

Module 1: Indian Contract Act

1 Introduction of law, Sources of law, Business Law – Meaning and definition

Introduction of Law

Law represents a systematic architecture of rules, codes, and directives established and enforced by a sovereign political authority to govern human behavior, maintain social order, and preserve justice within a state. Without law, commercial environments revert to unpredictability, making stable enterprise impossible.

Sources of Indian Law

The contemporary legal framework of India is derived from multiple primary sources:

- **Statutory Law (Legislation):** Enactments passed by the Parliament of India or State Legislatures (e.g., the Indian Contract Act, 1872 itself). This is the supreme legislative source.
- **Judicial Precedents (Common Law):** Decided cases and judgments delivered by appellate courts, primarily the Supreme Court of India. Under Article 141 of the Constitution, Supreme Court rulings are binding law across all lower territories.
- **Customs and Usages:** Long-established commercial traditions and practices that are continuous, reasonable, and not opposed to public policy or statutory enactments.
- **Personal Laws:** Religiously or culturally rooted structures (such as Hindu or Muslim personal codes) applied strictly to familial matters like inheritance and marriage.

Business Law: Meaning and Definition

Business Law—historically referred to as Mercantile or Commercial Law—is that specialized branch of civil law which encompasses the legal rules relating to commercial transactions, trade, industry, and corporate governance. It establishes the ground rules under which businesses interact, execute agreements, manage properties, and settle financial disputes.

Legal Scope: Business law dictates structural boundaries for a massive continuum of merchant operations: from basic contract formations and sale of goods parameters, to partnership liabilities, negotiable instruments, corporate compliance, and bankruptcy resolutions.

2 Contract: - Definition, Essentials of Valid Contract

Definition of a Contract

According to **Section 2(h)** of the Indian Contract Act, 1872, a contract is defined as: "**An agreement enforceable by law.**" This definition reveals a foundational two-part mathematical legal formula:

Contract = Agreement + Legal Enforceability

Breaking this down further under **Section 2(e)**, an agreement is defined as: "*Every promise and every set of promises, forming the consideration for each year.*" A promise occurs when a proposal/offer is accepted by another party (Section 2(b)). Therefore:

Agreement = Offer + Acceptance

Essentials of a Valid Contract (Section 10)

For an agreement to transition into a legally binding contract, it must satisfy the strict checklist of statutory prerequisites outlined in **Section 10** of the Act. If any element is compromised, the agreement remains legally dead:

- **1. Offer and Acceptance:** There must be a lawful, identifiable offer by one party and an absolute, unconditional acceptance of that exact offer by the other.
- **2. Intention to Create Legal Relationship:** The parties must explicitly intend that their arrangement will trigger legal consequences. Purely social, domestic, or moral arrangements do not form contracts. *(Leading Case: Balfour v. Balfour)*
- **3. Lawful Consideration:** The agreement must be supported by "Quid Pro Quo"—something in return. A bare promise without reciprocal value is non-binding.
- **4. Capacity of Parties:** The contracting entities must be legally competent. This requires them to be of the age of majority, of sound mind, and not explicitly disqualified from contracting by any law.
- **5. Free Consent:** The minds of the parties must meet voluntarily and sincerely on the same thing in the same sense (*Consensus ad idem*). Consent is not free if obtained via pressure or trickery.

- **6. Lawful Object and Consideration:** The objective of the agreement and the reciprocal exchange must be legal. It cannot be fraudulent, immoral, criminal, or opposed to public policy.
- **7. Not Expressly Declared Void:** The agreement must not belong to categories that the Indian Contract Act explicitly declares illegal or void from the start (such as agreements in restraint of trade or marriage).
- **8. Certainty and Possibility of Performance:** The terms must be definitive and clear; vague terms invalidate agreements. Furthermore, the contract must be physically and legally capable of execution. An agreement to discover gold by magic is void.

3 Classification of Contracts

Contracts within business operations are classified across three major structural dimensions: Validity, Formation, and Performance.

1. Classification Based on Validity or Enforceability

- **Valid Contract:** Satisfies all essentials of Section 10 and is fully enforceable by a court of law.
- **Void Agreement (Void-ab-initio):** An agreement that completely lacks legal effect from its inception (Section 2(g)). It cannot be enforced by either party (e.g., an agreement with a minor).
- **Void Contract:** A contract that was perfectly valid when formed but subsequently becomes unenforceable due to a sudden change in law or supervening impossibility (Section 2(j)).
- **Voidable Contract:** An agreement which is legally enforceable at the option of one party (the injured/aggrieved party) but not at the option of the other (Section 2(i)). This occurs when consent is compromised.
- **Illegal Agreement:** An agreement that involves an act forbidden by criminal law. All illegal agreements are void, and any collateral transactions connected to them are also void.

2. Classification Based on Formation

- **Express Contract:** Formed when terms are stated explicitly using spoken words or written language.
- **Implied Contract:** Created automatically by the conduct, actions, or behavior of the parties, or by the surrounding circumstances (e.g., boarding a public bus implies an agreement to pay the fare).
- **Quasi-Contract:** Not a true contract by intent. It is a legal obligation imposed by a court to prevent one person from gaining an unfair financial advantage over another.

3. Classification Based on Performance

- **Executed Contract:** Both parties have completely fulfilled their respective obligations under the agreement.
- **Executory Contract:** One or both parties have outstanding obligations that must be completed in the future. This can be *Unilateral* (one-sided promise remains outstanding) or *Bilateral* (both parties have reciprocal obligations pending).

4 Offer and Acceptance, Consideration, Capacity to Contract, Free Consent, Coercion, Undue influence, Misrepresentation, Fraud, Mistake

To truly understand how a contract operates, we must analyze the specific rules governing its individual structural building blocks.

Offer and Acceptance

An **Offer (Proposal)** occurs when one person signifies to another their willingness to do or abstain from doing something, with a view to obtaining the assent of that other person. An offer must be definite, communicated, and capable of creating a legal relationship. **Acceptance** is the expression of absolute, unconditional assent to the exact terms of the proposal. Under Section 4, communication of an offer is complete when it comes to the knowledge of the person to whom it is made.

Consideration (Section 2(d))

Consideration is the price paid for a promise. It represents "Quid Pro Quo"—something in return. When at the desire of the promisor, the promisee does or abstains from doing something, such act or abstinence is called consideration.

Core Legal Rules: Consideration must move at the desire of the promisor; it may move from the promisee or an entirely third party *(Chinnaya v. Ramaya)*; it can be past, present, or future; and it need not be financially adequate, but it must be real and hold value in the eyes of law.

Exceptions to 'No Consideration, No Contract' (Section 25): Agreements made out of natural love and affection between near relatives (written and registered); promises to compensate for past voluntary services; and promises to pay a written, signed time-barred debt.

Capacity to Contract (Section 11)

Not everyone is legally permitted to sign a contract. Section 11 defines competent parties as:

- **Age of Majority:** The party must be at least 18 years old. Any agreement made with a minor is completely void from the start (*Void-ab-initio*), and cannot be validated later through ratification.
(Leading Case: Mohori Bibee v. Dharmodas Ghose)
- **Sound Mind:** The person must be capable of understanding the terms of the contract and forming a rational judgment regarding its effects on their interests at the exact time of signing.
- **Not Disqualified by Law:** Includes foreign enemies, convicts undergoing sentences, and declared undischarged insolvents.

Free Consent and Its Flaws (Sections 13 - 22)

Consent exists when parties agree upon the same thing in the same sense (*Consensus ad idem*). Consent is ****Free**** under Section 14 only when it is completely untainted by any of the following five legal flaws:

Flaw	Statutory Clause	Operational Definition & Mechanism	Legal Outcome
Coercion	Section 15	Committing or threatening to commit any act forbidden by the Indian Penal Code, or unlawfully detaining property, with the explicit intent to force a person into an agreement via physical fear.	Voidable at option of aggrieved party.
Undue Influence	Section 16	One party occupies a position where they dominate the psychological will of another (e.g., Doctor/Patient, Guardian/Ward) and uses that dominant position to obtain an unfair advantage.	Voidable at option of aggrieved party.
Fraud	Section 17	Intentional deception or active concealment of material facts made with the clear motive to deceive a party into signing an agreement they would otherwise refuse.	Voidable + Right to sue for damages.

Flaw	Statutory Clause	Operational Definition & Mechanism	Legal Outcome
Misrepresentation	Section 18	An innocent, unintentional misstatement of material facts made by a party who genuinely believes the statement to be true, without any underlying motive to deceive.	Voidable at option of aggrieved party. No damages.
Mistake	Sections 20-22	An erroneous belief regarding facts or law. If it is a Bilateral Mistake of Fact (both parties misunderstand a critical core fact), the agreement is completely dead.	Bilateral Fact = Void. Unilateral = Valid.

5 Discharge of Contract, Breach of Contract and Remedies

Discharge of a Contract

Discharge means the termination of the contractual relationship between the parties. When a contract is discharged, all outstanding legal obligations are dissolved. A contract can be discharged through several distinct operational modes:

- **Discharge by Performance:** The most common mode. Both parties fully execute their respective promises (Actual Performance), or one party attempts to perform but the other refuses to accept it (Attempted Performance / Tender).
- **Discharge by Mutual Agreement:** Parties choose to substitute, alter, or terminate the existing contract via:
 - *Novation:* Substituting the old contract with an entirely new one.
 - *Rescission:* Canceling the contract altogether.
 - *Alteration:* Modifying specific terms without changing the parties.
- **Discharge by Supervening Impossibility:** Occurs when performance becomes physically or legally impossible after the contract is formed due to events beyond control (e.g., destruction of the subject matter). This is governed by the **Doctrine of Frustration**.
- **Discharge by Lapse of Time:** If a party fails to perform within the specific timeframe allowed by the Limitation Act, the contract expires.

- **Discharge by Operation of Law:** Occurs automatically via death of a party or insolvency.
- **Discharge by Breach:** Occurs when one party explicitly refuses to perform their mandatory duty.

Breach of Contract

Breach represents a direct violation of a contract when a party fails to perform their promise. It takes two structural forms:

Actual Breach: The party fails or explicitly refuses to perform their obligation on the exact date specified for delivery or performance.

Anticipatory Breach: A party communicates their intention *before* the scheduled arrival of the performance date, stating clearly via words or actions that they will not fulfill their future promise.

Remedies for Breach of Contract

When a breach occurs, the law provides the injured party with five distinct options to secure justice and recover losses:

1. Rescission

The injured party cancels the contract completely, freeing themselves from any remaining obligations under the agreement.

2. Suit for Damages

Claiming monetary compensation for the financial losses caused by the breach. *(Hadley v. Baxendale)* rules govern Ordinary and Special damages.

3. Quantum Meruit

Translates to "as much as earned." A legal claim to receive fair payment for work or services already completed before the contract was breached.

4. Specific Performance

A court order forcing the breaching party to carry out their exact promise. This remedy is granted when monetary compensation is insufficient (e.g., unique land sales).

5. Injunction

A preventive court order restraining a party from committing a negative act or violating a restrictive promise they previously agreed to.

6 Contingent Contracts, Quasi Contract

Contingent Contracts (Section 31)

A **Contingent Contract** is defined as: "**A contract to do or not to do something, if some event, collateral to such contract, does or does not happen.**" The entire performance of the contract is dependent upon an uncertain future event that is separate from the contract itself.

- **Classic Example:** All contracts of insurance, indemnity, and guarantee. An insurance firm promises to pay a factory owner a specific sum *only if* the factory burns down. If no fire occurs, the firm has no duty to pay.
- **Rules of Enforcement:** If the event depends on a happening, it cannot be enforced until that event occurs. If the event becomes impossible, the entire contract automatically becomes void.

Quasi-Contracts (Sections 68 - 72)

A **Quasi-Contract** is not a real contract. There is no offer, no acceptance, no negotiation, and no initial intent between the parties. Instead, it is an obligation created and imposed by law based on the fundamental principle of natural justice and equity: "**No person shall be allowed to enrich themselves unjustly at the expense of another.**"

The Act outlines five distinct situations where a quasi-contractual obligation is automatically triggered:

- **Section 68 (Supply of Necessaries):** If a person incapable of entering into a contract (such as a minor or a person of unsound mind) is supplied with necessaries suited to their condition in life, the supplier is entitled to be reimbursed from the property of that incapable person.
- **Section 69 (Payment by Interested Person):** A person who pays money that another is legally bound to pay, and who therefore has a financial interest in the payment, is entitled to be reimbursed by the other party.
- **Section 70 (Obligation to Pay for Non-Gratuitous Acts):** When a person lawfully does something or delivers an item to another, not intending to do so gratuitously (for free), and the receiving party accepts and enjoys the benefit of that act, they must compensate the provider.
- **Section 71 (Finder of Goods):** A person who finds goods belonging to another and takes custody of them is subject to the exact same legal responsibilities and duties as a *Bailee* (must take reasonable care of the items and locate the true owner).
- **Section 72 (Money Paid under Mistake or Coercion):** A person to whom money has been paid, or anything delivered, by mistake or under coercion, must repay or return it completely.

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