

## Contractual Condition and its Effect on Contract

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**Abstract:** Contractual condition is a secondary form of obligations that is not independently stated in contractual document but nevertheless is a part of contractual provisions and adheres to the contract. Being a secondary obligation or its dependence on the contractual document does not change the nature of contractual condition. Contractual condition is a part of mutual covenant and as binding as the other contractual provisions of the transaction. The intention of legislators in listing the principal conditions of valid transactions in article 190 of Civil Code may have been to exclude ineffective (unrealizable) conditions from contractual obligations. However, the word transaction may not have been used for its specific meaning in the context of provisions under article 190. The question is now whether contractual condition should conform to the principal provisions of a valid transaction. Legislators discussed invalid terms in article 233 of Iran Civil Code. Section 2 of this article mentions indeterminate conditions but with the wording that is confusing, produces ambiguity, and raises a few questions. Is an indeterminate condition independently valid or invalid notwithstanding its effect on the contract? Is an indeterminate condition effective in a contract when it does not produce ambiguity in considerations? If it is effective, then, what effects does it have on the contract? What affect the waver of indeterminate condition shall have on the contract when it produces ambiguity in considerations versus when it does not? And, is waver of indeterminate condition possible?

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### Introduction

Contractual conditions are similar to principal provisions of a contract and form a part of mutual intentions and wills when parties enter into an agreement. Contractual condition does not have equal power and significance as of the principal provisions; yet, affects the contract. It may even be as critical as the principal provisions in view of signatories and, therefore, act like them.

The close relationship between a contract and its contractual condition together with the existence of a mutual consent on the provisions and underlying terms of the contract make the effect of contractual condition unquestionably final and binding. Furthermore, any ambiguity in the contractual condition shall affect the contract. The effect of ambiguity may be of two types:

- (1) When ambiguity is so strong that makes contract considerations indefinite, and consequently, makes contract invalid; and
- (2) When ambiguity is negligible and does not make contract considerations indefinite, leaving the contractual condition as the only indefinite and ambiguous issue. In this case, the ambiguity does not affect the validity of principal provisions of the contract.

When considering the close relationship between contract and its contractual condition, plus the effect the contractual condition may have on the contract, together with the potential loss that

beneficiary of the contractual condition may suffer as the result of nonperformance of the condition, it is possible to conclude that ambiguity of indeterminate condition creates the right of termination for the beneficiary. The reason is that the contract and its condition remain inseparable and are entered into by parties with the same intention and will. Thus, the ensuing possible loss of beneficiary resulting from the contractual condition makes the contract excusable.

Islamic narrations, especially *نهى النبي عن الغرر* which is attributed to Prophet Mohammad (peace be upon him) forbid ambiguous contractual conditions with possible losses to beneficiary. Save when the ambiguity of indeterminate condition is negligible and does not produce losses to the beneficiary to become a cause for invalidating the contract.

There is no argument about the first type of indeterminate condition. When ambiguity is so strong that affects contract considerations, the contract loses one of its principal provisions and becomes invalid as the result. Nonperformance of a principal provision of the contract makes indeterminate condition invalid as well.

In the second type of indeterminate condition - a condition that does not introduce ambiguity to considerations - the right of termination for beneficiary needs proof and evidence. The evidences that are called for in this case are: no-loss-rule,

consensus, or the right of termination from infringement of contractual condition.

Some Islamic jurists have argued for the first two evidences as acceptable ones to grant termination right to beneficiary. In their view, right of termination is granted when either of the first two evidences is established. However, earning the right of termination is not limited to no-loss-rule and consensus. There are other evidences that can be used for demanding termination right by beneficiary, for example, by infringement of contractual condition.

Jurists and religious leaders disagree on the validity of indeterminate contractual condition regardless of its effect on the contract. Some believe that observation of the principal conditions for valid transactions or article 190 of Civil Code is not required for contractual conditions. They refer to the next articles of Civil Code and the use of "transaction" in these articles to prove their point that these conditions only apply to independent obligations.

However, it appears that "transaction" may have been used in these articles in its general meaning. The objective and philosophy behind stating the principal conditions may have been to prevent losses by addressing all contractual obligations including dependent and independent ones. Observation of the principal conditions for valid transactions is also required for contractual conditions and there is no reason for not doing so.

Legislators have listed three invalid conditions in article 232 of Civil Code. This article is not exclusive to certain conditions and applies to other conditions as well including indeterminate conditions. The stated conditions that invalidate contractual condition are listed in three groups. These grouping are similar to the grouping of Article 190 of Civil Code and the conditions for valid transaction.

Section 3 of article 232 refers to "condition that is unlawful (religiously forbidden)" which is similar to section 4 of article 190 which refers to conditions for valid transactions. Section 2 refers to "condition which does not produce any benefit" which is very similar to section 3 of article 190. However, nothing is mentioned in article 232 that is similar to sections 1 and 2 of article 190.

It is self-evident that intention, willingness, and capacity are required for any obligation including secondary, dependent, or independent ones. Therefore, observation of the principal conditions for transaction validity is undeniably required for contractual conditions.

When indeterminate condition creates ambiguity in considerations waiver of contractual condition is impractical and irrelevant. When one of the principal provisions of contract becomes

ineffective the contract becomes invalid. Thus, the ambiguity in consideration cannot be removed by waiving indeterminate condition intended to revalidate the contract.

When ambiguity in contractual condition does not lead to ambiguity in considerations and the ambiguous condition is not negligent, waiver of contractual condition makes contract valid. In this case, beneficiary gains the right of termination due to invalidity of contractual condition, non-performance of contractual condition, or losses resulting from performance of contract.

Beneficiary may choose not to exercise his right of termination and opt for performance of contract. This is commonly interpreted as waiver of contractual condition. Waiver of contractual condition is irrelevant, because waiver applies to valid rights that have been already created but not performed yet. In this case, ambiguous contractual condition is automatically invalid because of non-observation of principal conditions for valid transaction. Therefore, waiver is irrelevant.

This paper is organized into five sections and the findings of analysis are presented in the final section.

- (1) Effects of indeterminate contractual condition,
- (2) Right of termination when indeterminate condition does not produce ambiguity in considerations,
- (3) Validity or invalidity of indeterminate condition regardless of its effects on the contract,
- (4) Effect of indeterminate condition as an independent obligation, and
- (5) Effects of waiver of indeterminate condition.

### **Effects of Indeterminate Condition**

Contractual conditions are similar provisions as considerations but they are not parts of them. They are effective like considerations, but their effect is not as strong as the effects of the principal provisions of contract. Sometimes, a contract is concluded for performance of a contractual condition. In this case, the contractual condition has similar standing as principal provisions. Other times, parties alter consideration or subject of the contract because of a contractual condition or its performance.

Generally, completion of parties' intention and will is subject to the performance of contractual condition. According to such interpretation, ambiguity of contractual condition always introduces potential losses to the contract, no matter how small. Unless the material and immaterial relationships that usually exist between contract and its conditions do not hold. This is when contractual condition is an independent obligation and has a separate entity.

Legal experts divide indeterminate condition into two types. These are the two cases where indeterminate contractual conditions are acceptable.

1. Indeterminate condition whose ambiguity makes contract considerations ambiguous, and
2. Indeterminate condition whose ambiguity does not introduce ambiguity in contract considerations.

Ambiguous contractual condition may not introduce ambiguity in considerations but create causes in the contract for potential losses. This situation may not invalidate the contract but creates right of termination for beneficiary. Jurisprudence has prohibited contracts that produce losses without mentioning about ineffectiveness of such contracts, the level of potential losses that may invalidate the contract, or whether losses are to affect or not to affect contract considerations.

When ambiguity is negligible and a general understanding about contractual condition is sufficient for its performance, then, the contract is free of any potential losses to make the contract and its contractual condition ineffective.

Some legal experts believe that there is only one type of indeterminate condition is only one type and that is when it introduces ambiguity in considerations <sup>[1]</sup>. They argue that indeterminate conditions always create ambiguity in considerations. The wording of legislation in section 2 of article 233 of Civil Code follows this line of argument. This section repeatedly refers to only one indeterminate condition, quote: "an indeterminate condition whose ambiguity makes considerations ambiguous".

Contrary to this belief, indeterminate condition does not always create ambiguity in considerations, but affects the contract similar to consideration. Therefore, dividing indeterminate condition into two types is more prudent. There are times when indeterminate condition is vague that clearly introduces ambiguity in considerations making contract invalid. Other times, indeterminate condition is not so vague to make considerations ambiguous and invalidate the contract. This situation grants right of termination to the beneficiary because of the effect it has on the contract.

Indeterminate contractual condition may have two types of effects:

1. An indeterminate condition that introduces ambiguity in considerations. Such ambiguity invalidates the contract and its condition. The reason being that the ambiguity affects the principal provisions of the contract. Any ambiguity in principal provisions invalidates the contract according to article 190 of Civil Code.
2. An indeterminate condition that does not cause ambiguity in considerations, nevertheless, it

affects the contract. If indeterminate condition was intended to be as one of the principal provisions of the contract similar to considerations, the contract is invalid; otherwise, it creates the right of termination for beneficiary. Save when the ambiguity is negligible and does not strongly affect the contract and its consequences.

### **Right of Termination**

Indeterminate contractual condition has two forms:

- (1) When it introduces ambiguity in considerations.
- (2) When it does not introduce ambiguity in considerations but the ambiguity in the condition is not negligible.

In case of the former, article 190 of Civil Code has decided its fate by ruling such ambiguity invalidates the contract because it affects the principal provisions of the contract. So, there is not argument in this case.

In case of the latter, the beneficiary has the right of termination. The argument here is that since contract and its contractual condition are closely related, any ambiguity in condition affects the contract even when the it does not create ambiguity in considerations.

Some religious jurists agree on the notion that contractual condition is a part of mutual covenants; yet, they grant right of termination to beneficiary if he may suffer losses because of the ambiguity in the contractual condition. However, these jurists have not found any evidences to prove this notion. The reason is that "no-loss-rule" (by which many losses are proved) does not justify the right of termination as it does not make a decree and can only negate a decree.

Some religious authorities argue that if no-loss-rule were to spell a decree in this case, the issue of loss comes into play and this would require a new religious jurisprudence. Since this is not possible, therefore, religious requirements do not mandate any right of termination for beneficiary <sup>[2]</sup>.

Rebuttal to this line of argument is that establishing new religious jurisprudence or religious requirement does not fit in principle reasoning. The case has to be justified by reasonable and principle arguments. No decree among principles of jurisprudence "dictates non-establishment of new religious jurisprudence or religious requirement"; therefore, no-loss-rule may be applied to grant right of termination.

Even if we subscribe to the notion offered by this group of jurists and accept the rule which "dictates non-establishment of new religious jurisprudence or religious requirement", then, we can

state that no-loss-rule is not the only way to prove the possibility of loss in a contract. Infringement of contractual condition may be applied as the basis for granting right of termination; and one example may be right of termination for beneficiary when indeterminate contractual condition does not produce ambiguity in considerations and ambiguity in contractual condition is not negligible.

Another line of reasoning for granting right of termination is consensus which taken from Sunni jurisprudence and is not acceptable to Shiite as proof of evidence. Even if consensus were to be accepted by Shiite, there is no consensus in this case. Furthermore, consensus is a *Labbi* proof (Fazel Harandi, 1387/2008, p. 255) and cannot be generalized to cases where there is doubt.

### Indeterminate Condition: Valid or Invalid?

The questions here are whether an indeterminate condition which creates ambiguity in considerations is invalid and void because of: (1) its ambiguity and possible loss to beneficiary; or (2) its dependence to the contract and the probability of loss it introduces to the contract. In other words, whether indeterminate condition is valid or invalid on its own regardless of its effect on the contract?

Some legal jurists argue that the basic point here is that it is not necessary to observe the principal of transaction validity for contractual conditions. They refer to article 190 of Civil Code to back their argument and further elaborate that this article regulates contract as a legally independent mutual covenant. They believe the term *transaction* is used with its special meaning in this and following articles. In reference to article 232 of Civil Code, they explain that this article alludes to conditions that may invalidate a contract without any reference to any unknown descriptive condition. This article limits conditions that may invalidate contract to ineffective, useless, and illicit conditions (Shahidi, 1387/2008, p. 92).

However, in response to these arguments, one may say:

- 1) Article 190 of Civil Code states four basic conditions for validity of transactions. Section 1 refers to mutual intention and agreement of parties. The existence and validity of these two requirements are undoubtedly obligatory for any contract. Section 2 refers to capacity of parties for entering into an agreement. This is one of the principals of any obligation which equally applies to contractual condition in spite of being secondary and dependent term.

Parties consider contractual condition when they enter into contract and it becomes part of their mutual covenant. The capacity of signatories

together with their intention and agreement for inclusion and implementation of contractual condition are undeniably required for validity of the contract.

Section 4 of article 190 refers to enforceability and legality of obligations in any transaction. This section does not specifically address independent agreements and obligations like sections 1 and 2. Rather, it addresses all and any obligations. Therefore, one cannot say that the legislator's intention for using transaction in this article was to apply principal terms to independent transactions and agreements.

Therefore, the focus should not be on the apparent or special meaning of words because many written and lexical faults are observable in the text of legislatures. Even if we accept that there is no written or lexical fault in this section, one can say that the intention of legislature in using the word *transaction* has been for its general meaning.

The section that is subject of the most critical debates is section 3 of article 190 of Civil Code. This section refers to a *given subject of transaction*. Considering the comprehensiveness and inclusiveness of sections 1, 2, and 4, is it possible to say that section 3 is an exception and is related only to the main and independent obligations, thus, there is no need for contractual condition to be clear and definite?

There is no legal or religious justification for this argument and consider section 3 as specific for agreements and transactions, because, a little attention can reveal the intention of legislators for this article was to include all obligations. Thus, one cannot reject this logical and acceptable objective due to usage of a given word.

There is no reason to believe that the intention of legislator in using word *transaction* was its special meaning. If we assume that there was no mistake in using this word on the part of legislator, therefore, its general meaning was intended and the application of *every* before *transaction* at the beginning of this article may indicate extra emphasis.

- 2) Article 232 of Civil Code lists some of the most common situations that may invalidate contractual condition. This article is not exclusive for certain conditions and legislators have intended to group invalidating conditions into three general classifications. This grouping does not mean to make this article exclusive to the invalidating conditions mentioned under this article. Neither does it mean that invalidating conditions are limited to the ones mentioned.

Even if we were to accept the exclusiveness of this article, the ambiguous term can be treated as part of either section 1 or 3. The reason behind this line of argument is that according to article 190 of Civil Code, the validity conditions of transactions should be observed in contractual condition. Section 3 of article 232 of Civil Code refers to *an illicit condition*. Illicit condition may include any or all conditions that are against the law or interfere with public order (Katoozian, 1386/2007, p. 221).

An indeterminate condition does not fit the definition of section 3 of article 232 of Civil Code but may become subject to this article as an illicit condition. When subject of condition is not clear and defined, then, it may become invalid as a non-performable condition subject to section 1 of this article.

The reason for considering indeterminate conditions invalid is because there is no general knowledge on the subject of condition and the possibility of losses for beneficiary. The exception is when the implementation of contractual condition and avoidance of possible losses require detailed knowledge about the subject of condition. In this case, the existence of detailed knowledge about the subject of condition is sufficient<sup>[3]</sup>.

Indeterminate conditions are not alien to article 232 of Civil Code and could be covered by this article. Even if some do not agree to this conclusion, one may allude that this article is not exclusive to conditions that invalidate contract and these conditions are not limited to the three classifications. Therefore, indeterminate conditions may be invalid because they do not follow the main provisions for valid transactions.

### **Indeterminate Condition as an Independent Obligation**

Sometimes a contractual condition represents an independent agreement and/or obligation. The only reason for its inclusion in the contract is to initiate a specific performance under certain conditions necessitated by the principal provisions of the contract. There is no certain dependence between the contract and its condition here and nor was it intended by the parties to create a similar dependency that exists between contract and other provisions. Thus, the contractual condition loses its dependence nature. In this case, the contractual condition not only is not part of considerations, but also does not affect the contract.

The requirement for ambiguity of contractual condition to affect the contract rests on the existence

of an intellectual and dependent relation between the contract and its contractual condition. But, we cannot find such relation here. When an independent contractual condition is indeterminate, it does not affect validity of the main contract because there is no precedence that may produce losses to that contract. Such contractual condition does not invalidate the main contract nor does it create the right of termination for the beneficiary. Indeterminate conditions are undoubtedly invalid if they make the principal and independent obligations indefinite.

In response to those legal and religious jurists that consider indeterminate condition valid and do not consider *observation of principal conditions for transactions validity* applicable to contractual condition, we should say that this case is contrary to their views. We may subscribe to their view and say that indeterminate conditions are subject to article 190 of Civil Code and, therefore, invalid.

### **Waiver of Indeterminate condition**

A contractual condition is dependent to the contract. The intention of parties in entering into an agreement applies to its condition as well. Parties conclude a contract with certain conditions with mutual consent and will. Therefore, agreement on the contractual condition is not separable from agreement on the contract. Now, what happens when contractual condition is indefinite and what effects does it have on parties' mutual intention and will in drawing a contract?

We have to differentiate between two types of indeterminate condition:

- 1) An indeterminate condition that introduces ambiguity to considerations.
- 2) An indeterminate condition that neither produces ambiguity to considerations nor affects the principal provisions of the contract.

In the first case, indeterminate condition makes considerations indefinite from the outset and, consequently, affects the principal provisions of the contract. In other words, parties' mutual intentions are set on an indefinite subject and the ambiguity has affected parties' intention. The ambiguity in intention and the principal provisions of contract make contract ineffective as if there has not been a contract to begin with. Therefore, it is not possible to correct the contract by waving its contractual conditions. As mutual agreement and intention for entering into a contract are not separable from contractual condition and they together represent the wishes of both sides, therefore, it is possible to say that no condition was established to be waved. Only what is established and not yet performed can be waved, which is not the case we have in type one.



In the second case, the original intention of parties was to apply their mutual agreement in making the contract and its condition. Such indeterminate condition affects the contract but the effect is not such to invalidate it. For possible loss of beneficiary due to the ambiguity of the condition, dependence of contract on its condition, and applicability of mutual covenant and intention to both contract and its condition, the indeterminate condition only creates the right of termination for possible losses without affecting the validity of the contract. If the beneficiary decides to waive the condition, his right of termination becomes void. In this type of indeterminate condition, the beneficiary has the right to terminate the contract or waive his right and accept the possible loss he may suffer as the result of non-performance of the condition in order to allow the performance of the contract. Such waiver is viewed by secular law as waiver of the contractual condition.

#### Summary

1. Contractual condition affects the contract and the intention of parties. Ambiguity in contractual condition may affect the contract in two ways: a) when the ambiguity is so strong that makes considerations ambiguous; and b) when the ambiguity in contractual condition does not make considerations ambiguous. In the former case the contract becomes invalid. In the latter case, the contract remains valid but the beneficiary has the right to terminate the contract because the mutual agreement of parties applies to the contract condition and its implementation. In other word, the contract condition and its implementation are parts of mutual intention and will. Furthermore, the condition cannot be separable from the contract because the condition is dependent to the contract. This dependency together with the possible losses that the beneficiary may suffer from non-performance of the indeterminate condition provides right of termination to the beneficiary. This is true only if ambiguity is not negligible and produces loss to the beneficiary.
2. No-loss-rule and infringement of contractual condition are the two reasons for the beneficiary to demand right of termination. They apply to the cases when an ambiguous term does not make considerations indefinite and the ambiguity in contract condition is not negligible. Since religious jurists do not approve no-loss-rule as proof to invalidate contract, thus, the only evidence to demand right of termination is the rule of contractual condition infringement.
3. Indeterminate contractual condition is invalid regardless of its effect on the contract because observation of the principal conditions of transaction validity is required for contractual condition. The principle conditions are not limited to independent obligations. According to section 3 of article 232 of Civil Code, indeterminate condition is invalid on its own because any condition that does not conform to regulations is prohibited by religious rules. Indeterminate condition is against article 190 of Civil Code and does not meet the principal provisions for validity of obligations because of its indefinite subject.
4. Indeterminate condition affects the contract when there is a natural relation and dependency between contract and its condition. Sometimes, a contractual condition is an independent obligation and is included in a contract because of a given reason or a specific performance mandated by primary provisions of the contract. In this case, the ambiguity in contractual condition does not affect accuracy and validity of the contract.
5. When indeterminate condition produces ambiguity in considerations, the contract and its condition are assumed not established as if there was no contract to begin with. Consequently, the contractual condition becomes ineffective. So, waiver of such condition is irrelevant and does not revalidate the contract. Furthermore, when an indeterminate condition which does not produce ambiguity in considerations is waived by beneficiary it translates into a waiver of right of termination and represents his agreement to validity of contract and its performance.

#### Notes:

1. One of the religious jurists is Sheikh Morteza Ansari. He wrote in his book *Al-Makaseb* that indeterminate condition is always involved with some degree of loss and affects one of contract considerations. He believed that indeterminate condition always introduced ambiguity in considerations. However, this line of argument may not be without fault. The reason is that indeterminate condition does not always produce ambiguity in considerations. It is better to say that indeterminate condition affects contract but may not produce ambiguity in considerations.
2. One example for these religious jurists is Sheikh Morteza Ansari. He believed that proving the right of termination may be difficult for beneficiary. He listed no-loss-rule and consensus as evidences required for demanding

right of termination. If these two rules are rejected, then, there is no right of termination for beneficiary. The problem with this line of argument is that the evidences to prove right of termination are not limited to these two cases. For example, infringement of contractual condition produces right of termination for beneficiary.

3. Secular law is the criterion to decide whether contractual condition should be clear and definite in detail or in general. According to secular law, it is generally sufficient for contractual condition to be clear and definite. Save in special cases when the main criterion for deciding whether a contractual condition is valid or invalid rests on the potential loss it may produce. In this case either detailed or general knowledge may apply.

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