

GUIDELINES ON CONTRACTS

INTRODUCTION

1. What is a contract?

A contract is a legally binding agreement between two or more people. It is an agreement that aims to create a legal obligation or a duty enforceable by law.

2. What are the advantages of entering into a contract?

A contract helps people that are doing business, to carefully think through the deal before they enter into it.

Contracts help to create certainty. Because both parties have written down what they expect from and promised to each other, and added their signatures to confirm this, they can be more certain that the other person will fulfil her or his obligations stated in the contract.

This increased certainty also minimises the risks of doing business. Both parties to a contract are making an investment and they both expect to maximise their profits. For example, to protect her or his investment, a farmer may include a provision that allows him to vary the price according to prevailing market conditions. A trader may protect her or his investment by specifying that she or he will be entitled to reject the goods if they are of poorer quality than agreed.

REQUIREMENTS FOR A VALID CONTRACT

In order for a contract to be recognised as valid under the Laws of Uganda, the following conditions must be fulfilled:

1. There must be an *offer* made by one person, and an *acceptance* of that offer by another person. The offer and acceptance are the basis of the agreement.
2. The parties must have the intention to be *legally* bound. Agreements of a social or domestic nature, for example, an agreement that your business partner will buy you a drink, or an agreement made between a husband and wife, cannot be legally enforced.
3. Both parties to the contract must *freely* agree to be legally bound by the contract. A contract which involves the following elements will not be valid:
 - The use of force.
 - Fraud (being dishonest, cheating or using trickery) or misrepresentation (concealing or falsifying information).
 - Mistake (where one or both parties honestly misunderstand what the contract was all about).

4. Both parties must provide something of value (*consideration*). For example, the buyer provides money and the seller provides the goods.
5. Both parties must be in a position to sign a legal contract (they must have the *legal capacity* to contract). This means that:
 - They must be adults aged at least 18 years and above.
 - They must be of sound mind.
 - Companies and Co-operative Societies are recognised as artificial persons under the law, known as *bodies corporate*. They can also enter into contracts. An authorised representative of the company or cooperative society, for example, a director, chairperson or secretary, can sign on its behalf.

Note: Farmers' Associations or Groups that are registered as Community Based Organisations but not registered as companies or co-operative Societies **are not** recognised as artificial persons or *bodies corporate* under the Laws of Uganda. Any businessperson dealing with such groups or associations must bear in mind that he is dealing with the individuals in the group but not with the group as a single entity.

WHAT DOES A CONTRACT OR A SALE AGREEMENT LOOK LIKE?

A contract consists of several clauses, each of which controls a specific aspect of a contract. Contracts for the sale of agricultural produce usually contain the following clauses:

1. Names and Addresses of the Parties

The names and addresses of the parties to the contract must be mentioned at the beginning. For example, Mr. A, of P.O. Box 1, Kampala (a trader), and Mr. B, of P.O. Box 2, Luwero (a farmer). The physical addresses of the parties may be used instead or can be added, for example, Mr. A, Nakasero market stall 22, Nakasero, Kampala Central.

The parties are free to agree that the contract shall be binding upon the *representatives* or a person who has the legal authority to manage the business and property of a deceased person (*successors in title*) of both parties. This protects either party in case something happens to the original signatory and dealings have to be concluded with another person.

2. A statement of intention to enter into a legally binding agreement

There must be a statement of the parties' intention to enter into a binding agreement with one another, for example:

“The Farmer wishes to sell and the Trader wishes to buy goods consisting of Maize, on the terms and conditions set out in this contract.”

This also signifies the offer and acceptance.

3. Description of the Goods or Produce (*Subject Matter*)

The description of the goods or produce that are being sold or bought must be as accurate as possible. For example:

“The Farmer shall supply the Trader with produce consisting of 30 sacks of Maize of variety A, each sack weighing 50 kilograms.”

4. Price and terms of payment

The price or value of the goods must be specified. Terms of payment refer to the form of payment, that is, whether by cash or cheque, and whether the total amount will be paid at once or in instalments. For example:

“The price shall be Uganda Shillings 20,000/= per sack, totalling to Uganda Shillings 600,000/=. The sum shall be paid in cash and shall be payable in instalments as follows:

- An advance of Uganda shillings 50,000/= at the time of signing this agreement;
- Uganda shillings 400,000/= on delivery of the produce;
- Uganda shillings 150,000/= within 30 days after delivery.

In long-term agreements that cover a period of several months or seasons, it may be necessary to vary the price to take into account market fluctuations. The buyer and seller are free to change the price depending on prevailing market conditions, and any such change in price should be indicated by an amendment to the contract signed by both parties.¹

5. Warranties

A *warranty* is a promise or an assurance by the seller, firstly, that he is the rightful owner of the goods and therefore entitled to sell them, and secondly, that the goods sold are of the quality agreed and suitable for the purpose for which they are being sold.

A *warranty* that the seller is the owner is important to protect the buyer, who may later discover that he was dealing with a pretender or a thief. The seller therefore undertakes to cover (*indemnify*) the buyer from any loss that may arise as a result of third party claims on the goods.

A *warranty* on the quality of the goods is also important. For example, a trader who is buying maize to grind it into ugali or posho and then supply it to a school for feeding students will expect the maize to be of the proper type (not pop-corn!), and quality (not full of weevils!)

The relevant clause in the contract is usually to the effect that:

“The seller warrants that the goods shall correspond to the specifications given by the buyer and shall be fit for the purpose and of the agreed (*merchantable*) quality.”

The phrase “*merchantable quality*” is used in the law to mean that the standard or quality of the goods being sold corresponds to a certain standard. Literally, it means that the goods are saleable or marketable, i.e., the goods must have some value and must not be useless for the purpose for which they are being bought.

¹ See Number 9 on Amendment of the Contract.

6. Delivery and passing of ownership (*title*) and risk

A contract must specify the **time** and **place** for delivery of the goods.

It should be noted that time of delivery is usually very important to a transaction for sale of agricultural goods, especially perishable ones. It is an essential element of the deal between the buyer and the seller. In case the seller fails to collect the goods on time, the buyer may be entitled to end the contract to prevent his goods from perishing.

However, the parties can agree and specify alternative measures that can be taken in case of delays by either party.

It is important to agree on when the ownership or *title* and accordingly, the risk will pass from the seller to the buyer because the goods may be lost or destroyed before either delivery or payment is complete. In case of loss or destruction before completion of the contract, the person who bears the *title* bears the risk and is the one who suffers the loss.

A clause protecting the seller from liability in case of failure to deliver the goods due to weather changes, an outbreak of pests and diseases, war, or any other unforeseen circumstances should also be included.

7. Inspection of the goods before acceptance

Such a clause is included to protect the buyer from taking goods that may not correspond to the desired quality. The buyer should accept the goods only after an inspection has taken place to ensure that the goods are of the desired quantity, quality and type. If the goods do not correspond to what is desired by the buyer, the buyer may reject them within a reasonable time after inspection.

8. Time period (*duration*) of the Contract

The parties may wish the contract for sale of agricultural produce to be a long term contract, in which the farmer supplies a particular trader with a particular type of produce over several planting and harvesting seasons. This should be specifically mentioned. However, if it is a one-time transaction between a seller and a buyer, there is no need to mention this fact.

9. Severability and amendment of the contract

Once the contract has been signed, subsequent events may make some of the clauses or provisions of the contract inapplicable or unrealistic. For example, the quantity of produce available may reduce because of drought or other unforeseen factors. The parties may cater for such eventualities by providing specifically that such an event will not necessarily mean that the whole contract no longer applies.

A subsequent change in circumstances will require changes in the contract itself. A specific clause that allows the parties to amend the contract through mutual agreement is therefore included in the contract to cater for such a situation. Any changes or amendments to the contract must always be in writing and must be signed by both parties.

Even where circumstances do not change the parties are still free to change the provisions of the contract as long as such changes are written on the contract and both parties counter sign against them.

10. Conflict Resolution

As mentioned earlier, the major aim of entering into a legally binding contract is to protect the interests or investments of both parties. Subsequent breach of the contract by either party, for example, failure to pay on time, issuing a false cheque, or failure to deliver the goods on time should not result in the innocent party suffering loss. A breach of contract may also occur as a result of unforeseen misfortune, which is not the fault of either party.

A breach of the contract may lead to a dispute between the parties. Such an eventuality should be taken care of by providing for an amicable method of resolving any disputes that may arise.

Resolving the dispute amicably implies that the parties should try and solve the matter between them on their own. Should this fail, they may refer the dispute to a third party, mutually agreed upon, who will assist them to resolve the matter or make a decision on the matter. Such a third party is known as a *Mediator* or an *Arbitrator*.

A *mediator* is not a judge or magistrate, but someone whom both parties respect and whose authority they agree to recognise, who will assist them to arrive at a mutually agreeable decision on the matter. The mediator does not make the decision, but merely facilitates the parties to the dispute to come to a decision.

An *arbitrator* is also not a judge or magistrate, but someone whose authority to reach a decision on the matter the parties agree to recognise. The arbitrator listens to both sides of the dispute and makes a decision. The parties must then abide by the decision of the arbitrator.

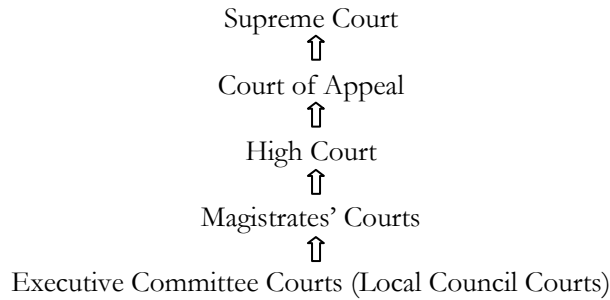
Taking the matter before the courts of law should be resorted to only when all other alternatives of resolving the dispute have failed.

Note: It is not necessary for the contract to specifically mention that in case of failure to resolve the dispute amicably or through a *mediator* or *arbitrator*, the matter shall proceed to the courts of law. Going to court is the automatic right of any person who has a complaint against another person.

Involving the Courts of Law

It is always better to resolve disputes without involving the courts of law because it is cheaper and less time consuming. However, sometimes, efforts to resolve the dispute through alternative means may fail. The Courts have been put in place to ensure that persons who feel that they have been wronged can obtain an appropriate remedy through a decision made by a judge or magistrate that is binding and enforceable under the laws of Uganda.

The following courts, shown below in order of their hierarchy, are established under the laws of Uganda:



An aggrieved party may file his case before the Local Council (LC) Courts, Magistrate Grade II, Magistrate Grade I, Chief Magistrate or the High Court; depending on the value of the subject matter of the contract. The case should be filed in a court within the geographical area where the dispute arose.

- LC Courts may preside over disputes involving contracts where the value of the subject matter does not exceed Uganda shillings 5,000/=.
- Grade II Magistrates may preside over cases where the value of the subject matter does not exceed Uganda shillings 500,000/=.
- A Grade I Magistrate may handle cases whose value does not exceed Uganda shillings 2,000,000/=.
- A Chief Magistrate has jurisdiction (power) to preside over a case where the value of the subject matter does not exceed Uganda Shillings 5,000,000/=.
- Where the value of the subject matter exceeds Uganda shillings 5,000,000/= the case must be filed before the High Court of Uganda, Commercial Division.

Note: The Commercial Division of the High Court strongly encourages parties to settle matters out of court. When a case is filed before the Commercial Court, it is always first referred to the Centre for Arbitration and Alternative Dispute Resolution (CADRE) for Mediation or Arbitration. Parties will be referred to CADRE even if they have already tried to use another Mediator or Arbitrator. The Commercial Court will hear the case only if CADRE fails to resolve the dispute.

Any party who is dissatisfied by the decision of a Court may appeal to a higher Court in accordance with diagram shown above.

An appeal lies from the LC I Court to the LC III and then to the Chief Magistrate's Court.

Remedies available from the Courts of Law

The decision of the Court in a matter involving a contract for sale of goods usually involves the following:

- The court may award the aggrieved party *damages* for breach of contract. Damages are compensation awarded by the court for the loss and inconvenience suffered by the aggrieved party
- The Court may order *specific performance* of the contract, i.e., the Court may order the parties to actually perform or carry out their obligations in accordance with the contract

11. Termination of the Contract

A contract is automatically terminated as soon as both parties have fulfilled their respective obligations under the contract, i.e., when the required quantity, quality and type of goods have been delivered and full payment for the goods has been made.

However, even though it is a legally binding agreement, a contract is not like a prison sentence and either party may terminate or end the contract at any time, if they wish to do so. For example, the seller may find that she or he is unable to supply the goods as agreed in the contract. The party wishing to end the contract must give the other party sufficient notice of the intention to terminate the contract. Accordingly, a clause on termination should be included and should specify a period of notice of termination agreeable to both parties. Fourteen days is usually sufficient.

A contract may also be terminated due to other circumstances which may make either the buyer or seller unable to fulfil their obligations, for example, war, weather changes, or where one of the parties becomes bankrupt or is wound up. Bankruptcy is a situation where a person is unable to pay or his debts and obtains a Court Order declaring her or him a bankrupt. This order protects a person from being harassed by the creditors. The Court appoints another person, called a receiver, to manage the business and property of the indebted person, sell off his assets, and arrange for creditors to be paid. Winding up is similar to bankruptcy but applies to companies, whereas bankruptcy applies to individuals. If any such and foreseen event takes place the affected party should notify the other party to the contract as soon as possible.

Please note that termination can only be done where no goods or money has yet been exchanged between the parties. Once goods or money has been exchanged, any failure by the other party to meet their obligations amounts to a breaking (*breach*) of the contract. In case of a breach, the parties may amicably agree on what course of action to take or if they fail to agree, they may refer the matter to a Mediator as provided for above.

12. The Law Applicable to the Contract

For the avoidance of doubt, the contract should contain a clause specifying which laws shall apply to the contract, particularly if one of the parties to the contract is not a Ugandan national. In Uganda, contracts for the sale of produce are governed by the Contract Act and the Sale of Goods Act.

13. Signatures and Witnesses

Once the parties have laid down their respective obligations and other terms and conditions that constitute the agreement, they must confirm their intention to create a legal document by signing the contract in the presence of witnesses. The date of signing must be clearly indicated. Witnesses must be present at the signing because they confirm the element of free consent, i.e. that both parties signed freely and were not forced by anyone.