

UNIT 2

CONTRACT LAWS

Contract Laws: Definition – types of contracts – essentials of valid contracts – offer, acceptance, consideration, the capacity of parties, free consent, the legality of object and consideration, various modes of discharge of a contract, performance of contracts, remedies for breach of contract.

INTRODUCTION

According to Oxford English Dictionary the word law means, “Rule made by authority for the proper regulation of a community or society or for correct conduct in life”

Indian Contract Act of 1872 came into effect from 1st September, 1872. It extends to the whole of India except the state of Jammu and Kashmir.

The law of contract is the branch of law which determines the circumstances in which promise made by the parties to a contract shall be legally binding on them. All of us enter into a number of contracts everyday knowingly or unknowingly. Each contract creates some right and duties upon the contracting parties. Indian Contract Act deals with the enforcement of these rights and duties upon the parties.

DEFINITION, MEANING AND NATURE OF CONTRACT

The term Contract has been defined under **Section 2(h) of Indian Contract Act, 1872** as, “an agreement ..enforceable by law is a contract”

A Contract therefore, is an agreement the object of which is to create a legal obligation, i.e. a duty enforceable by law.

Two main elements –

1. **Agreement-** As per Sec 2 (e) “ Every promise and every set of promises, forming the consideration for each other, is an agreement”
2. **Legal Obligation-** An agreement to become a contract must give rise to a legal obligation that is duty enforceable by law.

ESSENTIALS OF VALID CONTRACT

1-AGREEMENT: To form a contract there must be an agreement between the parties. Agreement is created by offer and acceptance. It is result of mutual exchange of promises between the parties.

Eg: an agreement between the tenant and the owner.

2-CREATION OF LEGAL RELATIONSHIP: Agreement made between parties must create legal relationship. Legal relationship consists of rights and obligations which can be claimed by the parties in the court of law.

3-LAWFUL CONSIDERATION: Agreement is a mutual exchange of promises between parties. Each party making a promise gets something in return of his promise. It constitutes a consideration for his promise .

4-CONTACTUAL CAPACITY: Parties making an agreement must have contractual capacity. Lack of contractual capacity would invalidate contract. Contractual capacity of the party means he or she must be legally competent for making a contact. The person to have contractual capacity must satisfy the following conditions:

- a) He must not be a minor.
- b) He must be of a sound mind and not lunatic, idiot or drunkard.
- c) He must not have been declared disqualified by law from contracting such as insolvent, convict and alien enemy etc.

5-FREE CONSENT OF THE PARTIES: State of mind of parties is involved in making offer and giving acceptance for it. As soon as offer is accepted it becomes a binding promise having a legal consequences. Two or more persons are set to have consent if they agree upon same thing in the same sense. And their consent is said to be free if it has not been induced by anyone one of the following factors;

- a) Coercion b)undue influence c)misrepresentation d)fraud e)mistake

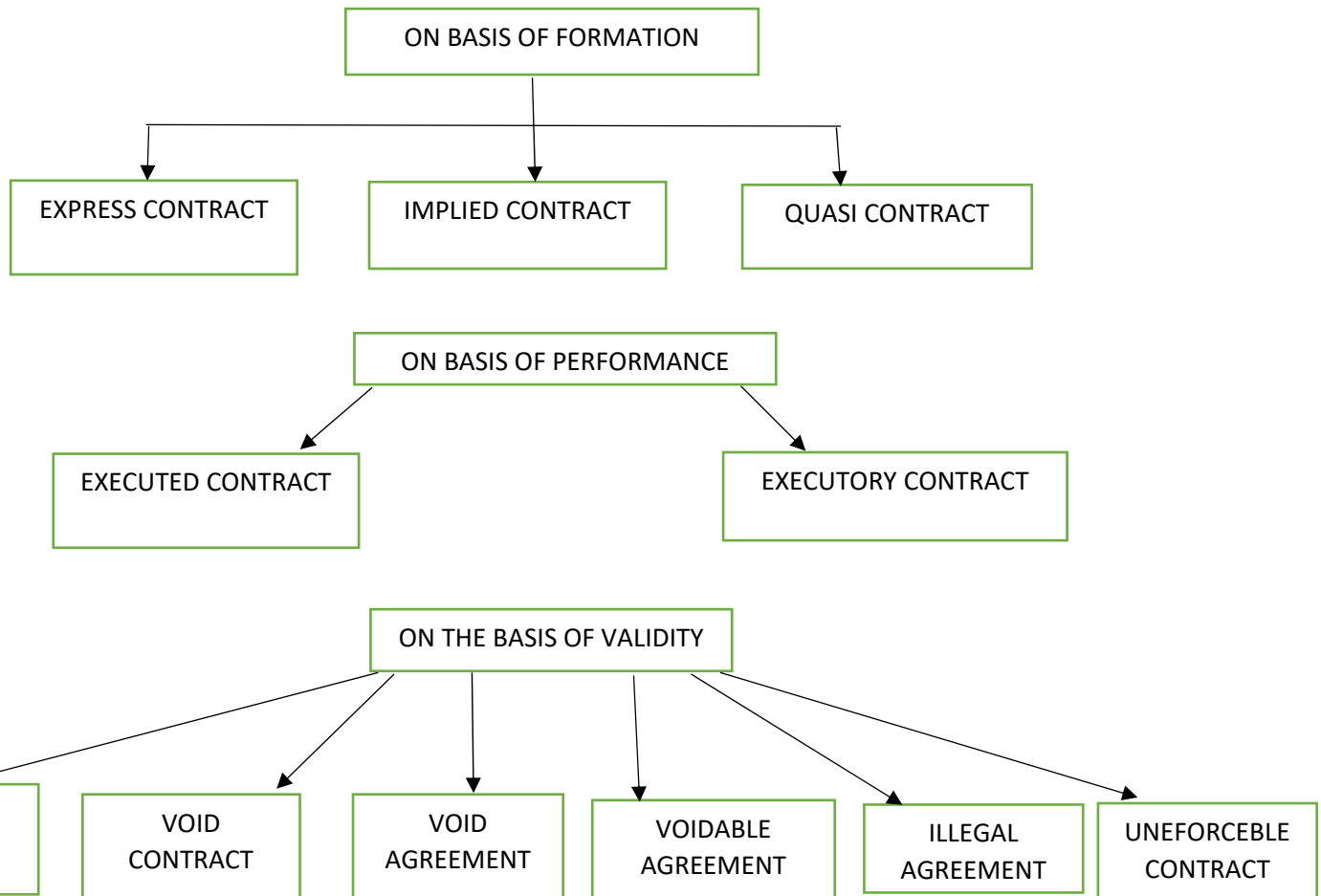
6-LAWFUL OBJECT OF AGREEMENT: Agreement is made for some object or purpose such object is formed on the basis of promises made by the parties. These promises are made either for doing or not doing anything.

7-AGREEMENT, NOT DECLARED EXPRESSLY VOID: There are certain agreements which have been expressly declared void by the law. Thus an agreement made by parties should not fall in that category. If it is so it would also meet same fate and cannot be enforced in the court of law.

8-CERTAINTY IN THE MEENING OF AGREEMENT: Agreement made by the parties must be certain or capable of being made certain in its meaning. It is because agreement would result in creating rights and obligations between the parties.

9-OTHER LEGAL FORMALITIES: agreement to be enforced, needs to satisfy other conditions of being in writing, registered and duly stamped. Generally Indian contract act does not make any discrimination between written and oral agreement. Oral agreements are as good as written agreement.

TYPES OF CONTRACTS:



ON BASIS OF FORMATION:

1.) EXPRESS CONTRACTS: These contracts result from express agreements. Express agreements are formed by making offer and giving acceptance in the words spoken or in writing. Acc to sec 9 of Indian Contract Act "in so far as the proposal and acceptance of any promise is made in words, the promise is said to be express. An express promise leads to the formation of express contract".

2.) IMPLIED CONTRACT: Implied contracts are formed on the basis of implied promises on the part of parties. Implied promises are those which are not made by the parties in writing or by the word of mouth. Rather these promises are inferred from the conduct of the parties or from the circumstances. In an implied contract, one of the party conduct himself or does some act which is being accepted by the other party either by his conduct or course of his dealing or circumstance. Thus in an implied contract, making of an offer and giving acceptance to it is manifested by the Act on the part of party.

3.) QUASI-CONTRACT: Quasi contracts are based on the principle of justice and equity. In spite of not having any contract between parties, the rights and obligations are created. These are resembling to rights and obligations as created by a formal contract. In such contracts, obligations between parties are created by operation of law rather than offer and acceptance.

ON BASIS OF PERFORMANCE:

1.) EXECUTED CONTRACT: Contract consists of legal obligations. On the complete discharge of these obligations, the contract is said to have been executed. In other words, both the parties have fulfilled their respective promises, which they have made in contract.

2.) EXECUTORY CONTRACT: This contract is one that has not been yet performed. In other words, parties having made promises for doing or not doing anything have not fulfilled their respective promises.

ON BASIS OF VALIDITY:

1.) VALID CONTRACT: Contract is said to be valid if it satisfies all conditions required for its enforceability. In other words, valid contract is enforceable in the court of law.

2.) VOID CONTRACT: A contract ceases to be enforceable by law becomes void. Literally the word void means not binding in law. It implies a useless contract which has no legal effect at all.

3.) VOID AGREEMENT: Agreement which is not enforceable by law is void agreement. In other words, if an agreement lacks any one of essentials of a valid contract except free consent it becomes void. Void agreements do not have any legal consequence and it is null and void in the eyes of law.

4.) VOIDABLE CONTRACT: According to Sec 2(i) "An agreement which is enforceable by law at the option of one or more parties, but not at the option of other or others is a voidable contract.

5.) ILLEGAL CONTRACT: Every contract is formed on the basis of promise made by the parties in that contract. The contract is said to be illegal if its object is illegal.

6.) UNENFORCEABLE CONTRACT: Sometimes, a contract maybe good in the eyes of law. But due to some technical reason it may not be allowed to be enforced in the court. Technical reasons such as contract is

not made in writing or is not registered or has no adequate stamp duty on it. Due to non-fulfillment of prescribed legal formalities these cannot be claimed in the court, once these reasons are rectified contracts may be allowed to be reinforced.

OFFER, ACCEPTANCE AND CONSIDERATION

1.) OFFER:

Offer is one of the essential elements of a contract. According to **Sec 2(a) of Indian Contract Act 1872**, defines the term Offer or Proposal "When one person signifies to another his willingness to do or to abstain, from doing anything with a view to obtaining, the assent of that other to such act or abstinence, he is said to make a proposal"

CLASSIFICATION OF OFFER:

- 1.) SPECIFIC OFFER:** Sometimes an offer is made to a particular person, part or org. , such offer is known as a specific offer. This specific offer can be accepted only by that particular person or org.
- 2.) GENERAL OFFER:** It is an offer which is made to a group of people or public at large. Such offer can be accepted by any member of that group or public.
- 3.) CROSS OFFER:** Two parties exchange identical offers with each other. They are ignorant about each other's offers.
- 4.) COUNTER OFFER:** Incomplete and conditional acceptance of an offer is known as a counter offer. In other words, the acceptor, instead of accepting the offer as such along with all its terms and conditions deviates from it. Such acceptance becomes a counter offer.

ESSENTIALS OF VALID OFFER:

- 1.) Offer must create a legal relationship and consequence:** The whole concept of contract is based on legal relationships or obligations of legal consequences .Thus the formation of contract with starts with an offer, its acceptance followed by the legal relationships and its consequences means the party making an offer must have clear intention to establish the legal relationship with other party.
- 2.) Offer may be express or implied:** The offer may be made either by the word of mouth or in writing. Such an offer is known as an express offer. On the other hand if the offer is inferred, or indirectly understood either from the conduct of parties or from the circumstances, such offer is known as implied offer.
- 3.) Offer may be specific or general:** The offer being made to a particular individuals or orgs. Is known as specific offer. On the other, if an offer has been made to a group of people or public at large is known as general offer.
- 4.) Offer must be communicated:** An offer is made with a view to create, legal relationships so it must be communicated to the person to whom it is made. Without communications the offer is incomplete and cannot be accepted.

5.) Offer must be distinguished from a mere expression of intention or invitation: Sometimes one party merely shows his intention for making an offer or invites other party for making it. Such intention or invitation for making an offer will not be considered as a valid offer.

6.) Offer maybe conditional: While making an offer the offeror may impose conditions for the acceptor, such conditional offer is valid subject to the following conditions:

a.) Offeror cannot impose any such condition the non-fulfillment of which would lead to acceptance of that offer.

b.) The terms and conditions imposed by the offeror must be mentioned in the offer in such a way that a person of a reasonable prudence may find indication for those conditions and those conditions must be reasonable eyesight.

REVOCAION OF OFFER:

Revocation of offer means withdrawal, cancellation or lapse of offer.

According to **Sec 6** of this act, Offer can be revoked under the following circumstances:

a) By notice, b) By lapse of time, c) Death or insanity of offeror

D) Non-fulfillment of prerequisite conditions, e) by counter offer, f) by compliance of prescribed mode or manner

2.) ACCEPCTANCE

According to **Sec 2(b) of Indian contract act 1872**, defines the term acceptance “as a proposal or offer is said to have been accepted when the person to whom the proposal is made signifies his assent to the proposal”.

ESSENTIALS OF VALID ACCEPTANCE:

1.) Acceptance must be absolute and unconditional: Offer may be made for a specific quantity, volume and price. It may also contain terms and conditions. It is necessary for the acceptor that he must give his acceptance for the entire quantity and volume offered.

2.) Acceptance must be given in a prescribed mode or manner: While making an offer the offeror may prescribe a particular mode or manner of acceptance and the acceptor must abide by it. If the acceptor does not follow that particular mode for sending his acceptance, the offeror that further insist the acceptor to abide by it. But if it is still not followed the offeror can reject the acceptance. On the other if no mode is prescribed, by the offeror then the acceptor can follow the usual mode of acceptance.

3.) Time of acceptance: To make it valid acceptance, it must be given within stipulated period of time if any. When no time is specified, acceptance must be given within reasonable period of time.

4.) Acceptance must be communicated: As the offer needs to be communicated, so does the acceptance. Acceptance to be legally effective must be communicated and brought to the knowledge of the offeror. Even if the acceptor has accepted the offer but if it is not communicated properly it would not result into an agreement.

5.) Acceptance may be expressed or implied: The acceptor may give his assent for the proposed act by the word of mouth or in writing. Such acceptance is known as express acceptance. If the acceptance is directly understood either from conduct of the party or from circumstance, it is known as implied acceptance.

6.) Acceptance must be made before offer is revoked: Acceptance implies mental readiness of the person for proposed act or abstinence. Therefore, it must be given before the offer lapses or is withdrawn or cancelled. Once the offer is dead due to any reason if it is dead for ever, and to revive it, such offer is to be made afresh.

7.) Acceptance is not implied from silence if the party: Acceptance of offer is not implied from silence. The offeror cannot impose condition on offered that his silence will amount to acceptance. Silence on the part of offered regarding the offer in no case may amount to acceptance.

REVOCAION OF ACCEPTANCE:

- 1) Failure of acceptor
- 2) Death or insanity of acceptor
- 3) No reasonable time and manner
- 4) By rejection
- 5) By supervising impossibility

CONSIDERATION

According to Sec 2(d) of this act, " When at the desire of promisor, promisee or other person has done or abstained from doing, does or abstains for doing or promises to do or to abstain from doing something, such act, abstinence or promise is called consideration for the promise"

ESSENTIALS OF VALID CONSIDERATION:

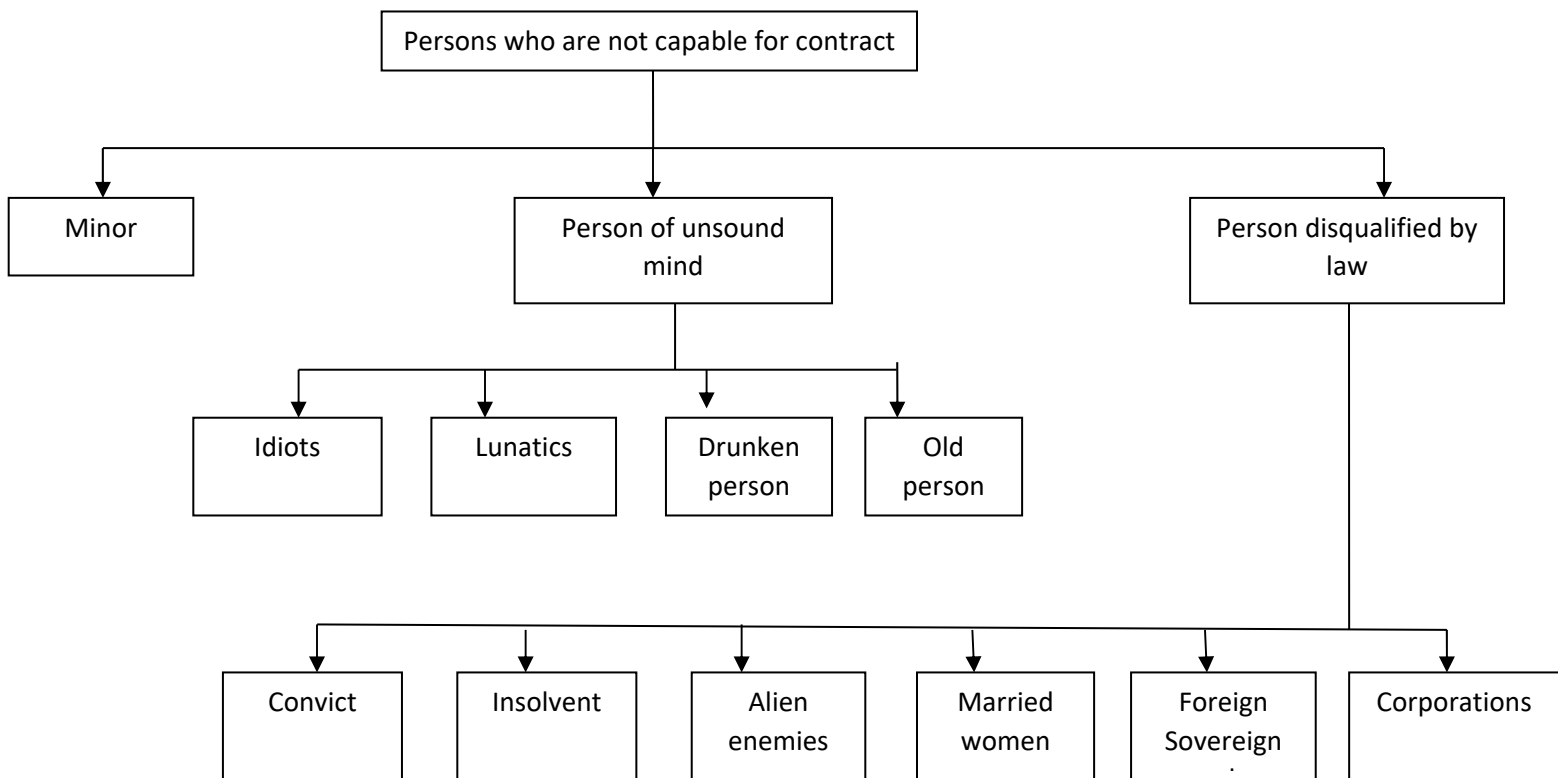
- 1.) **Form of consideration:** The consideration will always be in the form of some act or abstinence or a promise for doing or not doing something.
- 2.) **Consideration must be moved or given at the desire of promisor:** In agreement there are two parties i.e. promisor and promisee. The consideration is generally given by the promisee to promisor. According to this rule any act or promise will be valid consideration if such act has been done or promise is made at the desire or request of the promisor.
- 3.) **Consideration may be past, present or future:** Promisor makes a promise and consideration is given to him for his promise. If these two acts of making promise and getting consideration are done simultaneously, the consideration is known as present consideration. If the consideration has been given to the promisor before he makes a promise, it is known as past consideration. Consideration may be in the form of promise to be performed in future, such consideration is known as future consideration.
- 4.) **Consideration may be moved or given by promisee or any other person:** Generally in every agreement consideration is given by promisee to the promisor. But it is not necessary. Any other person on behalf of promisee may give consideration. Such consideration will also be valid.

5.) **Consideration need not be adequate:** According to Indian Contract Act it is not necessary that the value of promise should be equal to the value of consideration. Even if the value of consideration is less than the value of promise, the contract is valid.

6.) **Consideration must be real and not be illusory:** Consideration given must be real and must have some value in the eyes of law. It must not be illusory, factious, fraudulent, uncertain and illegal.

7.) **Consideration must be lawful:** Agreement to be enforced in the court must be made for lawful consideration. Any act which is illegal, immoral and against public policy will not constitute valid consideration for the contract.

CAPACITY OF PARTIES:



Contractual capacity is an essential ingredient of a valid contract.

According to Sec 10 of this act, parties making an agreement must have contractual capacity. Contractual capacity means they must be legally competent for making a contract.

To have a Contractual capacity, one must fulfill the following conditions:

Elements:

- 1.) Age
- 2.) Soundness of mind
- 3.) Legal Disqualification

1.) Minor:

A minor is a person, male or female, who has not completed the age of 18 years. In case a guardian has been appointed to the minor or where the minor is under the guardianship of the court of wards, the person continues to be a minor until he completes his age of 21 years.

According to Indian Contract Act, only a major person is competent to contract. Thus, contract with or by a minor is altogether void. The word "Void" when used in relation to a minor, it should be understood as "void against the **minor**".

2.) Soundness of mind:

According to Sec 12 of this act, "A person is said to be a sound mind for the purpose of making contract, if at the time, when he makes it he is capable of understanding it and forming a rational judgement as to its effects upon his interests".

- **Lunatics:** A lunatic is a person who is mentally affected due to some mental strain or other personal experience. He suffers from intermittent intervals of sanity and insanity. He can enter into a contract only during the period when he is of sound mind.
- **Idiot:** An idiot is a person who is permanently of unsound mind. He does not exhibit minor understanding of even minor objects or things. An idiot cannot enter into a valid contract.
- **Drunken Person:** A person who takes any intoxicants like alcohol or drugs etc. he is temporarily incompetent of entering into a contract. Thus, so long as one remains under the influence of intoxicants or drugs, he has no contractual capacity. Thus agreement made by such person are void.

3.) Legal Disqualification:

- **Alien enemy:** A person who lives in and is a citizen of a foreign country is known as an alien. He may be a friend or an enemy to the citizen of our country. Alien friend can make an agreement with Indian citizen. But if war is declared between the two countries, the citizens of those countries become alien enemies to each other. And agreements made with alien enemies are void.
- **Foreign sovereign:** Ambassadors, high commissioners or foreign diplomatic staff do represent their country. Therefore they have been provided some immunities. They can make an agreement with Indian citizens.

and can enforce those agreements against Indian citizens in India. But Indian citizens to sue upon them for the rights arising out of an agreement has to seek prior permission from central govt.

- **Corporations:** A corporation is an artificial person created by law, eg: A company registered under Companies act. A corporation exists only in contemplation of law and has no physical shape or form. The Indian contract act does not speak about the capacity of a corporation to enter into a contract. But if properly incorporated, it has a right to enter into a contract. It can sue and can be sued in its own name. There are some contracts into which a corporation cannot enter without its seal.
- **Insolvent:** Generally, when the assets of person fall short of liabilities and liabilities cannot be paid fully, such state of affair is called insolvency. The person is declared as an insolvent by the court. He has to handover his property to the official receiver. He cannot enter into contracts relating to his property. It is only when the court issues order of discharge in favour of that person he becomes competent.
- **Married women:** they have no right to make agreements regarding joint property of husband and wife, unless she is authorised to do so by husband. She is free to make any agreement to deal with their personal property such as bank balance in her name and jewellery etc on the failure of husband, to fulfill the basic necessities of her life, she becomes an agent of her husband by necessity. For the supply of such basic necessities she can make agreements binding on the property of her husband.
- **Convict:** A convict is incapable of entering into a contract during the continuance of sentence of imprisonment. However, he can enter into a valid contract after the expiration of his term of imprisonment. A convict can also, enter into, or sue on, a contract when on parole, bail or when he has been pardoned by the court.

FREE CONSENT

Sec 13 Indian Contract act, "two or more persons are said to consent when they agree upon the same thing in the same sense."

Sec 14 of this act states that, consent is said to be free when it is not caused by :

1. Coercion: Application of physical force
2. Undue influence: Use of mental pressure
3. Misrepresentation: Innocent false representation
4. Fraud: Cheating or deceiving
5. Mistake: Wrong impression about anything

ELEMENT OF FREE CONSENT:

1. **COERCION:** it implies use of some kind of physical force by doing some act forbidden by law to seek consent of other party.
2. **UNDUE INFLUENCE:** It implies unfair use of dominating position to cause the consent of other party for a contract. In undue influence some kind of mental and moral pressure is brought upon a party to cause his consent.
3. **MISREPRESENTATION:** While making a contract, one of the party may make any statement regarding the subject matter of a contract. Such statement, if turns to be untrue amounts to misrepresentation. It is a misstatement of material facts.
4. **FRAUD:** An intentional misrepresentation of the facts amounts to fraud. Fraud is always committed with a view to deceive to cheat another person. Thus, when one person does anything or makes false statement knowing to induce other for causing this consent, it is known as fraud.
5. **MISTAKE:** It may be defined as a wrong impression or erroneous opinion in the mind of a person about any subject matter, event or it may consent something.

LEGALITY OF OBJECT

Every contract is made for object or purpose . The object of a contract is formed on the basis of promises made by the parties. The contract to be legally valid , must contain lawful object . When the contract is made for doing something illegal defeating provisions of the law such contract is not valid in the eyes of law.

According to sec 23 of this act the unlawful acts are :

1. Forbidden by law
2. Prohibited by special legislation
3. It would defeat the provisions of any law
4. It is fraudulent
5. Involves enquiry to person/property if another
6. Courts to public policy
7. Opposed to public policy
8. Trade with alien enemies
9. Interference with course of justice
10. For superseding prosecution
11. For sale of public titles/offices and honors
12. Marriage brokerage

DISCHARGE/TERMINATION OF CONTRACT

Discharge of a contract implies termination of the contractual relationship between the parties. On the termination of the such relationship the parties are released from their obligations in the contract. And in this way contract comes to an end.

MODES OF DISCHARGE IN CONTRACT:

1. By performance
2. By mutual agreement
3. By supervening impossibility
4. By operation of law
5. By lapse of time
6. By material alteration
7. By breach of contract

REMEDIES OF BREACH OF CONTRACT

BREACH OF CONTRACT: A formation of contract results in creating contractual obligations between the parties. These contractual agreements are to be fulfilled by the parties on the due date as per terms and conditions of a contract . When the party does not fulfill his obligation or refuses to fulfill it or disables himself from fulfilling him it is known as breach of contract.

Breach of contract is of 2 types:

- 1) **Actual breach:** This contract takes place when the promiser fails to perform his obligation or refuses to do so on the due date of performance.
- 2) **Anticipatory breach:** This contract the promiser either refuses to perform or makes himself unable to perform a promise before the due date of performance . Anticipatory breach of contract takes place before the date of actual performance.

REMEDIES :

- **RESCISSION:** When a party makes breach of contract by not fulfilling his obligation, the aggrieved party has a right to rescind such contract. To exercise this right, the aggrieved has to file a suit for rescission of a contract. On granting rescission, the aggrieved party gets released from his obligation in that contract. He is no more liable to perform his promise.
- **SUIT OF DAMAGES:** On making a breach of contract by a party, the aggrieved party may suffer monetary loss. In the event of breach he may be put in a disadvantageous position or in a position of discomfort. In such case, the aggrieved party has a right to claim for compensation.
- **SUIT FOR SPECIFIC PERFORMANCE:** When, breach of contract takes place and aggrieved party suffers a loss. These losses may be of such a nature that damage granted for these by the court may be inadequate. It is because such losses cannot be measured in terms of money. In such cases, the aggrieved party is entitled to claim for order of specific performance.
- **SUIT FOR INJUNCTION:** In a contract if the party has made a promise for not doing something, and that party takes a breach of contract by doing that thing. To prevent such party from doing that act an order of injunction may be claimed by an aggrieved party. It is an order passed by court of law, directing upon the party and refraining him from performing what he has promised not to perform. An injunction is a preventive relief, which is provided to an aggrieved party where damages would not be an adequate relief, it is negative form of order of specific performance.
- **SUIT UPON QUANTUM MERUIT:** In a contract maybe in the process of performing his promise before he completes it, the promise makes a breach of contract. Quantum Meruit is a Latin dictum, which means "as much as earned or merited". That means under Quantum Meruit aggrieved party can also claim for the reasonable cost of work done by him in the contract.