



Interpretation of Contracts - The Dawn of a New Era?

On 17th January 2011 a new amendment to the Israeli Contracts Law was enacted which is aimed at reducing the traditionally almost unlimited discretion of the Israeli Courts in interpreting contracts – both in general and regarding insurance policies in particular.

According to the Israeli Contracts Law – General Part – 1973 (the Law), a contract will be interpreted in accordance with the parties' intent as it appears from the contract itself and in cases where the parties' intent cannot be inferred from the contract, then in accordance with the surrounding circumstances (Section 25).

Supreme Court precedents have ruled in the past that interpretation of a contract cannot be based solely on its wording. In order to determine the true intent of the parties, the surrounding circumstances are integrated in the construction process.

The leading precedent in Israel on this issue is the Supreme Court ruling in the case of Appropim (C.A. 4628/93 The State of Israel vs. Appropim, PDI 49(2), 265). In the case of Appropim, the Supreme Court ruled that the intention of the parties to the contract will be examined in light of the circumstances external to the contract, **even in cases where the wording of the contract is not ambiguous:**

In its ruling, the court emphasized that the language can only be seen as unambiguous after identifying the intent of the parties and the language of the contract must be construed on the basis of this intent. The language of a contract is clear only where it implements the parties' intent. Therefore, simple meaning of the contract wording does not supersede the parties' intent and only such meaning that actually reflects their intent can be accepted as the correct interpretation of the contract.

The Appropim ruling was vastly criticized. It was argued that Appropim prejudices the principles of commercial certainty whereby the party to the contract was no longer able to rely

on the clear language of the contract. The case of Appropim empowered the interpreter to give the contract a meaning beyond the contract's text.

The case of Appropim affected the rules of interpretation also when an insurance contract was involved.

In view of the uncertainty which the Appropim case has created, the legislator has decided to amend section 25 to the Law (interpretation of a contract).

On 17th January 2011 the suggested amendment to Section 25 was enacted and the Law now provides that a contract will be interpreted based on the parties' intent as such appears from the contract and the surrounding circumstances of the contract, however, in the event that the parties' intent can be inferred from the contract itself, the contract will be interpreted in accordance with its language.

In addition, in the framework of the amendment to the Law the Contra Proferentem rule was also included, namely, section 25 the Law now also provides that an ambiguous term will be construed against the party that imposed its inclusion in the contract – or, more accurately, against the interests of the party who imposed it.

Although the legislator's express intent in amending the Law was to revoke the Appropim precedent, doubts have been voiced as to whether the amendment as enacted will indeed succeed in doing so.

These skeptics contend that the amendment corresponds with the Appropim precedent and actually affords the Israeli court with broader discretion in determining when the language of the contract is clear and when interpretation is required.

The amendment is still young and only time will tell how and to what extent it will change contract interpretation in Israeli courtrooms.

