UNIT-I

LESSON-1

LAW OF CONTRACT

CONTENTS

AIMS AND OBJECTIVES

Business Law is a very important subject in that it equips the students to understand the various types of laws that are applicable to business. Unit I deals with the concept of Contracts, which is very vital for business.

This unit will help the students to understand:

- The significance of law in business
- What contracts are and the types of contracts
- The essential elements of valid contracts

INTRODUCTION

One should know the law to which he is subject because ignorance of law is no excuse. Mercantile law is not a separate branch of law. Basically, it is a part of civil law which deals with the rights and obligations of mercantile persons arising out of mercantile transactions in respect of mercantile property. It includes laws relating to various contracts, partnerships, companies, negotiable instruments, insurance, carriage of goods, arbitration etc.

1.1.1 INTRODUCTION

Law means a ‘set of rules’. It may be defined as the rules of conduct recognised and enforced by the state to control and regulate the conduct of people, to protect their property and contractual rights with a view to securing justice, peaceful living and social security.

The Law of Contract

The law of contract is that branch of law which determines the circumstances in which promises made by the parties to a contract shall be legally binding on them. Business law is of particular importance to people engaged in trade, commerce and industry as bulk of their business transactions are based on contracts.

1.1.2 THE INDIAN CONTRACT ACT, 1872

The law of contract is contained in the Indian Contract Act, 1872 which-

(a) Deals with the general principles of law governing all contracts, (Secs.1 to 75)
(b) Some special contracts only (Secs.124 to 238)

The first six chapters of the Act deal with the different stages in the formation of a contract, its essential elements, its performance or breach and the remedies for breach of contract. The remaining chapters deal with some of the special contracts, namely, Indemnity and Guarantee (Chapter VIII (Secs.124 to 147)), Bailment and Pledge (Chapter IX (Secs.148 to 181)) and Agency (Chapter X (Secs.182 to 238)).

Law of contract creates *jus in personam* as distinguished from *jus in rem*:

Jus in rem means a right against or in respect of a thing: *jus in personam* means a right against or in respect of a specific person. *Jus in rem* is available against the world at large; *jus in personam* is available only against particular persons.

Examples:

a. X owes a certain sum of money to Y. Y has a right to recover this amount from X. This right can be exercised only by Y and by none else against X. This right of Y is a *jus in personam*.
b. A is the owner of a house. He has a right to have quiet possession and enjoyment of that house against every member of the public. Similarly every member of the public is under an obligation not to disturb A's possession or enjoyment. This right of A is a *jus in rem*.

Meaning of Contract

According to Section 2(h) of the Indian Contract Act, 1872, "An agreement enforceable by law is a contract." In other words, an agreement which can be enforced in a court of law is known as a contract. A contract must have the following two elements.

a. An agreement, and
b. Its enforceability by law.

Sir William Anson defines a contract as, “a legally binding agreement between two or more persons by which rights are acquired by one or more to acts or forbearances (abstaining from doing something) on the part of the others”.

Pollock defines a contract as, “every agreement and promise enforceable at law is a contract”.

Agreement + Enforceability by law = Contract

Agreement

According to Section 2(e) of the Indian Contract Act, 1872, “Every promise and every set of promises forming the consideration for each other is an agreement.” A proposal when accepted becomes a promise.

Offer + Acceptance = Agreement

Enforceability of Agreement

An agreement is said to be enforceable by law if it creates some legal obligation. 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. Eg., in case of social or domestic agreements, the usual presumption that the parties do not intend to create legal relations.

Consensus ad idem

The essence of an agreement is the meeting of the minds of the parties in full and final agreement: there must, in fact, be *consensus ad idem*. This means that the parties to the agreement must have agreed about the subject-matter of the agreement in the same sense and at the same time. Unless there is consensus ad idem, there can be no contract.

Obligation

An agreement, to become a contract, must give rise to a legal obligation or duty. The term ‘obligation’ is defined as a legal tie which imposes upon a definite person or persons the necessity of doing or abstaining from doing a definite act or acts. It may relate to social or legal matters. An agreement which gives rise to a social obligation is not a contract. It must give rise to a legal obligation in order to become a contract.

Agreement is a very wide term

An agreement may be a social agreement or a legal agreement. If A invites B to a dinner and B accepts the invitation, it is a social agreement. A social agreement does not give rise to contractual obligations and is not enforceable in a Court of law. It is only those agreements which are enforceable in a Court of law which are contracts.

Examples:
(a) A invites his friend B to come and stay with him for a week. B accepts the invitation but when he comes to A, A cannot accommodate him as his wife had died the day before. B cannot claim any compensation from A as the agreement is a social one.

(b) A father promises to pay his son Rs. 500 every month as pocket allowance. Later he refuses to pay. The son cannot recover as it is a domestic agreement and there is no intention on the part of the parties to create legal relations.

To conclude: Contract = Agreement + Enforceability at law.

Thus all contracts are agreements but all agreements are not necessarily contracts.

1.1.3 ESSENTIAL ELEMENTS OF A VALID CONTRACT

According to Sec. 10, all agreements are contracts if they are made by the free consent of parties competent to contract, for a lawful consideration and with a lawful object and are not expressly declared to be void. In order to become a contract, an agreement must have the following essential elements:

1. Minimum two persons:

There must be at least two persons for a contract to come into existence. One person to make the offer and the other person to accept it.

2. Offer and acceptance:

There must be two parties to an agreement, i.e., one party making the offer and other party accepting it. The terms of the offer must be definite and the acceptance of the offer must be absolute and unconditional. The acceptance must also be according to the mode prescribed and must be communicated to the offeror.

3. Intention to create legal relationship:

When the two parties enter into an agreement, their intention must be to create legal relationship between them. If there is no such intention on the part of the parties, there is no contract between them. Agreements of a social or domestic nature do not contemplate legal relationship, as such they are not contracts.

Example:

A husband promised to pay his wife a household allowance of £ 30 every month. Later the parties separated and the husband failed to pay the amount. The wife sued for the allowance. Held, agreements such as these were outside the realm of contract altogether [Balfour vs. Balfour, (l919) 2 K.B. 571].

In commercial and business agreements, the presumption is usually that the parties intended to create legal relations. But this presumption is rebuttable which means that it must be shown that the parties did not intend to be legally bound.

Examples:

(a) There was an agreement between R Company and C Company by means of which the former was appointed as the agent of the latter. One clause in the agreement was:"This agreement is not entered into ..... as a formal or legal agreement, and shall not be subject to legal jurisdiction in the law courts." Held, there was no binding contract as there was no intention to create legal relationship [Rose & Frank Co. vs. Crompton Bros., (1925) A.C. 445].

(b) In an agreement, a document contained a condition “that it shall not be attended by or give rise to any legal relationship, rights, duties, consequences whatsoever or be legally enforceable or be the subject of litigation, but all such arrangements, agreements and transactions are binding in honour only.” Held, the condition was valid and the agreement was not binding [Jones vs. Vernon's Pools. Ltd. (1938) 2 All E.R. 626].

4. Lawful consideration:

An agreement to be enforceable by law must be enforceable by consideration. ‘Consideration’ means an advantage or benefit moving from one party to the other. It is the essence of a bargain. In simple words, it means ‘something in return’. The agreement is legally enforceable only when both the parties give something and get something in return. A promise to do something, getting nothing in return is usually not enforceable by law. Consideration need not necessarily be in cash or kind. It may be an act or abstinence (abstaining from doing something) or promise to do or not to do something. It may be past, present or future. But it must be real and lawful. [Secs. 2 (d), 23 and 25).

5. Capacity of parties – competency:

The parties to the agreement must be capable of entering into a valid contract. Every person is competent to contract if he

(a) is of the age of majority,

(b) is of sound mind, and

(c) is not disqualified from contracting by any law to which he is subject (Secs. 11 and 12).

Flaw in capacity to contract may arise from minority, lunacy, idiocy, drunkenness, etc., and status. If a party suffers from any flaw in capacity, the agreement is not enforceable except in special cases.

6. Free and genuine consent:

It is essential to the creation of every contract that there must be free and genuine consent of the parties to the agreement. The consent of the parties is said to be free when they are of the same mind on all the material terms of the contract. The parties are said to be of the same mind when they agree about the subject-matter of the contract in the same sense and at the same time (Sec. 13). There is absence of free consent if the agreement is induced by coercion, undue influence, fraud, misrepresentation, etc. (Sec. 14).

7. Lawful object:

The object of the agreement must be lawful. In other words, it means that the object must not be

(a) illegal,

(b) immoral, or

(c) opposed to public policy (Sec. 23).

If an agreement suffers from any legal flaw, it would not be enforceable by law.

8. Agreement not declared void:

The agreement must not have been declared void by law in force in the country (Secs. 24 to 30 and 56).

9. Certainty and possibility of performance:

The agreement must be certain and not vague or indefinite (Sec. 29). If it is vague and it is not possible to ascertain its meaning, it cannot be enforced.

Examples:

(a) A agrees to sell to B "a hundred tons of oil". There is nothing whatever to show what kind of oil was intended. The agreement is void for uncertainty.

(b) O agreed to purchase a motor van from S “on hire-purchase terms”. The hire-purchase price was to be paid over two years. Held, there was no contract as the terms were not certain about rate of interest and mode of payment. No precise meaning could be attributed to the words “on hire-purchase” since there was a wide variety of hire-purchase terms (Scammel vs. Ouston, (1941) A.C. 251].

The terms of the agreement must also be such as are capable of performance. Agreement to do an act impossible in itself cannot be enforced [Sec. 56 (1)]. For example, where A agrees with B to put life into B's dead wife, the agreement is void as it is impossible of performance.

10. Legal formalities:

A contract may be made by words spoken or written. As regards the legal effects, there is no difference between a contract in writing and a contract made by word of mouth. It is, however, in the interest of the parties that the contract should be in writing. There are some other formalities also which have to be complied with in order to make an agreement legally enforceable. In some cases, the document in which the contract is incorporated is to be stamped. In some other cases, a contract, besides being a written one, has to be registered. Thus where there is a statutory requirement that a contract should be made in writing or in the presence of witnesses or registered, the required statutory formalities must be complied with (Sec. 10, Para 2).

1.1.4 CLASSIFICATION OF CONTRACTS

Contracts may be classified according to their (1) validity, (2) formation, or (3) performance.

I. Classification according to validity

A contract is based on an agreement. An agreement becomes a contract when all the essential elements referred to above are present. In such a case, the contract is a valid contract. If one or more of these elements is/are missing, the contractt is either voidable, void, illegal or un-enforceable.

1. Voidable contract:

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 [Sec. 2(i)]. This happens when the element of free consent in a contract is missing. When the consent of a party to a contract is not free, i.e., it is caused by coercion, undue influence, misrepresentation or fraud, the contract is voidable at his option. The party whose consent is not free may either rescind (avoid or repudiate) the contract if he so desires, or elect to be bound by it. A voidable contract continues to be valid till it is avoided by the party entitled to do so.

Example: A promises to sell his car to B for Rs 2,00,000. His consent is obtained by use of force. The contract is voidable at the option of A. He may avoid the contract or elect to be bound by it.

A contract becomes voidable in the following two cases also:

i. When a person promises to do something for another person for a consideration but the other person prevents him from performing his promise, the contract becomes voidable at his option (Sec. 53).

Example: A and B contract that B shall execute certain work for A for Rs. 1,000. B is ready and willing to execute the work accordingly but A prevents him from doing so. The contract is voidable at the option of B and if he elects to rescind it, he is entitled to recover from A compensation for any loss which he has incurred by its non-performance.

ii. When a party to a contract promises to perform an obligation within a specified time, any failure on his part to perform his obligation within the specified time makes the contract voidable at the option of the promise (Sec. 55, Para 1).

When a person at whose option a contract is voidable rescinds it, the other party thereto need not perform any promise therein contained in which he is promisor. If the party rescinding the contract has received benefit under the contract from another party to such contract he shall restore such benefit, so far as may be, to the person from whom it was received (Sec. 64). The party rightfully rescinding the contract is also entitled to compensation for any damage which he has sustained through the non-fulfilment of the contract (Sec. 65).

2. Void agreement and void contract:

(i) Void agreement:

An agreement not enforceable by law is said to be void [Sec. 2 (g)]. A void agreement does not create any legal rights or obligations. It is a nullity and is destitute of legal effects altogether. It is void ab initio. i.e., from the very beginning as, for example, an agreement with a minor or an agreement without consideration.

(ii) Void contract:

A contract which ceases to be enforceable by law becomes void when it ceases to be enforceable [Sec. 2 (j)]. A contract, when originally entered into, may be valid and binding on the parties, e.g., a contract to import goods from a foreign country. It may subsequently become void, e.g., when a war breaks out between the importing country and the exporting country.

It is illogical to talk of a void contract originally entered into, for what is supposed to be a contract is no contract at all.

(iii) Illegal agreement:

An illegal agreement is one which transgresses some rule of basic public policy or which is criminal in nature or which is immoral. Such an agreement is a nullity and has much wider import than a void contract. All Illegal agreements are void but all void agreements or contracts are not necessarily illegal. An illegal agreement is not only void as between the immediate parties, but has this further effect that even the collateral transactions to it become tainted with illegality. A collateral transaction is one which is subsidiary, incidental or auxiliary to the principal or original contract.

Example: B borrows Rs. 5,000 from A and enters into a contract with an alien to import prohibited goods. A knows of the purpose of the loan. The transaction between B and A is collateral to the main agreement. It is illegal since the main agreement is illegal.

3. Unenforceable contract:
An unenforceable contract is one which cannot be enforced in a Court of law because of some technical defect such as absence of writing or where the remedy has been barred by lapse of time. The contract may be carried out by the parties concerned; but in the event of breach or repudiation of such a contract, the aggrieved party will not be entitled to the legal remedies.

II. Classification according to formation

A contract may be (a) made in writing or by word of mouth, or (b) inferred from the conduct of the parties or the circumstances of the case. These are the modes of formation of a contract.

Contracts may be classified according to the mode of their formation as follows:

1. Express contract:
If the terms of a contract are expressly agreed upon (whether by words spoken or written) at the time of formation of the contract, the contract is said to be an express contract. Where the offer or acceptance of any promise is made in words, the promise is said to be express (Sec. 9). An express promise results in an express contract.

2. **Implied contract:**
An implied contract is one which is inferred from the acts or conduct of the parties or course of dealings between them. It is not the result of any express promises by the parties but of their particular acts. It may also result from a continuing course of conduct of the parties. Where the proposal or acceptance of any promise is made otherwise than in words, the promise is said to be implied (Sec. 9). An implied promise results in an implied contract.

Examples:

a. there an implied contract when A –

i. takes a cup of tea in a restaurant,
ii. gets in to a public bus,
iii. obtains a ticket form an automatic weighing machine , or
iv. lifts B's luggage to be carried out of the railway station

b. A fire broke out in Ps farm. He called upon the Upton Fire Brigade to put out the fire which the latter did. P's farm did not come under the free service zone although he believed to be so. Held, he was liable to pay for the service rendered as the service was rendered on an implied promise to pay [Upton Rural District Council vs. Powell (1942) All E.R. 220].

3. Quasi-contract:

Strictly speaking, a quasi-contract is not a contract at all. A contract is intentionally entered into by the parties. A quasi-contract, on the other hand, is created by law. It resembles a contract in that a legal obligation is imposed on a party who is required to perform it. It rests on the ground of equity that "a person shall not be allowed to enrich himself unjustly at the expense of another."

Example:

X, a tradesman, leaves goods at Cs house by mistake. C treats the goods as his own. C is bound to pay for the goods.

4. E-Commerce contract:

An E-commerce contract is one which is entered into between two parties via Internet. In Internet, different individuals or companies create networks which are linked to numerous other networks. This expands the area of operation in commercial transactions for any person.

III. Classification according to performance

To the extent to which the contracts have been performed, these may be classified as -

1. Executed contract:

'Executed' means that which is done. An executed contract is one in which both the parties have performed their respective obligations.

Example:

A agrees to paint a picture for B for Rs. 1,000. When A paints the picture and B pays the price, i.e., when both the parties perform their obligations, the contract is said to be executed.

In some cases, even though a contract may appear to be completed at once, its effects may still continue. Thus when a person buys a bun containing a stone and subsequently breaks one of his teeth, he has a right to recover damages from the seller [Chaproniere vs. Mason, (1905) 21 T.L.R 633].

2. Executory contract:

'Executory' means that which remains to be carried into effect. An executor contract is one in which both the parties have yet to perform their obligations. Thus, in the example, the contract is executory if A has not yet painted the picture and B has not paid the price. Similarly, if A agrees to engage B as his servant from the next month, the contract is executory.

A contract may sometimes be partly executed and partly executory . Thus, if B has paid the price to A and A has not yet painted the picture, the contract is executed, as to B and executory as to A .

Another classification of contracts according to the performance is as follows:

1. Unilateral or one-sided contract:

A unilateral or one-sided contract is one in which only one party has to fulfil his obligation at the time of the formation of the contract, the other party having fulfilled his obligation at the time of the contract or before the contract comes into existence. Such contracts are also known as contracts with executed consideration.

Example:

A permits a railway coolie to carry his luggage and place it in a carriage. A contract comes into existence as soon as the luggage is placed in the carriage. But by that time the coolie has already performed his obligation. Now only A has to fulfil his obligation, i.e., pay the reasonable charges to the coolie

2. Bilateral contract:

A bilateral contract is one in which the obligations on the part of both the parties to the contract are outstanding at the time of the formation of the contract. In this sense, bilateral contracts are similar to executory contracts and are also known as contracts with executory consideration.

1.1.5 CONTINGENT CONTRACTS

A contract may be-

i. an absolute contract or

ii. a contingent contract.

An ‘absolute contract’ is one in which the promisor binds himself to performance in any event without any conditions.

‘Contingent’ means that which is dependent on something else.

A contingent contract' is a contract to do or not to do something, if some event, collateral to such contract, does or does not happen (Sec. 31). Where, for example, goods are sent on approval, the contract is a contingent contract depending on the act of the buyer to accept or reject the goods.

Examples:

a. A contracts to pay Rs. 10,000 if B's house is burnt. This is a contingent contract.

b. A agrees to sell a certain piece of land to B, in case he succeeds in his litigation concerning that land. This is a contingent contract.

There are three essential characteristics of a contingent contract:

i. Its performance depends upon the happening or non-happening in future of some event. It is this dependence on a future event which distinguishes a contingent contract from other contracts.

ii. The event must be uncertain. If the event is bound to happen, and the contract has got to be performed in any case it is not a contingent contract.

iii. The event must be collateral, i.e., incidental to the contract.

Contracts of insurance, indemnity and guarantee are the commonest instances of a contingent contract.

Rules regarding Contingent contracts:

i. Contingent contracts dependent on the happening of an uncertain future event cannot be enforced until the event has happened. If the event becomes impossible, such contracts become void (Sec. 32).

ii. Where a contingent contract is to be performed if a particular event does not happen, its performance can be enforced when the happening of that event becomes impossible (Sec. 33).

iii. If a contract is contingent upon how a person will act at unspecified time, the- event shall be considered to become impossible when such person does anything which renders it impossible that he should so act within any definite time, or otherwise than under futher contingencies (Sec. 34).

iv. Contingent contracts to do or not to do anything, if a specified uncertain event happens within a fixed time, become void if the event does not happen or its happening becomes impossible before the expiry of that time.

v. Contingent agreements to do or not do anything, if an impossible event happens, are void, whether or not the fact is known to the parties (Sec.36).

Wagering agreements or Wager (Sec.30)

A wager is an agreement between two parties by which one promises to pay money or money's worth on the happening of some uncertain event in consideration of the other party's promise to pay if the event does not happen. Thus, if A and B enter into an agreement that A shall pay B Rs.1,000 if it rains on Monday, and that B shall pay A the

same amount if it does not rain, it is a wagering agreement. The event may be uncertain either because it is to happen in future or if it has already happened, the parties are uncertain and express opposite views.

Essentials of a wagering agreement:

1. Promise to pay money or money's worth:

The wagering agreement must contain a promise to pay money or money's worth.

2. Uncertain event:

The promise must be conditional on an event happening or not happening. A wager generally contemplates a future event, but it may also relate to a past event provided the parties are not aware of its result or the time of its happening.

3. Each party must stand to win or lose:

Upon the determination of the contemplated event, each party should stand to win or lose. An agreement is not a wager if either of the parties may win but cannot lose or may lose but cannot win.

4. No control over the event:

Neither party should have control over the happening of the event one way or the other. If one of the parties has the event in his own hands, the transaction lacks essential ingredients of a wager.

5. No other interest in the event:

Lastly, neither party should have any interest in the happening or non-happening of the event other than the sum or stake he will win or lose. Thus an agreement is not a wager if the party to whom money is promised on the occurrence of an event has an 'interest' in its non-occurrence.

Difference between a wagering agreement and a contingent contract:

i. A wagering agreement consists of reciprocal promises whereas a contingent contract may not contain reciprocal promises.

ii. A wagering agreement is essentially of a contingent nature a contingent contract may not be of a wagering nature.

iii. A wagering agreement is void whereas a contingent contract is valid.

iv. In a wagering agreement, the parties have no other interest in the subject-matter of the agreement except the winning or losing of the amount of the wager. In other words, a wagering agreement is a game of chance. This is not so in case of a contingent contract.

v. In a wagering agreement the future event is the sole determining factor while in a contingent contract the future event is only collateral.

Check your progress - 1

Define contract. Enumerate the essentials of a valid contract.

LESSON-2

OFFER AND ACCEPTANCE

CONTENTS

1.2.1 VALID OFFER

Meaning of Offer [Section 2(a)]

An offer is the starting point in the making of an agreement. An offer is also called 'proposal'. According to Section 2(a) of The Indian Contract Act, 1872, "A person is said to have made the proposal when he signifies to another his willingness to do or to abstain from doing anything with a view to obtaining the assent of that offer to such act or abstinence."

Thus, an offer involves the following essential elements:

i. It must be made by one person to another person. In other words, there can be no proposal by a person to himself.

   Example: X says to Y that he wants to sell his car to himself for Rs 1 lakh. There is no proposal because there can be no proposal by a person to himself.

ii. It must be an expression of readiness or willingness to do (i.e. a positive act) or to abstain from doing something (i.e. a negative act).

   Example : X offers to sell his car to Y for Rs 1 lakh. It is a positive act on the part of X. Example : X offers not to file a suit against Y if Y pays X the outstanding amount of Rs 1,00,000. It is a negative act on the part of X.

iii. It must be made with a view to obtain the consent of that other person to proposed act or abstinence.

Example: X jokingly says to Y ”I am ready to sell my car for Rs 1,000.” Y, knowingly that X is not serious in making the offer, says “I accept your offer.” In this case, X’s offer was not the real offer as he did not make it with a view to obtain the consent of Y.

Meaning of “Offerer” (or ‘Promisor’), Offeree (or Promisee):

The person making the proposal is called the offerer or proposer. The person to whom the proposal is made is called the 'offeree' or 'proposee'.

Example X says to Y, “I want to sell my car to you for Rs 1 lakh.” Here, ‘to sell car’ is an offer or proposal. X who has made the offer is called offeror or promisor. Y to whom the offer has been made is called the offeree or proposee.

How to Make an Offer

An offer can be made by any act which has the effect of communicating it to another person. An offer may, either be an ‘express offer’ or ‘implied offer’.

1. Express Offer:
An express offer is one which is made by words spoken or written.

Example I: X says to Y, “Will you purchase my car for Rs 1,00,000?”

Example II: X writes to Y in a letter, “I want to sell my house for Rs 2,00,000”

Example III: X advertises in a newspaper that I will pay Rs 1,000 to anyone who traces my missing nephew.

2. Implied Offer:
An implied offer is one which is made otherwise than in words. In other words, it is inferred from the conduct of the person or the circumstances of the particular case.

Example I: A transport company runs buses on different routes to carry passengers. It is an implied offer by the transport company to carry passengers for a certain fare.
Example II: A bid at an auction is an implied offer to buy.

3. Specific Offer:
A specific offer is one which is made to a definite person or particular group of persons. A specific offer can be accepted only by that definite person or that particular group of persons to whom it has been made.

Example: X offers to buy car from Y for Rs 1.0 lakh. This offer is a specific offer which has been made to a definite person Y. No person other than Y can accept this offer. [Boulton vs. Jones].

Similarly an offer made to a company is an offer to a group of persons and hence a specific offer.

4. General Offer:

A general offer is one which is not made to a definite person, but to the world at large or public in general. A general offer can be accepted by any person by fulfilling the terms of the offer. In case of general offer, the contract is made with person who having the knowledge of the offer comes forward and acts according to the conditions of the offer.

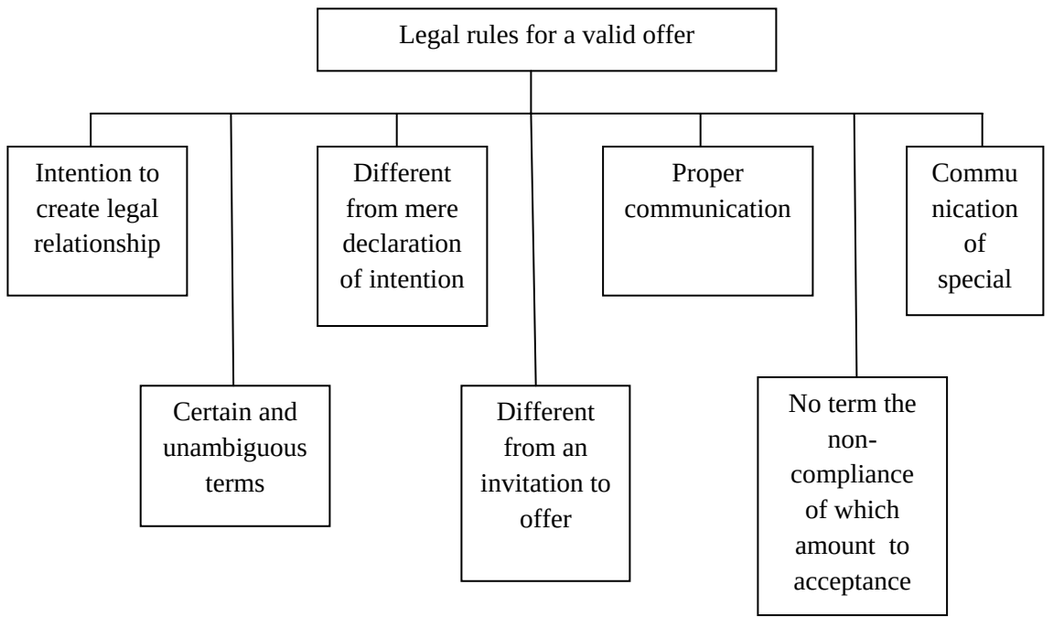
Example I: X advertised in the newspaper that he would pay Rs 5,000 to anyone who traces his missing boy. Y, who knew about the reward traced that boy and sent a telegram to X that he had found his son. It was held that X was entitled to receive the amount of reward.

[Harbhajan Lal vs. Harcharan Lal (AIR All 539)].

Example II: Carbolic Smoke Ball Co. advertised in the newspaper that it would pay Rs 1,000 to anyone who contracts influenza after using the smoke ball of the company according the printed instructions. Mrs. Carlil uses the smoke ball according to the printed directions but subsequently contracted influenza. On a suit for the reward she was held entitled to recover the same because she had accepted the offer by fulfilling the terms of the offer. [Carlil vs. Carbolic Smoke Ball Co.]

1.2.2 LEGAL RULES OF A VALID OFFER

An offer to be valid must fulfil the following conditions:



1. **Intention to Create Legal Relationship**: An offer must intend to create legal relations. An offer must be such that when accepted, it will create legal relationship among the parties.

The question whether or not the parties have intention to create legal relationship can be answered with reference to type and terms of agreement and the circumstances under which the agreement is made.

2. **Certain and Unambiguous Terms**: The terms of the offer must be certain and unambiguous and not vague. If the terms of the offer are vague, no contract can be entered into because it is not clear as to what exactly the parties intended to do.

Example I : X offers to sell to Y"a 100 tons of oil." If X is a dealer in coconut oil and mustard oil, his offer is not certain because it is not clear that he wants to sell coconut oil or mustard oil. But if X is a dealer in coconut oil only, it is clear that he wants to sell coconut oil. Hence, the offer is certain.

Example II: X offers to sell to Y his car for Rs 1,00,000 or Rs 1,50,000. Here X's offer is not certain because it is not clear which of the two prices was to be given by Y.

Note: If the terms of the offer are capable of being made certain, the offer is not regarded as vague. For example, X offers to sell to Y "a 1 00 tons of coconut oil." Here, the offer cannot be said to be uncertain on the ground that it is not clear what price is to be given for oil because in such a case if such an offer is accepted by Y, Y has to give only a reasonable price.

3. **Different from a Mere Declaration of Intention**: The offer must be distinguished from a mere declaration of intention. Such statement or declaration merely indicates that an offer will be made or invited in future.

Example I: A father wrote to his would be son-in-law that his daughter would have a share of what he left after the death of his wife. It was held that the letter was a mere statement of intention and not an offer. [Farine vs. Fickar]

Example II: X, a broker of Mumbai wrote to Y, a merchant of Ghaziabad stating the terms, on which he is willing to do business. It was held that the letter was a mere statement of intention and not an offer. [Devidatt vs. Shriram]

Example III: A notice that the goods stated in the notice will be sold by tender does not amount to an offer to sell. [Spencer vs. Harding]

Example IV: An auctioneer advertised in a newspaper that a sale of office furniture will be held on a particular day. Mr X, with the intention to buy furniture came from a distant place for the auction but the auction was cancelled. It was held that Mr X cannot file a suit against the auctioneer for his loss of time and expenses because the advertisement was merely a declaration of intention to hold auction and not an offer to sell. [Harris vs. N. Nickerson]

4. **Different from an Invitation to Offer:** An offer must be distinguished from an invitation to offer. In case of an invitation to offer, the person making an invitation invites others to make an offer to him. It is prelude to an offer inviting negotiations or preliminary discussions.

Example I: Goods were displayed in the shop for sale with price tags attached on each article and self service system was there. One customer selected the goods. It was held that the display of goods was only an intention to offer and the selection of the goods was an offer by the customer to buy and the contract was made when the cashier accepted the offer to buy and received the price. [Pharmaceutical Society of Great Britain vs. Boots Cash Chemists Ltd.]

Example II: A prospectus issued by a company for subscription of its shares and debentures is only an invitation to general public to make an offer to buy the shares/debentures which may or may not be accepted by the company.

Similarly, an advertisement inviting quotations of lowest price in response to an enquiry amounts to invitation to offer but not an offer capable of acceptance, e.g. in Harvey vs. Facie (1893), X sent a telegram to Y asking "Will you sell us Bumper Hall Penn? Telegraph Lowest Cash Price." Y replied through a telegram "Lowest Price for Bumper Hall Penn £900: X replied telegraphically stating "We agree to buy Bumper Hall Penn for £900 asked by you". Held, the quotation of price by Y was a mere invitation to offer. Consent of X to purchase the estate for £900 was an offer.

5. **Communication:** An offer must be communicated to the person to whom it is made. An offer is complete only when it is communicated to the offeree. One can accept the offer only when he knows about it. Thus, an offer accepted without its knowledge does not confer any legal rights on the acceptor.

Example I: G sent his servant L to trace his lost nephew. When the servant had left, G announced a reward of Rs 500 to anyone who traces the missing boy. L found the boy and brought him home. When L came to know about reward, he filed a suit against G to recover the reward. It was held that L was not entitled to the reward because he did not know about the reward when he found the missing boy. [Lalman Shukla vs. Gauri Dutt]

Example II: S offered a reward to anyone who traces his lost dog. F brought the dog without knowledge of the offer of reward. It was held that F was not entitled to the reward because F cannot be said to have accepted the offer which he did not know. [Filch vs. Snedakar].

6. **No Term the Non-compliance of which Amounts to Acceptance**: The offer must not contain a term the non-compliance of which would amount to acceptance. It means that while making the offer, the offerer cannot say that if offer is not accepted before a certain date, it will be presumed to have been accepted.

Example: X writes a letter to Y. I offer to sell my car for Rs 1,00,000. If I do not receive your reply by Friday next, I shall assume that you have accepted the offer. Here if Y does not reply, it does not mean that he has accepted the offer.

7. **Communication of Special Terms or Standard Form Contracts**: The special terms of the offer must also be communicated along with the offer. If the special terms of the offer are not communicated, the offeree will not be bound by terms. The question of special terms arises generally in case of standard form contracts. Standard contracts are made with big companies such as insurance companies, railways, shipping companies, banking companies, hotel companies, cleaning companies. Since such companies are in position to exploit the weakness of general public by including certain terms in the contract which may limit their liabilities, it is provided that the special terms of the offer must be brought to notice of general public.

Example I: X purchased a steamer ticket for travelling from Dablin to White Haven and on the back of the ticket, certain conditions were printed one of which excluded the liability of the company for loss, injury or delay to the passengers or his luggage. X never looked at the back of the ticket and there was nothing to draw his attention to the conditions printed on the back. His luggage was lost due to the negligence of the servants of the shipping company. It held that X was entitled to claim compensation for the loss of his luggage in spite of the exemption clause because there was no indication on the face of the ticket to draw his attention to the special terms printed on the back of the ticket. [Handerson vs. Stevenson]

Notes:

i. In case the special conditions are printed in a language which the offeree does not understand, it is the offeree's duty to ask for the translation of the condition before accepting the offer and if he does not ask, it shall be presumed that he knows them and he will be bound by them.

ii. The special terms and conditions must be brought to the knowledge of the offeree before the contract is concluded and not afterwards. A subsequent communication will not bind the acceptor unless he himself agrees thereto. For example, Mr X and Mrs X hired a room in hotel for a week. When they entered the room, they found a notice on the wall disclaiming the owner's liability for damages, loss or theft of articles. Some of their items were stolen. It was held that owner was liable because the notice was not a part of the contract as it came to the knowledge of the customer after the contract was entered into. [Olley vs. Marlborough Court Ltd.]

iii. The special terms and conditions must be reasonable. What is reasonable is a question of facts. If terms and conditions are unreasonable, the other party will not be bound by them. For example, if a dry cleaner limits his liability to 25% of the market price of the article in case of loss, the customer will not be bound by this condition because it means that the dry cleaner can purchase garments at 25% of the market price. In Lily White Drycleaners vs. Munnuswamy AIR 1966 (Mad.), the receipt issued by the drycleaner stated that the drycleaner would be liable only to the extent of 10 times the dry-cleaning charges in the event of any damage to the clothes. Held, such a clause was unreasonable and opposed to public policy, and therefore, couldn't bind the parties.

1.2.3 MEANING OF CROSS OFFERS

Two offers which are similar in all respects made by two parties to each other, in ignorance of each other's offer are known as "cross offers". Cross offers do not amount to acceptance of one's offer by the other. Hence, no contract is entered into on cross offers.

Example: X of Agra sends a letter by post to Y of Delhi offering to sell his car for Rs 1 lakh. The letter is posted on 1st January and the same day, Y of Delhi sends a letter by post to X of Agra offering to buy X's car for Rs 1 lakh. These two letters cross each other. Y's letter is merely an offer and not the acceptance of X's letter. Here, both the parties are making offer and no party has accepted the offer. Therefore, no contract has been entered into. If they want to enter into a contract, at least one of them must send his acceptance to the offer made by the other.

1.2.4 MEANING OF STANDING OFFER

An offer of a continuous nature is known as "standing offer". A standing offer is in the nature of a tender. It is the same thing as an invitation to an offer. A contract is said to have been entered into only when an order is placed on the basis of the tender.

Example: X Ltd. requires a large quantity of certain goods during the 12 months period and gives an advertisement inviting tender in the leading newspaper. Z submitted the tender to supply those goods at a specific rate. Z's tender is accepted or approved. Now, Z's tender becomes a standing offer. Each order given by X Ltd. will be an acceptance of the offer.

1.2.5 ACCEPTANCE

Meaning of Acceptance

Acceptance means giving consent to the offer. It is an expression by the offeree of his willingness to be bound by the terms of the offer. According to Section 2(b) of the Indian Contract Act, 1872, "A proposal is said to be accepted when the person to whom the proposal is made signifies his assent thereto. A proposal when accepted becomes a promise."

In other words, an acceptance is the consent given to offer.

Example: X offers to sell his car to Y for Rs 1,00,000. Y agrees to buy the car for Rs 1,00,000. Y's act is an acceptance of X's offer.

Who Can Accept?

In general, an offer can be accepted only by the person or persons to whom it is made. The specific answer to this question can be given with reference to type of offer as under:

i. In Case of Specific Offer: An offer made to a definite person or particular group of persons (called specific offer) can be accepted only by that definite person or that particular group of persons to whom it has been made and none else.

Example: X sold his business to Y but this fact was not known to an old customer Z. Z placed an order for certain goods to X by name. Y supplied those goods to Z. It was held that there was no contract between Y and Z because Z never made any offer to Y. [Boulton vs. Jones]

ii. In Case of General Offer: An offer made to the world at large or public in general (called general offer) can be accepted by any person having knowledge of the offer by fulfilling the terms of the offer.

Example: A Company advertised that it would pay $100 to anyone who contracts influenza after using the smoke balls of the company according to the printed directions. Mrs Carlil used the smoke balls according to the printed directions but subsequently she contracted influenza. She filed a suit for the reward. It was held that she was entitled to recover the reward because she had accepted the offer by complying with the terms of the offer. [Carli vs. Carbolic Smoke Ball Company]

How to Make Acceptance?

Like an offer, an acceptance may also be either an “implied acceptance” or “express acceptance”.

a. Express Acceptance: An express acceptance is one which is made by words spoken or written.

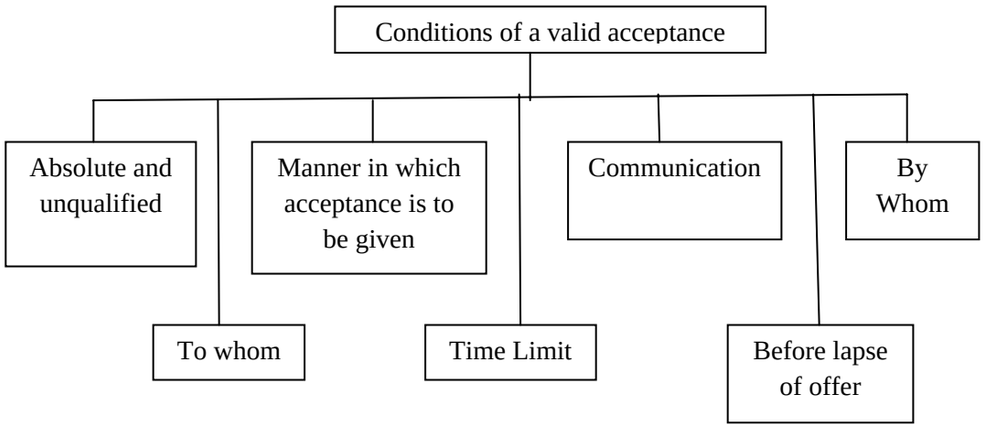
Example: X says to Y, “Will you purchase my car for Rs 1,00,000?”. Then Y says, “I am ready to purchase your car for Rs 1,00,000.”

b. Implied Acceptance: An implied acceptance is one which is made otherwise than in words. In other words, it is inferred from the conduct of the person or the circumstances of the particular case.

Example: A transport company runs buses on different routes to carry passengers. X, a passenger boards the bus. X’s act is an implied acceptance by X and he is bound to pay the fare.

1.2.6 LEGAL RULES FOR A VALID ACCEPTANCE

An acceptance to be valid must fulfil certain conditions which are as follows:



1. **Absolute and Unqualified**: According to Section 7(1) of the Indian Contract Act, 1872, "In order to convert a proposal into a promise, the acceptance must be absolute and unqualified." It means that an offer must be accepted as it is without any reservation, variation or condition. A qualified and conditional acceptance amounts to marking of a counter offer which puts an end to the original offer and it cannot be revived by subsequent acceptance.

Example I: X offered to sell his car for Rs 1,00,000 to Y. B agreed to buy it for Rs 90,000. V's act is a counter offer and not an acceptance of X's offer. Now, if Y accepts the original offer to buy the car for Rs 1,00,000, X will not be bound to sell the car because V's counter offer has put an end to the original offer. [Nihal Chand vs. Amar Nath]
Example II: X offered to sell two plots of land to Y at a certain price. Y accepted the offer for one plot. It was held that the acceptance was not valid because it was not for the whole of the offer. [Bhawan vs. Sadula]

2. **Manner**: According to Section 7(2) of the Indian Contract Act, 1872, the acceptance of an offer must be given in the following manner.

(a) If the proposal does not prescribe the manner in which it is to be accepted.	The offer must be accepted in some usual and reasonable manner.
(b) If the proposal prescribes the manner in which it is to be accepted.	The offer must be accepted in the prescribed manner.

The consequences of not accepting the offer in the prescribed manner: If the offer is not accepted in the prescribed manner, the offerer may approve or reject such acceptance. If the offerer wants to reject it, he must inform the acceptor within a reasonable time that he

is not bound by acceptance because it is not in the prescribed manner. If he does not do so within a reasonable time the presumption will be that he doesn't mind the offer being accepted in a different mode and will be bound by such acceptance.

Example: X of Agra sends a letter by post to Y of Delhi offering to sell his car for Rs 1,00,000 and also writes "send your acceptance by telegram." Y sends his acceptance by an ordinary letter. X can reject such acceptance on the ground that it was not accepted in the prescribed manner. But if he does not inform Y within the reasonable time, he shall be deemed to have accepted such acceptance and a valid contract will be formed between X and Y.

3. **Communication:** The acceptance must be signified (i.e. indicated or declared). In other words, the acceptance is complete only when it has been communicated to the offerer. A mere mental determination to accept is no acceptance in the eyes of law unless there is some external manifestation of that determination by words or conduct.

Example: X offered to supply coal to a Railway Company. The manager of the company accepted the offer and put it in the drawer of his table and forgot all about it. It was held that no contract was made because acceptance was not communicated. (Brogden vs. Metropolitan Railway Co.]

Note:

In case of acceptance made by post, the proposer becomes bound by the acceptance as soon as the properly addressed and stamped letter of acceptance is duly posted even if such letter of acceptance is lost or delayed in post.

4. **By Whom:** Acceptance must be communicated by the offeree himself or by a person who has the authority to accept. In other words, if acceptance is communicated by an unauthorised person, it will not give rise to legal relations.

Example: P applied for the post of a headmaster in a school. The managing committee passed a resolution approving P to the post but this decision was not communicated to P. But one member of the managing committee in his individual capacity and without any authority informed P about the decision. Subsequently, the managing committee cancelled its resolution and appointed someone else. P filed a suit for breach of contract. It was held that P's suit was not maintainable because there was no communication of acceptance as he was not informed about his appointment by some authorised person. [Powell vs. Lee]

Note:
The communication of acceptance is not necessary in case of unilateral contracts where the offerer prescribed a particular mode of acceptance. In such cases, it is sufficient if that prescribed mode is followed as in case of Carlil vs. Smoke Ball Co. and Har Bhajan Lal v. Harcharn Lal.

5. **To Whom**: Acceptance must be communicated to the offerer himself. In other words, if acceptance is communicated to an unauthorised person, it will not give rise to legal relations.

Example: F offered by a letter to buy his nephew's horse for $30 saying "If I hear no more about him, I shall consider the horse mine." The nephew sent no reply at all but told B his auctioneer, not to sell that particular horse as he intended to sell that horse to F. B sold the horse by mistake. It was held that F will not succeed because his nephew had not communicated acceptance to him. [Felthouse vs. Bindley]

6. **Time Limit:** The acceptance must be given within the time prescribed (if any) or within a reasonable time (if no time is prescribed). What is reasonable time depends upon the facts and circumstances of the case.

Example: An offer to buy shares of a company was made in June but the acceptance was communicated in November, it was held that the offerer was not bound by the acceptance because the acceptance was not given within a reasonable time. [Ramsgate Victoria Hotel Co. vs. Montefiore]

7. **Before Lapse of Offer:** The acceptance must be given before the offer lapses or is withdrawn. In other words, if an acceptance is made after the lapse or withdrawal of the offer, it will not give rise to legal relations.

Example: X offered by a letter to sell his car for Rs 1,00,000. Subsequently, X withdrew his offer by a telegram which was duly received by Y. After the receipt of telegram, Y sent his acceptance to X. In this case, the acceptance is invalid because it was made after the effective withdrawal of the offer.

1.2.7 COMMUNICATION OF OFFER AND ACCEPTANCE

The communication of offer and acceptance must complete so as to bind the concerned parties because as soon as the communication is complete the parties loose the right of withdrawal or revocation. The legal provisions relating to the communication of offer and acceptance are as under:

i. **Communication of Offer**: The communication of offer is complete when it comes to the knowledge of the person to whom it is made. In case an offer is made by post, its communication will complete when the letter containing the offer reaches the offeree.

Example: X of Agra sends a letter by post to Y of Delhi offering to sell his car for Rs 1,00,000. The letter is posted on 1st January and this letter reaches on 7th January. The communication of the offer is complete on 7th January.

Note:

An offer accepted without its complete communication does not bind the offeror.

Example: In case of Lalman vs. Gauri Duff, G sent his servant L to trace his lost nephew. When the servant had left, G announced a reward to anyone who traces the boy. L found the boy and brought him home. When L came to know of the reward, he claimed the reward. It was held that L was not entitled to the reward because he did not know about the offer when he found the missing boy.

ii. **Communication of Acceptance**: The communication of acceptance is complete at different times for the proposer and acceptor. The rules regarding the Communication of acceptance are as under:

The communication of acceptance is complete ...	*When does the communication of acceptance complete...*
i. As against the proposer	When it is put in a course of transmission to him, so as to be out of the power of the acceptor. In case of acceptance made by post, the proposer becomes bound by the acceptance as soon as the properly addressed and stamped letter of acceptance is duly posted even if such letter of acceptance is lost or delayed in post.
ii. As against the acceptor	When it comes to the knowledge of the proposer. In case of acceptance made by post, the acceptor becomes bound by the acceptance only when the letter of acceptance is actually received by proposer.

Note:

The time gap between the date on which the letter of acceptance is posted and the date on which the letter of acceptance is received by the proposer, can be utilized by the acceptor to withdraw his acceptance by a speedier mode of communication so that the revocation notice reaches the proposer before the letter of acceptance.

Example: X of Agra sends a letter by post to Y of Delhi offering to sell his car for Rs 1,00,000. The letter is posted on 1st January and this letter reaches Y on 7th January. Y sends his acceptance by post on 10th January but X receives this letter of acceptance on

15th, January. In this case the legal position relating to the communication of offer and acceptance is as under:

Communication	*When does the communication complete*	*Reason*
i.Communication of offer	7th Jan.	The letter containing the offer reaches the offeree on 7th Jan.
ii.Communication of acceptance as against the proposer	10th Jan.	The letter of acceptance is posted on 10th Jan.
iii. Communication of acceptance as against the acceptor	15th Jan.	The letter of acceptance is received by the proposer on 15th Jan.

After posting the letter of acceptance on 10th January, Y can withdraw his acceptance by a speedier mode of communication so that the revocation notice reaches the proposer before the letter of acceptance.

Contracts over telephone/telex/fax:
A contract by telephone/telex/fax is treated on the same principle as an oral agreement made between two parties when they are face to face with each other. In such cases, the contract will complete only when the acceptance is received by the proposer and not when it is transmitted by the acceptor. Therefore, the acceptor must ensure that his acceptance is properly received by the proposer.

Example: X made an offer to Y over telephone. While Y was conveying his acceptance, the line went dead and X could not hear anything. In this case, there was no contract at that moment.

Note:
In case of contracts over telephone, telex or fax, the question of revocation (i.e. withdrawal of acceptance) does not arise because there is instantaneous communication of the offer and its acceptance (i.e. the offer is made and accepted at the same time).

1.2.8 REVOCATION OF OFFER AND ACCEPTANCE

Meaning of Revocation:

The term ‘revocation’ means ‘taking back’ or ‘withdrawal’.

Time Limit within which Offer can be Revoked [Section 5]:

According to Section 5 of the Indian Contract Act, a proposal may be revoked at any time before the communication of its acceptance is complete as against the proposer, but not afterwards. We know that communication of acceptance is complete as against the proposer when a properly addressed and stamped letter of acceptance is duly posted by the acceptor. Hence, an offer can be revoked at any time before the letter of acceptance is duly posted by the acceptor. Thus, the proposer may revoke his offer by a speedier mode of communication which will reach before the letter of acceptance is posted by the acceptor.

Example: X of Agra offers by a letter dated 1st January sent by post to sell his car to Y of Delhi for Rs. 1,00,000. Y accepts the offer on 7th January at 1 p.m. by letter sent by post. Here, X may revoke his offer at any time before 1 p.m. on 7th Jan. but not afterwards.

Notes:

i. Revocation must always be expressed.
ii. Revocation must move from the offerer himself or a duly authorised agent.
iii. Notice of revocation of a general offer must be given through the same channel by which the original offer was made.
iv. Offer cannot be revoked even if the letter of acceptance is lost or delayed in transit.

Time Limit within which Acceptance can be Revoked [Section 5]:

According to Section 5 of the Indian Contract Act, "An acceptance may be revoked at any time before the communication of the acceptance is complete as against the acceptor, but not afterwards." We know that communication of acceptance is complete as against the acceptor when the letter of acceptance is actually received by the proposer. Hence, an acceptance can be revoked at any time before the letter of acceptance is actually received by the proposer. Thus an acceptor may revoke his acceptance by a speedier mode of communication which will reach before the letter of acceptance is received by the proposer.

Example: X of Agra offers by a letter dated 1st January sent by post to sell his car to Y of Delhi for Rs 1,00,000. Y accepts the offer on 7th Jan. at 1 p.m. by a letter sent by post. X receives the letter of acceptance on 15th Jan. at 3 p.m. Here, Y may revoke his acceptance at any time before 3 p.m. on 15th Jan. but not afterwards.

Acceptance is to Offer what a Lighted Match is to a Train of Gunpowder:

The position relating to revocation of proposal and acceptance has been described by Anson in the following words,
"Acceptance is to offer what a lighted match is to a train of gunpowder. It produces something which cannot be recalled or undone."

This statement primarily holds good under English law.

Here, gunpowder = offer and lighted match = acceptance

When a lighted match is shown to a train of gunpowder, it explodes and something happens which cannot be undone. Similarly, an offer once accepted cannot be revoked. But so long a lighted match is not shown, the gunpowder remains inert and can be removed, similarly an offer can be revoked before it is accepted.

Similarly, once acceptance is given it cannot be revoked. But under Indian Contract Act, acceptance can be revoked by resorting to quicker means of communication so that the offerer learns about it before acceptance. Thus, the above statement doesn't hold in relation to revocation of acceptance under Indian law.

Simultaneous Delivery of Letter of Acceptance and the Telegram containing Revocation of Acceptance:

In case the letter of acceptance and the telegram containing revocation of acceptance are delivered to the proposer at the same time, the formation of contract depends upon the fact which one is read first by the offerer. The contract shall be said to have been formed if the letter of acceptance is read first but shall not be said to have been formed if the telegram containing revocation of acceptance is read first. Generally, it is presumed that a man of ordinary prudence will first read the telegram. Hence the revocation will be quite effective.

No Revocation in case of Contract over Telephone or Telex of Fax:

In case of contracts over telephone or telex or fax, the question of revocation does not arise because there is instantaneous communication of the offer and its acceptance (i.e. the offer is made and accepted at the same time).

Communication of Revocation [Section 4]:

The communication of revocation is complete at different times for person who makes it and the person to whom it is made. The rules regarding the communication of revocation are as under:

The communication of revocation is complete ...	*When does the communication of revocation complete ...*
(i) As against the person who makes it	When it is put in a course of transmission to the person to whom it is made so as to be out of the power of the person who makes it.
(ii) As against the person to whom it is made	When it comes to his knowledge.

Example: X proposes by letter to sell his car to Y for Rs 1,00,000. Y accepts X's proposal by a letter sent by post. If X revokes his proposal by telegram, the revocation of offer is complete as against X when the telegram is dispatched and it is complete as against Y when Y receives the telegram. If Y revokes his acceptance by telegram, the revocation of acceptance is complete against Y when the telegram is despatched and as against X when it reaches him.

Lapse of an Offer:

An offer must be accepted before it lapses (i.e. comes to an end). An offer may come to end in any of the following ways:

1. **By Revocation**: An offer lapses if the offerer revokes the offer before its acceptance by the offeree. According to Section 5 of the Indian Contract Act, a proposal may be revoked at any time before the communication of acceptance is complete as against the proposer but not afterwards.

Example I: X of Agra offers by a letter dated 1st January sent by post to sell his car to Y of Delhi for Rs 1,00,000. Y accepts the offer on 7th January at 1 p.m. by a letter sent by post. Here, X may revoke his offer at any time before 1 p.m. on 7th Jan. but not afterwards.

Example II: At an auction sale, the highest bidder can revoke his offer to buy before the fall of the hammer.

2. **By Lapse of Time:** An offer lapses if it is not accepted within the fixed time (if any prescribed in the offer) or within reasonable time (if no time is prescribed in the offer).

Example: An offer to buy shares of a Company was made in June but the acceptance was communicated in November. It was held that offer to buy shares had lapsed because it was not accepted within a reasonable time. [Ramsgate Victoria Hotel Co. vs. Montefiore]

3. **By Death or Insanity of the Offeror or Offeree**: An offer lapses by the death or insanity of the offeror if the fact of his death or insanity comes to the knowledge of the acceptor before he makes his acceptance. In other words, if the offer is accepted in ignorance of the death or insanity of the offeror, there will be a valid contract. It may be noted that in English law the death of the offeror terminates the offer even if acceptance is made in ignorance of the death.

An offer also comes to an end by the death or insanity of the offeree if the offeree dies or becomes insane before accepting the offer because an offer can be accepted only by the offeree and not by any other person.

4. **By Failure to Accept Condition Precedent**: An offer lapses if it is accepted without fulfilling the conditions of the offer.

Example: X offered to sell his car to Y for Rs 1,00,000 subject to the condition that Y should pay an advance of Rs 20,000 before a certain date. Y accepted the offer but did not send an advance of Rs 20,000. In this case, the offer has lapsed because the advance was not paid.

5. **By Counter Offer**: An offer lapses if the counter offer is made because a counter offer amounts to rejection of the original offer. Counter means making a fresh offer instead of accepting the original offer.

Example: X offered to sell his car to Y for Rs 1,00,000. Y said that he would buy it for Rs 90,000. X refused to sell for Rs 90,000. Subsequently, Y offered to buy the car for Rs 1,00,000. Here, V's offer to buy for Rs 90,000 is a counter offer which terminates the original offer. V's second offer to buy for Rs 1,00,000 is a fresh offer and not an acceptance of the original offer. [Hyde vs. Wrench)

6. **By not Accepting in the Prescribed Mode or Usual Mode:** An offer if it is not accepted in the specific manner (if any, prescribed in the offer) or in some usual and reasonable manner (if no manner has been prescribed in the offer).

Example: X offered to sell his car to Y for Rs 1,00,000 and wrote to Y "Send your acceptance by telegram." Y sent acceptance by an ordinary letter. X can reject such acceptance.

7. **By Rejection of Offer by Offeree**: An offer lapses if it is rejected by the offeree. An offer is said to be rejected if the offeree expressly rejects it or accepts it subject to certain conditions. It may be noted that once an offer is rejected, it cannot be revived subsequently.

8. **By Subsequent illegality or Destruction of Subject Matter of the Offer:** An offer lapses if it becomes illegal or the subject matter is destroyed before its acceptance by offeree.

Example I: X of Delhi offered supply of 100 tons of sugar to Y at Mumbai on a certain date. Before this offer is accepted by Y, the Central Government issued an order prohibiting the inter-state movement of sugar. Here, X's offer has come to an end.

Example II: X of Delhi offered to sell his car to Y of Agra for Rs 1,00,000. Before the offer is accepted by Y, the car is destroyed by fire. Here X's offer has come to an end.

Check your progress – 2

Explain Offer, Acceptance and Revocation

LESSON-3

CAPACITIES OF PARTIES

CONTENTS

According to Section 11 of the 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." Thus, all the three tests (viz. age, soundness, disqualification) must be applied to determine whether a person is competent to contract or not.

Position of agreements with a Minor:

A minor is a person who has not attained majority. According to Section 3 of the Indian Majority Act, 1875, a person is deemed to have attained majority as under:

(a) Where a guardian of a minor's person or property is appointed under the Guardian and Wards Act, 1890	On completion of 21 years
(b) Where minor's property has passed under the superintendence of the court of wards	On completion of 21 years
(c) In other cases	On completion of 18 years

1.3.1 POSITION OF AGREEMENTS BY MINOR

The law protects minor's rights because they are not mature and may not possess the capacity to judge what is good and what is bad for them. The position of agreements with or by a minor may be summarised as under:

1. **Validity:** An agreement with a minor is void ab-initio [Leading case Law Mohiri Bibee vs. Dhannodas Ghosh]

   D, a minor borrowed a sum from M by executing a mortgage of his property in favour of M. Subsequently, D sued for setting aside the mortgage. The Privy Council held that Sections 10 and 11 of the Indian Contract Act make the minor's agreement void and therefore the mortgage was not valid. M prayed for refund of the amount by the minor. It was held that the money advanced to minor cannot be recovered because minor's agreement was void.

2. **No Estoppel**: A minor is not estopped from setting up the plea of minority.
   He may plead infancy to escape from being liable. In G. Bhimappa Meti vs. Balangowda Bhimangowda; the Bombay High Court held that "Where an infant represents fraudulently or otherwise that he is of age and thereby induces another to enter into a contract with him, he in an action founded on the contract, is not estopped from setting up infancy."

3. **In case of fraudulent representation of age by minor:** According to Sections 30 and 33 of the Specific Relief Act, 1963, in case of a fraudulent misrepresentation of his age by the minor inducing the other party to enter into a contract, the court may award compensation to the other party. The Lahore High Court in Khan Cui vs. Lakha Singh held that where the contract is set aside, the status quo ante should be restored and the court may direct the minor on equitable grounds to restore the money or property to the other party if the money or property could be traced.

4. **Ratification on attaining the age of majority**: An agreement with a minor cannot be ratified even after he attains majority. Ratification relates back to the date of the making of the agreement and therefore an agreement which was then void cannot be made valid by subsequent ratification. In Indran Ramaswamy vs. Anthaoppa, a person on attaining majority, gave a promissory note in satisfaction of one executed by him for money borrowed when he was a minor. It was held that the claim under the promissory note could not be enforced because there was no consideration.

5. **Validity of minor's agreement jointly with a major person**: The agreements made by a minor jointly with a major person are void vis-a-vis the minor but can be enforced against the major person who has jointly promised to perform.

6. **Minor as a partner**: A minor cannot become a partner in a partnership firm.

   However, according to Section 30 of Indian Partnership Act 1932, with the consent of all the partners for the time being be admitted to the benefits of partnership. In other words, he can share the profits without incurring any personal liability.

7. **Minor as an agent:** A minor can act as an agent and bind his principal by his acts without incurring any personal liability.

8. **Minor as a shareholder or member of a company:** A minor can become a shareholder or member of a Company if
(a) the shares are fully paid up and
(b) the articles of association do not prohibit so.

9. **Minor as an insolvent**: A minor cannot be declared insolvent because he is not competent to contract.

10. **Contract for the benefit of a minor:** A minor can be a promisee. In Raghva Chariar vs. Srinivasa, the Madras High Court held that a mortgage executed in favour of a minor who has advanced the mortgage money is enforceable by him or by any other person on his behalf. Similarly, in case of sale of goods by a minor, he is entitled to recover the price from the buyer. Thus, he may be a promisee but not promisor on a promissory note or a drawer but not drawee on a bill of exchange.

11. **Contract by minor's guardian:** The contracts entered into on behalf of a minor by his guardian or manager of his estate can be enforced by or against the minor if the contract
(a) is within the scope of the authority of guardian or manager, and
(b) is for the benefit of the minor. [Subramanyam vs. Subba Rao].
It may also be noted that his guardian cannot enter into a valid contract for purchase of the immovable property for his/her service.

12. **Contract for supply of necessaries:** A person who has supplied the necessaries to a minor or to those who are dependent on him is entitled to be reimbursed from the property of such minor. [Section 68].
Meaning of necessaries: The term necessaries includes articles required to maintain a particular person in the state, degree and station in life in which he is. According to Section 2 of English Sale of Goods Act, the necessaries mean the goods which are suitable to the condition in life of a minor and to his actual requirement at the time of sale and delivery. In India, food, clothing, shelter, education arid marriage of a female has been held to be necessaries. Section 68 covers the reimbursement for the supply of such items or loans for the same.

Example:
In case of Nash vs. Inman, a minor bought eleven fancy coats from N for his own use. It was held that eleven coats at a time cannot be a necessity.

Section 68 also covers the rendering of necessary services to a minor.
For example, the lending of money to a minor for the purpose of defending him in prosecution is deemed to be a service rendered to the minor.

'*Claim against property and not against person*': A claim for the payment of necessaries supplied can be made against the minor's property and not against the minor personally. In other words, a minor cannot be asked to expend labour in exchange.

Liability of minor's guardian: The parent or guardian of a minor cannot be held liable unless those goods/services are supplied/rendered to a minor as the agent of the parent or guardian.

13. **Minor's liability in Tort:** A minor may be held liable in Tort (civil wrong).
But if in the course of doing what he is entitled to do under the contract, he is found guilty of negligence, he cannot be made liable on tort if he is not liable on the contract, e.g. in Burnard vs. Huggis, a minor hired a horse promising not to jump it. He lent the horse to his friend who used the horse against the instructions and this led to the death of the horse. The minor was held liable on Tort. But in another case a horse was hired for riding. The horse was injured due to over-riding. The minor could not be held liable since the injury resulted from negligence in the course of what he was entitled to do under the contract. Since he was not liable on the contract himself, he could not be held liable in tort too. (Jennings vs. Randal].

1.3.2 POSITION OF PERSONS OF UNSOUND MIND

Who is a Person of Unsound Mind?

According to Section 12 of the Indian Contract Act, "A person is said to be of sound mind for the purpose of making a contract, if at the time when he makes it, is capable-

(a) to understand the terms of the contract,

(b) to form a rational judgment as to its effect upon his interests."

Thus, if a person is not capable of both, he is said to have suffered from unsoundness of mind. The examples of persons having an unsound mind include idiots, lunatics and drunken persons. A person who is so mentally deficient by birth as to be incapable of ordinary reasoning or rational conduct is said to be an "idiot". A person affected by lunacy is said to be "lunatic'. A person can become lunatic at any stage of his life.

Position of a Person who is Usually of Unsound Mind but Occasionally of Sound Mind:

According to Section 12, "A person who is usually of unsound mind but occasionally of sound mind may make a contract when he is of sound mind."

Example: A patient in a lunatic asylum who is at intervals of sound mind may contract during those lucid intervals.

Position of a Person who is Usually of Sound Mind but Occasionally of Unsound Mind:

According to Section 12, "A person who is usually of sound mind but occasionally of unsound mind may not make a contract when he is of unsound mind."

Example: A sane man who is so drunk that he cannot understand the terms of a contract or form a rational judgment as to its effect on his interest, cannot enter into contract whilst such drunkenness lasts.

Burden of Proof:

The rules regarding the burden of proof are summarised as under:

Case	*The burden of proof lies on ...*
i. Where a person is usually of sound mind	The burden of proving that he was of unsound mind at the time of contract lies on the person who challenges the validity of contract
ii. Where a person is usually of unsound mind	The burden of proving that he was of sound mind at the time of contract lies on the person who affirms it
iii. In case of drunkenness or delirium from fever or other causes	The burden of proving that he was delirious from fever or was so drunk at the time of contract, lies on the person who challenges the validity of the contract

Position of Agreements with Persons of Unsound Mind:

Persons of unsound mind	*Capacity to enter into contract*
1.Lunatic (i.e. a person who is mentally deranged due to some mental strain or other personal experience but who has some lucid intervals of sound mind) (a) While he is of unsound mind (b) While he is of sound mind	He cannot enter into any contract. Any agreement entered into by him during this period is altogether void and he cannot be held liable thereon. He can enter into a valid contract and he is liable for such contracts.
2.Idiots (i.e. a person who is permanently of unsound mind)	He cannot enter into any contract. Any agreement entered into by him is altogether void and he is not liable thereon.
3.Drunken person (i.e. a sane person who is delirious from fever or who is so drunk that he cannot understand the terms of a contract or form a rational judgment as to its effect on his interest)	He cannot contract while such delirium or drunkenness lasts.

1.3.3 PERSONS DISQUALIFIED BY LAW

Besides minors and persons of unsound mind, there are others who are disqualified from contracting under the provision of some other laws.

1. Alien Enemy:

An alien is a person who is the citizen of a foreign country. An alien may either an alien friend or an alien enemy.
An alien whose country is at peace with the Republic of India is called as alien friend. He has usually the full contractual capacity.

An alien whose country is at war with the Republic of India is called an alien enemy. His contractual capacity can be summarised as under:

Position of contracts entered during the war	An alien enemy can neither enter into any contract nor can be sued in an Indian Court except by licence from the Central Governnment.
Position of contracts entered into before the war a. If such contracts are against the public policy or are such that may benefit the enemy b. If such contracts are not against public policy	a. Such contracts stand dissolved b. Such contracts are merely suspended for the duration of the war and revived after the war is over unless they have already become time barred under the Law of Limitation Act.

Example:
X, an Indian, carries on a business in Pakistan. He enters into a contract with Y who carries on business in India. Immediately after the formation of the contract, a war broke out between India and Pakistan. In this case, X becomes an alien enemy though he is Indian and the contract between X and Y (if not against the public policy) will be suspended for the duration of the war and revived after the war is over.

2. Foreign Sovereigns and Ambassadors:
They can enter into contracts and enforce those contracts in our courts but they cannot be sued in our courts without the sanction of the Central Government unless they choose to submit themselves to the jurisdictions of our Courts.

Notes:

(i) An ex-king can be sued in our Courts.

(ii) Where a foreign sovereign etc. enter into a contract through an agent residing in India, the agent shall be held liable on the contract.

3. Convicts:

A person is called a convict during his period of sentence. His contractual capacity is summarised as under:

1. During the period of sentence	He cannot enter into any contract.
2. After the expiration of the period of sentence or when he is on parole.	He can enter into a contract. He can sue on a contract.

4. Company under the Companies Act or Statutory Corporation under the Special Act of Parliament:

The contractual capacity of the company and the statutory corporation is summarised as under:

1. In case of a Company	Its contractual capacity is determined by the 'object clause' of its Memorandum of Association.
2. In case of Statutory Corporation	Its contractual capacity is determined by the statute creating it.

Any act done in excess of the power given is ultra vires (i.e. beyond power) and hence void.

5. Insolvents :

When a person's debts exceed his assets, he is adjudged insolvent and his property stands vested in the Official Receiver or Official Assignee appointed by the Court.

Such person-

(i) cannot enter into contracts relating to his property,

(ii) cannot sue,

(iii) cannot be sued

Note : When the insolvent is discharged, the aforesaid disqualification is removed.

Check your progress – 3:

Discuss ‘capacity to contract’.

LESSON-4

CONSIDERATION

CONTENTS

Consideration is one of the essential elements of a valid contract.

The term 'consideration' means something in return, i.e. quid-pro-quo. What is 'something' has been explained by Justice Lush J. in a leading English case Currie vs. Misa as under:

"A valuable consideration in the sense of the law, may consist either in some right, interest, profit or benefit accruing to one party or some forbearance, detriment, loss or responsibility given, suffered or undertaken by the other."

Thus, consideration must result in a benefit to the promisor, and a detriment or loss to the promisee or a detriment to both. Section 2(d) of the Indian Contract Act, 1872 defines consideration as under:

"When, at the desire of the promisor, the promisee or any other person has done or abstained from doing, or does or abstains from doing, or promises to do or abstain from doing something, such act or abstinence or promise is called a consideration for the promise."

Example I: X promises to deliver his good to Y and Y promises to pay Rs 1,000 on delivery. In this case, the consideration for each of these promises is as under:

For X's promise - Y's promise to pay Rs 1,000 on delivery
For Y's promise - X's promise to deliver his goods

Example II: X owes Y Rs 10,000. Y promises X not to file a suit against him for one year on X's agreeing to pay him Rs 500 more. In this case, the consideration for each of the promise is as under:

For X's promise - Forbearance on the part of Y to file a suit
For Y's promise - X's promise to pay Rs 500 more

1.4.1 ESSENTIAL ELEMENTS OF VALID CONSIDERATION

On the basis of definition of consideration as per Section 2(d), the essential elements of valid consideration are:

1. It must be given only at the Desire of the Promisor:

An act constituting consideration must have been done at the desire or request of the promisor. Thus, an act done at the desire of a third party or without the desire of the promisor cannot constitute a valid consideration.

Example I: A's son is lost and B goes in search for him. Can B claim remuneration from

A. (a) if B does this act voluntarily

(b) if B does this act at the request of A

(c) if B does this act at the request of C?

(a) if B does this act voluntarily?
B cannot claim remuneration from A because he has not done at A's request.

(b) if B does this act at the request of A?
B can claim remuneration from A because he has done at A's request.

(c) if B does this act at the request of C?
B cannot claim remuneration from A because he has not done at A's request.

Example II: X spent Rs 1,00,000 on the construction of shops at the request of the collector of the District. In consideration of this Y a shopkeeper promised to pay some money to X. It was held that this agreement was void being without consideration because X had constructed the shops at the request of collector and not at the desire of Y. [Ourga Prasad vs. Baldeo]

2. It may Move from any Person:

An act constituting consideration may be done by the promisee himself or any other person (i.e. stranger to consideration). Thus, it is immaterial who furnishes the consideration and therefore, may move from the promisee or any other person.

3. It may be Past or Present or Future:

The consideration may be past, present or future.

Past Consideration	The consideration which has already moved before the formation of agreement. Example: X renders some service to Y at Ys request in the month of May. In June, Y promises to pay X Rs 1,000 for his past services. Past services amount to past consideration. X can recover Rs 1,000 from Y.
Present Consideration	The consideration which moves simultaneously with the promise is called present consideration. Example: In case of cash sale, promise to pay the price and promise to deliver the goods are performed simultaneously.
Future Consideration	The consideration which is to be moved after the formation of agreement is called future consideration. Example: X promises to deliver certain goods to Y after 10 days and Y promises to pay after 10 days from the date of delivery.

4. It must be of Some Value:

The consideration need not be adequate to the promise but it must be of some value in the eye of the law. It is understood in the sense of something in return and that something can be anything, adequate or grossly inadequate. According to Explanation 2 of Section 25, an agreement to which the consent of the promisor is freely given is not void merely because the consideration is inadequate; but the inadequacy of the consideration may be taken into account by the Court in determining the question whether the consent of the promisor was freely given.

Example: A agrees to sell a horse worth Rs 1,000 for Rs 10. A denies that his consent to the agreement was freely given. The inadequacy of the consideration is a fact which the Court should taken into account in considering whether or not A's consent was freely given.

5. It must be Real and not lllusory:

The consideration must be real and not illusory.

Example I: X engages Y for doing a certain work and promises to pay reasonable remuneration. This promise is not enforceable because the consideration is uncertain.

Example II: X promises to put life into Y's dead wife and Y promises to pay Rs 1,00,000. This agreement is void because consideration is physically impossible to perform.

6. Something other than the Promisor's Existing Obligation:

The act constituting consideration must be something which the promisor is not already bound to do because a promise to do what a promisor is already bound to do adds nothing to the existing obligation.

Example I: X promises Y, his advocate, to pay an additional sum if the suit was successful. The suit was declared in favour of X but X refused to pay additional sum. It was held that Y could not recover additional sum because the promise to pay additional sum was void for want of consideration as Y was already bound to render his best services under the original agreement. [Ramchandra Chintamana vs. Kalu Raju]

Example II: X had received summons to appear before a court of law as witness on behalf of Y who promised to pay some money for his trouble. It was held that the promises to pay money were void for want of consideration because X was under a legal duty to appear as witness before court of law. [Collins vs. Godefroa]

7. Lawful:

The consideration must neither be unlawful nor opposed to public policy.

Example I: X promises Y to pay Rs 1,000 to beat Z, Y beats Z and claims Rs 1,000 from X, X refuses to pay. Y cannot recover because the agreement is void on the ground of unlawful consideration.

Example II: X promises Y to obtain an employment in the public service and Y promises to pay Rs 1,000 to X. The agreement is void on the ground of unlawful consideration.

1.4.2 STRANGER TO A CONTRACT

Though a stranger to consideration can sue because the consideration can be furnished or supplied by any person whether he is the promisee or not, but a stranger to a contract cannot sue because of the absence of privity of contract. (i.e., relationship subsisting between the parties to a contract).

Example I: X owes Y Rs 1,00,000 and sells his property to Z. Z promises to payoff X's debt to Y. Z fails to pay. Y cannot sue Z because he is a stranger to a contract.

Example II: X bought tyres from Dunlop Rubber Co. and sold them to Y, a sub-dealer who agreed with X not to sell below Dunlop's list price and to pay to Dunlop Co. Rs 150 as damages on every tyre he undersold. Y sold two tyres at less than the list price and

there upon, Dunlop Co. sued him for the breach. It was held that the Dunlop Co. could not maintain the suit because it was a stranger to the contract. [Dunlop P. Tyre Co. Ltd. vs. Self ridge & Co. Ltd.]

Exceptions

The rule that a stranger to a contract cannot sue, is subject to the following exceptions:

a. **In case of Trusts**:

The beneficiary (i.e. the person for whose benefit the trust has been created) may enforce the contract.

Example I: X transferred certain properties to be held by Y for the benefit of Z. Z can enforce the agreement even though he is not a party to the agreement. [M.K. Rapai vs. John]

Example II: X sent an insured parcel to Y. On loss of such parcel, Y sued the post office. It was held that Y was entitled to sue though he was stranger to the contract because on receipt of such article, the post office becomes a trustee for the addressee. [Amir Ullah vs. Central Govt.]

Example III: X, the father of a minor daughter D, and Y, the father of a minor son S, entered into an agreement of marriage for D and S on the condition that after the marriage, Y would pay his daughter-in-law D, Rs 500 as kharch-e-paan daan (betel box money). After the marriage took place, X died. On Y's refusal to pay the agreed amount to D, the Court held that D was entitled to recover the amount as a beneficiary of trust even if she was a stranger to the contract between X and Y. [Khwaja Mohd. vs. Hussaini Begum (1910) 37.1A 152]

b. In Case of Family Settlement:

The person for whose benefit the provision is made under family arrangements may enforce the contract.

Example: A provision of marriage expenses of a female member was made in a Joint Hindu Family. On partition, the female member sued for such expenses. It was held that she was entitled to sue. [Rakhmanbai vs. Govindj

c. Acknowledgement:

The person who becomes an agent of third party by acknowledgement or otherwise, can be sued by such third party.

Example: X receives Rs 1,000 from Y for paying the same to Z. X acknowledges this receipt to Z. Z can recover the amount from X because X will be regarded as Z's agent. [Surjan vs. Nanaf].

d. Assignment of a Contract:

Where a benefit under a contract has been assigned, the assignee can enforce the contract subject to all equities between the original parties to the contract e.g. the assignee of an insurance policy.

1.4.3 CONTRACTS WITHOUT CONSIDERATION

General Rule:

According to Section 10, consideration is one of the essential elements of a contract. According to Section 25, an agreement made without consideration is void. For example, X promises to pay Rs 5,000 to his girlfriend Y. This promise cannot be enforced by Y because she is not giving anything to X for this promise.

In Abdul Aziz vs. Mazum Ali, a promise to donate Rs 500 towards construction of a mosque was held unenforceable as it was a gratuitous promise lacking consideration. But gratuitous promise shall be enforceable by law if the promisee on the faith of such promise suffered a liability as suffering of detriment forms a valid consideration [Kedarnath vs. Gorie Mohd.]

Exceptions to the General Rule – 'No Consideration, No Contract'

The following are the exceptions to the general rule No Consideration, No Contract:

i. Agreements Made on Account of Natural Love and Affection [Section 25(1)]: Such agreement made without consideration is valid if:

a. it is expressed in writing,

b. is registered under the law,

c. it is made on account of love and affection, and

d. it is between parties standing in a near relation to each other.

Note: Nearness of relation by itself does not necessarily import love and affection.

Example I: A Hindu husband by a registered document promised to pay his wife Rs 1,000 per month as her pin-pocket money. This agreement is valid.

Example II: A Hindu husband by a registered document, after referring to quarrels and disagreements between himself and his wife, promised to pay his wife Rs 1,000 p.m. for her maintenance. It was held that this agreement was void because there was no natural love and affection. (Rajlakhi Devi vs. Bhoot Nath Mookherjee]

ii. Promise to Compensate [Section 25(2)]:

Such promise made without consideration is valid if:

a. it is a promise to compensate (wholly or in part); and

b. the person who is to be compensated has already done something voluntarily or has done something which the promisor was legally bound to do.

Example I: X finds Y's purse and gives it to him. Y promises to give Rs 500 to X. This is a valid contract even though the consideration did not move at the desire of Y, the promisor.

Example II: X, a neighbour helped putting down the fire in Y's house. Afterwards, Y promised X to give Rs 1,000. This is a valid contract even though the consideration did not move at the desire of the promisor.

Example III: X, supported Y's infant son. Y promised to pay X's expenses in so doing. This is a valid contract. Here, X has done that act which Y was legally bound to do.

iii. Promise to Pay Time Barred Debt [Section 25(3):

Such promise without consideration is valid if:

a. it is made in writing,

b. it is signed by the debtor or his agent, and

c. it relates to a debt which could not be enforced by a creditor because of limitation.

Note: According to the law of limitation, a debt which remains unpaid or unclaimed for a period of 3 years, becomes a time barred debt which is legally not recoverable. But a promissory note issued in personal capacity by the wife of a debtor to pay his time barred debt of her husband is not enforceable [Pestonjee vs. Bai Meharbai].

iv. Completed Gifts [Explanation to Section 25]:
The gifts actually made by a donor and accepted by the donee are valid even without consideration. Thus, a completed gift needs no consideration.

Example: X transferred some property to Y by a duly written and registered deed as a gift. This is a valid contract even though no consideration moved.

v. Agency [Section 185]:
No consideration is necessary to create an agency.

Check your progress – 4:

What is consideration?

LESSON-5

FREE CONSENT

CONTENTS

1.5.1 MEANING OF CONSENT

The consent means an act of assenting to an offer. According to Section 13, "Two or more persons are said to consent when they agree upon the same thing in the same sense." Thus, consent involves identity of minds in respect of the subject matter of the contract. In English Law, this is called 'consensus-ad-idem'.

Effect of absence of Consent:

When there is no consent at all, the agreement is void ab-initio, i.e. it is not enforceable at the option of either party.

Example I: X has one Maruti car and one Fiat car. He wants to sell Fiat car. Y does not know that X has two cars. Y offers to buy X's Maruti car for Rs 50,000. X accepts the offer thinking it to be an offer for his Fiat car. Here, there is no identity of mind in respect of the subject matter. Hence there is no consent at all and the agreement is void ab-initio.

Example II: X, an illiterate woman, signed a gift deed thinking that it was a power of attorney. This gift deed was not explained to her. It was held that her mind did not go with that writing and she never intended to sign a gift deed. Hence, there was no consent at all and the agreement was void ab-initio. [Bala Devi vs. S. Majumdar].

Meaning of Free Consent [Section 14]

Free consent is one of the essential elements of a valid contract as it is evidenced by Section 10 which provides that all agreements are contracts if they are made by the free consent of the parties . . .
According to Section 14, Consent is said to be free when it is not caused by (a) coercion, or (b) undue influence, or (c) fraud, or (d) misrepresentation, or (e) mistake.

Effect of absence of Free Consent [Section 19]
When there is consent but it is not free (i.e. when it is caused by coercion or undue influence or fraud or misrepresentation), the contract is usually voidable at the option of the party whose consent was so caused.

Example: X threatens to kill Y if he does not sell his house to X. Y agreed to sell his house to X. In this case, Y's consent has been obtained by coercion and therefore, it cannot be regarded as free.

1.5.2 COERCION

Meaning of Coercion [Section 15]

Coercion means compelling a person to enter into a contract under a pressure or a threat. According to Section 15, a contract is said to be caused by coercion when it is obtained by-

a. committing any act which is forbidden by the Indian Penal Code; or

b. threatening to commit any act which is forbidden by the Indian Penal Code; or

c. unlawful detaining of any property; or

d. threatening to detain any property.

Example I: X beats Y and compels him to sell his car for Rs 50,000. Here, Y's consent has been obtained by coercion because beating someone is an offence under the Indian Penal Code.

Example II: A Hindu widow of 13 years was forced to adopt a boy under threat that her husband's dead body would not be allowed to be removed if she does not adopt the boy. She adopted the boy. Here, widow's consent has been obtained by coercion because preventing the dead body from being removed for cremation is an offence under Section 297 of the Indian Penal Code. [Ranganayakamma vs. Alwar Setti]

Note: The Indian Penal Code need not be in force in place where the coercion is employed.

Against whom/by Whom Coercion may be exercised:

Coercion may proceed from any person, and may be directed against any person, even a stranger.

Example I: X threatens to kill Z, Y's son, if Y refuses to sell his house to him. Y agrees to sell his house. Here, Y's consent has been obtained by coercion though Z is a stranger to the contract.

Example II: X threatens to kill Y if Y refuses to sell his house to Z. Y agrees to sell his house. Here, Y's consent has been obtained by coercion though X is a stranger to the contract.

Effect of threat to file a suit:

A threat to file a suit (whether civil or criminal) does not amount to coercion unless the suit is on false charge. Threat to file a suit on false charge is an act forbidden by the Indian Penal Code and thus will amount to an act of coercion.

Effect of threat to commit suicide:

A ‘suicide’ and a ‘threat to commit suicide’ are not punishable but an attempt to commit suicide is punishable under the Indian Penal Code. It does not mean that ‘suicide’ and threat to commit suicide are permitted by Indian Penal Code. The question whether a ‘threat to commit suicide’ amounts to coercion or not was considered by Madras High Court in the case of Chikham Ammiraju vs. Seshamma. In this case, a person threatened to commit suicide if his wife and son did not execute a release deed in favour of his brother in respect of certain property. It was held that though a threat to commit suicide is not punishable under the Indian Penal Code, it is deemed to be forbidden by that code. Hence, the threat to commit suicide amounted to coercion and the release deed was therefore, voidable.

The English law uses the term 'duress' for coercion. However, the two are different in the following way:

a. Duress does not include detaining of property or threat to detain property.

b. Duress can be employed only by a party to the contract or his agent.

Effects of Coercion [Sections 19, 64, 72]
The effects of coercion are as follows:

Effects	*Provision*
(a) Option of aggrieved party to avoid the contract	When consent to an agreement is obtained by coercion, the agreement is a contract voidable at the option of the party whose consent was obtained by coercion (also called aggrieved party). [Section 19]
(b) Obligation of aggrieved party to restore benefit	The party rescinding a voidable contract shall restore the benefit received by him under the contract, to the person from whom the benefit was received. [Section 64]
(c) Obligation of other party to repay or return	A person to whom money has been paid or anything delivered under coercion must repay or return it. [Section 72]

Example I: X threatens to kill Y if he does not sell his house for Rs 1,00,000 to X. Y sells his house to X and receives the payments. Here, Y's consent has been obtained by coercion. Hence, this contract is voidable at the option of Y. If Y decides to avoid the contract, he will have to return Rs 1,00,000 which he had received from X.

Example II: A railway company refused to deliver certain goods to the consignee, except upon the payment of an illegal charge for carriage. The consignee pays the sum charged in order to obtain the goods. He is entitled to recover so much of the charge as was illegally excessive.

Burden or Onus of Proof

The burden of proving that consent was obtained by coercion, and the aggrieved party would not have entered into contract had coercion been employed, lies on the party intending to avoid the contract.

1.5.3 UNDUE INFLUENCE

Meaning of Undue Influence [Section 16(1)]

The term 'undue influence' means dominating the will of the other person to obtain an unfair advantage over the other. According to Section 16(1), a contract is said to be induced by undue influence-

a. where the relations subsisting between the parties are such that one of them is in a position to dominate the will of the other, and

b. the dominant party uses that position to obtain an unfair advantage over the other.

Presumption of Domination of Will [Section 16(2)]

According to Section 16(2), a person is deemed to be in a position to dominate the will of another in the following three circumstances:

Circumstances	*Examples*
(a) Where he holds a real or apparent authority over the other	Master and servant, parent and child, Income Tax Officer and assessee, Principal and a temporary teacher
(b) Where he stands in a fiduciary relation to the other	Trustee and beneficiary, spiritual adviser (Guru) and his disciples, solicitors and client, guardian and ward
(c) Where he makes a contract with a person whose mental capacity is temporarily or permanently affected by reason of age, illness or mental or bodily distress	Medical attendant and patient

No Presumption of Domination of Will

According to judicial decisions held in various cases, there is no presumption of undue influence in the following relationships:

(a) Husband and wife (other than pardanashin)

(b) Landlord and tenant

(c) Creditor and debtor

Example I: X advanced Rs 10,000 to his son Y during his minority and obtained upon Y's coming of age, a bond from Y for Rs 1,00,000. Here, there is misuse of parental influence.

Example II: A poor Hindu widow agreed to pay interest at 100% p.a. because she needed the money to establish her right of maintenance. It was held that the lender was in position to dominate the will of widow. [Ranee Annpurni vs. Swaminath]

Example III: A devotee gifted her property to her spiritual guru to secure benefits to her soul in next world. It was held that spiritual guru was in position to dominate the will of devotee. [Mannu Singh vs. Umadat Pander]

Example IV: X, an illiterate old man of about 90 years, physically infirm and mentally in distress, executed a gift deed of his properties in favour of Y his nearest relative who was

looking after his daily needs and managing his cultivation. It was held that Y was in a position to dominate the will of X. [Sher Singh vs. Prithi Singh]

Effect of Undue Influence [Section 19A]:

When consent to an agreement is caused by undue influence, the agreement is a contract voidable at the option of the party whose consent was so caused.

Discretion of Court:

Any such contract may be set aside either absolutely or, the party who was entitled to avoid it has received any benefit thereunder, upon such terms and conditions as the court may seem just.

Example I: A's son forged B's name to a promissory note. B, under threat of prosecuting A's son, obtains a bond from A, for the amount of the forged note. If B sues on this bond, the Court may set the bond aside.

Example II: A, a money-lender, advances Rs 10,000 to B, an agriculturist, and by undue influence, induces B to execute a bond for Rs 20,000 with interest at 6 per cent per month. The court may set the bond aside, ordering B to repay Rs 10,000 with such interest as may just.

Burden of Proof:

When a contract is avoided on the ground of undue influence, the liabilities of dominant party and weaker party to prove are as under:

The weaker party has to prove- a. that the other party was in a position to dominate the will b. that the other party actually used his influence to obtain an unfair advantage c. that the transaction is unconscionable (unreasonable)	In case of unconscionable transaction, the dominant party has to prove that such contract was not induced by undue influence. Note: A transaction is said to be unconscionable if the dominant party makes an exorbitant profit of the other's distress.

Contracts with Pardanashin Woman:

Meaning of Pardanashin Woman: A woman who observes complete seclusion (i.e.,who does not come in contact with people other than her family members) is pardanashin woman.

Legal Presumption: A contract with a pardanashin woman is presumed to have induced by undue influence.

Burden of Proof:

The other party who enters into a contract with a pardanashin woman must prove-

a. that he made full disclosure of all the facts to her;

b. that she understood the contracts and the implications of the contract;

c. that she was in receipt of competent independent advice before entering into the contract.

Comparison between Coercion and Undue Influence

Similarities: In case of both coercion and undue influence, the consent is not free and the contract is voidable at the option of the aggrieved party.

Distinction: Coercion differs from the undue influence in the following respects:

Basis of distinction	Coercion	Undue influence
1. Relationship	Parties to a contract may or may not be related to each other.	Parties to a contract are related to each other under some sort of relationship.
2.Consent	Consent is obtained by giving a threat of an offence or committing an offence.	Consent is obtained by dominating the will.
3. Nature of pressure	It involves physical pressure.	It involves moral pressure.

4. Who can exercise	It can be exercised even by a stranger to the contract.	It can be exercised even by a party to a contract and not by a stranger.
5.Restoration of benefit	The aggrieved party has to restore the benefit received under Sec. 64.	The party avoiding the contract may or may not return the benefit under Sec. 19A.
6.Presumption	Coercion has to be proved by the party alleging it, in no case it is presumed by the law.	It may be presumed by the law under certain circumstances. The party against whom such presumption lies must disprove it.
7.Nature of liability	The party committing the crime may be punishable under I.P.C.	It doesn't involve any criminal liability.

Rebutting Presumption

The presumption of undue influence can be rebutted by showing-

a. that the dominant party has made a full disclosure of all the facts to the weaker party before making the contract;
b. that the price was adequate; and
c. that the weaker party was in receipt of competent independent advice before entering into the contract.

1.5.4 FRAUD

Meaning and Essential Elements of Fraud [Section 17]

Meaning: The term ‘fraud’ means a false representation of fact made wilfully with a view to deceive the other party. Section 17 defines the fraud as follows:

‘Fraud’ means and includes any of the following acts committed by a party to a contract, or with his connivance, or by his agent, with intent to deceive another party thereto or his agent, or to induce him, to enter into the contract:

a. the suggestion, as to a fact, of that which is not true, by one who does not believe it to be true; e.g., X sells to Y, locally manufactured goods as imported goods charging a higher price, it amounts to fraud.

b. the active concealment of a fact by one having knowledge or belief of the fact. Mere concealment is no fraud. But where steps are taken by a seller concealing some material facts so that the buyer even after a reasonable examination cannot trace the defects, it will amount to fraud, e.g. X a furniture dealer, conceals the cracks in furniture sold by him by using some packing material and polishing it in such a way that the buyer even after reasonable examination cannot trace the defect, it would tantamount to fraud through active concealment.

c. a promise made without any intention of performing it; e.g. in Shireen vs. John, AIR(1952) Punj 227, a man and a woman underwent a ceremony of marriage with the husband not regarding it as a real marriage. Held, the husband had no intention to perform the promise from the time he made it and hence the consent of the wife was obtained under fraud.

d. any such act of omission as the law specially declares to be fraudulent, e.g. under Companies Act and Insolvency Acts, certain kinds of transfers have been declared to be fraudulent.

e. any other act fitted to deceive. It covers those acts which deceive but are not covered under any other clause.

Essential Elements:

On the basis of aforesaid definition of fraud, the essential elements of fraud are:

1. By a party to a contract:

The fraud must be committed by a party to a contract or by anyone with his connivance or by his agent. Thus, the fraud by a stranger to the contract does not affect the validity of the contract.

Example: The directors of a company issued a prospectus containing false statements. A shareholder who had subscribed for the shares on the faith of the prospectus wanted to avoid the contract. It was held that he could do so because the false statement made by directors amounted to fraud. [Reese River Silver Mining Co. vs. Smith]

2. False representation:

There must be a false representation and it must be made with the knowledge of its falsehood. Where the representation was true at the time when it was made but becomes untrue before the contract is entered into and this fact is known to the party who made the representation, it must be corrected. If it is not so corrected, it will amount to a fraud.

Example: I X fraudulently informs Y that X's estate is free from encumbrance. On the faith of X's statement, Y buys the estate. Actually the estate is subject to mortgage. Here, Y may avoid the contract because X with the intention to deceive Y induced Y to enter into a contract.

3. Representation as to fact:
The representation must relate to a fact. In other words, a mere opinion, a statement of expression or intention does not amount to fraud.

4. Actually deceived:
The fraud must have actually deceived the other party who has acted on the basis of such representation. In other words, an attempt to deceive the other party by which the other party is not actually deceived is not a fraud.

Example: X had a defective cannon. In order to conceal the defect, he put a metal plug on it. Y bought this cannon without examining. When Y used it, it brust. Y refused to pay the balance. It was held that Y was liable to pay as he was not actually deceived by fraud because he would have bought it even if no deceptive plug was inserted. [Horsefull vs. Thomas].

5. Suffered loss:
The party acting on the representation must have suffered some loss.

Effects of Fraud [Section 19]

The effects of fraud are as follows:

a. The party whose consent was caused by fraud can rescind (cancel) the contract but he cannot do so in the following cases:

i. where silence amounts to fraud, the aggrieved party cannot rescind the contract if he had the means of discovering the truth with ordinary diligence;
ii. where the party gave the consent in ignorance of fraud;
iii. where the party after becoming aware of the fraud takes a benefit under the contract;
iv. where an innocent third party before the contract is rescinded acquires for consideration some interest in the property passing under the contract,
v. where the parties cannot be restored to their original position.

b. The party whose consent was caused by fraud may, if he thinks fit, insist that the contract shall be performed and that he shall be put in the position in which he would have been if the representation made had been true.

Example: A fraudulently informs B that A’s estate is free from encumbrance. B there upon buys the estate. The estate is subject to a mortgage. B may either avoid the contract, or may insist on its being carried out and the mortgage-debt redeemed.

The party whose consent was caused by fraud, can claim damage if he suffers some loss.

Silence as to fraud:

According to explanation to Section 17, “Mere silence as to facts likely to affect the willingness of a person to enter into a contract is not fraud.”

Example I: A sells, by auction, to B a horse which A knows to be unsound. A says nothing B about the horse’s unsoundness. This is not fraud by A.

Example II: A and B, being traders, enter upon a contract. A has private information of a change in prices which would affect B’s willingness to proceed with the contract. A is not bound to inform B.

Example III: In Shri Krishna vs. Kurukshetra University (AIR 1976 SC 376) a candidate failed to mention the fact of shortage of attendance in the examination form. Held, no fraud.

Exceptions to the General Rule:
The general rule that silence doesn’t amount to fraud has the following exceptions.

Where the circumstances of the case are such that, regard being had to them, it is the duty of the person keeping silence to speak. Such duty arises in the following two cases:

1. Where parties stand in fiduciary relationship like parent-child, trustee-beneficiary.

A sells by auction to B, a horse which A knows to be unsound. B is A’s daughter and has just come of age. Here, the relation between the parties would make it A’s duty to tell B if the horse is unsound.

2. Half Truth: Half truth is worse than a blatant lie. Partial truthful disclosures may easily deceive the other party, e.g. prospectus of a company disclosing only average dividend declared by the company in the last 5 years instead of the actually declining dividends over that period is a glaring example of half truth amounting to fraud.

1.5.5 MISREPRESENTATION

Meaning:

The term ‘Misrepresentation’ means a false representation of fact made innocently or non-disclosure of a material fact without any intention to deceive the other party. Section 18 defines the term ‘misrepresentation’ as follows:

“Misrepresentation” means and includes-

i. the positive assertion, in a manner not warranted by the information of the person making it, of that which is not true, though he believes it to be true;

ii. any breach of duty which, without an intent to deceive, gains an advantage to the person committing it, or anyone claiming under him, by misleading another to his prejudice or to the prejudice of anyone claiming under him;

iii. causing, however innocently, a party to an agreement, to make a mistake as to the substance of the thing which is the subject of the agreement.

Essential Elements:

On the basis of the aforesaid definition of misrepresentation, the essential elements of misrepresentation are:

1. By a party to a contract:

The representation must be made by a party to a contract or by anyone with his connivance or by his agent. Thus, the representation by a stranger to the contract does not affect the validity of the contract.

2. False representation:

There must be a false representation and it must be made without the knowledge of its falsehood i.e. the person making it must honestly believe it to be true.

3. Representation as to fact:

The representation must relate to a fact. In other words, a mere opinion, a statement of expression or intention does not amount to misrepresentation.

4. Object:

The representation must be made with a view to inducing the other party to enter into contract but without the intention of deceiving the other party.

5. Actually acted:

The other party must have acted on the faith of the representation.

Effects of Misrepresentation [Section 19]:

a. Right to Rescind the Contract:

The party whose consent was caused by misrepresentation can rescind (cancel) the contract but he cannot do so in the following cases:

i. where the party whose consent was caused by misrepresentation had the means of discovering the truth with ordinary diligence;

ii. where the party gave the consent in ignorance of misrepresentation;

iii. where the party after becoming aware of the misrepresentation, takes a benefit under the contract;

iv. where an innocent third party, before the contract is rescinded, acquires for consideration some interest in the property passing under the contract;

v. where the parties cannot be restored to their original position.

b. Right to Insist upon Performance:

The party whose consent was caused by misrepresentation may if he thinks fit, insist that the contract shall be performed, and that he shall be put in the position in which he would have been if the representation made had been true.

Comparison between Fraud and Misrepresentation:

Similarities:

There are basically two similarities in case of fraud and misrepresentation as follows:

i. In both the cases, a false representation is made by a party;

ii. In both the cases, the contract is voidable at the option of the party whose consent is obtained by fraud or misrepresentation.

Distinction Fraud differs from misrepresentation in the following respects:

Basis of distinction	Fraud	Misrepresentation
1. Intention	A wrong representation is made wilfully with the intention to deceive the other party.	A wrong representation is made innocently, i.e. without any intention to deceive the other party.
2. Knowledge of falsehood	The person making the wrong statement does not believe it to be true.	The person making the wrong statement believes it to be true.
3. Right to claim damages	The aggrieved party can claim damages.	The aggrieved party cannot claim damages.
4. Availability of means to discover the truth	Except where silence amounts to fraud, the contract is voidable even if the aggrieved party had the means of discovering the truth with ordinary diligence.	The aggrieved party cannot avoid the contract if he had the means of discovering the truth with ordinary diligence.

1.5.6 MISTAKE

Meaning of Mistake [Section 20]

A mistake is said to have occurred where the parties intending to do one thing by error do something else. Mistake is an erroneous belief concerning something. The mistake can be of two types.

I. Mistake of law [Section 21]:

a. Mistake of Indian Law - The contract is not voidable because everyone is supposed to know the law of his country.

b. Mistake of Foreign Law i.e. - A mistake of foreign law is treated as mistake of fact, the contract is void if both the parties are under a mistake as to a foreign law because one cannot be expected to know the law of other country.

II. Mistake of Fact:

Mistake of fact can be either bilateral mistake or unilateral mistake.

a. Bilateral Mistake [Section 20]:

The term 'bilateral mistake' means where, both the parties to the agreement are under a mistake. According to Section 20, "Where both the parties to an agreement are under a mistake as to a matter of fact essential to the agreement, the agreement is void." Thus, the following three conditions must be satisfied before declaring a contract void under this section:

i. Both the parties must be under a mistake

ii. Mistake must be of fact but not of law.

iii. Mistake must relate to an essential fact.

Example I: A agrees to sell to B a specific cargo of goods supposed to be on its way from England to Mumbai. It turns out that, before the date of the bargain, the shop conveying the cargo had been cast away and the goods lost. Neither party was aware of facts. The agreement is void.

Example II: A agrees to buy from B a certain horse. It turns out that the horse was dead time of the bargain, though neither party was aware of the fact. The agreement is void.

Example III: A, being entitled to an estate for the life of B, agrees to sell it to C. B was dead at the time of the agreement, but both parties were ignorant of the fact. The agreement is void.

Bilateral mistake as to the Subject matter:

An agreement is void where there is a bilateral mistake as to the subject matter. A bilateral mistake as to the subject matter includes the following:

i. Mistake as to the existence of subject matter
ii. Mistake as to the quantity of subject matter
iii. Mistake as to the quality of subject matter
iv. Mistake as to the price of subject matter
v. Mistake as to the identity of subject matter
vi. Mistake as to the title of subject matter

Example I: A agrees to buy from B a certain horse. It turns out that the horse was dead at the time of bargain though neither party was aware of the fact. The agreement is void because there is bilateral mistake as to the existence of subject matter.

Example II: A agrees to buy from B all his horses believing that B has two horses but B actually has three horses. The agreement is void because there is bilateral mistake as to the quantity of subject matter.

Example III: A agrees to buy a particular horse from B. Both believe it to be a race horse but it turns to be a cart horse. The agreement is void because there is bilateral mistake as to the quality of the subject matter.

Example IV: A agrees to buy a particular horse from B who mentioned in his letter the price as Rs 1,150 instead of 5,150. The agreement is void because there is bilateral mistake as to the price of the subject matter.

Example V: A agrees to buy from B a certain horse. B has one race horse and one cart horse. A thinks that he is buying race horse but B thinks that he is selling cart horse. The agreement is void because there is bilateral mistake as to the identity of subject matter.

Example VI: A agrees to buy a particular horse from B. That horse is already owned by A. The agreement is void because there is bilateral mistake as to the title of the subject matter.

Bilateral Mistake as to the Possibility of Performance:

The agreement is void where there is a bilateral mistake as to the possibility of performance. In other words, where the parties to an agreement believe that the agreement is capable of performance, while in fact it is not so, the agreement is treated as void. The impossibility may either be physical or legal.

b. Unilateral Mistake [Section 22]:

The term ‘unilateral mistake’ means where only one party to the agreement is under a mistake. According to Section 22, “A contract is not voidable merely because it was caused by one of the parties to it being under a mistake as to matter of fact.”

Example: X sold Oats to Y by sample and Y, thinking that they were old Oats, purchased them. In fact, the Oats were new. It was held that Y was bound by the contract. [Smith vs. Hughes]

Exceptions: The agreement is void where a unilateral mistake relates to the identity of the person contracted with or as to the nature of the contract.

Example: A woman by falsely misrepresenting her to be wife of a well known Baron (a millionaire) obtained two pearl necklaces from a firm of jewellers on the pretext of showing them to her husband before buying. She pledged them with a broker, who in good faith paid her Rs 1,00,000. A suit was filed by the jeweller against the broker. It was held that there was no contract between the jeweller and the broker as the jeweller never intended to contract with her and as such, the broker did not get a good title and hence he must return the goods. [Lake vs. Simmons]

Example: An old illiterate man was induced to sign a Bill of Exchange by means of a false representation that it was a mere guarantee. It was held that he was not liable for the bill of exchange because he never intended to sign a Bill of Exchange. [Foster v. Mackinnon]

But the contract shall be valid and binding in spite of the mistake as to the identity of the parties in all those cases where the parties were willing to enter into contract with any person. Thus, if the mistake only relates to the attributes or motives of the person such as creditworthiness, it will not make the contract void. It may at the most make it voidable for fraud, e.g. in Phillips vs. Brooks. One Mr North entered a Jeweller’s shop, selected a ring which the jeweller agreed to sell against payment by cheque which North signed in the name of Sir G B, a man of credit and standing. North pledged the ring with Brooks. In the meanwhile the cheque got dishonoured. It was held that the contract between North and the Jeweller was valid as the jeweller agreed to sell goods to the very person who entered the shop. Thus, the contract had been made before the goods were delivered to North. As the contract was induced by fraud, the jeweller could rescind the contract. However, the pledge made by North was valid. The jeweller’s right was only confirmed to filing a suit against North to recover damages.

Effects of Mistake:

The effects of mistake are as follows:

(a) In case of Bilateral Mistake as to essential fact	The agreement is void.
(b) In case of Unilateral Mistake	
a. as to the identity of the person contracted with	The agreement is void
b. as to the nature of contract	The agreement is void.
c. as to other matter	The agreement is not void
(c) Obligation of aggrieved party	He must restore any benefit received by him under the contract to the other party from whom the benefit had been received [Section 64]
(d) Obligation of other party	The person to whom money has been paid or anything delivered by mistake must repay or return it. [Section 72]

Check your progress – 5:

Differentiate between Coercion and Undue influence.

LESSON- 6

LEGALITY OF OBJECT AND CONSIDERATION, AND AGREEMENTS OPPOSED TO PUBLIC POLICY

CONTENTS

1.6.1 CIRCUMSTANCES UNDER WHICH THE OBJECT OR CONSIDERATION IS DEEMED TO BE UNLAWFUL

The object and the consideration of an agreement must be lawful, otherwise, the agreement is void. According to Section 23 of The Indian Contract Act, 1872, the consideration or the object of an agreement is unlawful in the following cases:

i. If it is forbidden by Law:

If the object or the consideration of an agreement is the doing of an act which is forbidden (i.e. prohibited) by law, the agreement is void. An act is said to be forbidden by law when it is punishable either by the criminal law of the country or by special legislation.

Example I: A promises B to drop a prosecution which he has instituted against B for robbery, and B promises to restore the value of the things taken. The agreement is void, as its object is unlawful. [William vs. Bayley].

Example II: X granted a loan to the guardian of a minor to enable him to celebrate the minor's marriage. It was held that X could not recover back because agreement is void as its object (i.e., minor's marriage) is illegal. [C. Srinivas vs. K. Raja Rama Mohana Rao].

ii. If it defeats the provisions of any law:

If the object or the consideration of an agreement is of such nature that, if permitted, it would defeat the provisions of any law, the agreement is void.

Example : X borrowed Rs 1,00,000 from Y and agreed not to raise any objection as to the limitation and that Y may recover the amount even after the expiry of limitation period. This agreement is void as it defeats the provisions of the Law of Limitation Act. [Rama Murthi vs. Goppayya]

iii. If it is Fraudulent:
If the object of an agreement is to defraud others, the agreement is void.

Example : A, Band C enter into an agreement of the division among them of gains acquired, or be acquired, by them by fraud. The agreement is void, as its object is unlawful.

iv. If it Involves or Implies Injury to a Person or Property of Another:
If the object of an agreement is to injure a person or the property of another, the agreement is void.

Example : X borrowed Rs 100 from Y and executed a bond under which he promised to work for Y without pay for 2 years and agreed to pay interest at 10% per month and the principal amount at once. It was held that the agreement was void because it involved injury to X. [Ramsaroop vs. Bansi Mandar].

v. If the Court Regards it as Immoral or Opposed to Public Policy:
If the object or consideration is immoral or is opposed to the public policy, the agreement is void.

Example : A, who is B's mukhtar, promises to exercise his influence, as such, with B in favour of C, and C promises to pay Rs 1,000 to A. The agreement is void, because it is immoral.

Example : X let a flat to Yon a monthly rent of Rs 10,000. Y was a prostitute and used the flat for prostitution and did not pay the rent. X cannot recover the rent if he knew the purpose otherwise he can. [Pearce v. Brooks]

1.6.2 ILLEGAL AGREEMENTS

Illegal agreements are those agreements which are-

i. void ab-initio, i.e. void from the very beginning, and

ii. punishable by the criminal law of the country or by any special legislation/ regulation.

Effects of illegal agreements are as under:

a. The collateral transactions to an illegal agreement also become illegal and hence cannot be enforced.

b. No action can be taken for the recovery of money paid or property transferred under an illegal agreement and for the breach of an illegal agreement.

c. In case of an agreement containing the promise, some part of which is legal and other part illegal, the legal position is as under:

Example: X pays Y Rs 1,000 to beat Z. Y does not beat. X cannot recover from Y because the agreement between X and Y is illegal.

Example: X lent Rs 1,00,000 to Y to enable him to purchase certain smuggled goods from Z. X cannot recover the amount from Y if he knows the Y's purpose of borrowing.

1.6.3 VOID AGREEMENTS IF CONSIDERATION OR OBJECTS UNLAWFUL IN PART

According to Section 24, if one of the several considerations or objects of an agreement is unlawful, the agreement is void.

Example: A promises to superintend, on behalf of B, a legal manufacturer of indigo and illegal traffic of other articles. B promises 10 pay to A, a salary of Rs 10,000 a year. The agreement is void, the object of A's promise and the consideration for B's promise being in part unlawful.

1.6.4 AGREEMENTS OPPOSED TO PUBLIC POLICY

It is not easy to define the term 'Public policy' with any degree of precision because 'public policy' by its very nature, is highly uncertain and keeps on fluctuating with the passage of time. An agreement which conflicts with morals of the time and contravenes any established interest of society may be said to be opposed to public policy. In India, it has been left to Court to hold any contract as unlawful on the ground of being opposed to public policy.

The following agreements have been held to be opposed to public policy:

1. Agreements of Trading with Enemy:

   All agreements made with an alien enemy are illegal on the ground of public policy.

2. Agreement for Stifling Prosecution:

   An agreement for stifling prosecution is illegal on the ground of public policy.

Example: X, who knows that Y has committed a murder, receives Rs 7,00,000 from Y in consideration of not exposing Y. This agreement is illegal.

3. Agreements in the Nature of Maintenance and Champerty:

   Maintenance is an agreement whereby one party having no interest in suit, agrees to assist another to maintain suit. For example, X promises to pay Y Rs 5,000 if Y files a suit against Z. This is a maintenance agreement.

Champerty is an agreement whereby one party agrees to assist another in recovering property and in turn is to share in the proceeds of the action.

Example :X, agreed to pay Rs 10,000 to Y to enable him to file a suit for the recovery of his property and Y promised to give him 3/4th share in the property, if recovered. The agreement was held to be champertous and void. [Nuthahi Venkataswami vS. Katta Nagi]

Position in England: Both of these agreements are declared illegal and void.

Position in India: All of these agreements are not illegal. The Court will refuse to enforce such agreements if its object is not bonafide or the terms of reward are unreasonable in the opinion of court.

4. Agreement for the Sale / transfer of Public Offices and Titles:

   The agreements for the sale or transfer of public offices or to obtain public titles like Padma Shree, are illegal on the ground of public policy.

   Example: X promises to pay Y Rs 50,000 if Y secures him an employment in Govt. service. This agreement is opposed to public policy.

5. Agreements in Restraint of Parental Rights:

   An agreement which prevents a parent to exercise his right of guardianship is void on the ground of public policy.

6. Agreements in Restraint of Personal Liberty:

   An agreement which unduly pets the personal liberty of any person is void on the ground of public policy.

7. Agreement Tending to Create Monopoly:

   An agreement which tends to create monopoly is void on the ground of public policy.

8. Agreements Interfering with Course of Justice:

   An agreement which interferes with course of justice is void on the ground of being opposed to public policy.

9. Marriage Brokerage Contracts:

   A marriage contract is one whereby one or persons receives money or money’s worth in consideration of marriage.

10. Agreement in Restraint of Marriage [Section 26]:

    Every agreement in restraint of marriage of any person other than a minor is void.

11. Agreement in Restraint of Trade [Section 27]:

    Every agreement by which anyone is restrained from exercising a lawful profession, trade or business of any is to that extent void.

12. Agreement in Restraint of Legal Proceeding [Section 28]:

    An agreement which restricts a party absolutely from enforcing his legal rights arising under a contract or an agreement which curtails the period of limitation within which the rights may be enforced is void.

1.6.5 VOID AGREEMENTS AND CONTINGENT CONTRACTS

According to Section 2(g) of the Indian Contract Act, 1872, a void agreement is an agreement which is not enforceable by law. The agreements which are not legal by law right from the time when they are made are void-ab-initio.

The following types of agreements have expressly been declared void under sections of the Indian Contract Act.

i. Agreements by or with persons incompetent to contract (Sections 10 & 11).
ii. Agreements entered into through a mutual mistake of fact between the parties (Section 20).
iii. Agreement, the object or consideration of which is unlawful (Section 23).
iv. Agreement, the consideration or object of which is partly unlawful (Section 24).
v. Agreement made without consideration (Section 25).
vi. Agreements in restraint of marriage (Section 26).
vii. Agreements in restraint of trade (Section 27).
viii. Agreements in restraint of legal proceedings (Section 29).
ix. Wagering agreement (Section 30).
x. Impossible agreement (Section 56).
xi. An agreement to enter into an agreement in the future.

Agreements in restraint of marriage:
According to Section 26 of the Indian Contract Act, every agreement in restraint of the marriage of any person other than a minor is void.

Example I: X promised to marry Y only and none else, and to pay Rs 2,000 in default. X married Z and Y sued X for recovery of Rs 2,000. It was held that Y could not recover anything because the agreement was in restraint of marriage. [Lowe vs. Peers]

It may be noted that an agreement which provides for a penalty upon remarriage may not be considered as a restraint of marriage.

Example II: An agreement between two co-widows that if one of them remarried, she should forfeit her right to her share in the deceased husband's property, was not void because no restraint was imposed upon either of the two widows from remarrying. [Roa Rani vs. Gulab Rani]

1.6.6 AGREEMENTS IN RESTRAINT OF TRADE

According to Section 27 of Indian Contract Act, 1872, "every agreement by which anyone is restrained from exercising a lawful profession, trade or business of any kind, is to that extent void." This is because Article 19(g) of the Constitution of India regards the freedom of trade and commerce as a right of every individual. Therefore, no agreement can deprive or restrain a person from exercising such a right.

Onus of Proof :
Where an agreement is challenged on the ground of its being in restraint of trade, the party supporting the contract must show that the restraint is reasonably necessary to protect his interests, and the party challenging the contract must show that the restraint is injurious to the public.

Meaning of Expression 'that Extent':
The expression 'that extent' may be interpreted in the sense that only that portion of such agreement is void which is considered either as unreasonable or as opposed to public policy being in restraint of trade. The rest of the agreement would continue to be valid.

Example : X and Y carried on business in a certain locality in Calcutta. X promised to stop business in that locality if Y paid him Rs 1,000. X stopped his business but Y did not pay him the promised money. It was held that X could not recover anything from Y because the agreement was in restraint of trade and was thus void. [Madhub Chander vs. Raj Coomer}

Exceptions to the Rule that 'An Agreement in Restraint of Trade is Void':
The exceptions here mean the cases where agreements in restraint of trade are not considered as void.

I. Exceptions Under Statutory Provisions:

1. Sale of Goodwill [Exception 1 to Section 27]:

An agreement which restrains the seller of a goodwill from carrying on a business is valid if all the following conditions are fulfilled:

a. Such restriction must relate to a similar business.

b. Such restriction must be within specified local limits.

c. Such restriction must be for the time so long as the buyer or any person deriving title to the goodwill from him carries on a like business in the specified local limits.

d. Such specified local limits must be reasonable having regard to the nature of the business.

Thus, the buyer of goodwill may restrain the seller for carrying on any business "to the one sold by him within certain vicinity and for a certain period of time provided the restrictions in regard to time and vicinity are found reasonable.

2. Partners Agreements:

The Indian Partnership Act, 1932, recognises the following agreements in restraint of trade as valid:

a. Restriction on existing partner [Section 11 (2)]-A partner shall not carry on any business other than that of the firm while he is a partner.

b. Restriction on outgoing partner [Section 36(2)]-An outgoing partner may agree with his partners that he will not carry on any business similar to that of the firm within a specified period or within specified local limits. Such agreement shall be valid only if the restrictions are reasonable.

c. Restriction on partners upon or in anticipation of the dissolution of the firm [Section 54]-Partners may, upon or in anticipation of the dissolution of the firm, make an agreement that some or all of them will not carry on a business similar to that of the firm within a specified period or within specified local limits. Such agreement shall be valid only if the restrictions are reasonable.

d. Restriction in case of sale of goodwill [Section 55(3)]-A partner may upon the sale of the goodwill of a firm, make an agreement that such partner will not carry on any business similar to that of the firm within a specified period or within specified local limits. Such agreement shall be valid if the restrictions are reasonable.

II. Exceptions under Judicial Interpretations:

1. Trade Combinations:
Trade combinations which have been formed to regulate the business or to fix prices are not void, but the trade combinations which tend to create monopoly and which are against the public interest are void.

Example: An agreement among four ginning factories to fix uniform rate for ginning cotton and to divide the profits in a certain proportion is not void because such agreements are neither in restraint of trade nor opposed to public policy. [Haribhai vs. Sharafali]

2. Sole Dealing Agreements:
   An agreement to deal in the products of a single manufacturer or to sell the whole produce to a single dealer are valid if their terms are reasonable.

Example: An agreement by a person to sell all the mica produced by him to the plaintiffs and not to any other firm, and not to keep any in stock, is valid. [Subha Naidu vs. Haj Badsha Sahib]

3. Service Agreements:
   A clause in service agreement may or may not be in restraint of trade. An analysis of some of the clauses of service agreement is as under:

1.6.7 WAGERING AGREEMENTS (SEC. 30)

Meaning of Wagering Agreements

An agreement between two persons under which money or money's worth is payable by one person to another on the happening or non-happening of a future uncertain event is called a wagering event. Such agreements are chance oriented and therefore, completely uncertain.

Example: X promises to pay Rs 1,000 to Y if it rained on a particular day, and Y promises to pay Rs 1,000 to X if it did not. Such agreement is a wagering agreement.

Essentials of a Wagering Agreement:

a. Promise to Pay Money or Money's Worth:
   The wagering agreement must contain a promise to pay money or money's worth.

b. Uncertain Event:
   The performance of the promise must depend upon the determination of an uncertain event. An event is said to be uncertain when it is yet to take place or it might have already happened but the parties are not aware of its result.

c. Mutual Chances of Gain or Loss:
   Each party must stand to win or lose upon the determination of an uncertain event. If either of the parties may win but cannot lose, or may lose but cannot win, it is not a wagering agreement.

d. Neither Party to have Control over the Event:
Neither party should have control over the happening of the event one way or the other.

e. No other Interest in the Event:
Neither party should have interest in the happening or non-happening of the event other than the sum or stake he will win or lose.

Examples of Wagering Agreements:

a. An agreement to settle the difference between the contract price and market price of certain goods or shares on a particular day.

b. A lottery (i.e. a game of chance). But parties running a Govt. approved lottery cannot be prosecuted .

c. An agreement to buy a lottery ticket.

d. A crossword puzzle in which prizes depend upon correspondence of the competitor's solution with a previously prepared solution kept with the Editor of newspapers is a lottery and hence a wagering transaction.
[State of Bombay vs. R.M.D. Chamarbaugwala]. But a crossword puzzle is generally a game of skill and intelligence and hence not a wager.

Examples of Transactions Held not Wagers:

a. Prize competitions which are games of skill, e.g., picture puzzles, athletic competitions. For example, an agreement to enter into a wrestling event in which winner was to be rewarded by the entire sale proceeds of tickets was held not to be a wagering contract. [Babasaheb vs. Rajaram]

b. According to the Prize Competition Act, 1955, prize competition in games of skill are not wagers provided the prize money does not exceed Rs 1,000.

c. An agreement to contribute to a plate or prize of the value of above Rs 500 to be awarded to the winner of a horse race. [Section 30]

d. Contracts of insurance.

Effects of Wagering Agreements [Section 30]:

The effects of wagering agreements are given as under:

i. Agreements by way of wager are void in India.

ii. Agreements by way of wager have been declared illegal in the states of Maharashtra and Gujarat.

iii. No suit can be filed to recover the amount won on any wager.

iv. Transaction which are collateral to wagering agreements are not void in India except in the states of Maharashtra and Gujarat.

v. Transactions which are collateral to wagering agreements are illegal in the states of Maharashtra and Gujarat.

Example: A Cricket match is to be held between India and Pakistan. X agrees to pay Rs 1,00,000 to Y if India wins the match and agrees to deposit the money with Z, a third person of confidence for this purpose. X borrows Rs 1,00,000 from W. The implications of this case are summarised as under:

a. The agreement between X and Y is a wagering agreement because the performance of an agreement depends upon the happening or non-happening of a future uncertain event and each party stands to win or lose.

b. If India wins the match, Y (a winner) cannot recover the amount but X (a loser) can recover if the amount has not been paid to Y. Thus, a winner cannot recover the amount but a loser can if the amount has not been paid to the winner.

c. If India wins the match and Z (a stakeholder) pays the money to Y (a winner), X (a loser) cannot recover it from Z. [Bridger vs. Savage]

d. The agreement between X and W which is a collateral to wagering agreement, is valid in India except in the States of Maharashtra and Gujarat. Thus, W can recover the money from X if the agreement between X and Y is entered into in India except in the States of Maharashtra and Gujarat but W cannot recover the money from X if the agreement between X and Y is entered into in the States of Maharashtra or Gujarat

AGREEMENTS CONTINGENT ON IMPOSSIBLE EVENTS [SEC. 36]
According to Section 36 of the Indian Contract Act, 1872 contingent agreements to do or not to do anything, if an impossible event happens are void whether the impossibility of the event is known or not to the parties to the agreement at the time it is made.

Example: A agrees to pay Rs 1,000 if B marries C (a Hindu) who is already married to D. This agreement is void.

AGREEMENTS TO DO IMPOSSIBLE ACTS [Section. 56]:

According to Section 56 of the Indian Contract Act, 1872, “An agreement to do an impossible act is void.”

Example: A undertakes to put life into the dead wife of B. This agreement is void.

1.6.8 RESTITUTION [SECTIONS. 64 AND 65]

Restitution means 'return or restoration of benefit.' The provisions relating to restitution are given below:

Case	*Provision*
When a person at whose option a contract is voidable rescinds it [Section 64].	The party rescinding a voidable contract must restore the benefit to the person from whom he has received it.
When an agreement is discovered 11) be void or the contract becomes void [Section 65].	The person who has received any benefit or advantage under such agreement or contract must restore it or compensate for it to the person from whom he has received it.

Example I: A, a singer contracts with B the manager of a theatre to sing at his theatre for two nights every week during the next two months and B agrees to pay her Rs 100 for each night's performance. On the sixth night, A wilfully absents herself from the theatre and B in consequence rescinds the contract, B must pay A for the five nights on which she had sung.

Example II: A contracts to sing for B on a specified day and receives an advance of Rs 1,000 but is unable to sing due to serious illness on that day. Since the contract has become void. A must return Rs 1,000 to B.

Non-applicability of the Principle of Restitution:

The principle of restitution does not apply to contracts which are void ab-initio with the exception where the minor has entered into agreement by misrepresenting his age.

Example I: X pays Rs 1,000 to Y to beat Z. Y does not beat Z. X claims Rs 1,000 from Y. X cannot recover anything because this agreement is void ab-initio.

Example II: X advances Rs 10,000 to Y, a married woman to enable her to obtain a divorce from her husband. Y agrees to marry X as soon as she obtained a divorce. Y obtains the divorce but refuses to marry X. X cannot recover anything from Y because this agreement is void ab-initio. [Baiviji vs. Hamda Nagar].

1.6.9 QUASI-CONTRACTS

Meaning
A Quasi-contract is not a contract at all because one or the other essentials for the formation of a contract are absent. It is an obligation imposed by law upon a person for the

benefit of another even in the absence of a contract. It is on the principle of equity, which means no person shall be allowed to unjustly enrich himself at the expense of another. Such obligations are called quasi-contracts or implied contracts because the outcome of such obligations resemble those created by a contract.

Features of a Quasi-contract:

The salient features of a quasi contract are as under:

i. It is imposed by law and does not arise from any agreement.

ii. The duty of a party and not the promise of any party is the basis of such contract.

iii. The right under it is always a right to money and generally, though not always, to a liquidated sum of money.

iv. The right under it is available against specific person(s) and not against the world.

v. A suit for its breach may be filed in the same way as in case of a complete contract.

QUASI-CONTRACTS AND OTHER CONTRACTS
Distinction between Quasi-Contracts and Contracts

Quasi-contracts differ from other contracts in the following respects:

Basis of distinction	*Quasi-contract Contract*	*Contract*
1. Essential for the formation of a valid contract	The essentials for the formation of a valid contract are absent.	The essentials for the formation of a valid contract are present.
2. Obligation	Obligation is imposed by law.	Obligation is created by the consent of the parties.

Check your progress – 6:

Discuss the agreements that are opposed to public policy.

LESSON-7

PERFORMANCE OF A CONTRACT

CONTENTS

Performance of the contract is one of the various modes of discharge of the contract. A contract is said to have been performed when the parties to a contract either perform or offer to perform their respective promises. Section 37 of the Indian Contract Act lays down the obligation of the parties regarding performance. According to this section,

"The parties to a contract must either perform or offer to perform their respective promises, unless such performance is dispensed with or excused under the provisions of this Act, or of any other law."

1.7.1 TYPES OF PERFORMANCE

There may be two types of performance as follows:

a. Actual Performance:

Where a promisor has made an offer of performance to the promisee and the offer has been accepted by the promisee, it is called an actual performance.

Example: X contracted to deliver to Y at his warehouse on 1st Oct., 100 bales of cotton of particular quality. X brought the cotton of requisite quality to the appointed place on the appointed day during the business hours, and Y took the delivery of goods. This is an actual performance.

b. Attempted Performance (or Tender) [Section 38]

Where a promisor has made an offer of performance to the promisee, and the offer has not been accepted by the promisee, it is called an attempted performance (Section 38).

Example: If in the aforesaid example, Y refused to take the delivery of goods, it is a case attempted performance because X has done what he was required to do under the contract.

1.7.2 EFFECTS OF TENDER

There are two effects of tender as under:

a. The promisor is not responsible for non-performance.

b. The promisor does not lose his rights under the contract.

Types of tender

Types of tender	*Meaning*	*Effects*
1. Tender of goods or services	Where the promisor offers to deliver the goods or services but the promisee refuses to accept the delivery.	a. Goods or services need not be offered again. b. Promisor may sue the promisee for non-performance c. Promisor is discharged from his liability.
2. Tender of money	Where the promisor offers to pay the amount but the promisee refuses to accept the same.	a. Promisor is not discharged from his liability to pay the amount. b. Promisor will not be liable for interest from the date of a valid tender.

1.7.3 ESSENTIALS OF A VALID TENDER

1. Unconditional:
   It must be unconditional. Tender is said to be unconditional when it is made in accordance with the terms of the contract.

Example: X offers to deliver 100 bales of cotton to Y if Y sells his one machine to X. It is a conditional tender and hence invalid.

2. At Proper Time:
   It must be at proper time, i.e. at the stipulated time (if there is an agreement as to time) or during business hours (if there is no agreement as to time). Tender of goods or money before the due date is also not a valid tender.

3. At Proper Place:
   It must be at proper place, i.e. at the stipulated place (if there is an agreement as to place) or at promisee's business place (if there is business) or at promisee's residence (if there is no business place).

4. Reasonable Opportunity to Promisee:
   It must give a reasonable opportunity to the promisee of ascertaining that the goods offered are the same as the promisor is bound to deliver.

5. For Whole Obligation:
   It must be for the whole obligation and not for a part of the whole obligation. However, a minor deviation from the terms of the contract may not render the tender invalid.

Example: Delivery of 100.10 tons of wheat in a contract for 100 tons of wheat is a valid r but delivery of 120 tons of wheat is invalid tender.

6. To Proper Person:
   It must be made to the promisee or his duly authorised agent. In case of several joint promisees, a tender made to one of them has the same legal consequences as tender to all of them.

7. Of Exact Amount and in Legal Tender:
   In case of tender of money, it must be of exact amount and in legal tender.

1.7.4 EFFECT OF REFUSAL OF PARTY TO PERFORM PROMISE WHOLLY

When a party to a contract has refused to perform or disabled himself from performing his promise in its entirety, the promisee may put an end to the contract, unless he has signified, by words or conduct, his acquiescence in its continuance.

Example I: A, a singer enters into a contract with B, the manager of a theatre, to sing at theatre two nights in every week during the next two months, and B engages to pay her 100 for each night's performance. On the sixth night, A wilfully absents herself from the theatre. B is at liberty to put an end to the contract.
Example II: A, a singer enters into a contract with B, the manager of a theatre, to sing at theatre two nights every week during the next two months and B engages to pay her at rate of Rs 100 for each night. On the sixth night, A wilfully absents herself. With the assent of B, A sings on the seventh night. B has signified his acquiescence in the continuation of the contract, and cannot now put an end to it, but is entitled to compensation for damage sustained by him through A's failure to sing on the sixth night.

1.7.5 PERSONS WHO CAN DEMAND PERFORMANCE

The persons who can demand performance are:

1. Promisee:
   Promisee can only demand the performance of the promise under a contract. For example, X promises Y to pay Rs 1,000 to Z. It is only Y who can demand performance and not Z.

2. Legal Representative:
   In case of death of the promisee, his legal representative can demand performance unless a contrary intention appears from the contract or the contract is of a personal nature. For example, X promises to marry Y on the specified day. Y dies before the specified day. The legal representatives Y cannot demand performance of the promise from X because the contract is of personal nature.

3. Third Party:
   A third party can also demand the performance of the contract in some exceptional cases like beneficiary in case of trust, the person for whose benefit the provision is made in family arrangements.

4. Joint Promisees:
   In case of several promisees, unless a contrary intention appears, the performance can be demanded by the following persons:

Case	*Who can demand the performance of promise*
I. In case all the promisees are alive	All the promisees jointly.
II. In case of death of any of joint promisees	Representatives of deceased promisee jointly with the surviving promisee(s)
III. In case of death of all joint promisees	Representatives of all of them jointly.

Example: X promises Y and Z jointly to repay loan of Rs 1,000 on a specified day. Y dies before that specified day. Y's representative jointly with Z can demand the performance from X on specified day. If Y and Z die before that specified day, the representatives of Y and Z jointly can demand the performance from X on specified day.

1.7.6 PERSONS WHO MUST PERFORM

1. Promisor:

   If it appears from the nature of the case that it was the intention of the parties to any contract that any promise contained in it should be performed by the promisor himself, such promise must be performed by the promisor.

Example I: X promises to marry Y. X must perform this promise personally.

Example II: X promises to paint a picture for Y. X must perform the promise personally.

2. Promisor's Agent:
   If it was not the intention of the parties that the promise be performed by the promisor himself, such contracts can be performed by the promisor himself or any competent person employed by him.

Example: A promises to pay B a sum of money. A may perform this promise either by personally paying the money to B, or by causing it to be paid to B by another, and if A dies before the time appointed for payment, his representatives must perform the promise, or employ some proper person to do so.

3. Legal Representatives:
   In case of death of promisor, his legal representative can perform the contract unless a contrary intention appears or the contract is of personal nature .

Example: X promises to marry Y. X dies. X's legal representative cannot perform this promise.

4. Third Party [Section 41]:
   A contract can be performed by a third party if the promisee accepts the arrangement. According to Section 41, when a promisee accepts performance of the promise from a third person, he cannot afterwards enforce it against the promisor.

5. Joint Promisors [Section 42]:
   In case of several promisors, unless a contrary intention appears, the following persons must perform the promise:

Case	*Who must perform the promise*
In case all the promisors are alive	All the promisors jointly.
In case of death of any of joint promisors	Representatives of the deceased promisor jointly with the surviving promisor(s).
In case of death of all joint promisors	Representatives of all of them jointly.

Check your progress – 7:

Who can demand performance of contracts?

LESSON-8

DISCHARGE OF A CONTRACT

CONTENTS

Discharge of a contract means termination of the contractual relations between the parties to a contract. A contract is said to be discharged when the rights and obligations of the parties under the contract come to an end.

1.8.1 MODES OF DISCHARGE OF CONTRACT

A contract may be discharged in various modes.

I. Discharge by Performance:
A contract can be discharged by performance in any of the following ways:

1. Actual Performance:
A contract is said to be discharged by actual performance when the parties to the contract perform their promises in accordance with the terms of the contract.

2. Attempted Performance or Tender:
So far as the tenderer of performance is concerned, a contract is said to be discharged by attempted performance when the promisor has made an offer of performance to the promisee but it has not been accepted by the promisee.

II. Discharge by Mutual Agreement

Since a contract is created by mutual agreement, it can also be discharged by mutual agreement. A contract can be discharged by mutual agreement in any of the following ways:

1. Novation [Section 62]:
Novation means the substitution of a new contract for the actual contract. Such a new contract may be either between the same parties or between different parties. The consideration for the new contract is the discharge of the original contract.

Example: A owes money to B under a contract. It is agreed between A, B and C that B shall henceforth accept C as his debtor, instead of A. The old debt of A to B no longer exists a new debt from C to B has been contracted.

2. Rescission [Section 62]:
Rescission means cancellation of the contract by any or all the parties to a contract.

Example: X promises Y to sell and deliver 100 Bales of cotton on 1st Oct. at his godown and Y promises to pay for goods on 1st Nov. X does not supply the goods. Y may rescind the contract.

3. Alteration [Section 62]:
   Alteration means a change in the terms of a contract with mutual consent of the parties. Alteration discharges the original contract and creates a new contract. However, parties to the new contract must not change.

Example: X promises to sell and deliver 100 bales of cotton on 1st Qct. and Y promises to pay for goods on 1st Nov. Afterwards, X and Y mutually decide that the goods shall be delivered in five equal instalments at Z's godown. Here, original contract has been discharged and a new contract has come into effect.

4. Remission [Section 63]:
   Remission means acceptance by the promisee of a lesser fulfilment of the promise made. According to Section 63, "Every promisee may dispense with or remit, wholly or in part, the performance of the promise made to him, or may extend the time for such performance, or may accept instead of it any satisfaction which he thinks fit."

Example I: A promises to paint a picture for B. B afterwards forbids him to do so. A is no longer bound to perform the promise.

Example II: A owes B Rs 5,000. A pays to B, and B accepts, in satisfaction of the whole debt Rs 2,000 paid at the time and place at which Rs 5,000 were payable. The whole debt is discharged.

5. Waiver:
   Waiver means intentional relinquishment of a right under the contract. Thus, it amounts to releasing a person of certain legal obligation under a contract. e.g., A promises to supply goods to Y. Subsequently, Y exempts X from carrying out the promise. This amounts to waiving the right of performance on the part of Y.

III. Discharge by Operation of Law

A contract may be discharged by operation of law in the following cases:

1. By Death of the Promisor;
   A contract involving the personal skill or ability of the promisor is discharged on the death of the promisor.

2. By Insolvency:
   When a person is declared insolvent, he is discharged from his liability up to the date of his insolvency.

3. By Unauthorised Material Alteration:
   If any party makes any material alteration in the terms of the contract without the approval of the other party, contract comes to an end.

4. By the Identity of Promisor and Promisee:
   When the promisor becomes the promisee, the other parties are discharged.

Example: X draws a bill receivable on Y who accepts the same. X endorses the bill in favour of Z who in turn endorses in favour of Y. Here, Y is both promisor and promisee and hence the other parties are discharged.

IV. Discharge by impossibility of Performance.

The effects of impossibility of the performance of a contract may be discussed under the following two heads:

1. Effects of Initial Impossibility [Section 56 Para 1 and 3]:
   Initial impossibility means the impossibility existing at the time of making the contract.

2. Effects of Supervening Impossibility [Section 56 Para 2]:
   Supervening impossibility means impossibility which does not exist at the time of making the contract but which arises subsequently after the formation of the contract.

Cases when a Contract is discharged on the Ground of Supervening Impossibility:

A contract is discharged by supervening impossibility in the following cases:

a. Destruction of Subject Matter:
   The contract is discharged if the subject matter the contract is destroyed after the formation of the contract without any fault of party.

Example: X agreed to sell his crop of wheat. The entire crop was destroyed by fire though fault of the party. The contract was discharged.

b. Death or Personal Incapacity:
   The contract is discharged on the death or incapacity or illness of a person if the performance of a contract depends on his personal skill or ability.

Example: X agreed to sing on a specified day. X fell seriously ill and could not perform on that day. The contract was discharged.

c. Declaration of war:
   The pending contracts at the time of declaration of warvare either suspended or declared as void.

Example: X contracts to take in cargo for Y at a foreign port. X’s government afterwards declares war against the country in which the port is situated. The contract becomes when void when the war is declared.

d. Change of Law:
The contract is discharged if the performance of the con becomes impossible or unlawful due to change in law after the formation of contract.

Example: X agreed to sell his land to Y. After the formation of the contract, the Government issued a notification and acquired the land. The contract was discharged. [Shyam Sunder vs. Durga]

e. Non-existence or Non-occurrence of a Particular State of Things necessary for performance:
The contract is discharged if that particular state of thing which forms the basis of a contract ceases to exist or occur.

Example: X and Y contract to marry each other. Before the time fixed for the marriage, X goes mad. The contract becomes void.

Cases when the Contract is not discharged on the Ground of Supervening Impossibility:

Impossibility of performance is, as a rule, not an excuse from performance. It means that when a person has promised to do something, he must perform his promise unless the performance becomes absolutely impossible. A contract is discharged by the supervening impossibility in the following cases:

a. Difficulty of Performance:
A contract is not discharged simply on the ground that its performance has become more difficult, more expensive or less profitable than that agreed at the time of its formation.

Example: X agreed to supply coal within a specified time. He failed to supply in because of government's restriction on the transport of coal from collieries. Here X will be discharged because the coal was available in the open market from where X could have obtained it.

b. Commercial Impossibility:
A contract is not discharged simply on the ground of commercial impossibility, i.e. when the contract becomes commercially unviable or unprofitable.

Example : X, a furniture manufacturer agreed to supply certain furniture to Y at an agreed rate. Afterwards, there was a sharp increase in the rates of the timber and rates of wages. Since it was no longer profitable to supply at the agreed rate, X did not supply. X will not be discharged on the ground of commercial impossibility.

c. Default of a Third Party:
A contract is not discharged if it could not be performed because of the default of a third party on whose work the promisor relied.

Example: X entered into a contract with Y for the sale of goods to be manufactured by Z, a manufacturer of those goods. Z did not manufacture those goods. X will not be discharged be and will liable to Y for damages.

d. Strikes, Lockouts and Civil Disturbances:
A contract is not discharged on the grounds of strikes, lockouts and civil disturbances unless otherwise agreed by the parties to the contract.

Example: X agreed to supply to Y certain goods to be imported from Algeria. The goods could not be imported due to riots in that country. It was held that this was no excuse for non-performance of the contract. [Jacobs vs. Credit Lyonnais]

e. Partial Impossibility:
A contract is not discharged simply on the ground of impossibility of some of the objects of the contract.

V. Discharge by lapse of time

A contract is discharged if it is not performed or enforced within a specified period, called period of limitation. The Limitation Act, 1963 has prescribed the different periods for different contracts, e.g. period of limitation for exercising right to recover a debt is 3 years, and to recover an immovable property is 12 years. The contractual parties cannot exercise their rights after the expiry of period of limitation.

VI. Discharge by breach of contract

A contract is said to be discharged by breach of contract if any party to the contract refuses or fails to perform his part of the contract or by his act makes it impossible to perform his obligation under the contract. A breach of contract may occur in the following two ways:

1. Anticipatory Breach of Contract:
Anticipatory breach of contract occurs when the party declares his intention of not performing the contract before the performance is due.

2. Actual Breach of Contract:
Actual breach of contract occurs in the following two ways:

a. On Due Date of Performance:
If any party to a contract refuses or fails to perform his part of the contract at the time fixed for performance, it is called an actual breach of contract on due date of performance.

b. During the Course of Performance:
If any party has performed a part of the contract and then refuses or fails to perform the remaining part of the contract, it is called an actual breach of contract during the course of performance.

Consequences of Breach of Contract:
The aggrieved party (i.e. the party not at fault) is discharged from his obligation and gets rights to proceed against the party at fault.

Check your progress – 8:

How can contracts be discharged?

LESSON-9

REMEDIES FOR BREACH OF CONTRACT

CONTENTS

A breach of contract occurs if any party refuses or fails to perform his part of the contract or by his act makes it impossible to perform his obligation under the contract. In case of breach, the aggrieved party (i.e. the party not at fault) is relieved from performing his obligation and gets a right to proceed against the party at fault. A breach of contract may arise in two ways,

1. Anticipatory Breach of Contract:
   Anticipatory breach of contract occurs when the party declares his intention of not performing the contract before the performance is due.

2. Actual Breach of Contract:
   Actual breach of contract occurs in the following two ways:

i. On Due Date of Performance:
   If any party to a contract refuses or fails to perform his part of the contract at the time fixed for performance, it is called an actual breach of contract on due date of performance.

ii. During the Course of Performance:
   If any party has performed a part of the contract and then refuses or fails to perform the remaining part of the contract, it is called an actual breach of contract during the course of performance.

1.9.1 CONSEQUENCES OF BREACH OF CONTRACT

The aggrieved party (i.e. the party not at fault) is discharged from his obligation and gets rights to proceed against the party at fault.

Options Available to Aggrieved Party [Section 39]:

In case of anticipatory breach, the aggrieved party has the following two options

1. He can rescind the contract and claim damages for breach of contract without waiting until the due date for performance, or
2. He may treat the contract as operative and wait till the due date for performance and claim damages if the promise still remains unperformed.

Consequences of Treating Contract as Operative:

In case of anticipatory breach, if the aggrieved party treats the contract as operative and waits till the due date for performance, the consequences will be as follows:

1. The promisor may perform his promise on or before the due date of performance and the promisee will be bound to accept the performance.
2. The promisor may take advantage of the discharge by supervening impossibility arising between the date of breach and the due date of the performance and in such a case, the promisee shall lose his right to sue for damages.

Amount of Damages:

The amount of damages in each of the options exercised by an aggrieved party will be calculated as under:

Option exercised	*Amount of damages*
1. When the aggrieved party rescinds the contract at the date of breach	The amount of damages will be equal to the difference between the prices prevailing on the date of breach and the contract price.
2. When the aggrieved party does not rescind the contract at the date of breach	The amount of damages will be equal to the difference between the price prevailing on the due date of performance and the contract price.

ACTUAL BREACH OF CONTRACT

Actual breach of contract may take place in any of the following two ways:

1. On due Date of Performance:
   If any party to contract refuses or fails to perform his part of the contract at the time fixed for performance, it is called an actual breach of contract on due date of performance.

Example: X agreed to sell to Y 10 tons of wheat @ Rs 8,000 per ton to be delivered in two instalments on 20th October and on 21st October. On 20th October, X refused to deliver the goods. It is an actual breach of contract on due date of performance.

2. During the Course of Performance:
   If any party has performed a part of the contract and then refuses or fails to perform the remaining part of the contract, it is an actual breach of contract during the course of performance.

Example: X agreed to sell to Y 10 tons of wheat@ Rs 8,000 per ton to be delivered in two instalments on 20th October and 21st October. On 20th October, X delivered 5 tons and refused to deliver remaining 5 tons. It is an actual breach of contract during the course of performance.

1.9.2 REMEDIES FOR BREACH OF CONTRACT

Meaning of Remedy

A remedy is the course of action available to an aggrieved party (i.e. the party at default) for the enforcement of a right under a contract.

I. Rescission of contract [Section 39]:
   Rescission means a right not to perform obligation.
   In case of breach of a contract, the promisee may put an end to the contract. In case, the aggrieved party is discharged from all the obligations under the contract and is entitled to claim compensation for the damage which he has sustained because of the non-performance of the contract.

II. Suit for Damages:
   Damages are monetary compensation allowed for loss suffered by the aggrieved party due to breach of a contract. The object of awarding damages is not to punish the party at fault but to make good the financial loss suffered by the aggrieved party due to the breach of contract.

Compensation for Loss or Damage Caused by Breach of Contract [Section 73]:
Section 73, of the Indian Contract Act which deals with compensation for damage caused by breach of contract is based on the judgement in the previous cases of such nature. It states that the aggrieved party may claim the damages as follows:

i. Ordinary Damages:

   Ordinary damages are those which naturally arise in the usual course of things from such breach. These damages can be recovered if the following two conditions are fulfilled:

a. The aggrieved party must suffer by breach of contract, and

b. The damages must be proximate (i.e. direct) consequence of the breach of contract and not the indirect consequence.

Measure of Ordinary Damages: In a contract for the sale of goods, the measure of ordinary damages is the difference between the contract price and the market price of such goods on the date of breach.

ii. Special Damages:
Special damages are those which may reasonably be supposed to have been in the contemplation of both parties as the probable result of the breach of a contract. These damages can be recovered if the special circumstances which would result in a special loss in case of breach of a contract are communicated to the promisor, e.g. loss of profits on account of default by the other party to the contract can be claimed only when an advance notice of such damages has been given before.

iii. Exemplary or Punitive or Vindictive Damages;
Exemplary damages are those which are in the nature of punishment. The court may award these damages in case of

a. a breach of promise to marry, where damages shall be calculated on the basis of mental injury sustained by the aggrieved party,

b. wrongful dishonour of a cheque by a banker. In case of wrongful dishonour of a cheque, the rule is smaller the amount of the cheque, larger will be the amount of damages awarded. A trader may recover such damages as wrongful dishonour of cheque shall adversely affect his goodwill but a non-trader whose cheque is wrongfully dishonoured will have to prove the loss of goodwill before claiming such damages.

iv. Nominal Damages:
Nominal damages are those which are awarded where there is only a technical violation of a legal right but the aggrieved party has not in fact suffered any loss because of breach of contract. These damages are called nominal because they are very small, say, one rupee. The court may or may not award these nominal damages.

v. Damages for inconvenience and discomfort:
If a party has suffered physical inconvenience and discomfort due to breach of contract, that party can recover the damages for such inconvenience and discomfort.

vi. Liquidated damages and penalty:

When the parties to a contract at the time of formation of contract, specify a sum which will become payable by the party responsible for breach, such specified sum is called:

a. *Liquidated Damages* if the specified sum represents a fair and genuine pre-estimate of the damages likely to result due to breach;

b. *Penalty* if the specified sum is disproportionate to the damages likely to result due to breach.

vii. Stipulation of Interest:
The stipulation of interest may or may not be in the nature of penalty. If the stipulation for interest is in the nature of penalty, the court may award reasonable compensation only.

viii. Forfeiture of Security Deposit (or Earnest Money):
A clause in a contract which provides for forfeiture of security deposit in the event of failure to perform is in the nature of a penalty. In such cases, the court may award reasonable compensation only.

III. Suit for Specific Performance:
Suit for specific performance means demanding the court's direction to the defaulting party to carry out the promise according to the terms of the contract.

Example: X agreed to sell an old painting to Y for Rs 50,000. Subsequently, X refused to sell the painting. Here, Y may file a suit against X for the specific performance of the contract.

Cases where suit for specific performance is not maintainable.

a. Where the damages are considered as an adequate remedy.
b. Where the contract is of personal nature, e.g. contract to marry.
c. Where the contract is made by a company beyond its powers as laid down in its Memorandum of Association.
d. Where the court cannot supervise the performance of the contract.
e. Where one of the parties is a minor.
f. Where the contract is inequitable to either party.

IV. Suit for Injunction:
Suit for injunction means demanding court's stay order. Injunction means an order of the court which prohibits a person to do a particular act. Where a party to a contract does something which he promised not to do, the court may issue an order prohibiting him from doing so.

V. Suit for Quantum Meruit:
Quantum Meruit means as much as is earned. Right to Quantum Meruit means a right to claim the compensation for the work already done.

Example: C an owner of a magazine engaged P to write a book to be published by instalments in his magazine. After a few instalments were published, the publication of the magazine was stopped. It was held that P could claim payment for the part already published [Planche vs. Calburn].

Check your progress – 9:

What are the remedies for breach of contract?

LESSON-10

INDEMNITY AND GUARANTEE

CONTENTS

The contract of Indemnity and Contract of Guarantee are specific types of contracts. The specific provisions relating to these contracts are contained in Secc124 to 147 of the Indian Contract Act, 1872. In addition to these specific provisions, the general principles of contracts are also applicable to such specific contracts.

1.10.1 CONTRACT OF INDEMNITY

'Indemnity' means to make good the loss or to compensate the party who suffered some loss.

Meaning of Contract of Indemnity [Section 124]
A contract by which one party promises to save the other from loss caused to him conduct of the promisor himself, or by the conduct of any other person, is a 'contract of indemnity'.

Example: A contracts to indemnify B against the consequences of any proceedings which C may take against B in respect of a certain sum of Rs 2,00,000. This is a contract of indemnity.

Meaning of Indemnifier :
The person who promises to make good the loss is called the 'indemnifier'. In the example, A is the indemnifier.

Meaning of Indemnity-Holder

The person whose loss is to be made good is called 'indemnity-holder'. In the example, B is the indemnity-holder.

Whether Contract of Indemnity Covers the Cases of Loss Caused by the Events or Accidents which do not Depend upon the Conduct of the Promisor or other Person:

If the definition of contract of indemnity as per Section 124 is strictly interpreted, it would not cover the cases of loss caused by the events or accidents which do depend upon the

conduct of the promisor or any other person. In other words, contracts of insurance would be outside the purview of the contract of indemnity.

Since the intention of law makers had never been to exclude the contracts of insurance from the purview of contracts of indemnity, the courts in India have decided to apply the same equitable principles that the courts in England do. As English law, a contract of indemnity is defined as ‘a promise to save another less from loss caused as a result of a transaction entered into at the instance of promisor.’ This definition covers a promise to make good the loss arising from any cause whatsoever.

Thus, Indian courts follow the English law in respect of contract of indemnity which covers the contracts of insurance also.

Rights of Indemnity-holder:
An indemnity holder is entitled to recover the following amounts from the indemnifier provided he acts within the scope of his authority.

1. All damages which he may be compelled to pay in any suit in respect of matter to which the promise to indemnify applies;
2. All costs which he may be compelled to pay, in bringing or defending suit if, he did not contravene the orders of the promisor, and acted as would have been prudent for him to act in the absence of any contract indemnity, or if the promisor authorized him to bring or defend the suit.
3. All sums which he may have paid under the terms of any compromise of such suit, if the compromise was not contrary to the orders of the promisor and was one which it would have been prudent for the promisee to make in the absence of any contract of indemnity, or if the promisor authorized him to compromise the suit.

Modes of Contract of Indemnity
A contract of indemnity may be express or implied.

a. A contract of indemnity is said to be express when a person expressly promises to compensate the other from loss.
b. A contract of indemnity is said to be implied when it is to be inferred from the conduct of the parties or from the circumstances of the case.

Essential Elements of Contract of Indemnity:
In addition to the implied or express promise to indemnify, all the essentials of a contract must also be present.

1.10.2 CONTRACTS OF GUARANTEE

Meaning of a Contract of Guarantee [Section 126]

A contract of guarantee is a contract to perform a promise or discharge the liability of a third person in case of his default.

Example: X and his friend Y enter a shop and X says to Z "Supply the goods required by Y and if he does not pay you, I will." It is a contract of guarantee.

Parties to a contract of Guarantee:

There are three parties to a contract of guarantee.

Principal Debtor [Section 126]:

The person in respect of whose default the guarantee is given is called the 'Principal debtor'. Y is the principal in the aforesaid example.

Creditor [Section 126]:

The person, to whom the guarantee is given, is called the 'creditor'. Z is the creditor in the aforesaid example.

Surety [Section 126]:

The person who gives the guarantee is called 'Surety'. X is the surety in the aforesaid example.

Essential Features of a contract of guarantee:

1. Tripartite Agreement:

   A contract of guarantee is a tripartite agreement between the principal debtor, creditor and surety.

2. Consent of Three Parties:

   There must be consent of all the three parties.

3. Existence of a Liability:

   There must be an existing liability or a promise whose performance is guaranteed. Such liability or promise must be enforceable by law. Hence, guarantee can be given only for liability or promise which is enforceable by law. But there is an exception to this rule. The exception is a g given for minor's debt. Though minor's debt is not enforceable by law, yet the guarantee given for minor's debt is valid.

4. Essentials of a Valid Contract:

   All the essentials of a valid contract must be present in a contract of guarantee.

5. Guarantee not to be Obtained by Misrepresentation [Section 142]:

   Any guarantee which has been obtained by means of misrepresentation made by the creditor, or with his knowledge and assent, concerning a material part of the transaction, is invalid.

6. Guarantee not to be Obtained by Concealment [Section 143];

   Any guarantee which the creditor has obtained by means of keeping silence as to material circumstances is invalid.

Basis	*Contract of indemnity*	*Contract of guarantee*
1. No. of parties	There are two parties-indemnifier and the indemnity-holder.	There are three parties-principal debtor, creditor and surety.
2. No. of contracts	There is only one contract between indemnifier and indemnity-holder.	There are three contracts, one between creditor and principal debtor, second between surety and principal debtor, and the third between surety and the creditor.
3. Undertaking	The indemnifier undertakes to save the indemnity-holder from any loss.	The surety undertakes for payment of debts of principal debtor.
4. Nature of liability	The liability of indemnifier is primary and unconditional.	The liability of surety is secondary and conditional. Surety' liability is secondary in the sense that the primary liability is principal debtor. Surety's liability is conditional in the sense it arises only on default of principal debtor.
5.Nature of event	The liability arises only on the happening of a contingency.	The liability arises only on the non-performance of an existing promise or non-payment of existing debt.
6.Request	The indemnifier need not act at the request of indemnity-holder.	The surety acts at the request of the principal debtor.

7.Right to sue	The indemnifier cannot sue a third party in his own name because of absence of privity of contract between him and a third party. He can sue the third party in his own name if there is an assignment in his favour.	A surety, on discharging the debt of principal debtor, can sue principal debtor in his own name.

Check your progress – 10:

What are contracts of indemnity and guarantee?

LESSON-11

BAILMENT AND PLEDGE

CONTENTS

Indian Contract Act, 1872 deals with the general rules relating to bailment but not with all types of bailment for which separate acts have been enacted, for example, The Carrier Act 1865, The Railways Act, 1890, The Carriage of Goods by Sea Act, 1925.

1.11.1 MEANING OF BAILMENT

The word 'Bailment' is derived from a French word 'baillier' which means 'to deliver'. According to Section 148, a "bailment" is the delivery of goods by one person to another for some purpose, upon a contract that they shall, when the purpose is accomplished, be returned or otherwise disposed off according to the directions of the person delivering them.

Explanation:
If a person already in possession of the goods of another contracts to hold them as a bailee, he thereby becomes the bailee, and the owner becomes the bailor of such goods, although they may not have been delivered by way of bailment.

The person delivering the goods is called the 'bailor'.

The person to whom the goods are delivered is called the 'bailee'.

Examples of bailment:

1. X who is going out of station delivers a horse to Y for proper care.
2. X lends a horse to Y for his riding only without charge.
3. Y hires a horse from X for riding.
4. X delivers a horse to a doctor, Y, for medical treatment.
5. X sells a horse to Y who leaves the horse in the possession of X.

Essential elements of a Bailment:

1. Agreement:

   There must be an agreement between the bailor and the bailee. This agreement may be either express or implied. However, a bailment may be implied by law also. For example, bailment between a finder of goods and owner of goods.

2. Delivery of Goods:

   There must be delivery of goods. It means that possession of goods must be transferred.

a. The delivery must be voluntary; for example, the delivery of jewellery its owner to a thief who shows a revolver, does not create a bailment because the delivery is not voluntary.

b. Delivery may be actual or constructive.
   Actual Delivery:
   A delivery is said to be actual where the goods are physically handed over by one person to another. For example, delivery of a car for repairs a workshop dealer.
   Constructive Delivery [Section 149]:
   A delivery is said to be constructive when it is made by doing anything which has the effect of putting goods in the possession of the intended bailee or of any person authorized to hold them on his behalf. For example, delivery of the key of a car to a workshop dealer for the repair of the car.

3. Purpose:
   The delivery of goods must be for some intended purpose. For example, wrong delivery of goods to Jaipur Golden Roadways instead of Patel Roadways, does not create any bailment.

4. Return of Specific Goods:
   The goods which form the subject matter of bailment must be returned to the bailor or otherwise disposed off according to directions of the bailor, after the accomplishment of purpose or after the expiry period of the bailment. It may be noted that the same goods (which were delivered by bailor to bailee) must be returned in their original form or desired form (if any required by the bailor). Thus, the goods must be retured in specie (same) though they may undergo a change in form.

1.11.2 PLEDGE

Meaning of Pledge (or Pawn) [Section 172]

The bailment of goods as security for payment of a debt or performance of a promise is called pledge (or pawn).

Example: X borrows Rs 1,00,000 from Citi Bank and keeps his shares as security for payment of a debt. It is a contract of pledge.

Meaning of a Pawnor (or Pledgor) [Section 172]

The person who delivers the goods as security for payment of a debt or performance of a promise is called the Pawnor or Pledgor. In the aforesaid example, X is the pawnor.

Meaning of Pawnee (or Pledgee) [Section 172]

The person to whom the goods are delivered as security for payment of a debt or performance of a promise is called the Pawnee or Pledgee. In the aforesaid example, Citi Bank is the pawnee.

Special Feature of Pledge:

It is the special property in goods and not the general property in goods, which passes to the pledgee. General property means the ownership of goods and special property means the possession of goods.

Example: A producer of a film borrowed Rs 10,00,000 from a financier-distributor and agreed deliver the final prints of the film when ready. This agreement was not a pledge because there was no actual transfer of possession. [Revenue Authority vs. Sudarshan Pictures]

Distinction between Pledge and Bailment:

Basis of distinction	Pledge	Bailment
I. Purpose	Pledge is bailment of goods for a specific purpose, i.e. repayment of a debt or performance of a duty.	Bailment is for a purpose of any kind.
III. Right to use	Pawnee cannot use the goods pledged.	Bailee can use the goods as per terms of bailment.
IV. Right to sell	Pawnee can sell the goods pledged after giving notice to the pawnor in case of default by the pawnor.	Bailee can either retain the goods or sue the bailor for his dues.

Check your progress – 11:

Define bailment and pledge.

LESSON-12

CONTRACT OF AGENCY

CONTENTS

AIMS AND OBJECTIVES

On reading this unit, you will be able to

i. Understand the concepts of agency, agents and principal
ii. Analyse the need for contract of agency
iii. Differentiate between the various types of agents
iv. Have an idea about the rights and duties of agents
v. Discuss the methods by which agency relationships can be established

INTRODUCTION

Since it is not always possible for a person to do everything by himself, it becomes necessary to delegate some of the acts to be performed by another person. Such another person is called an agent. The person represented is called the principal.

1.12.1 CONTRACT OF AGENCY

The law relating to agency is contained in Chapter X (Sections 182 to 238) of the Indian Contract Act, 1872.

Definition of Agent and Principal

AGENT

Meaning of an Agent (Section 182):

An agent is a person employed to do any act for another person or to represent another person in dealings with third persons. Thus, an agent establishes a contract between such another person and third person.

Who may be an Agent (Section 184):

As between the principal and third persons, any person (whether he has contractual capacity or not) may become an agent. Thus, a minor or person of unsound mind can also become an agent.

Agent's responsibility to his Principal:

An agent who is not of the age of majority and of sound mind is not responsible to his principal.

Example: X hands over to Y, a minor, a TV set worth Rs.18,500 and instructs him not to sell it for below Rs.19,000. Y sells the same to Z for Rs.18,000. X will be responsible to Z for the act of Y, but Y himself will not be responsible to X since he has no contractual capacity.

PRINCIPAL

Meaning of Principal (Section 182):

The person for whom act is done by an agent or who is represented in dealings with third persons by an agent is called the Principal.

Who may employ Agent (Section 183):

Any person who is of the age of majority according to the law to which he is subject, and who is of sound mind, may employ an agent. Thus, a minor or a person of unsound mind cannot appoint an agent. It has been held that a guardian of a minor can appoint an agent to minor. [Madan Lal Vs. Bheru Lal].

1.12.2: ESSENTIALS OF RELATIONSHIP OF AGENCY

Following are the essentials of the relationship of agency:

1. Agreement between the principal and the agent:
   Agency depends on agreement but not necessarily on contract. As between the principal and third persons, any person may become an agent (Sec.184). As such, even a minor or a person of unsound mind can be an agent. The principal is, however, liable for the acts of such an agent.

2. No consideration necessary:
   No consideration is necessary to create an agency (Sec.185). The fact that the principal has agreed to be represented by the agent is sufficient.

3. Intention of the agent to act on behalf of the principal:
   Whether a person does intend to act on behalf of another is a question of fact. Where a person does intend to act on behalf of another person, agency may arise, although the contract between the parties provides that there is no such relationship.

1.12.3 RULES OF AGENCY

There are two important rules of an agency:

1. Whatever a person can do personally, he can do through an agent:
   This rule is of course subject to certain well-known exceptions as when the act to be performed is personal in character. Eg. The principal cannot ask his agent to become insolvent on his behalf or to marry on his behalf.

2. He who does an act through another does it by himself:
   What a person does by another, he does by himself. Thus, the acts of the agent are the acts of the principal.

1.12.4 TEST OF AGENCY

The true test of agency lies in answering the question whether a person has the capacity to create contractual relationship between the principal and a third party and to bind the principal by his acts. If the answer to this question is yes, there exists the relationship of agency, otherwise not.

Check your progress – 12:

What do you understand by contract of agency?

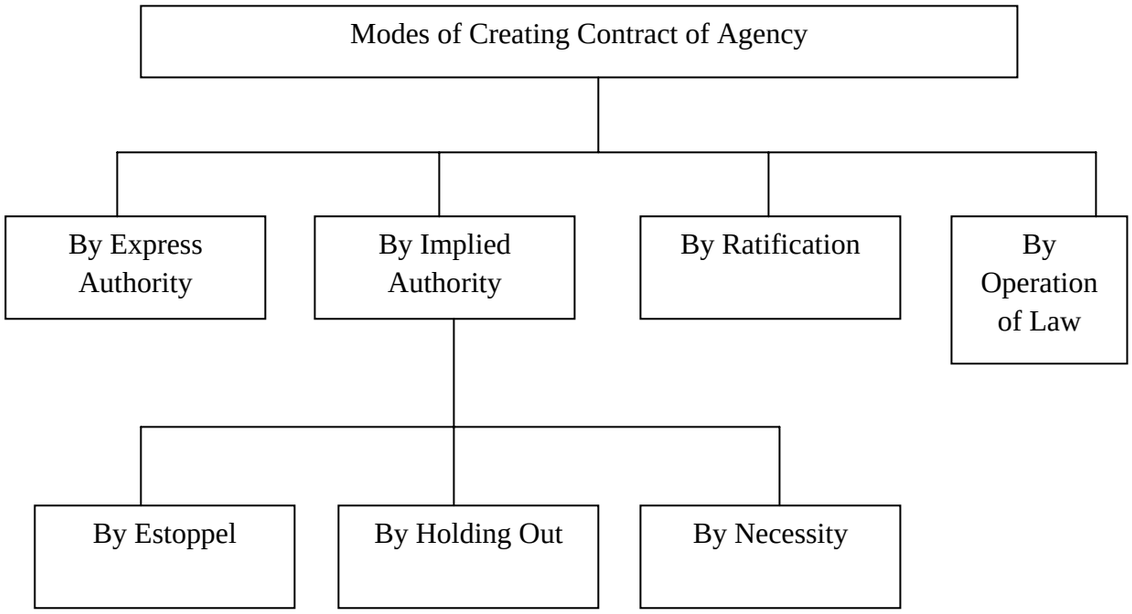
LESSON-13

CREATION OF AGENCY

CONTENTS

1.13.1 MODES OF CREATION OF AGENCY

The various modes to create the contract of agency are shown below:



I.Agency by Express Authority (Sections 186 and 187)
An agency by express authority is created when an express authority is given to the agent by spoken or written words.
Example: X owns a shop, appoints Y to manage his shop by executing a power of attorney in Y's favour. Here, the relationship of principal and agent has been created between X and Y by an express authority.
II.Agency by Implied Authority (Section 187)
An agency which has to be understood from the conduct and behaviour of the parties is called implied agency. It is to be inferred from the circumstances of the case and things

spoken or written, or the ordinary course of dealing may be accounted as circumstances of the case.

Example: A owns a shop in Ooty, but he lives in Chennai. He visits his shop occasionally. The shop is managed by B, and he is in the habit of ordering goods from C in the name of A for the purposes of the shop and of paying for them out of A's funds with A's knowledge. B has an implied authority from A to order goods from C in the name of A for the purposes of the shop.

Implied agency includes the following:
Agency by Estoppel:
Agency by estoppel arises where a person by his words or conduct induces third persons to believe that a certain person is his agent. The person who induces as such is stopped or prevented from denying the truth of agency. Section 237 of the Act deals with agency by estoppel.

Example: X tells Y, in the presence and within the hearing of Z that he (X) is Z's agent. Z does not say anything against this statement. Later on Y enters into a contract with X believing that X is Z's agent. In such a case, Z is bound by this contract and in a suit (case) between Z and Y, Z cannot be permitted to say that X was not his agent, even though X was not actually his agent.

Agency by Holding Out:
Agency by holding out is almost similar to agency by estoppel. Such agency arises when a person by his past affirmative or positive conduct makes third person to believe that person doing some act on his behalf is doing with authority.
Example: X allows Y, his servant to purchase goods for him on credit from Z and later on pays for them. One day X pays cash to Y to purchase goods. Y keeps the money and purchases goods on credit from Z. Z can recover the price of his goods from X because X had held out Z as his agent on earlier occasions.

Agency by Necessity:
Agency by necessity arises under the following two conditions:
There is an actual and definite necessary for acting on behalf of the principal, and
It is impossible to communicate with the principal and get his consent
The act must have been done for the benefit of the principal.

Example I : X consigned some vegetables from Deli to Mumbai by a truck. The truck met with an accident. The vegetables, being perishable were sold by the transporter. This sale is binding on X. In this case, the transporter became an agent by necessity. [Sim & Co. Vs. Midland Railway Co.]

Example II : X stored some furniture in Y's house free of charge. After three years, Y needed the space occupied by the furniture. He obtained X's address from is bank and wrote two letters to him but he received no reply. Y then sold the furniture. It was held

that the sale was not binding on the owner because there was no emergency which required the sale of furniture. [Sachs Vs. Mikos]

III.Agency by Ratification (Section 196)
A person may act on behalf of another person without his knowledge or consent. For example, A may act as P's agent though he has no prior authority from P. In such a case, P may subsequently either accept the act of A or reject it. If he accepts the act of A, done without his consent, he is said to have ratified that act and it places the parties in exactly the same position in which they would have been if A had P's authority at the time he made the contract. Likewise, when an agent exceeds the authority given to him by the principal, the principal may ratify the unauthorised act.

Thus, when the principal approves an act of the agent who never had the authority to undertake such an act, it is called Ratification.
Ratification may be express or may be implied by the conduct of the person on whose behalf the acts are done.
Ratification relates back to the date when the act was done by the agent.
Example: A insures P's goods without his authority. If P ratifies A's act, the policy will be as valid as if A had been authorised to insure the goods [Williams Vs. North China Insurance Co., (18760]

Requisites of a valid ratification:

1. No valid ratification can be made by a person whose knowledge of the facts of the case is materially defective.

2. The ratification must be made for the whole transaction and not for a part of transaction. When a person ratifies a part of the unauthorised transaction, it is treated as the ratification of the whole transaction.

3. An act which has the effect of subjecting a third person to damages or of terminating any right or interest of a third person cannot be ratified.

4. The acts done by the agent on behalf of another person can only be ratified. Thus, the acts done by the agent in his own name cannot be ratified.

5. The principal must be in existence at the time when the act is done in his name.

6. The principal must have contractual capacity both at the time of contract and at the time of ratification.

7. The ratification must be done within a reasonable time, otherwise it will not be binding.

8. Only those acts which are lawful can be ratified.

9. Only those acts which are within the principal's power can be ratified. Thus, an act which is beyond the competence of a principal cannot be ratified.

10. The ratification must be communicated to the third party so as to be binding on the third party.

IV.Agency by Operation of Law:

Agency by operation of law is said to arise where the law treats one person as an agent of another.

Example: On formation of a partnership, every partner becomes the agent of other partner. Such agency is said to be arisen by operation of law.

When a company is formed, its promoters are its agents by operation of law.

Check your progress – 13:

Explain the modes by which agencies can be created.

LESSON-14
CLASSIFICATION OF AGENTS

CONTENTS

1.14.1 GENERAL CLASSIFICATION OF AGENTS

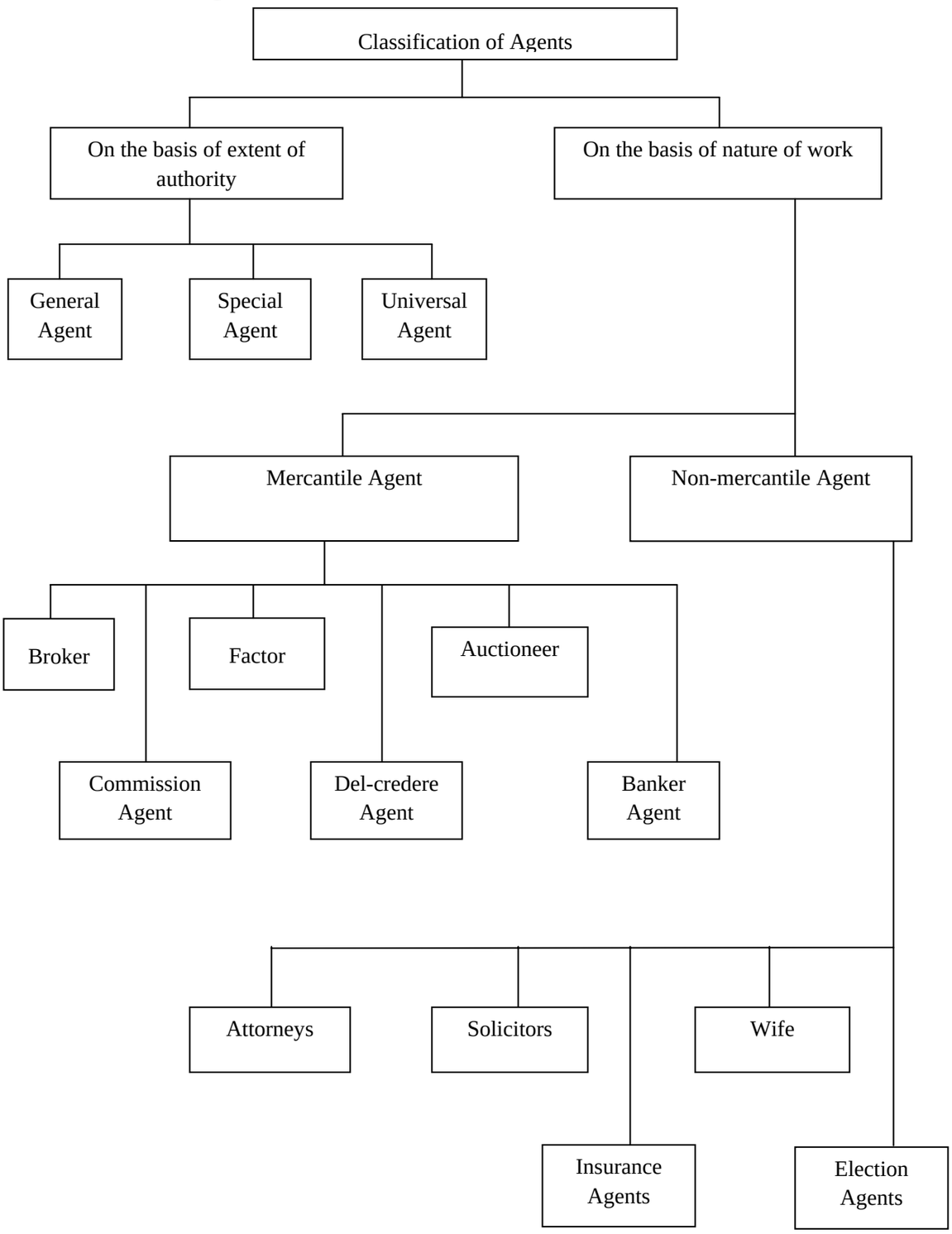
A general classification of agents from the point of view of the extent of their authority is as follows:

1. **Special Agent**: A special agent is one who is appointed to perform a particular act or to represent his principal in some particular transaction as, for example, an agent employed to sell a house or an agent employed to bid at an auction. Such an agent has a limited authority and as soon as the act is performed, his authority comes to an end. He cannot bind his principal in any matter other than that for which he is employed. The persons who deal with him are bound to ascertain the extent of his authority.

2. **General Agent**: A general agent is one who has authority to do all acts connected with a particular trade, business or employment. For example, the manager (general agent) of a firm has an implied authority to bind his principal by doing anything necessary for carrying on the business of the firm or which falls within the ordinary scope of the business. Such authority of the agent is continuous until it is put to an end. If the principal, by secret instructions, limits the authority of the general agent, and the agent exceeds the authority, the principal is bound by the agent's acts done within the scope of his authority, unless the third parties dealing with the agent have a notice of the curtailment of the authority of the agent.

3. **Universal Agent**: A universal agent is one whose authority to act for the principal is unlimited. He has authority to bind his principal by any act which he does, provide that act
   i. Is legal
   ii. Is agreeable to the law of the land.

Classification of Agents:



I. Commercial or Mercantile Agents:

A 'Mercantile agent', according to Sec.2 (9) of the Sale of Goods Act, 1930, means a "mercantile agent having in the customary course of business as such agent, authority either to sell goods, or to consign goods for the purposes of sale, or to buy goods, or to raise money on the security of goods".

a. Factor: A factor is a mercantile agent entrusted with the possession of goods and who has the authority to buy, sell or otherwise deal with the goods or to raise money on their security. He has general lien on the goods.

b. Broker: A broker is one who negotiates and makes contracts between the principal and the third party. He is not entrusted with the possession of goods and hence he has no lien on the goods.

c. Auctioneer: An auctioneer is one who is entrusted with the possession of goods for sale at a public auction. He has only a particular lien on the goods for his charges.

d. Commission Agent: The term 'commission agent' is a general term which is used in practice even for a factor or broker. He is employed to buy and sell goods, or transact business generally for other person receiving for his labour and trouble a money payment, called commission.

e. Del-credere Agent: A del-credere agent is one who gives guarantee to his principal to the effect that the third person with whom he enters into contracts shall perform his obligation. He gives such guarantee for an extra remuneration which is called the Del-credere Commission. For example, an agent who also undertakes the risk of bad debts due to the insolvency of customers to whom the goods were sold on credit will be called the del-credere agent.

f. Banker: Banker acts as an agent of the customer when he collects cheques or drafts or bills or buys or sells securities on behalf of his customers. He has a general lien in respect of the general balance of account.

II. Non-Mercantile Agents:

These include attorneys, solicitors, insurance agents, election agents, clearing and forwarding agents and wife. etc.

Check your progress – 14:

Write about types of agents

LESSON-15

EXTENT OF AGENT'S AUTHORITY

CONTENTS

1.15.1 AGENT'S AUTHORITY

An agent's authority means the capacity of the agent to bind his principal. The authority of the agent to bind the principal may be-

a. Actual or Real Authority, or

b. Ostensible or Apparent Authority

a. Actual or Real Authority
Actual Authority of an agent is the authority conferred on him by the principal. It may be expressed or implied (Sec.186)
Express Authority: Authority is said to be express when it is given by words spoken or written (Sec.187)
An authority is said to be Implied when it is to be inferred from the circumstances of the case; and things spoken or written r the ordinary course of dealing may be accounted circumstances of the case (Sec.187)

b. Ostensible or Apparent Authority
When an agent is employed for a particular business, persons dealing with him can presume that he has authority to do all such acts as are necessary or incidental to such business. Such authority of the agent is called ostensible or apparent authority as distinguished from actual or real authority. The scope of an agent's authority is determined by his ostensible authority. If the act of

Extent of agent's authority means the scope of authority of an agent. In other words, it means what a person can do as an agent on behalf of his principal. Extent of agent's authority may be discussed under normal circumstances and emergency circumstances.

1.15.2 EXTENT OF AGENT'S AUTHORITY

Extent of Agent's Authority under Normal Circumstances (Section 188)

An agent having an authority to do an act has authority to do every lawful thing which is necessary in order to do such act. An agent having an authority to carry on a business has authority to do every lawful thing necessary for the purpose or usually done in the course of conducting such business.

Example: A appoints B, his agent to carry on his business of a ship-builder. B may purchase timber and other materials, and hire workmen for the purpose of carrying on the business.

Extent of Agent's Authority in Emergency (Section 189)

An agent has authority, in an emergency, to do all such acts for the purpose of protecting his principal from loss as would be done by a person of ordinary prudence, in his own case, under similar circumstances.

Example: Where butter was in danger of becoming useless owing to delay in transit and it was impossible to obtain instructions of the principal, the railway company sold the butter for the best available price. It was held that the principal was bound by this sale. [Sim & Co. Vs. Midland Rail Co.]

1.15.3 DELEGATION OF AUTHORITY OF AGENT

The general rule is that an agent is not entitled to delegate his authority to another person without the consent of his principal. 'Delegatus non potest delegare' is the maxim which means that a person to whom authority has been given, cannot delegate that authority to another. Sec.190 also prohibits delegation of such authority. This is because when the principal appoints a particular agent to act on his behalf, he relies upon the agent's skill, integrity and competence.

Sub-agent:

A 'Sub-agent' is a person employed by, and acting under the control of, the original agent in the business of the agency (Sec.191). This means he is an agent of the original agent. The relation of the sub-agent to the original agent is, as between themselves, that of the agent and principal.

Exceptions:

Sec.190 provides that an agent may appoint a sub-agent and delegate the work to him if-

i. There is a custom of trade to that effect, (eg. Article clerks employed by a Chartered Accountant) or
ii. The nature of work is such that a sub-agent is necessary.

There are some more exceptions recognised by the English law. These exceptions are also recognised in India and are as follows:

iii. Where the principal is aware of the intention of the agent to appoint a sub-agent but does not object to it.
iv. Where unforeseen emergencies arise rendering appointment of a sub-agent necessary.
v. Where the act to be done is purely ministerial not involving confidence or use of discretion.
vi. Where the principal permits appointment of a sub-agent.
vii. Where the duties of the agent do not require any personalised skill, confidence or discretion and the work involved is of routine nature.

Relationship between principal and sub-agent: As a general rule, an agent cannot delegate his authority to a sub-agent. But in certain exceptional cases, he is permitted to do so. In such cases, the delegation of authority to a sub-agent is proper. In all other cases, the appointment of a sub-agent is improper. The legal relation between the principal and the sub-agent depends upon the crucial question, as to whether the appointment of the sub-agent is proper or improper.).

Co-agent or Substituted agent

A Co-agent or a substituted agent is a person who is named by the agent, on an express or implied authority from the principal, to act for the principal. He is not a sub-agent but an agent of the principal for such part of the business of the agency as is entrusted to him. He is the agent of the principal, though he is named, at the request of the principal, by the agent (Sec.194).

In selecting a co-agent for his principal an agent is bound to exercise the same amount of discretion as a man of ordinary prudence would exercise in his own case; and if he does this, he is not responsible to the principal for the acts or negligence of the co-agent (Sec.195).

Check your progress – 15:

Who are co-agents and sub-agents?

LESSON-16

POSITION OF PRINCIPAL AND AGENT IN RELATION TO THIRD PARTIES

CONTENTS

1.16.1 POSITION OF PRINCIPAL AND AGENT IN RELATION TO THIRD PARTIES

The position of a principal and his agent as regards contracts made by the agent with third parties may be discussed under the following three heads:

1. Where the principal's existence and name are disclosed by the agent, ie., where the principal is named
2. Where the principal's existence is disclosed but not his name, ie., where the principal is unnamed
3. Where both the existence and the name of the principal are not disclosed, ie., where the principal is undisclosed.

I. Named Principal:

The position of the named principal for the acts of his agent is as follows:

i. Acts of the agent are the acts of the principal:

The principal is liable for the acts of the agent with third persons provided his acts are done

a. Within the scope of his authority, and
b. In the course of his employment as an agent

He is also liable for such acts of the agent which are necessary for the proper execution of his (agent's) authority. Sec.226 further provides that contracts entered into through an agent, and obligations arising from acts done by an agent may be enforced in the same manner and will have the same legal consequences, as if the contracts had been entered into and the acts done by the principal.

Example: A is P's agent with authority to receive money on his behalf. He receives from T a sum of money due to P. T is discharged of his obligation to pay the sum in question to P.

ii. *When the agent exceeds his authority:*

When an agent exceeds his authority to do work of the principal, the principal is bound by that part of the work which is within his authority and which can be separated from the part which is beyond his authority (Sec.227)

Where an agent exceeds his authority, the principal may repudiate the whole of the transaction if what he (the agent) does beyond the scope of his authority cannot be separated from the rest (Sec.228)

iii. Notice given to agent as notice to principal:

The principal is bound by the notice given to or information obtained by the agent in course of the business of the principal (Sec.229). The principal is also bound by the admissions made by the agent.

But where the agent has committed a fraud on his principal, any information obtained by him or notice given to him is not regarded as having been obtained by the principal. In such cases the knowledge of the agent is not imputed to the principal because of the extreme improbability of the agent communicating his fraud to the principal. [Cave vs. Cave, (1880) 15 Ch. D. 630]

iv. *Principal inducing belief that agent's unauthorised acts were authorised:*

Where a person by his conduct, or by words spoken or written leads wilfully another person to believe that a certain state of affairs exists and induces him to act on that belief so as to alter his previous position, he is prohibited from denying subsequently the fact of that state of affairs [Pickard vs. Sears, (1837) 6 A. & E. 474].

v. Misrepresentation or fraud of agent:

The principal is liable for the misrepresentations made or frauds committed by the agent in the course of his business for the principal. Such misrepresentations or frauds have the same effect on agreements made by such agent as if these had been made or committed by the principal. However, misrepresentations made or frauds committed by the agent in matters, which do not fall within his authority, do not affect his principal. (Sec. 238).

II. Unnamed Principal:

When an agent contracts as an agent for a principal but does not disclose his name, the principal is liable for the contract of the agent, unless there is a trade custom or a term, express or implied, to the effect which makes the agent personally liable. If the third party

contracts knowing that there is a principal although his identity is not disclosed, he cannot sue the agent. If, however, the agent declines to disclose the identity of the principal, he will become personally liable on the contract.

III. Undisclosed Principal:

Sometimes, an agent not only conceals the name of the principal but also the fact that he is an agent. This gives rise to *the doctrine of undisclosed principal*. The agent in such case gives an impression to the third party as if he is contracting in an independent capacity.

Sec. 231 deals with rights of parties to a contract made by an agent for the undisclosed principal. The position of parties to such a contract may be discussed under the following heads:

a. The position of principal:

When an undisclosed principal is subsequently discovered or he himself intervenes, the other contracting party (if he has not already obtained judgment against the agent) may sue either the principal or the agent or both. The principal may also if he likes, require the performance of the contract from the other contracting party. But in such a case he must allow to the third party the benefit of all payments made by the third party to the agent.

b. The position of agent:

As between the principal and the agent, the agent has all the rights of an agent as against the principal; but as regards the third party, he is personally liable on the contract. He may be sued on the contract and he has the right to sue the third party.

c. The position of third parties:

i. In a contract with an agent for an undisclosed principal, the third party may elect to sue either the principal or the agent or both.

ii. If the principal discloses himself before the contract is completed, the other contracting party may refuse to fulfil the contract, if he can show that, if he had known who the principal was or that the agent was not the principal, he would not have entered into the contract (Sec. 231).

iii. The third party can also claim a right of set-off against the agent. Where the principal requires the performance of the contract, he can only obtain such performance as is subject to the rights and obligations subsisting between the agent and the other party to the contract (Sec. 232).

Liability of Pretended Agent

A person may sometimes untruly represent himself to be the authorised agent of another, and thereby induce a third person to deal with him as such agent. He is, in such a case, liable, if his alleged employer does not ratify his acts, to make compensation to the third person in respect of any loss or damage which he has incurred by so dealing (Sec. 235).

While the third person has the right to claim compensation from the pretended agent, the agent has no right to proceed against that person for the contract. Thus, a person with whom a contract has been entered into in the character of agent is not entitled to require the performance of it, if he was in reality acting, not as agent, but on his own account (Sec. 236).

1.16.2 PERSONAL LIABILITY OF AGENT

The general rule is that only the principal can enforce, and can be held liable on, a contract entered into by the agent except when there is a contract to the contrary.

General Rule [Section 230]

In the absence of any contract to that effect, an agent cannot personally enforce contract entered into by him on behalf of his principal, not is he personally bound by them.

When the agent becomes personally liable:

The circumstances under which an agent becomes personally liable are as follows:

a. In case of foreign principal:
Where the contract is made by an agent for the sale or purchase of goods for a merchant residing abroad, in the absence of any contract to the contrary, it is presumed that the agent is personally liable for such contracts.

b. In case of undisclosed principal:
Where the contract is made by an agent for an undisclosed principal, in the absence of any contract to the contrary, it is presumed that the agent is personally liable.

c. In case of incompetent principal:
Where a contract is made by an agent for a person who cannot be sued (e.g. minor, lunatic, foreign ambassador), in the absence of any contract to the contrary, it is presumed that the agent is personally liable.

d. In case of principal not in existence:
Where a contract is made by the promoter for a company not yet incorporated, the promoters are personally liable.

e. In case of act not ratified:
A person untruly representing himself to be the authorised agent of another, and thereby inducing a third person to deal with him as such agent, is liable, if his alleged employer does not ratify his acts, to make compensation to the other in respect of any loss or damage which he has incurred by so dealing.

f. In case of acts in his own name:
Where a contract is made by an agent without disclosing that he is contracting as an agent, the agent is personally liable.

g. In case of express agreement:
Where a contract made by an agent specifically provides for the personal liability of the agent, the agent will be personally liable.

h. In case of custom or usage of trade:
Where there is a custom or usage of trade making the agent personally liable, in the absence of any contract to the contrary, the agent is personally liable.

1.16.3 RIGHTS OF AN AGENT

The rights of an agent are as follows:

a. Right of Retainer [Section 217]

An agent has the right to retain, out of any sum received on account of the principal in the business of the agency, all money due to himself in respect of the following:

i. Advance made by him
ii. Expenses properly incurred by him in conducting such business.
iii. Such remuneration as may be payable to him for acting as an agent

b. Right to receive remuneration [Section 219 to 220]

The agent has the right to receive agreed remuneration (if there is an agreement to that effect) or usual remuneration as per the custom of the trade in which he has been employed (if there is not agreement to that effect)

c. Right of Lien [Section 221]

In the absence of any contract to contrary, an agent is entitled to retain goods, papers and other property whether movable or immovable, of the principal received by him, until the amount due to him for commission, disbursement and services in respect of the same has been paid or accounted for to him. Thus, this right of lien arises-

i. Only if there is no contract to the contrary
ii. Only in respect of those properties the possession of which has been lawfully acquired by the agent
iii. Only in respect of those properties in respect of which some amount is due to the agent

Thus, this lien is only a particular lien.

d. Right to be indemnified against consequences of lawful acts [Section 222]

The employer of an agent is bound to indemnify him against the consequences of all lawful acts done by such agent in exercise of the authority conferred upon him.

e. Right to be indemnified against consequences of acts done in good faith [Section 223]

Where one person employs another to do an act, and the agent does the act in good faith, the employer is liable to indemnify the agent against the consequences of that act, though it causes an injury to the rights of third person.

f. Right to receive compensation for injury caused by principal's neglect [Section 225]

The principal must make compensation to his agent in respect of injury caused to such agent by the principal's neglect or want of skill.

1.16.4 DUTIES OF AN AGENT

The various duties of an agent are as follows:

An agent owes a number of duties to his principal which varies in degree according to the nature of agency. These duties are as follows:

1. To carry out the work undertaken according to the directions given by the principal:

   In the absence of any such directions, he must acct according to the custom which prevails in doing business of the same kind at the place where he conducts such business. When he acts otherwise, if any loss be sustained, he must make it good to his principal, and, if any profit accrues, he must account for it [Sec.211]. If the agent's disobedience is material, the principal may even terminate the agency.

2. To carry out the work with reasonable care, skill and diligence:

   An agent is bound to conduct the business of the agency with as much skill as is generally possessed by persons engaged in similar business, unless the principal has notice if his want of skill. He is always bound to act with reasonable diligence, to use skill as he possesses, and to make compensation to his principal in respect of the direct consequence of his neglect, want of skill or misconduct. But he is not liable to his principal in respect of loss or damage which indirectly or remotely caused by such neglect, want of skill or misconduct [Sec. 212]

3. To render proper accounts to his principal:

4. An agent is bound to render proper accounts to his principal on demand. [Sec. 213]

5. To communicate with the principal in case of difficulty:

   It is the duty of an agent, in cases of difficulty, to use all reasonable diligence in communicating with his principal and in seeking to obtain his instructions [Sec. 214]

6. Not to deal on his own account:

   An agent must not deal on his own account in the business of the agency without first obtaining the consent of the principal and acquainting him with all the material circumstances which have come to his knowledge.

7. To pay sums received for the principal:

   An agent is bound to pay to his principal all sums received on his account [Sec. 218]. He may deduct therefrom all moneys due to himself in respect of advances made or expenses properly incurred by him in conducting such business and also such remuneration as may be payable to him for acting as agent [sec.217].

8. To protect and preserve the interests of the principal in case of his death or insolvency:

   When an agency is terminated by the principal dying or becoming of unsound mind, the agent is bound to take, on behalf of the representatives of his late principal, all reasonable steps for the protection and preservation of the interests entrusted to him [Sec. 209].

9. Not to use information obtained in the course of the agency against the principal:

   It is the duty of the agent to pass on any information which he receives in the course of the agency to his principal. Where he uses any such information against the interest of principal and the principal suffers a loss, he is bound to compensate the principal. The principal may also restrain the agent from using such information by an injunction.

10. Not to make secret profit from agency:

    An agent occupies fiduciary position. He must not, except with the knowledge and assent of the principal, make any profit beyond the agreed commission or remuneration.

11. Not to set up an adverse title:

    An agent must not set up his own title or the title of a third person (unless he proves a better title in that person) to the goods which he receives from the principal as an agent. If he does so, he will be liable for conversion (any act in relation to goods of another person which constitutes an unjustifiable denial of his title to them).

12. Not to put himself in a position where interest and duty conflict:

    An agent is under a duty, in all cases, to act in the interest of the principal. He must not put himself in a position where his duty to the principal and his personal interest conflict unless he has made full disclosure of his interest to his principal, specifying its exact nature and obtained his assent.

13. Not to delegate authority:

    An agent must not, as a general rule, depute another person to do what he has himself undertaken to do. This is subject to certain exceptions [Sec.190]

Check your progress – 16:

Discuss the duties of agents.

LESSON - 17

TERMINATION OF AGENCY

CONTENTS

Termination of agency implies the end of the relationship of principal and agent.

1.17.1 MODES OF TERMINATION OF AGENCY

The various modes in which the agency may be terminated are as follows:

I. Termination of agency by act of the parties

1. By Mutual agreement: An agency is terminated if the principal and agent mutually agree to do so.

2. By revocation of authority by the principal: An agency is terminated if the principal revokes the authority of his agent. It may be noted that the principal may revoke the authority of his agent at any time before the authority has been exercised so as to bind the principal.

3. By renunciation of agency by the agent: The agency is terminated if the agent himself renounces the business of agency.

II. Termination of agency by operation of law

1. On completion of the business of the agency [Section 201]
An agency is automatically terminated when the business of the agency is completed.

2. On death/ or on becoming of unsound mind of principal/agent [Section 201]
An agency is automatically terminated when the principal or agent dies or becomes of unsound mind.

3. On insolvency of the principal:
   An agency is automatically terminated when the principal becomes insolvent because an insolvent person is incompetent to enter into a contract.

4. On expiry of fixed period:
   An agency is automatically terminated when the fixed term of agency expires even though the business of the agency has not yet been completed.

5. On destruction of the subject-matter:
   An agency is automatically terminated when the subject matter of the contract ceases to exist.

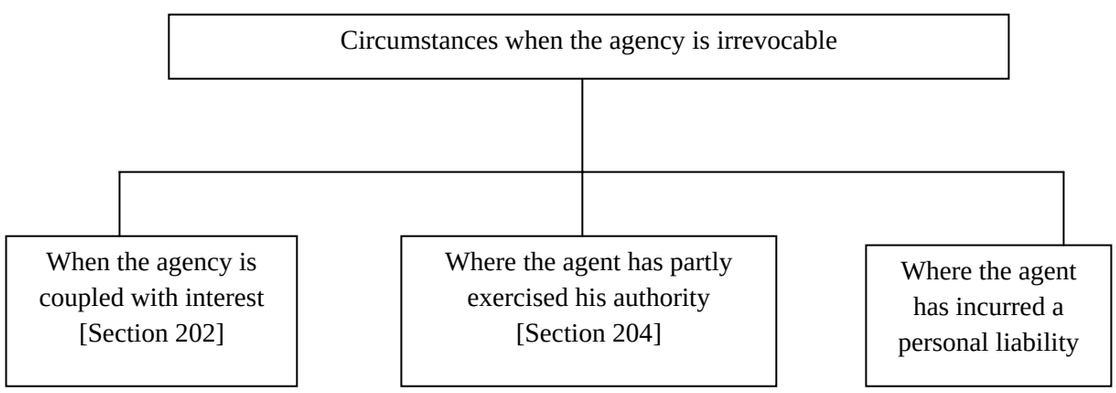
6. On winding up of company:
   An agency is automatically terminated when the principal or agent is a company and the company is wound up.

7. On principal becoming an alien enemy:
   An agency is automatically terminated when the principal and agent are citizen of two different countries and a war breaks out between these two countries.

1.17.2 IRREVOCABLE AGENCY

The term 'Irrevocable agency' means an agency which cannot be revoked or terminated by the principal.

The circumstances when the agency is irrevocable are:



a. Where the agency is coupled with interest:
   An agency is said to be coupled with interest when the object of creating the agency is to secure some benefit to the agent in addition to his remuneration as agent

b. Where the agent has partly exercised his authority:
The principal cannot revoke the authority given to his agent after the authority has been partly exercised, so far as regards such acts and obligations as arise from acts already done in the agency. Thus, the principal cannot revoke the agent's authority for the acts already done.

c. Where the agent has incurred a personal liability:
The principal cannot revoke the agent's authority for the authorised acts in respect of which the agent has already incurred a personal liability.

Check your progress – 17:

How are agencies terminated?

Lesson end activities:

1. X the principal, instructed Y his agent to insure the goods. Y failed to do so and the goods are destroyed by fire. Is Y liable to X?
2. Analyse various types of contracts and give your own examples for each of them.
3. Solve the following:

a. X invites Y to dinner. Y accepts the invitation but fails to turn up. Can X sue Y for damages?

b. X agrees to pay Rs.1,00,000 to Y if Y does not marry throughout his life. Y promises not to marry at all but later on X refuses to pay rs.1,00,000. Advise Y.

4. X the principal, instructed Y his agent to insure the goods. Y failed to do so and the goods are destroyed by fire. Is Y liable to X?

Let us sum up:

- CONTRACT
  According to Section 2(h) of the Indian Contract Act, 1872, "An agreement enforceable by law is a contract." In other words, an agreement which can be enforced in a court of law is known as a contract. A contract must have the following two elements.
  An agreement, and
  Its enforceability by law

- ESSENTIAL ELEMENTS OF A VALID CONTRACT

  Offer and acceptance

  Minimum two persons

  Intention to create legal relationship

  Lawful consideration

  Capacity of parties – Competency

  Free and genuine consent

  Lawful consideration

  Agreement not declared void

  Certainty and possibility of performance

  Legal formalities

- An offer is the starting point in the making of an agreement. An offer is also called 'proposal'. According to Section 2(a) of The Indian Contract Act, 1872, "A person is said to have made the proposal when he signifies to another his willingness to do or to abstain from doing anything with a view to obtaining the assent of that offer to such act or abstinence."

- Acceptance means giving consent to the offer. It is an expression by the offeree of his willingness to be bound by the terms of the offer. According to Section 2(b) of the Indian Contract Act, 1872, "A proposal is said to be accepted when the person to whom the proposal is made signifies his assent thereto. A proposal when accepted becomes a promise."

- The term 'revocation' means 'taking back' or 'withdrawal'.

- Minors, persons of unsound mind and persons prohibited by law cannot enter into contracts.

- The term 'consideration' means something in return.

- The consent means an act of assenting to an offer. "Two or more persons are said to consent when they agree upon the same thing in the same sense."

- The object and the consideration of an agreement must be lawful, otherwise, the agreement is void.

- Restitution means 'return or restoration of benefit.'

- A breach of contract occurs if any party refuses or fails to perform his part of the contract or by his act makes it impossible to perform his obligation under the contract. In case of breach, the aggrieved party (i.e. the party not at fault) is relieved from performing his obligation and gets a right to proceed against the party at fault.
- 'Indemnity' means to make good the loss or to compensate the party who suffered some loss.
- A contract of guarantee is a contract to perform a promise or discharge the liability of a third person in case of his default.
- An agent is a person employed to do any act for another person or to represent another person in dealings with third persons. Thus, an agent establishes a contract between such another person and third person.
- An agent's authority means the capacity of the agent to bind his principal.
- Termination of agency implies the end of the relationship of principal and agent.
- The term 'Irrevocable agency' means an agency which cannot be revoked or terminated by the principal