

INDIAN CONTRACT ACT 1872

INTRODUCTION

The Law of Contract deals with the law relating to the general principles of contract. It is the most important part of Mercantile Law. It affects every person in one way or the other, as all of us enter into some kind of contract every day.

Contract: According to **Section 2(h)** of the Indian Contract Act, a contract is “an agreement enforceable by law.”

This definition shows that a contract must have the following two elements:

1. An agreement, and
2. Enforceability by law.

In other words: Contract = Agreement + Enforceability

Agreement (Section 2(e)): Every promise and every set of promises forming the consideration for each other is an agreement.

Promise (Section 2(b)): A proposal when accepted becomes a promise.

Every agreement is not a contract. When an agreement creates some legal obligations and is enforceable by law, it is regarded as a contract.

ESSENTIAL ELEMENTS OF CONTRACT

1. Offer and acceptance
2. Intention to create legal relationship
3. Free consent.
4. Capacity to contract.
5. Lawful consideration.
6. Lawful object.
7. Agreements not expressly declared void.
8. Possibility of performance.
9. Legal formalities.

CLASSIFICATION OF CONTRACTS

1. Classification according to validity

- a) Valid
- b) Voidable
- c) Void contracts or agreements
- d) Illegal.
- e) unenforceable

2. Classification according to mode of formation

- a) Express contract
- b) Implied contract
- c) Quasi contract

3. Classification according to Performance

- a) Executed contract
- b) Executory contract
- c) Unilateral Contract
- d) Bilateral Contract

OFFER AND ACCEPTANCE

Offer/Proposal [Section 2(a)]: “When one person signifies to another his willingness to do or to abstain from doing anything, with a view to obtaining the assent of that other to such act or abstinence, he is said to make a proposal.”

Essential requirements of a valid offer

1. An offer may be specific or general.
2. The terms of offer must be definite and certain.
3. The offer must be communicated to the offeree.
4. An offer must be distinguished an invitation to offer.
5. The offer must be made with a view to obtain acceptance.
6. The offer must be made with the intention of creating legal relations.

Acceptance [Section 2(b)]: “When the person to whom the proposal is made signifies his assent thereto, the proposal is said to be accepted”.

Essentials of a valid acceptance

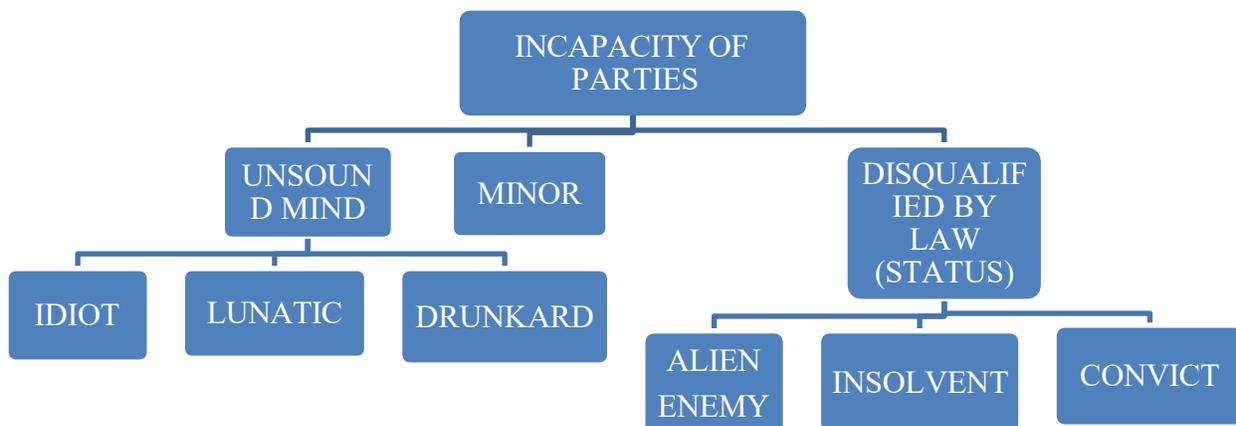
- 1) Acceptance should be by the person to whom the offer is made.
- 2) Acceptance must be absolute and unqualified.
- 3) Acceptance must be communicated to the offeror.
- 4) Acceptance must be according to the mode prescribed.
- 5) Mental acceptance is no acceptance
- 6) An offer must be accepted within the time fixed.
- 7) Acceptance must be made before the offer lapses or is revoked.

“**CONSIDERATION** is the price for which the promise of the other is bought and the promise thus given for value is enforceable. When a transaction takes place each party gets something. This something is called consideration”. (Pollock).

In simple words, it means ‘something in return.’

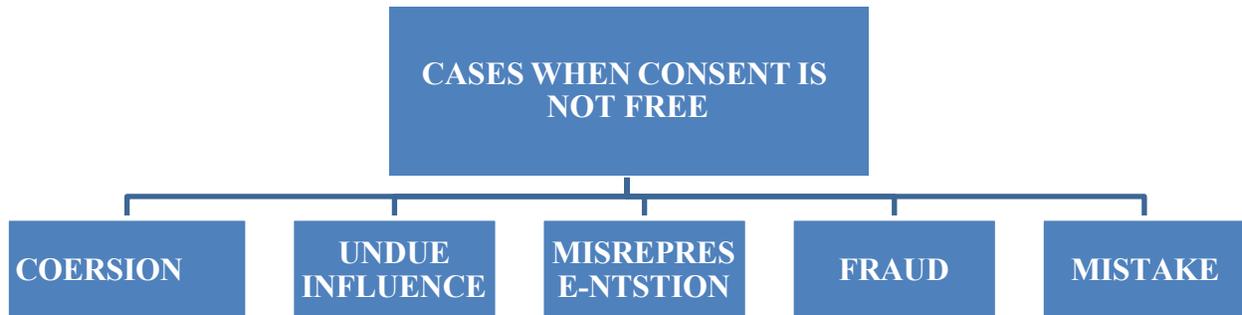
As a general rule “No consideration, no contract”.

CAPACITY TO CONTRACT (Section 11): “Every person is competent to contract who is of the age of majority according to the law to which he is subject, who is of sound mind and is not disqualified from contracting by any law to which he is subject”.



FREE CONSENT

When two or more persons agree upon the same thing in the same sense, they are said to consent.
(Section 13)



LEGALITY OF OBJECT (Section 23)

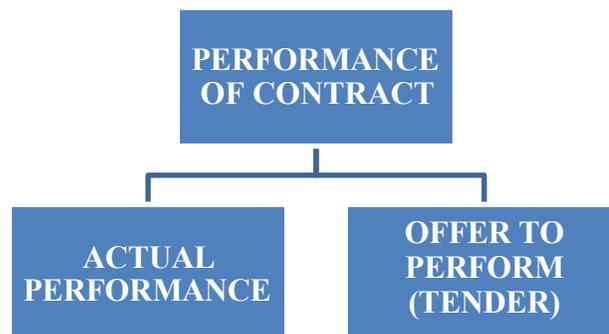
An agreement will not be enforceable if its object or the consideration is unlawful.

Consideration and objects which are unlawful – **agreement VOID**

1. If it is forbidden by law
2. If it is of such a nature that if permitted, it would defeat the provisions of any law.
2. If it is fraudulent.
4. If it involves or implies injury to the person or property of another.
5. If the Court regards it as immoral or opposed to public policy.

PERFORMANCE OF CONTRACTS

Performance means the parties have done whatever they had agreed to do. Performance may be:



(1) Actual Performance: When the parties have done whatever they had undertaken to do or have fulfilled their obligations arising out of the contract. Ex. A agrees to sell his watch to B for Rs.200. A delivers the watch and B makes the payment.

(2) Attempted Performance/Offer to perform (Section 38): If a valid offer/tender is made and it is not accepted by the promisee, the promisor shall not be responsible for non-performance nor shall he lose his rights under the contract. A tender or offer of performance to be valid must satisfy the following conditions:

1. It must be unconditional.

2. It must be made at proper time and place, and performed in the agreed manner.

WHO MUST PERFORM

- Promisor
- Agent of the promisor
- Legal Representative of the deceased promisor,

DISCHARGE OF CONTRACTS

BY PERFORMANCE

BY MUTUAL CONSENT

BY IMPOSSIBILITY

BY LAPSE OF TIME

BY OPERATION OF LAW

BY BREACH OF CONTRACT

REMEDIES FOR BREACH OF CONTRACT

As soon as either party commits a breach of the contract, the other party becomes entitled to any of the following reliefs: -

- a) Rescission of the contract
- b) Right to claim Damages (monetary compensation):
 - Ordinary damages
 - Special damages
 - Vindictive or exemplary damages
 - Nominal damages

CONTRACTS OF INDEMNITY [SECTIONS 124]

A contract of indemnity is a contract whereby one party promises to save the other from loss caused to him by the conduct of the promisor himself or by the conduct of any other party.

Ex. A and B two friends went to a shop. A says to the shopkeeper “Let B have the goods; I shall see you are paid.” It is a contract of indemnity.

Parties:

Indemnifier: The person who promises to make good the loss.

Indemnity Holder/Indemnified: the person whose loss is to be made good.

Rights of the Indemnity Holder: The indemnity holder is entitled to recover from the promisor

a) **All the damages which may be compelled to pay** in any suit in respect of any matter to which the promise to indemnify applies

b) **All costs of suit which he may have to pay to such third party** provided in bringing or defending the suit (i) he acted under the authority of the indemnifier or (ii) he did not act in contravention of the orders of the indemnifier and in such a such as a prudent man would act in his own case.

c) **All sums which he may have paid under the terms of any compromise** of any such suit, if the compromise was not contrary to the orders of the indemnifier, and was one which it would have been prudent for the promisee to make.

CONTRACT OF GUARANTEE [SECTION 126]

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

Parties:

- **Surety:** The person who gives the guarantee.
- **Principal Debtor:** The person in respect of whose default guarantee is given.
- **Creditor:** The person to whom the guarantee is given.

It must be noted that in a contract of guarantee there must, in effect be two contracts, a principal contract - the principal debtor and the creditor; and a secondary contract - the creditor and the surety.

Special Features of a Contract of Guarantee

1. Surety's obligation is dependent on principal-debtor's default.
2. Separate consideration for guarantee not necessary.
3. Principal-debtor need not be competent to contract.
4. There must be existing debt or promise whose performance is guaranteed.

Rights of Surety

1. Rights against the Creditor: In case of fidelity guarantee, the surety can direct creditor to dismiss the employee whose honesty he has guaranteed, in the event of proved dishonesty of the employee.

2. Rights against the Principal Debtor

(a) **Right of Subrogation (stepping into the shoes of the original):** Where a surety has paid the guaranteed debt on its becoming due or has performed the guaranteed duty on the default of the principal debtor, he is invested with all the rights, which the creditor has against the debtor.

(b) **Right to be indemnified:** The surety has the right to recover from the principal debtor, the amounts which he has rightfully paid under the contract of guarantee.

3. Rights of Contribution: Where a debt has been guaranteed by more than one person, they

are called as co-sureties. When a surety has paid more than his share, he has a right of contribution from the other sureties who are equally bound to pay with him.

Discharge of surety

I. By Revocation

1. **Revocation by notice:** A continuing guarantee may at any time be revoked by the surety, as to future transactions, by notice to the creditor.
2. **Revocation by death:** The death of the surety operates, in the absence of any contract to the contrary, as a revocation of a continuing guarantee, so far as regards future transactions.
3. **Discharge by novation:** A contract of guarantee is discharged by substituting a new contract in place of the old one.

II. By act or conduct of the Creditor

1. **By variation in the terms of the contract:** Any change made without the surety's consent, in the terms of the contract between the principal-debtor and the creditor, discharges the surety as to transactions subsequent to the variance.
2. **By release or discharge of principal-debtor:** Any contract between the creditor and the principal-debtor by which the principal-debtor is released, the surety is also discharged.
3. **By compounding by the creditor with the principal debtor:** If the creditor makes a composition with, or promises to give time to, or not to sue the principal-debtor, discharges the surety, unless such contract is made with the consent of the surety.
4. **By creditors act or omission impairing surety's eventual remedy:** In case the creditor does any act which is inconsistent with the rights of the surety, or omits to do any act which is required, thereby impairing the eventual remedy of the surety himself against the principal-debtor, the surety is discharged.
5. **By loss of security:** If the creditor loses, or without the consent of the surety, parts with any security given at the time of contract, the surety is discharged to the extent of the value of security.

III. By invalidation of the contract of guarantee

1. **By obtaining guarantee by misrepresentation:** Any guarantee obtained by means of misrepresentation made by the creditor concerning a material part of the transaction is invalid.
2. **By obtaining guarantee by concealment:** Any guarantee which the creditor has obtained by means of keeping silence as to material part of circumstances is invalid.
3. **By failure of co-sureties to join:** The guarantee is not valid if the other person does not join.

Difference between Contract of Indemnity & Guarantee

S.N	BASIS FOR COMPARISON	INDEMNITY	GUARANTEE
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1.	Meaning	It is a contract to make good the loss of other party.	It is a contract to perform the promise or discharge the liability of a third person in case of his default.
2.	Defined in Section	Section 124 of Indian Contract Act 1872.	Section 126 of Indian Contract Act 1872.
3.	Parties	There are two parties: Indemnifier and Indemnity Holder.	Three parties: Principal Debtor, Creditor and Surety
4.	Number of agreements	There is only one agreement i.e. between the Indemnifier and Indemnity Holder.	There are three agreements: 1. between the Principal Debtor & Creditor 2. between the Creditor & Surety. 3. between the Surety & Principal Debtor.
5.	Nature of surety's lia	The liability of the indemnifier is primary.	The liability of the surety is secondary i.e. the surety is liable only if the principal

			debtor does not pay the amount. The liability of the principal-debtor is primary.
6.	Right to sue after performance	In case of indemnity, except in rare cases, indemnifier cannot recover his loss from a third party.	In case of guarantee, if surety has paid the debt, he steps into the shoes of the creditor and can recover his loss from the principal-debtor.
7.	Indemnity holder cannot sue in his own name	An indemnity-holder cannot sue a third party in his own name. Assignment in favour of indemnity-holder is necessary.	A surety can sue in his own name. No such assignment is necessary.
8.	Request to act	Indemnifier does not act at the request of the indemnified.	A surety has to act at the request of the debtor.
9.	Capacity contract	All the parties must be capable of contracting.	The principal-debtor may be a minor. In that case, the surety will be liable.

10.	Scope	Its scope is limited. It does not include contract of guarantee.	Its scope is wide. It involves contract of indemnity.
11.	Nature	It is for reimbursement of loss.	It is for the security of the creditor.

CONTRACT OF BAILMENT AND PLEDGE BAILMENT

[SECTIONS 148 –181]

What is ‘Bailment‘

When one person delivers some goods to another person under a contract for a specified purpose and when that specified purposes is accomplished the goods shall be delivered to the first person, it is known as Bailment

The person delivering the goods is called the “Bailor”, and the person to whom goods are delivered is called the “Bailee”.

Features of Bailment

1. There should be a contract.
2. Delivery of goods by one person to another.
3. The goods are delivered for certain purpose.
4. The same goods must be returned.

DUTIES OF BAILOR

1. To disclose faults in the goods
2. Liability for breach of warranty as to title.
2. To bear expenses in case of Gratuitous bailments
4. In case of non-gratuitous bailments, the bailor is held responsible to bear only extra-ordinary expenses.

DUTIES OF THE BAILEE

1. To take care of the goods bailed
2. Not to make unauthorised use of goods
2. Not to Mix Bailor’s goods with his own
4. To return the goods bailed
5. To return any accretion to the goods bailed

RIGHTS OF BAILEE

1. The bailee can sue bailor for:
 - (a) claiming compensation for damage resulting from non-disclosure of faults in the goods;
 - (b) for breach of warranty as to title and the damage resulting therefrom; and
 - (c) for extraordinary expenses.

2. Lien

RIGHTS OF THE BAILOR

1. The bailor can enforce by suit all duties or liabilities of the bailee.

2. In case of gratuitous bailment (i.e., bailment without reward), the bailor can demand their return whenever he pleases, even though he lent it for a specified time or purpose.

TERMINATION OF BAILMENT

1. On the expiry of the stipulated period.

2. On the accomplishment of the specified purpose.

3. By bailee's act inconsistent with conditions.

FINDER OF GOODS

Finding is not keeping. A finder of lost goods is treated as the bailee of the goods found as such and is charged with the responsibilities of a bailee, besides the responsibility of exercising reasonable efforts in finding the real owner.

However, he enjoys certain rights also. His rights are summed up hereunder

1. Right to retain the goods

2. Right to Sell -the finder may sell it:
 - (1) when the thing is in danger of perishing or of losing the greater part of its value;
 - (2) when the lawful charges of the finder in respect of the thing found, amount to 2/3rd of its value.

PLEDGE

- A pledge is the bailment of goods as security for payment of debt or performance of a promise. The person who delivers the goods, as security is called the 'pledgor' and the person to whom the goods are so delivered is called the 'pledgee'. The ownership remains with the pledgor. It is only a qualified property that passes to the pledgee.

- Delivery Essential - A pledge is created only when the goods are delivered by the borrower to the lender or to someone on his behalf with the intention of their being treated as security against the advance. Delivery of goods may, however, be actual or constructive.

CONTRACT OF AGENCY [SECTION 182 – 238]

Who is an ‘Agent‘?

- An agent is defined as a “person employed to do any act for another or to represent another in dealings with third person”. In other words, an agent is a person who acts in place of another. The person for whom or on whose behalf he acts is called the Principal.
- Agency is therefore, a relation based upon an express or implied agreement whereby one person, the agent, is authorised to act for another, his principal, in transactions with third person.
- The function of an agent is to bring about contractual relations between the principal and third parties.

WHO CAN EMPLOY AN AGENT

Any person, who is capable to contract may appoint as agent. Thus, a minor or lunatic cannot contract through an agent since they cannot contract themselves personally either.

WHO MAY BE AN AGENT

In considering the contract of agency itself (i.e., the relation between principal and agent), the contractual capacity of the agent becomes important.

Modes of creation of AGENCY

- (1) Express Agency
- (2) Implied Agency
- (3) Agency by Estoppel
- (4) Agency by Holding Out
- (5) Agency of Necessity
- (6) Agency By Ratification

DUTIES OF AGENT

1. To conduct the business of agency according to the principal’s directions
2. The agent should conduct the business with the skill and diligence that is generally possessed by persons engaged in similar business, except where the principal knows that the agent is wanting in skill.
3. To render proper accounts.
4. To use all reasonable diligence, in communicating with his principal, and in seeking to obtain

his instructions.

5. Not to make any secret profits
6. Not to deal on his own account
7. Agent not entitled to remuneration for business misconducted.
8. An agent should not disclose confidential information supplied to him by the principal
9. 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.

RIGHTS OF AN AGENT

1. Right to remuneration
2. Right Of Retainer
2. Right of Lien
4. Right of Indemnification
5. Right to compensation for injury caused by principal's neglect

PRINCIPAL'S DUTIES TO AGENT

- (i) bound to indemnify the agent against the consequences of all lawful acts done by such agent in exercise of the authority conferred upon him;
- (ii) liable to indemnify an agent against the consequences of an act done in good faith.
- (iii) 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.

TERMINATION OF AGENCY

1. By revocation by the Principal.
2. On the expiry of fixed period of time.
2. On the performance of the specific purpose.
4. Insanity or Death of the principal or Agent.
5. An agency shall also terminate in case subject matter is either destroyed or rendered unlawful.
6. Insolvency of the Principal. Insolvency of the principal, not of the agent, terminates the agency.
7. By renunciation of agency by the Agent.