken on by individual underwriters that collect money exposed to the same risk. The under writer was served as a means for distributing risk among different people by the money collected in advance. Today's giant insurance companies are fruits of formula devised for distributing happened on similarly situated persons. Whatever the case, insurance is existed because of the existence of business risk.

An over view of risk

Insurance

It is a device that protects people from the financial costs that result from loss of life, loss of health, property damage. A person or an organization may merely assume a risk of some kind that may or may not happen. Whether the risk happens or not happen, it is difficult to be certain. Nobody knows, when, how and to what extent the risk may happen. If this fact had been known before hand, everyone would have avoided it. The uncertainty and fear of unfortunate moment may hamper commerce or industry. The uncertainty surrounding potential losses could be referred as risk. If risk is insured, the person may operate business without fear of risk. And again the following are the advantages employed by insured person.

-If a person works without fear of loss, he may increase production

-Insurance helps to budget money for unknown loss.

-Insurance distributes risk among different people.

-Insurance facilitates bank loan

-The insurance companies again create job opportunity for the society, etc... 7.3-Insurance policy

7.1.1. Contractual requirement

Art.654-714 of the commercial code declares rules regulating parties to the contract of insurance. Art.654 (1) of the commercial code defines contract of insurance as follows. An insurance policy is a contract where by a person called the insurer, undertakes against payment of one or more premium pay to a person called the beneficiary, a sum of money where specified risk materials. Hence insurance is a special contract; it shall satisfy all the requirement of a valid contract.

The insurance contract shall be entered for lawful cause. This means the promise of the insured and the insurance company makes each other a lawful agreement. A contract shall specify the respective obligation of the parties to the contract of insurance. The risk insured the premium to be paid and all the other annexed duties shall be clearly set out in the contract of insurance. Defect to the object of the contract of agency makes the contractof no effect.

Parties to the contract of insurance are the insurer and the insured. The insurance company (the insurer) will pay the sum stated in the contract of insurance if a risk happens to the insured. The insured person on the other hand promises to pay a specified sum, usually periodically known as the premium.
Art 1725(b) of the civil code provides that the contract of insurance to be made in writing. If the law demands a given kind of formality and not followed, there will be no contract (Art.1720 of the civil code)

You can enter in to valid and binding contract of insurance, if the agreement is made in writing (art.657 of the commercial code). The written contract of insurance shall be supported by the insurance policy. The policy can only varied where the variation agreement is made in writing. The document is continuing a varied contract of agency calledendorsement. (Art 657(2) of the commercial code.
Sub article 3 of article 657 of the commercial code states: "the insurer and the beneficiary shall be bound where prior to the signature of the policy or endorsement, the insurer hands to the beneficiary a document setting up a provisional guarantee until the policy endorsement is signed. This is called provisional guarantee, the function of which is almost similar to that of normal insurance apart from its provisional nature.
The provisional guarantee may be permitted until the main insurance is finalized, until the p[policy or endorsement is completed. The contract of insurance shall contain:-
a-the place and date of the contract

b-the names and address of the parties, c-the item, liability or person insured d-the nature of risk insured
e-the amount of the guaranteef-the amount of premium
g-the term for which the contract is made

Unless otherwise agreed, the contract of insurance shall be effective from the moment the contract is signed. The contracting parties are free to extend the effective date of the contract of insurance. It is accepted practice to extend the effective date until the first premium is paid.

7.1.2. **Parties to the contract of insurance**

A person capable of contracting may enter in to the contract of insurance. The person insuring against a given risk is called the insurer. The person may be subscribing an insurance company for his/her own benefit or for the benefit of the other people. This means the beneficiary could be an insured or the third party. Until the beneficiary (the

assured) accepted the insurance on his/her own behalf, the subscriber is responsible to discharge all obligation that may arise from the contract. If the beneficiary accepts the contract of insurance, a direct contractual link is established between the insurer and the insured. The beneficiary may accept the insurance at any time, even after the risk has materialized (Art. 661 of the commercial code).

7.1.3. The subject matter of insurance

The subject matter of the contract of insurance may be property (car, building, etc…), payment of debt, and liability to third parties. In general it could be categorized as a physical object, intangible property, and liability.

-Physical object-refers to something that can be touched, seen and the like. For instance, car accident, fire destruction and the like

-Intangible property- this could be something that cannot be seen. For instance insurance of receivables

-Liability- a person may be insured against happening of a given liability to third party. If your car or your property causes damage to third parties in order to benefit from the insurance, you may have third party insurance.

The subject matter of insurance may be described in two ways, Specific description and general description. Where a particular property is insured, the exact nature of the property shall be described in the policy in order to be more concise and clear and this is specific description. For example if you by insurance for your car, the model and other things that differentiate your car from others should be described.

7.2. Insurable interest

A person is said to have insurable interest if he/she has interest in the subject matter of insurance to whom the advantage may arise or prejudice may happen. The person should have some kind of relation to the subject matter of insurance. Insurance shall protect the relation or the concern on the property. If happening of a given peril is assumed to affect the relation or the concern on the subject matter of insurance proved to affect the interest of an insured, we may say that the person has an insurable interest. The happening of a risk shall cause damage or prejudice the person insuring. The insured should be benefitedfrom the existence of a thing or an interest insured or should be prejudiced by its destruction. In the case of life insurance, the insurable interest is constituted by the fact that the subject matter of insurance (a physical object) exposed to certain peril.

7.2.1. Rights and Duties of the parties in the contract of insurance

7.2.1.1-Duties of the insurer

The insured has to indemnify the insured where the risk insured materializes. Art.663 (1) of the commercial code states, “The insurer shall guarantee the beneficiary against therisks specified in the policy.” The risk has to be determined in the contract of insurance. Determination of the risk is important for different purposes. The extent of the premiumis determined by the risk. The insurer can insure the risk weighting the profit that mightbe drawn. The risk cover of the policy helps the assured to know precisely the extent of his cover, so that he/she may if he requires taking additional insurance and so that he/she may

avoid uneconomical double insurance.

7.2.1.2-Duties of the insured

1-payment of the premium

2-Disclose material information-since insurance is a contract depending upon speculation, it is necessary for the insured to disclose matters only he/she knows based on article 667 of the civil code.

3-Notify the occurrence of the risk insured- this is as soon as possible during the occurrence to the insurer based on article 670 of the civil code.

7.3. Classification of contract of insurance

For more clarification, you can refer to your introduction to business and related courses. The classifications are as follows.

A-classification based on nature of event i-marine insurance like, fire insurance, life insurance & accident insurance.

B-classification based on nature of interest affected i-personal insurance like, property insuranceiii-liability insurance

7.4. Insurance of object

7.4.1. The concept of proximate cause

The loss to be compensated shall be caused by the peril insured. The cause and effect relationship is very important. The cause of loss shall be proximate. That is, an insurer to compensate the insured, the risk caused of the subject matter may be destroyed or loss because of contribution of different causes. The risk insured shall have approximate cause. This is to say, the cause of destruction should have close relationship. If property is lost by some intervening factor, we say the caused rendered destruction has remote relationship and the insured cannot be responsible to compensate loss.

7.4.2-Making claim for compensation

Where the subject matter is lost, the insured to collect compensation has to:

-to notify the insurer on or within 5 days

-indicate how the risk is happened caused loss

-prove the loss

7.4.3-Subrogation

The insurer after compensating the insured may step at his/her shoes and demand indemnity and this is called subrogation. Where the insured impairs this right of the insurer, the insurer will be released from the obligation of compensating the insured. The insurer cannot claim the compensation from the people that have relationship with the insurer. If for example, the insured's son caused the damage to the property negligently, and loss happened as a result, the insurer cannot be indemnified. If the son pays compensation to the insurer, it would be nonsense to the insured. Art.683 (3) of the civil code states"…the insurer may not

claim against ascendants, agents or employees of the insured person nor against persons living with him, unless such persons have acted maliciously"

7.4.4-Insurance of liability

One of the most important and frequent type of insurance is liability insurance. In this type of insurance the insurer promises to compensate the insured if he/she has to compensate the third party. The first important procedural requirement for collecting compensation from the insurer in the case of liability insurance is the third party has to demand compensation either amicably through arbitration or by court of law (Art.658 of the commercial law). The insurance policy may contain a provision depriving the insured to admit liability or to compromise without consent of the insurer.(Art.686(1) of the common code.

7.4.5-Insurance of persons

Insurance against person may be subdivided in to two. Namely: life insurance and insurance against accident or illness.

Life insurance

The beneficiary of the life insurance may be named in the policy when the insurance is purchased for the benefit of the third party. The insured person or his/her spouse shall give consent in writing. Where the policy is purchased for incapable person, it shall be of no effect unless agreed by the incapable person or by his or her representative. The policy purchased for the life of incapable person may be invalidated by any interested party.

There are cases in which beneficiary of life insurance may not be enjoyed. These are: -i- suicide (based on art.699 of the common code) & ii - murder of the beneficiary (see article 700 of the common code)

Summery

Insurance facilitates commerce by strengthening the actual and psychological confidence of the traders. Because, traders or business men, act and perform in the environment where risk is inevitable. But insurance distributes risk and minimizes risk per individual. Business men could buy a policy that makes them to be satisfied by decreasing the potential losses. Of course the degree of risk varies from one sector of business to the other sector. Whatever the case, depending on the knowhow and interest of individuals and as well risk venerability, we may buy life insurance ,liability insurance, property insurance or all or two of them. In so doing there are policies and principles between the insured in addition to the existing commercial codes related to insurance that should be followed. We hope, this chapter help you a lot in giving highlights about law of insurance

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7.5. Self-test exercises

1-Insurance distribute loss to different people susceptible- Discuss2-what is premium?

3-Explain insurable interest

4-Distinguish remote and proximate cause of loss

5-What is the difference between personal, property and liability insurance? 6-Discuss defenses that may make an insurer free in life insurance?

7-Explain the preconditions in liability insurance

7.6. Progress Questions

Multiple choices

Choose the best appropriate answer form given alternatives

1, Insurance against person may be subdivided in _____.

A, life insurance B, insurance against accident C, A&B D, none

2, One of the most important and frequent type of insurance is _____.

A, insurance of persons B, insurance of liability C, insurance of object D, all

3. Historically, most scholars believe that, first insurance was emerged in ____.

A, Egypt B, contract is made C, Rome D, Babylon

4, _____ is a device that protects people from the financial costs that result from loss of life, loss of health, property damage.

A, Insurance B, risk C, Contractual requirement D, parties to the contract of insurance

5. Which one of the followings is not part of Duties of the insured?

A, Notify the occurrence of the risk insured B, notify the insurer on or within 5 days

C, Disclose material information D, payment of the premium

Chapter Eight

Negotiable instruments

Introduction

Dear students, in this part, you will study about negotiable instruments. These are instruments that are used for transaction or for your convenience near cash assets. Negotiable instruments have their own legal procedures to use them as cash or in the business transaction. You can go nearby bank and get a brief description to widen your understanding of studding this unit. We go through the points from the perspective of global general grounds since ours is not quite different.

Learning objectives

At the end of this unit, you will be able:-

- Define negotiable instruments
- Distinguish bill of exchange ,promissory note and cheques
- Discuss legal rule governing negotiable instruments

8.1. Negotiable instruments

In the last two study units of the course we will be considering the law relating to negotiable instruments, with particular reference to bills of exchange and cheques. The term "negotiable instrument" encompasses a wide variety of documents, e.g. bank notes, promissory notes, dividend warrants and exchequer bills. We will not consider these separately, because much of the law relating to bills of exchange applies equally to such instruments. Before we look closely at the law, you should note that any document is capable of being called a "negotiable instrument" as long as the following conditions are met:

- The holder of the instrument may sue in his own name.

- Title to the instrument must pass on delivery, or on delivery and endorsement.

A "holder in due course" takes the instrument free from the defects in title of hispredecessors.

Negotiable instruments are an essential part of a business-orientated society because of the ease with which they can be transferred from one person to another.

8.2. Characteristics of a bill of exchange

As we have already seen, the law ascribes certain privileges to the holder of any negotiable instrument and because of this it is important to be able to establish whether or not the document concerned in a dispute is a negotiable instrument. We have seen that a bill of exchange is recognized as a negotiable instrument all that we require, therefore, is a strict definition of what constitutes a bill of exchange.

Definition

"An unconditional order in writing, addressed by one person to another, signed by the person giving it, requiring the person to whom it is addressed to pay on demand or at a fixed or determinable future time a sum certain in money to or to the order of a specified

person, or to bearer." The following example of a bill of exchange will be useful to you.

Important Terms

- The order to pay must be **unconditional**. For example, if the drawer stipulates "provided the balance in my account amounts to £100", this is not a bill of exchange since there is a condition imposed. If the bill orders payment to be made out of aparticular fund, this is invalid as it is conditional on the fund being adequate to meet the bill, but if the drawer says "pay the bill and debit" a particular fund, this is in order since the acceptor can allow an overdraft.

The instrument must be in the form of an **order**. To say "I shall be pleased if you will pay is not an order but a mere request, but the expression "please pay " is a polite order.

- The instrument must be **in writing**. This includes print and typewriting, and also writing done with a pencil, though the latter is clearly undesirable, as it is open to fraudulent alteration.

- The instrument must be **signed** by the drawer, i.e. the person who makes out the bill of exchange. However, a person's "signature" can be put to a bill by his agent.

- The instrument must be an order **to pay**. If the instrument orders any act to be done in addition to the payment of money, it is not a bill of exchange.
- It must be to pay **a sum certain in money**. An order to pay "all moneys due" is not a bill of exchange, but if the bill is drawn for a certain amount "plus interest" this will be a valid bill.
- Payments may be expressed to be made **on demand**. This means that it must be met when the holder presents it for payment, whenever that might be: "on sight" or "on presentation" are comparable expressions in this context. Note that, where no time for payment is expressed in the bill, it will be treated as **payable on demand**.
- Instead of being payable on demand, it may be payable **at a fixed or determinable future time**, e.g. "three months after date" (i.e. after the date of the bill) or "thirty days after sight"

(I.e. after it is presented to the drawer for acceptance, the drawer being the person to whom it is addressed or "drawn"). This maturity date of the bill may be fixed by reference to the occurrence of some event and this will be valid, provided the event is something that is **bound** to happen, e.g. "three months after I die"; if the event is not certain to happen (e.g. "three months after I marry") the bill will be invalid, and the occurrence of the event will not make it valid.

- Payment may be expressed to be made **to bearee**, which means that the acceptor must pay the sum stated to whoever is the holder of the bill when it is duly presented for payment, i.e. the bill specifies no particular payee.
- It may be payable **to, or to the order of, a named payee**, in which case the drawer will have named the payee in the bill; but he can pass on the bill to someone else if he endorses it to this effect.

Note the following points concerning **payees**:

(i) A bill not payable to "bearer" must indicate the payee with **reasonable certainty** or it

will be inoperative.

(ii) Where the payee is a fictitious or non-existent person, the bill may be treated as **payable to bearer**; this point will be considered further in a later study unit.

(iii) A bill may be drawn payable to two or more payees **jointly**, or it may be drawn payable to one of two (or several) payees **in the alternative**.
(iv) A bill drawn in favor of the **drawer himself** will be a valid bill, e.g. making a cheque out to "Cash" or "Self". A bill drawn payable to the drawee will also be in order,
E.g. when making payment to a creditor by credit transfer one can give one's bank a cheque for the amount instead of handing over cash.
(v) A bill may be drawn payable to the holder for the time being of a **particular office**.

(vi) A bill drawn for "Cash" (usually a cheque) will generally be treated as **payable to bearer**. Strictly speaking, it is not a valid bill at all, and the acceptor may require the endorsement in blank of the holder.
The following points about **drawers** should be noted also:

(i) Where the drawer is a fictitious person, or a holder not having the capacity to contract, the holder may treat it there and then as **dishonored.**
(ii) Where the drawer and drawee the same person, again the bill may be treated aseither a **bill of exchange** or a promissory note.
(iii) Where the drawee is not indicated with reasonable certainty, but someone "accepts"it, the instrument may be treated as a promissory note (***Mason v. Lack (1929)***).
(iv) A bill may be addressed to two or more drawee jointly, but an order to **alternative drawee** will not constitute a valid bill and will be of no effect.

C. Acceptance

Definition and Use

The term "acceptance" used in relation to bills of exchange has a special meaning. In common parlance, a person to whom something is given takes or accepts that thing, but you should be careful to avoid this use of the word when talking about bills of exchange. Acceptance of a bill of exchange is the signification by the drawee that he accepts **the order of the drawer to pay over the sum stated to the payee**. As we have already mentioned, a bill of exchange is used by a debtor to settle his account with his creditor, but, it being an **order** to someone else to pay the sum stated (as opposed to a **promise** by the drawer to pay), the creditor is not normally going to take the bill of exchange in settlement unless the drawee acknowledges that he will meet the bill (and, in addition, isa person of substance); until he does make such acknowledgement, the drawee is under no liability on the bill. In practice, the bill is normally handed to the payee to present it to the drawee for acceptance. If the drawee agrees to pay the bill, he will sign his name across it, and by that act he accepts the liability to meet the bill when it is duly presented for payment.
You may, at this stage, ask why a third party should undertake to pay a bill of exchange drawn by a debtor to settle an account with his creditor. The answer is simply that the

person drawing the bill will have an arrangement with the drawee to reimburse him for any bills met. This, of course, leads one to the question, why go through this procedure of drawing a bill of exchange instead of the creditor just waiting for the debtor to pay? The answer to this is that, by using a bill of exchange, the supplier can send the debtor goods on credit even if he is not sure of the latter's credit status, because before he releases the goods he receives this document, accepted by a person on whose credit he knows he can rely. Nowadays, bills of exchange are most commonly used in international trade and are drawn on bankers. You will appreciate how useful an arrangement is that allows goods to be sold on credit to someone the seller has never heard of, and against whom he would have great difficulty in bringing an action for recovery of the debt. There are also other advantages in that there is a market for the "discounting" of bills, so that the creditor can receive immediate cash (for a charge, by way of interest), but this need not concern you here.

8.3. Technicalities of Acceptance

(a) Presentment for Acceptance

Although a bill must be presented for acceptance and accepted by the drawee in order to render the latter liable on the bill, it is not in fact **necessary**, as a general rule, for the holder of a bill to present it for acceptance. He can hold on to it, unaccepted, until maturity, or he can negotiate it to a third party, although a bill that has not been accepted will in practice be much harder to pass on for value.

The only occasions when the Act actually stipulates that the bill **must** be presented for acceptance are:

- Where the bill is payable a certain period "after sight". In this case, the bill must be presented for acceptance in order to **fix the maturity date**.
- Where the bill **expressly stipulates** that it shall be presented for acceptance.

(b) Requirements of Valid Presentment

The Act lays down the following requirements for a valid presentment for acceptance:

- The presentment must be made **by or on behalf of the holder to the drawee** or some person authorized to accept or refuse acceptance on his behalf.
- Presentment must be at **reasonable hour**, on a business day, and before the bill isoverdue.
- Where the bill is addressed to two or more drawees, who are not partners, presentment must be made to **them all**, unless one has authority to accept for all, in which case presentment may be made to him alone.
- Where the drawee is dead, presentment may be made to his **personal representative**.
- Where the drawee is bankrupt, presentment may be made to **him or to his trustee**.
- Where authorized by agreement or usage, a presentment through the **post office** is sufficient.

(c) Requirements of Valid Acceptance

For an acceptance to be valid, it must:

- Be written on the bill and be signed by the drawee: the mere signature of the drawee without further words is sufficient.
- Not express that the drawee will perform his promise by any other means than thepayment of money.

Acceptance is incomplete and revocable and does not bind the acceptor until the bill has been delivered – that is to say, hand back to the person presenting it, with his signature of acceptance on it.

In ***Baxendale v. Bennett (1878)*** the defendant received from H a draft in blank as to the drawer "name, written in H"s handwriting. The defendant wrote his name across the draftas acceptor and sent it to H who, finding he did not need it, returned it to the defendant. The defendant placed it in an unlocked drawer in his chamber in the Temple, from which it was taken. When it came into the hands of the complainant, a bona fide holder forvalue, the document had been completed by the insertion of the name of W. Cartwright as the drawer. No such person as Cartwright was known to the defendant, and the name was inserted without his knowledge or consent. **Held**: the defendant was not liable on the document, as, although he had accepted it, he had not delivered it

Dishonor by Non-acceptance

If the drawee is not prepared to meet the bill, he will return it to the holder with a note to this effect, and the bill is then said to be **dishonored by non-acceptance**. The holder then knows that the debtor has given him a valueless scrap of paper, and will commence proceedings against him (the debtor, the drawer of the bill, not the drawee) to recover his **debt**. Technically, such action is not an action on the debt but an action on the bill, for in drawing the bill the drawer "engages that on due presentment it will be accepted and paid according to its tenor and that if it is dishonored he will compensate the holder..."

In certain circumstances, the bill can be treated as dishonored by non-acceptance without ever having been presented for acceptance; these circumstances are where:

- The drawee is dead or bankrupt
- The drawee is a fictitious person
- The drawee is a person not having the capacity to contract.
- After the exercise of reasonable diligence, such presentment cannot be effected.
- Although the presentment has been irregular, acceptance has been refused on some other ground.

8.3.1. Qualified Acceptance

It may be that the drawee is prepared to accept the bill but only subject to some modification. Any acceptance that varies the effect of a bill as originally drawn is termed a qualified acceptance. A qualified acceptance may be any of the following:

(a) Partial

An acceptance to pay only part of a bill, e.g. a bill drawn for the amount of birr 5,000 may be accepted for birr 4,000 only.

(b) Local

An acceptance to pay the bill only at a certain place; the acceptor stipulates that he will pay the bill at this place only, and nowhere else.

Conditional

An acceptance to pay the bill only on fulfillment of a certain condition (e.g. an acceptance to pay the bill on delivery of the bills of lading)

(c) Qualified as to Time

An acceptance say to pay a bill drawn payable after one month, only after six months.

(d) Acceptance by Some Only of Several Drawees

This is self-explanatory. Note, however, that a bill may be drawn on joint drawees and, if both accept, payment may be demanded of either of them.

An acceptance will be construed as general unless clearly qualified, the acceptance being construed most strongly against the acceptor (***Smith v. Vertue (1860)***).

If the holder of the bill takes such a qualified acceptance, this has the effect in most cases of discharging from liability all prior parties to the bill except in so far as any prior party consents to the holder taking such qualified acceptance. Such consent will be implied if the holder gives notice of the qualified acceptance and the prior party does not object. In the case of a partial acceptance, prior parties are discharged only if the holder fails to give notice that he has taken the qualified acceptance. They have no right to object thereto. On the other hand, the holder of a bill who is offered only a qualified acceptance is entitled to reject it and to treat the bill as dishonored by non-acceptance.

Acceptance for Honor

Where a bill is dishonored by non-acceptance the holder of the bill may allow any other person to accept it in place of the drawer. The acceptance for honor must:

- Be written on the bill and indicate that it is an acceptance for honor, **and**

- Be signed by the acceptor for honor.

The effect is that the acceptor for honor becomes liable to pay the bill.

Promissory notes

Art. 823 of the commercial code merely lists down requirements that have to be satisfied in order to have a valid promissory note .Therefore, a complete promissory note shall contain the following requirements.

-The instruments shall contain the word “promissory note”

-Unconditional promise to pay a sum certain in money

The maker shall not attach any condition to the note. As that of the bill of exchange, the promissory note shall not be backed by a condition subsequent. If condition is attached to the note, the note loses the character of money. So, we can define promissory note as:- “(1) A promissory note is an unconditional promise in writing made by one person toanother,

signed by the maker, engaging to pay, on demand or at a fixed or determinablefuture time, a sum certain in money, to or to the order of, a specified person or to bearer.

(2) An instrument in the form of a note payable to maker's order is not a note within the meaning of this section unless and until it is endorsed by the maker.

(3) A note is not invalid by reason only that it contains also a pledge of collateral security with authority to sell or dispose thereof.

The following is a specimen of a promissory note payable on demand.

Necessity of Delivery

"A promissory note is inchoate and incomplete until delivery thereof to the payee or bearer"

No precise form is necessary for a promissory note, but the essential feature is that there must be an unconditional promise in writing to pay a certain sum in money. In a similar manner to a bill of exchange, the note must not be made payable on a contingency, although a note may contain a pledge of collateral security with authority to sell or dispose thereof.

Liability of Maker

"The maker of a promissory note, by making it:

(1) Engages that he will pay it according to its tenor.

(2) Is precluded from denying to a holder in due course the existence ofthe payee and his then capacity to endorse."

Joint Notes

"A promissory note may be made by two or more makers, and they may be liable thereon jointly, or jointly and severally, according to its tenor"

Joint liability is not the individual liability of each of the makers but the collective liability of them all together. Thus a joint note is good against the makers jointly. Should one of the makers of a joint note die or become bankrupt his estate is freed from all liability, and the liability falls entirely on the remaining maker or makers. Again, all the parties of a joint note must be sued together. If any party is not included in the action he will be released from liability. Should judgment be obtained against one or some of the parties, whether that judgment is satisfied or not, then the other or others will be released. ***Joint and Several Notes***

Joint and several liability is the liability of all the makers together collectively and of each of them separately. In other words, where a note is a joint and several one made by two or more makers. The note is good against all the makers jointly or against each one of them separately for the full amount of the note. If one of the makers to a joint and several notes dies or becomes bankrupt his estate is not freed from liability. Again, it is not necessary for the holder of a joint and several notes to sue all the parties together; the holder can sue the parties singly or in any way he pleases and the remedy against them is not satisfied until "twenty shillings in the pound" (i.e. the full amount) has been recovered.

8.4. The nature of a cheque

General Comparison with Bills of Exchange

Bills of Exchange for most countries defines a cheque as

"A bill of exchange drawn on a banker payable on demand" Note the two special requirements for a cheque:

- It must be drawn on a banker.

- It must be payable on demand.

Although cheques are a special type of bill of exchange, and the Bills of Exchange Act applies to cheques, there are a number of important points of difference:

(a) Because of the contractual relationship between banker and customer, there are a number of **special obligations** on these parties.

(b) The **rules relating to acceptance do not apply to cheques**; the banker on whom the cheque is drawn never "accepts" it, so that the drawer is the party primarily liable on the instrument.

(c) There are special provisions for the **crossing** of cheques which do not apply to ordinary bills of exchange. Special statutory protection is given to bankers in relation to **forged endorsements**.

It may be observed further that, in practice, cheques are rarely used in the way of bills of exchange as negotiable instruments. The vast majority of cheques are presented forpayment by the person to whom they are initially given, and negotiation of a cheque is comparatively rare. In effect, cheques are generally used merely as a directive by the drawer to his bank to transfer money from his account to the account of the payee.

The requirements for validity of a cheque

A cheque to be valid and binding, the following requirements shall be satisfied.

- Unconditional order to pay the sum of certain in money
- The name of the person who is to pay (drawee)
- The place of payment
- The date when and place where the cheque is drawn
- The signature of the person who draws the cheque (drawer) Art.832 negotiation of a cheque

1-Not with standing any provision to the contrary, a cheque in respect of which cover is available to the drawer may be certified by the drawee if the drawer so requests

2-The cover in respect of a certified cheque shall remain blocked in a separate account for the benefit of the holder until the expiry of the period of time for presentment provided in Art.855

3-Certification is effected by the signature of the drawee on the face of a cheque

In addition to the principal points of difference between cheques and bills of exchange referred to above, there are a number of other special features of cheques that may be noted. Prior to 1957, it was common practice for the payee of a cheque to endorse it on the back as he paid it into his bank for collection, and a cheque so endorsed was sufficient evidence of receipt of payment for the drawer of the cheque (to whom, of course, the paying bank would return the discharged cheque in due course). This practice wasgenerally found rather tedious, and in the Britain law of the **Cheques Act 1957** contained various provisions to make it unnecessary, of which S. 3 provides that "an unendorsed cheque which appears to have been paid by the banker on whom it is drawnis evidence of the receipt by the payee of the sum named in the cheque".

Thus a paid cheque, whether or not endorsed by the payee (but not if endorsed in favor of some other person) will nowadays normally be adequate evidence of receipt of payment by the payee (for auditors, etc.), and the payer is unlikely to ask for any other receipt. However, if he does do so the payee is bound to provide it. In this connection it may be noted that some cheques are found with a form of receipt attached, and require as a condition thatthe receipt must be duly completed before the cheque can be paid. Since such an instrument does not constitute "an unconditional order in writing", it is not strictly a cheque, and falls outside the **Bills of Exchange.**

Negotiation of a cheque

A cheque could be transferred from one person to another person by means of endorsement. It may be endorsed payable to certain person to his/her order or to the bearer. If it is to bearer, the drawee may write the word "to bearer" on the face of the cheque or simply may put his or her bar signature at the back of the cheque. As a cheque is best substitute of money, it may be rendered at a different time. That is you may endorse to kebede and Kebede may endorse to chala and chala may endorse to someone else. Endorsement shall not be attached to any condition and it shall be absolute. A partof money expressed in the cheque cannot be endorsed. A cheque may be endorsed to the drawee bank but the cheque in such a case is taken as receipt. Therefore a drawee bank to which the cheque is endorsed cannot re-endorse it (Art.843 of the commercial code). The endorsement shall be written on the back side of the cheque.

Summery

In this unit, we have learned issues related to negotiable instrument. Negotiable encompasses a wide variety of documents, e.g. bank notes, promissory notes, dividend warrants and exchequer bills. They facilitate business transactions if valid. To be valid all instruments should satisfy that the law demands from them. Therefore it is quite compulsory for any business man the requirements each negotiable instruments requires.

8.5. Self-test exercises

1-What is the requirement of a complete promissory note?

2-What are the two special requirements for the cheque?

4-What are the requirements for validity of a cheque?

8.6. **Progress Questions**

True or False

Write true if the statement is correct or false if the statement is wrong.

1. A cheque could be transferred from one person to another person by means of endorsement.

2. The term "acceptance" used in relation to bills of exchange has a special meaning.

3. A bill drawn for "Cash" usually a cheque will generally be treated as not payable to bearer.

4. To be valid all instruments should satisfy that the law demands from them.

5, Title to the instrument must pass on delivery, or on delivery and endorsement.

Appendix

Answer Keys

Chapter One

Multiple choices

1. C
2. A
3. A
4. B
5. D

Chapter Two

True or False

1. T
2. F
3. T
4. F
5. T
6. F

Chapter Three

Multiple choices

1. B
2. A
3. C
4. D
5. B
6. D

Chapter Four

True or False

1. T
2. T
3. F
4. F
5. T
6. T
7. F

Chapter Five

Multiple choices

1. B
2. D
3. E
4. A
5. C
6. E

Chapter Six

True or False

1. F
2. T
3. T
4. F
5. F
6. T

Chapter Seven

Multiple choices

1. C
2. B
3. D
4. A
5. B

Chapter Eight

True or False

1. T
2. T
3. F
4. T
5. T