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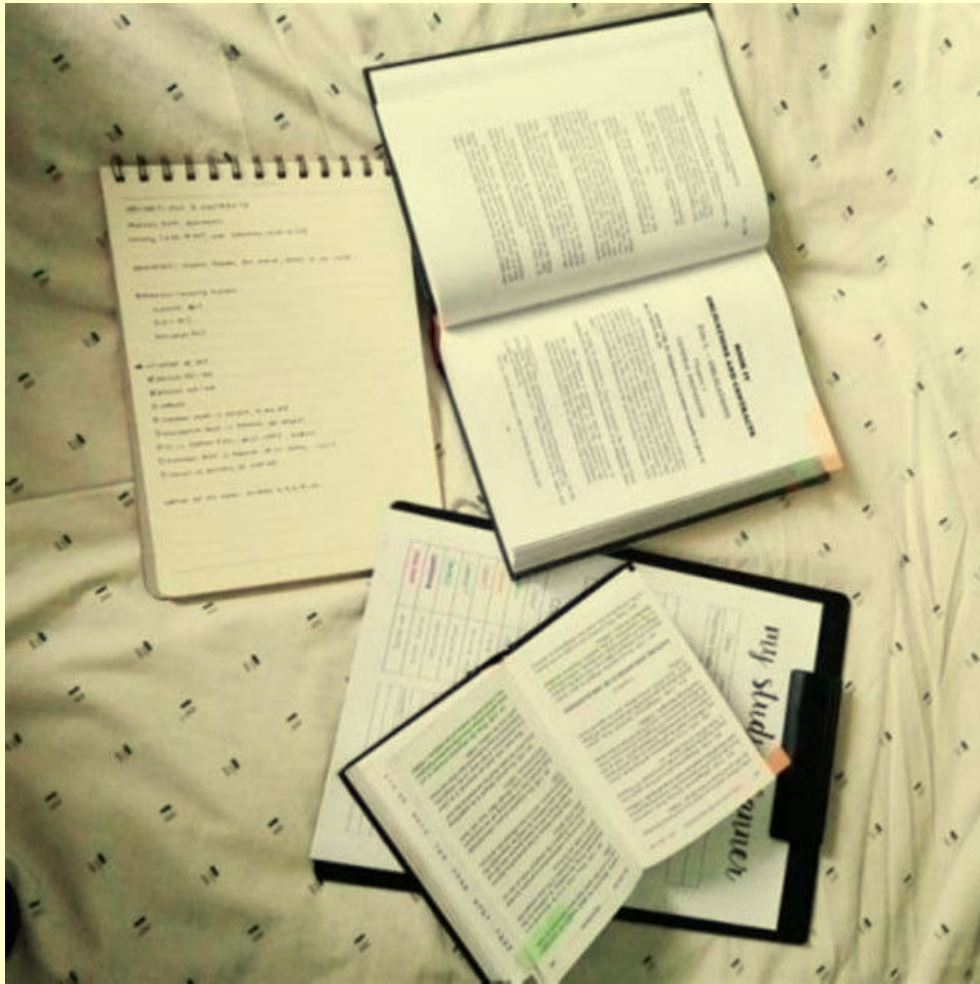
- ⇒ Injurious to person and property
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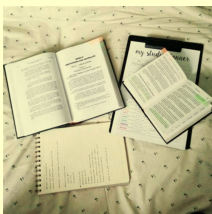
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Law of Contract is the most important and basic part of Mercantile law. It is the foundation for many other laws falling in the category of mercantile laws. It is not only the mercantile or trader but every person who lives in the organised society, consciously or unconsciously enters into contract from sunrise to sunset. When a person hires a taxi, or orders something in a hotel or buys something from a shop, purchases a newspaper, ride a bus etc. he actually enters into and performs contract though he may be unaware of this fact. Such contracts at times create legal relations giving rise to certain rights and obligations.

The law relating to contracts in India is contained in **Indian Contract Act, 1872**. The Act came into force with effect from **September 1, 1872**. It is applicable to the whole of India except the State of Jammu & Kashmir (*As per Section 1*).

SCHEME OF THE ACT: The scheme can be divided into two main groups. The Act as enacted originally had 266 Sections divided into following groups:

PROVISIONS	SECTIONS
General Principles of Law of Contract	1 to 75
Contract relating to contract of Sale of Goods	76 to 124*
Special kinds of Contracts (for example: Indemnity, Guarantee, Bailment, Pledge and Agency)	125 to 238
Contracts relating to Partnership	239 to 266**

These sections were repealed from the Contract Act, 1872 and two new Acts were enacted for the same:

- * SALE OF GOOD ACT, 1930
- ** PARTNERSHIP ACT, 1932

PRESENT FORM OF INDIAN CONTRACT ACT

Law of Contract basically relates to the essentials of a valid contract, the rules for performance and discharge of a contract and the remedies available to the aggrieved party in cases of the breach of the contract.

The Indian Contract Act, in its present form may be divided into two parts-

- ⇒ The First part of the enactment i.e. Section 1 to 75 deals with the **general principles of the law of contract** which apply to all types of contracts irrespective of their nature.
- ⇒ The second part (i.e. Section 124 to 238) deals with special types of contracts namely indemnity and guarantee, bailment and pledge, agency etc.

Enforcement of Act: The Indian Contract Act was passed in 1872 and came into force from 1st September, 1872. Prior to this English law of contract was followed in India. Law of contract creates jus in personam and not jus in rem. It extends to whole of India except state of Jammu and Kashmir.

OBJECTIVE OF THE ACT: The objective of the Contract Act, 1872 is to ensure that the rights and obligations arising out of a contract are honoured and that legal remedies are made available to an aggrieved party against the party failing to honour his part of agreement. Act lays down the basic

principles of the formation, performance and enforceability of contracts. Although, law of contract is not the whole law of agreements or that of obligations.

DEFINITIONS OF CONTRACT

POLLOCK

“Every agreement and promise enforceable at law is a contract.”

HALSBURY

“A contract is an agreement between two or more persons which is intended to be enforceable at law and is contracted by the acceptance by one party of an offer made to him by the other party to do or abstain from doing some act.”

SALMOND

“A contract is an agreement creating and defining obligation between the parties”

SIR WILLIAM ANSON

“A legally binding agreement made between two or more persons by which rights are acquired by one or more to acts or forbearances on the other or others.”

In essence, an agreement may be or may not be enforceable by law, and so all agreements are not contracts. Only those agreements are contracts, which are enforceable by law.

AGREEMENT + ENFORCEABILITY BY LAW = CONTRACT

Hence, it can be concluded that “All contracts are agreements, but all agreements are not contracts.”

DISTINCTION BETWEEN CONTRACT & AGREEMENT

BASIS OF DISTINCTION	CONTRACT	AGREEMENT
Section	Sec. 2(h)	Sec. 2(e)
Definition	A contract is an agreement enforceable by law.	Every promise or every set of promises forming consideration for each other is an agreement.
Enforceability	Every contract is enforceable	Every promise is not enforceable.
Inter-relationship	All contracts are necessarily agreements.	Every agreement need not necessarily be a contract.
Scope	The scope of a contract is limited, as it includes only commercial agreements.	Its scope is relatively wider, as it includes both social agreement and commercial agreements.

Validity and legal obligation	Only legal agreements are called contracts. Every contract contains a legal obligation.	An agreement may be both legal and illegal. It is not necessary for every agreement to have legal obligation.
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VARIOUS DEFINITIONS UNDER INDIAN CONTRACT ACT, 1872

- **Proposal (i.e. offer) [Section 2(a)]:** 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 person to such act or abstinence, he is said to make a proposal.
- **Acceptance [Section 2(b)]:** When the person to whom the proposal is made, signifies his assent there to, the proposal is said to be accepted.
- **Promise [Section 2(b)]:** A Proposal when accepted becomes a promise. In simple words, when an offer is accepted it becomes promise.
- **Promisor and promisee [Section 2(c)]:** When the proposal is accepted, the person making the proposal is called as promisor and the person accepting the proposal is called as promisee.
- **Consideration [Section 2(d)]:** When at the desire of the promisor, the promisee or any other person has done or abstained from doing something or does or abstains from doing something or promises to do or abstain from doing something, such act or abstinence or promise is called a consideration for the promise. Consideration is actually the price paid by the one party for the promise of the other. Technically it is termed as "**QUID PRO QUO**" i.e. something in return.
- **Agreement [Section 2(e)]:** Every promise and set of promises forming the consideration for each other.
- **Contract [Section 2(h)]:** An agreement enforceable by law is a contract.
- **Void agreement [Section 2(g)]:** An agreement not enforceable by law is void.
- **Voidable contract [Section 2(i)]:** An agreement is a voidable contract if it is enforceable by law at the option of one or more of the parties there to (i.e. the aggrieved party), and it is not enforceable by law at the option of the other or others.
- **Void contract [Section 2(j)]:** A contract which ceases to be enforceable by law becomes void when it ceases to be enforceable.

ESSENTIAL ELEMENTS OF A VALID CONTRACT

There are two basic essential elements of a contract-

⇒ An agreement

⇒ **Its enforceability by law**

These two components together constitute the basis for a contract and are explained as follows:

AGREEMENT Agreement has been defined in **Section 2(e)** as "**every promise or every set of promises forming the consideration for each other**" Further, promise is defined in **Section 2 (b)** as, "**a proposal when accepted become a promise.**"

In other words, an agreement consists of a proposal or an offer by one party and its acceptance by the other party. It also implies that the parties have a common intention about the subject-matter of their agreement. Two parties must be thinking of the same thing in the same sense. Thus agreement is the outcome of two consenting minds i.e. '**consensus ad idem**'.

WHAT IS ENFORCEABILITY OF CONTRACT??

Agreements are two types-

- Unenforceable agreement
- Enforceable agreement

All agreements to become a contract must give rise to legal obligations. In other words, the parties to an agreement must be bound to perform their promises and in case of default by either of them, must intend to sue and be sued. On the other hand, all those agreements are said to be unenforceable in which an aggrieved party cannot go to a law court and that is left at the mercy of the parties only. It is a gentleman's promise which may or may not be fulfilled by the promisor.

All these agreement remain only an agreement between the parties and they never become a contract in the eyes of law, because they are merely social, domestic or moral arrangements, which lack a basic intention to create legal relations. All those agreements are said to be enforceable in which the aggrieved party has a right to approach a law court to get the agreement enforced and the other party is held liable either to perform the agreement or to face the consequence for breach of that agreement. Usually it is a legal presumption that all commercial agreements do have a basic intention to create a legal relationship and therefore they are enforceable at law. All these agreement which are enforceable at law are contracts

This also implies that unenforceable agreements remain agreements only and cannot be converted into a valid contract and only enforceable agreements are converted into a valid contract. Therefore we can conclude that: "**All contracts are agreements but all agreements are not contracts.**" An agreement, to be enforceable by law, must possess the essential elements of a valid contract as contained in **Section 10 of the Indian Contract Act.**

According to Section 10, "**All agreements are contract if they are made by the free consent of the parties, competent to contract, for a lawful consideration and with a lawful object and are not expressly declared to be void.**"

Simplifying the same, all agreements are contracts, if they are made-

- ⇒ by free consent of the parties,
- ⇒ competent to contract,
- ⇒ for a lawful consideration
- ⇒ with a lawful object, and
- ⇒ not hereby expressly declared to be void

Along with the elements mentioned under Section 10 there are certain other basic elements of a valid contract which may be mentioned as follows -

1. **Proper Offer and Acceptance:** There must be at least two parties- one making the offer and the other accepting it. Such offer and acceptance must be valid. An offer to be valid must fulfill certain conditions, such as it must intend to create legal relations, its terms must be certain and unambiguous, it must be communicated to the person to whom it is made, etc. An acceptance to be valid must fulfill certain conditions, such as it must be absolute and unqualified, it must be made in the prescribed manner and it must be communicated by an authorized person before the offer lapses.
2. **Intention to Create Legal Relationship:** The requirement of intention to create legal relations in contract law is aimed at sifting out cases which are not really appropriate for court action. Not every agreement leads to a binding contract which can be enforced through the courts. For example you may have an agreed to take a friend for a movie or for dinner. You may have a moral duty to honour that agreement but not a legal duty to do so. This is because in general the parties to such agreements do not intend to be legally bound and the law seeks to mirror the party's wishes. In order to determine which agreements are legally binding and have an intention to create legal relations, the law draws a distinction between social, moral, domestic and religious agreements and agreements made in a commercial context. There must be an intention among the parties to create a legal relationship. In case of social or domestic agreements, the usual presumption is that the parties do not intend to create legal relationship but in commercial or business agreements, the usual presumption is that the parties intend to create legal relationship unless otherwise agreed upon.

Example: X invited Y to a dinner Y accepted the invitation. It is a social agreement. If X fails to serve dinner to Y, Y cannot go to the courts of law for enforcing the agreement. Similarly, if Y fails to attend the dinner, X cannot go to the courts of law for enforcing the agreement.

RELEVANT CASES ON THIS POINT:

- ***Rose & Frank Co. v. Crompton Bros. (1925)***
- ***Balfour v. Balfour (1919)***

3. **Capacity of Parties:** As per the requirement of Sec. 10, the parties to an agreement must be competent to contract. In other words, they must be capable or competent to enter into a contract. If either of the parties does not have the capacity to contract, the contract is not valid. According to **Section 11** of Indian Contract Act, 1872, **"Every person is competent to contract who is of the age of majority according to the law to which he is subject and who is of sound mind and is not disqualified from contracting by any law to which he is subject."** Therefore, other way round, following persons are incompetent to contract-
 - (a) Minors,
 - (b) Persons of unsound mind, and
 - (c) Persons disqualified by law to which they are subject.

So, the person to be competent to contract must be major, must be of sound mind and must not be declared disqualified from contracting by any law to which he is subject. If the parties to agreement are not competent to contract, then no valid contract comes into existence.

RELEVANT CASE: ***Mohiri Bibi v. Dharmodas Ghosh*** (Landmark case on minor's contract. Minor's contract has been held as void ab initio.)

4. **Lawful Consideration:** An agreement must be supported by lawful consideration. Consideration means something in return. In the words of Pollock, "Consideration is the price for which the promise of another is bought." Consideration is known as quid pro-quo i.e. **something in return**. Contract Act not only requires a consideration rather it prescribes for a lawful consideration. Now, what constitutes a lawful consideration has been explained under **Section 23** of the Indian Contract Act, 1872, according to which, "**The consideration is considered lawful unless it is forbidden by law or is of such a nature that if permitted would defeat the provisions of any law, or is fraudulent or involves or implies injury to the person or property of another or is immoral or is opposed to public policy.**"

Example: A agrees to sell his car to B for Rs.1,00,000. Here B's promise to pay Rs.1,00,000 is the consideration for A's promise to sell the car and A's promise to sell the car is the consideration for B's promise to pay Rs.1,00,000.

5. **Lawful Object:** The object of an agreement must be lawful. According to **Section 23** of the Indian Contract Act, 1872, "the object is considered lawful unless-
- o **it is forbidden by law;**
 - o **it is of such nature that if permitted it would defeat the provision of any law;**
 - o **it is fraudulent;**
 - o **it involves an injury to the person or property of any other;**
 - o **the court regards it as immoral or opposed to public policy."**

Example: X, Y and Z enter into an agreement for the division among them of gains acquired or to be acquired by them by fraud. The agreement is void because its object is unlawful.

6. **Free Consent:** There must be free consent of the parties to the contract. Free consent of all the parties to a contract is one of the essential elements of a valid contract as per requirement of Section 10. The parties to a contract should have identity of minds. This is called **consensus ad idem** in English Law. Consent has been defined under **Sec. 13** of the Contract Act as follows- "**Two or more person are said to consent when they agree upon the same thing in the same sense**" (**consensus ad idem**). It means that there is no contract if the parties have not agreed upon the same thing in the same sense.

Further, Contract Act requires not only consent but a free consent. According to **Section 14**, consent is said to be free when it is not caused by-

- o **Coercion, or**
- o **Undue influence, or**
- o **Fraud, or**
- o **Misrepresentation, or**
- o **Mistake.**

A contract which is valid in all other respects may still fail because there is no real consent to it by one or both of the parties.

7. **Agreement not expressly declared void:** The agreement must not have been expressly declared void under the provisions of **Sections 24 to 30** of the Indian Contract Act, 1872. (For example- Agreements in restraint of trade, marriage, legal proceedings and agreement by way of wager have been expressly declared as void under the Act itself.

Example: X promised to marry none else except Y and in default pay her Rs.1,00,000. X married Z and Y sued X for the recovery of Rs.1,00,000. It was held that Y was not entitled to recover anything because this agreement was in restraint of marriage and as such void.

8. **Certainty of meaning:** The terms of the agreement must be certain and unambiguous. According to **Section 29** of the Indian Contract Act, 1872, **“Agreements the meaning of which is not certain or capable of being made certain are void.”**

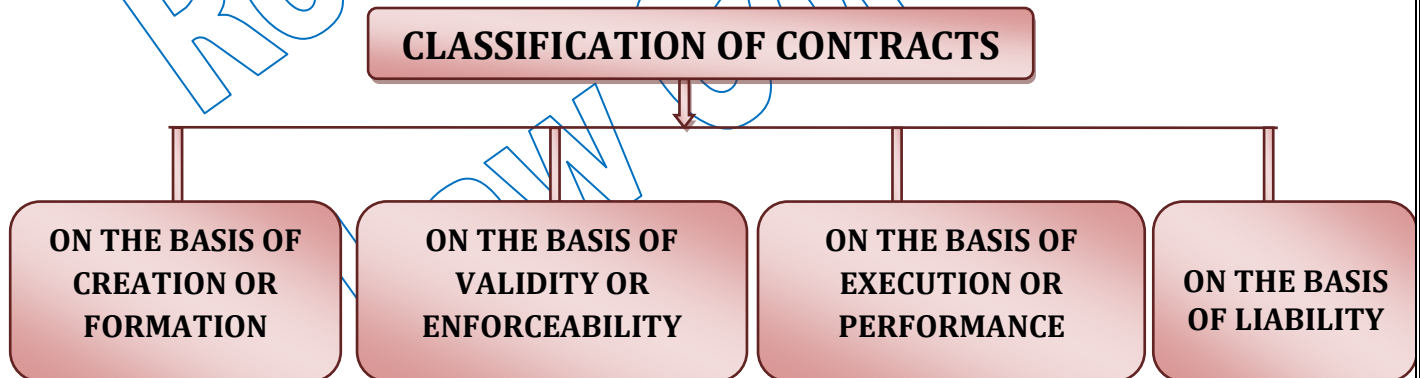
9. **Possibility of Performance:** The terms of the agreement must be such as are capable of performance. If the act is impossible in itself, physically or legally, it cannot be enforced at law. According to **Section 56**, **“An agreement to do an impossible act is void.”**

Example: X agrees with Y to discover treasure by magic and Y agrees to pay Rs 1,000 to X. This agreement is void because it is an agreement to do an impossible act. Example II: X agrees with Y to enclose some area between two parallel lines and Y agrees to pay Rs 1,000 to X. This agreement is void because it is an agreement to do an impossible act.

10. **Legal Formalities must be complete:** The agreement must comply with the necessary formalities as to **writing, registration, stamping etc.**, if any required in order to make it enforceable by law. An oral contract is a perfectly valid contract, except in those cases where writing, registration etc. is required by some statute. In India, writing is required in cases of sale, mortgage, lease and gift of immovable property, negotiable instruments, memorandum and articles of association of a company, etc. Registration is required in cases of documents falling within the scope of **Section 17 of the Registration Act.**

Example: An oral agreement for arbitration is unenforceable because the law requires that arbitration agreement must be in writing.

CLASSIFICATION OF CONTRACTS



A. On the basis of creation or formation-

1. **Express Contracts:** An express contract is one entered into by words which may be either spoken or written. Where the proposal and acceptance is made in words, it is an express contract.

Example 1: A says to B, “Will you buy my furniture for Rs. 50,000?” B says to A, “I am ready to buy your car for Rs. 50,000.” It is an express contract made orally.

Example 2: A writes a letter to B, I offer to sell my furniture to you for Rs. 50,000.” B send a letter to A, “I am ready to buy your furniture for Rs. 50,000.” It is an express contract made in writing.

- 2. Implied Contracts:** Where the proposal or acceptance is made otherwise than in words, it is an implied contract. Implied contract can be inferred from the surrounding circumstances and the conduct of the parties who made them.
Example: A, a coolie in uniform picks up the baggage of B to carry it from railway platform to the taxi without being asked by B to do so and B allows it. In this case there is an implied offer by the coolie and an implied acceptance by the passenger. Now, there is an implied contract between the coolie and the passenger and the passenger is bound to pay for the services of the coolie.
- 3. Quasi Contracts or constructive contracts:** It is contract in which there is no intention on either side to make a contract, but the law imposes a contract. In such a contract, rights and obligations arise not by any agreement between the parties but by operation of law. Thus, a finder of lost goods is under an obligation to find out the true owner and return the goods. Similarly, where certain goods are delivered to a wrong addressee, the addressee is under an obligation either to pay for them or return them.
- 4. E. Com. Contracts/Contracts over Internet:** These contracts are entered into between the parties using internet. In electronic commerce, different parties/persons create network which are linked to other network through EDI (Electronic Data Inter-change). This helps in doing business transactions using electronic mode.

B. On the basis of validity or enforceability-

- 1. Valid Contract:** An agreement enforceable at law is a valid contract as per Sec. 2(h). An agreement becomes a contract when all the essentials of a valid contract as laid down in Section 10 are fulfilled.
- 2. Void Contract [Sec. 2(j)]:** The term 'Void contract' is a contradiction in terms. But according to **Section 2(j), "A contract which ceases to be enforceable by law becomes void when it ceases to be enforceable"** In other words, a void contract is a contract which was valid and legally enforceable when entered into but which subsequently became void due to supervening or subsequent impossibility of performance, change of law or some other reason.
- 3. Void Agreements:** According to **Section 2(g), "An agreement which is not enforceable by law by either of the parties is void."** Such agreements are **void ab initio** i.e. they are unenforceable from the very inception. No legal rights or obligations can arise out of a void agreement. For example an agreement without consideration or with a minor is a void agreement. A void agreement never matures into a contract.
- 4. Voidable Contract:** According to **Section 2(i), "An agreement which is enforceable by law at the option of one or more of the parties thereto but not at the option of the other or others is a voidable contract."** Note that the word used here is 'contract' and not just 'agreement'. This is the result of absence of free consent in the contract. The consent is said to be not free when it was obtained by coercion, undue influence, fraud, misrepresentation or mistake. The other party who although took a consent cannot be allowed to take advantage of his own fraud because this is a judicial principle that **"He who comes into equity (i.e. before law) must come with clean hands."** Thus, a voidable contract is one which can be set aside or repudiated or avoided at the option of that aggrieved party whose consent was not free. Also, a voidable contract is valid and enforceable until it is repudiated (i.e. avoided) by the party entitled to avoid it.