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Chanda Chungu
University of Zambia

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Phinate Chona v ZESCO Limited CAZ Appeal No. 66/2019

Chanda Chungu¹

Facts

In *Phinate Chona v ZESCO Limited*,² an employee claimed that her retirement benefits were underpaid because her last received service allowance was a different amount to what was used to calculate her final package. The employee received a higher service allowance and did not pay tax on it, as her employer paid the tax on this amount during employment but when she retired, they calculated the benefits on the net amount.

Holding

The Court of Appeal endorsed the view that in construing a contract, a court may resolve any ambiguity by looking at its commercial purpose and the factual background against which it was made.

The Court of Appeal found that the clause on retirement benefits provided a different formula for calculation of retirement benefits and was not dependant on the service allowance she received whilst in employment. In this case, the Court of Appeal stated that a court is permitted to look at the factual background to determine the calculation of her final retirement benefits. As such, the Court held that the employee was only entitled to what her contract provided for and not the additional benefits she was claiming.

Significance

The Zambian law of contracts is heavily reliant on principles from the English courts. Recently, there has been an attempt by the Court of Appeal to ‘domesticate’ several of these principles. The *Phinate Chona* case is the latest example of the court taking a decisive step in developing Zambia’s law of contract.

Many contractual disputes are as a result of disagreements over the proper interpretation of a particular phrase in a contract and most of them depend upon the precise wording and context of the contract. As such, when a dispute arises, the court must construe or interpret the terms

¹ LL.B. (Cape Town), LL.M (Cape Town), MSc (Oxford). Lecturer of Law, University of Zambia.

² CAZ Appeal No. 66/2019.

of the contract to determine their true meaning and legal effect. Construing the terms of the contract refers to the process by which a court arrives at the meaning to be given to the language used by the parties in express terms of a contract. The Court of Appeal in this case dealt with the crucial issue of the law in relation to the construction and interpretation of contracts.

The Zambian courts have provided in a number of cases such as *National Drug Company Limited and Zambia Privatisation Agency v Mary Katongo*,³ that when parties freely and voluntarily enter into contracts, they are bound to the terms of the contract. In these cases, the courts have aptly provided that the courts have a role to merely give efficacy to the contract to ensure it is respected, upheld and enforced.

Based on this authority, the traditional approach has been for the courts to merely look at the ordinary meaning of words in the contract to determine the true intention of the parties and give effect to that intention. The reason for this is that it is presumed that the parties have intended what they in fact said, so that their words must be construed as they stand – a court should not ordinarily be called to interpret the intention of the words used. The ‘rule’ that words should be given their ‘natural and ordinary meaning’ reflects the common sense proposition that we do not easily accept that people have made linguistic mistakes, particularly in formal documents. On the other hand, if one would nevertheless conclude from the background that something must have gone wrong with the language, the law does not require judges to attribute the parties an intention which they plainly could not have had.

The above traditional approach has been an important tool in the interpretation of contracts by the courts. However, the literal approach taken is not the only rule of interpretation that the courts rely upon when giving meaning to the intention of the parties. The law also recognises the exceptions to the parole evidence rule and the use of background information.

The parole evidence rule espouses that “evidence cannot be admitted (or, even if admitted, cannot be used) to add to or vary or contradict a written instrument”.⁴ This was certainly discussed in the case of *Holmes Limited v Buildwell Construction Company Ltd*,⁵ where Bruce-Lyle J held that:

³ SCZ Appeal 79 of 2001.

⁴ See also *Jacobs v Batavia and General Plantations Trust* [1924] 1 Ch 287.

⁵ (1973) ZR 97.

Where the parties have embodied the terms of their contract in a written document, the general rule is that extrinsic evidence is not admissible to add to, vary, subtract from or contradict the terms of the written contract.

Therefore, as a general rule, where the parties have embodied the terms of their contract in a written document, extrinsic evidence will not be considered. This rule can easily be justified. Firstly, if the contract had been reduced to writing then it was only logical to suppose that things omitted from the written document actually formed no part of the agreement. Secondly, the danger is that adding terms in after the written agreement leads to uncertainty. However, over time a number of exceptions to the strict rule have emerged rendering the rule unworkable.

One exception to the general rule is in circumstances where the written agreement is not intended to express the whole agreement. In *Holmes Limited*, the court highlighted that the general rule that where the parties have embodied the terms of their contract in a written document, extrinsic evidence may be admitted if it shows that the instrument was not intended to express the whole agreement between the parties. The court held:

...extrinsic evidence maybe admitted to show that the instrument was not intended to express the whole agreement between the parties. (*Chitty on Contract* 23rd Edition, Vol. I, para. 620.) In the case of *Mercantile Bank of Sydney v Taylor* their Lordships stated at page 321: 'It had been proved that the whole terms of the agreement under which Griffin became entitled to his release were embodied in the bank's letter of the 5th April, 1889, which he accepted without reservation or qualification. On that assumption, it is plain that the previous verbal communications which had passed between him and the bank were completely superseded, and could not be legitimately referred to, either for the purpose of adding a term to their written agreement, or of altering its legal ordinary construction.'⁶

The statement from *Holmes Limited* was confirmed in the case of *Ringford Habwanda v Zambian Breweries Plc*⁷ which held that where a contract is not intended to fully embody all the terms of the agreement, then other evidence or documents can be used. The case also provided that where parties intend a contract to be partly written and partly oral, then this shall act as an exception to the parol evidence rule.

⁶ Ibid

⁷ (2012) ZR (3) 75.

Clearly in some circumstances, the *Phinate Chona* case illustrates that the court is prepared to accept that oral representations, because of their significance, are intended to be as much a part of the agreement as those included in the written document.

Another exception to the parol evidence rule is where the extrinsic evidence is necessary to give effect to the true nature of the agreement. The Court of Appeal judgment in *Phinate Chona* proves that extrinsic evidence may also be used to interpret or explain the terms of the contract. It is for these reasons the courts are empowered to use background information where necessary to ascertain the intention of the parties. There is a recognition that contracts are not made in a vacuum and thus information such as the commercial purpose, background and context can be used to interpret the contract.

The Court of Appeal confirmed a principle of the rules of contractual interpretation that when interpreting the meaning which contracts convey, a court is permitted to deduce what a reasonable person having all the background knowledge which would reasonably have been available to the parties in the situation in which they were at the time of the contract, would have understood the contract to convey. This clearly illustrates that the interpretation of a contract is not purely literal, but the courts can delve into the purpose of the agreement.

It is worth pointing out that the Court of Appeal confirmed that what can be regarded as background information for the purposes of determining the true meaning and intention of the parties is wide, and the courts have leeway to admit what should have been reasonably available to the parties. In the *Investors Compensation Scheme Ltd*⁸ case, the court declared that the extent of the surrounding circumstances includes anything which would have affected the way in which the language of the contract would have been understood by a reasonable man.

The Court of Appeal referred to the case of *Bank of Credit and Commerce International v. Ali*⁹ which held that there is no conceptual limit to what can be regarded as background. In other words, courts are not bound to merely interpret terms on a purely linguistic basis but ought to place express terms in their proper context and not read terms in isolation.

⁸ *Investors Compensation Scheme Ltd v West Bromwich Building Society* [1997] UKHL 29

⁹ *Bank of Credit and Commerce International v. Ali* [2001] UKHL 8

This notwithstanding, the court's discretion in looking at background information and circumstances is not unfettered or unlimited. It is crucial to note that only what a reasonable man would have regarded as relevant will be admitted as background. Therefore, although there is no conceptual limit, the court is limited to only consider what is relevant by a reasonable man seeking to deducing the intention of the parties.

It is important to note that the use of background information was explored in the earlier case of *Friday Mwamba v Sylvester Ntenge and Others*,¹⁰ where the Supreme Court stated that:

...the meaning of the document or a part of it is to be sought in the documents itself: one must consider the meaning of the words used, not what one may guess to be the intention of the parties. However, no contract is made in a vacuum. In construing a document, the court may resolve the ambiguity by looking at its commercial purpose and the factual background against which it is made.

Nevertheless, the *Phinate Chona* went further by providing the circumstances in which background information and surrounding circumstances can be relied upon, as outlined above. There is no doubt that loyalty to the text of the commercial contract, instrument or document is of paramount importance. This notwithstanding, a contract needs to be read in its contextual setting and the necessary background information. A reasonable interpretation of *Phinate Chona* is that such an approach to the construction of contract is more likely to give effect to the true intention of the parties.

It should be noted that the law still excludes from the admissible background the previous negotiation of the parties and their declarations of subjective intent. Therefore, the court is not entitled to look at what the parties said or did whilst the matter was in negotiation for the purposes of drawing inferences about the contract means. The previous negotiations between the parties are only relevant in relation to the evidence of the facts about which the parties were negotiating as this forms part of the background, and for the purposes of supporting an action for rectification.

In some cases, once the contract has been interpreted, one of the parties may argue that the written contract or document, as interpreted, fails to reflect accurately the agreement which the parties had actually reached. In such a case, the court may be called upon to rectify the

¹⁰ SCZ Appeal 174 of 2010.

document so that it accurately reflects the agreement which the parties did in fact reach. This case is significant because it illustrates that where it can be shown that a written contract inaccurately represents the actual agreement reached by the two parties then equity will allow rectification of the written document, and the court may look at background information. The background information as an exception to the parol evidence rule can be introduced to show what the real agreement was. The inaccuracies are removed and replaced if necessary, with the substance of the real agreement.

In summary, this case clearly illustrates that the Court of Appeal is taking steps into developing the manner in which contracts are interpreted in this jurisdiction. In short, this case illustrates that the interpretation of a contract involves ascertaining the meaning that the words would convey to a reasonable person having all the background knowledge which would reasonably have been available to the parties in which the situation in which they were at the time of the contract. As such, a literal approach is untenable and would necessarily involve looking at the background information to determine the parties intention.