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LAW OF CONTRACT

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INTRODUCTION

The term law refers to rules of conduct enforced by the State to maintain peace and order in the society. Broadly speaking, law may be defined as the rules of conduct recognized 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.

Definition:

1. According to Salmond, “Law is the body of principles recognized and applied by the state in administration of justice”.
2. Austin says, “A law is a rule of conduct imposed and enforced by the sovereign”.
3. In the words of Holland, “law is a rule of external human actions enforced by sovereign political authority”.
4. According to Woodrow Wilson, “Law is that portion of the established habit and thought of mankind which has gained distinct and formal recognition in the shape of uniform rules backed by authority and power of the government”.

Mercantile Law Law being a wider subject touches all walks of our life. There are various branches of law concerning specific aspects e.g., civil, criminal, administrative, constitutional, business, labour laws, etc. The legal framework within which different business firms have to operate are largely governed by General Laws applicable to all forms of organisations-irrespective of their size and ownership. These laws fall into the category of mercantile laws. The terms business laws, commercial law and mercantile law are synonymous. The term ‘Mercantile Law’ is used to denote that branch of law which is concerned with such matters as are usually the subject of what may be called mercantile transactions. Basically, mercantile law 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. A mercantile person may be a single individual, a partnership or a joint stock company. These laws denote the aggregate body of legal rules connected with trade, industry and commerce. They provide for rules regarding the validity of making contracts and their performance. They deal with various types of contracts such as those relating to partnership, sale of goods, agency, bailsmen, indemnity and guarantee. Mercantile law also includes in its fold the laws relating to the joint stock companies, carriage of goods, negotiable instruments, insurance, arbitration, consumer protection, etc. However, the scope of mercantile law is ever widening due to increasing complexities of business world. The following laws are included in business or mercantile law:

1. Contract Act
2. Sale of Goods Act
3. Partnership Act
4. Companies Act
5. Negotiable Instruments Act
6. Banking Companies Act

7. Insurance Companies Act
8. Carriers and Carriage of Goods act
9. Commercial Securities Act
10. Patents and Copyright act
11. Insolvency Act
12. Arbitration Act

LAW OF CONTRACT

Law of contract is the most important and basic part of Mercantile law. It is not only the merchant or trader but every person who lives in the organized society, consciously or unconsciously enters into contracts from sunrise to sunset. The law of contract is contained in the Indian Contract Act, 1872 which — a. Deals with the general principles of law governing all contracts, and b. Covers the special provisions relating to special contracts like ailment, pledge, indemnity, guarantee and agency. When a person buys a computer or hires a taxi or goes to video library to buy a video cassette or takes a credit card from a bank or gives loan to another or he does booking for an orchestra/DJ for marriage party, he enters into and performs a contract though he may be unaware of this fact. Such contracts create legal relations giving rise to certain rights and obligations. The law of contract is designed to enforce rights and obligations in connection with the above activities. The object of Law of Contract is to ensure that the rights and obligations created by a contract are honored. That the expectations created by the promises of the parties to an agreement are fulfilled and that legal remedies are available to an aggrieved party against the party failing to perform his part of the agreement.

NATURE OF LAW OF CONTRACT

The law of contract is that branch of law which determines the circumstances in which a promise or an agreement shall be legally binding on the person making it. Unlike other branches of law, law of contract does not state a number of rights and duties, but lays down certain limiting principles within the framework of which the parties to an agreement may lay down their own terms and conditions. These will be upheld by the courts as long as they do not infringe upon any provisions of the law. The contracts being the basis of most of the business transactions, the law of contract is of particular significance to people (i.e., traders, factory owners, partnership firms, joint stock companies, banks, insurance companies, etc.) engaged in trading, commercial and industrial activities. In simple words, it may be said that the purpose of the law of contract is to ensure the realization of reasonable expectation of the parties who enter into a contract.

THE INDIAN CONTRACT ACT, 1872 The law relating to contracts in India is contained in the Indian Contract Act, 1872. The Act came into force with effect from September 1, 1872. It is applicable to the whole of India except the State of Jammu & Kashmir. The Act deals with a) The general principles of the law of contract (Secs. 1 to 75) which apply to all types of contracts irrespective of their nature and b) Some special contracts only (Secs. 124 to 238) The first six chapters of the Act (which embody the general principles) 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, viz., indemnity and guarantee [Chapter VIII (Secs. 124 to 147)], ailment and pledge [Chapter IX (Secs. 148 to 189)] and agency [Chapter X (Secs. 182 to 238)]. The Act

does not affect any usage or custom of trade (Sec. 1, para 1). The Act is not exhaustive. The Indian Contract Act does not profess to be a complete and exhaustive code because while enforcement it depends on English common law. It deals with the general principles of the law of contract and with some special contracts only. Some of the contracts not dealt with by the Act are those relating to partnership, sale of goods, negotiable instruments, insurance, bill of lading, etc. There are separate Acts which deal with these contracts. According to Section 1, "Nothing herein contained shall affect the provisions of any statute, Act or Regulation not hereby expressly repealed, nor usage or custom of trade, not inconsistent with the provisions of this Act".

CONTRACT

A contract is an agreement made between two or more parties which the law will enforce. A contract is an agreement to do or not to do an act. It is a legally binding agreement, which is enforceable at law.

Definition Sec. 2 (h) of the Indian Contract Act, 1872 defines contract as an agreement enforceable by law. According to Salmond, "contract is an agreement creating and defining obligations between the parties". In the words of Sir William Anson, "a legally binding agreement made between two or more persons by which rights are acquired by one or more to acts or forbearances (abstaining from doing something) on the part of other or others". Halsbury defines contract as, an agreement between two or more persons which is intended to be enforceable at law and is constituted by the acceptance by one party of an offer made to him by the other party to do or to abstain from doing some act. Sir Fredrick Pollock says, "Every agreement and promise enforceable at law is a contract". So, the subject matter of contract consists of two essential elements: a) Agreement and b) Its enforceability at law. a) Agreement: An agreement is defined in Section 2 (e) as every promise or every set of promises forming the consideration for each other. A promise is defined in Section 2 (b) as a proposal when accepted becomes a promise. An agreement involves a proposal or offer by one party and acceptance of the same by the other party. It requires existence of two or more persons i.e., plurality of persons because a person cannot enter into an agreement with himself. It also implies that the parties have a common intention about the subject matter of their agreement. Two parties should be thinking of the same thing in the same sense at the same time. Thus, an agreement is the outcome of two consenting minds i.e., consensus ad idem. Thus, Agreement = Offer + Acceptance b) Enforceable at Law: An agreement to become a contract must give rise to a legal obligation. The common acceptance formed and communicated between the two parties must create legal relations and not merely the relations which are purely social or domestic in nature. If the parties specify or the circumstances indicate that the parties intend to create legal relationship through it-even an agreement between husband and wife will be legally enforceable. On the other hand, if the two parties rule out legal obligation expressly the agreement will not be enforceable though it may be a trade agreement. Thus, Contract = Agreement + Enforceability at Law Therefore, all contracts are agreements but all agreements are not contracts.

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. All agreements are not contracts. Only that agreement which is enforceable at

law is a contract. In order to become a contract, an agreement must have the following essential elements:

1. Offer and Acceptance: In order to create a valid contract, there must be two or more parties because an individual cannot enter into an agreement with himself. It implies that one party makes a lawful proposal (offer) and the other party makes a lawful acceptance of the offer. The term lawful means offer and its acceptance must confirm to the rules laid down in the Indian Contract Act regarding valid offer and acceptance and its communication. For example, if Kumar makes a proposal to sell his house to Mahesh for Rs. 50,00,000 and Mahesh accepts the proposal, there will be a valid agreement between the two.
2. Intention to Create Legal Relationship: When 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.
3. Lawful Consideration: An agreement to be enforceable by law must be supported by consideration. 'Consideration' means an advantage or benefit moving from one party to the other. For a valid contract, the consideration need not necessarily be in terms of a price — the consideration can even be in the past, present or future — but the consideration needs to be real and lawful. [Secs. 2 (d), 23 and 25]. As per Section 2 (d), “when at the desire of the promisee, the promisee or any other person has done or abstained from doing, or does or abstains from doing, or promises to do or to abstain from doing an act, such act or abstinence or promise is called a consideration for the promise”.
4. Competency or Contractual Capacity of Parties: The parties to the agreement must be legally competent to enter into a valid contract. According to Section 11 of the Act, 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. If a party suffers from any flaw in capacity, the agreement is not enforceable except in some special cases.
5. 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. According to Section 13, the consent of the parties is said to be free when they are of the same mind on 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. The identity of views is the prerequisite. If such identity is not there, no agreement is possible. As per section 14, consent is said to be free when it is not caused by coercion or undue influence or fraud or misrepresentation or mistake.
6. Lawful Object: The object of an agreement must be lawful. Object has nothing to do with consideration. It means the purpose or design of the contract. Thus, when one hires a house for use as a gambling house, the object of the contract is to run a gambling house. The object is said to be unlawful if — a) it is forbidden by law; b) it is of such nature that if permitted it would defeat the provisions of any law; c) it is fraudulent; d) it involves an injury to the person or property of any other and e) the court regards it as immoral or opposed to public policy.
7. Certainty of Meaning: According to Section 29, agreements the meaning of which is not certain or capable of being made certain are void. The terms of the contract must be precise and certain and not vague or indefinite. A contract may be void on the ground of uncertainty. For example, a purported acceptance of an offer to buy lorry on

hire-purchase terms does not constitute a contract if the hire-purchase terms are never agreed.

8. Possibility of Performance: If the act is impossible in itself, physically or legally, it cannot be enforced at law.

9. Agreement not Declared Void or Illegal: The agreement though satisfying all the conditions for a valid contract must not have expressly declared void by any law in force in the country. Agreements mentioned in Sections 24 to 30 of the Contract Act have been expressly declared void for example agreements in restraint of trade, marriage, legal proceedings, etc.

10. Legal Formalities: An oral contract is a perfectly valid contract, except in those cases except where writing, registration, etc. is required by some statute. In India, writing is required in cases of sale, mortgage, lease and gift of immovable property, negotiable instruments, memorandum and articles of association of a company, etc. Registration is required in case of documents coming within the scope of section 17 of the Registration Act. If an agreement does not meet the above criteria, then it cannot be a contract. It will remain an agreement.

CLASSIFICATION OF CONTRACTS

Contracts may be classified into different categories depending upon their enforceability or validity, mode of creation or formation and extent of execution or performance.

A. CLASSIFICATION OF CONTRACTS ON THE BASIS OF ENFORCEABILITY

1. Valid Contracts: An agreement enforceable at law is a valid contract. An agreement becomes a contract when all the essentials of a valid contract as laid down in Section 10 are fulfilled. For example, A offers to sell his house for Rs. 10 lakh to B and B agrees to buy it for this price is a valid contract. Agreements falling short of legal requirements of Section 10 are Invalid contracts. These are:

2. Void Contract: An agreement which was legally enforceable when entered into but which has become void later on due to certain reasons such as supervening impossibility of performance or illegality are known as void contracts for e.g. when a war breaks out between the importing country and exporting country.

3. Void Agreements: According to Section 2 (g), an agreement which is not enforceable by law by either of the parties is said to be void. A void agreement does not create any legal rights or obligations. It is void initiation, i.e., from its very inception, for example, an agreement without consideration or with a minor.

4. 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 essential 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 (Secs. 19 and 19-A). Thus, a voidable contract is valid and enforceable until it is repudiated by the party entitled to avoid it.

5. 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. Such contracts will not be enforced by the courts until and unless the defect is rectified. 6. Illegal Contracts: A contract which is either prohibited by law or otherwise against the policy of law is an illegal agreement. It is void initiation. Thus, a contract to commit

audacity is an illegal contract and cannot be enforced at law. All illegal agreements are void but all void agreements or contracts are not necessary illegal.