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Certified Contract Law Sample Material VS-1158

1. INTRODUCTION

Law is a basic necessity of every civilized society. Law is the bundle of rules and principles to be followed by the members of the society. When there is a law in a country, it brings uniformity and balance in human actions, and provides justice to the aggrieved persons.

According to Holland, "Law is a rule of external human action enforced by the sovereign political authority." In the words of Blackstone," Law is a rule of civil conduct, prescribed by the supreme power of state, commanding what is right and prohibiting what is wrong."

Law is a system of rules that are enforced through social institutions to govern behavior. Laws can be made by a collective legislature or by a single legislator, resulting in statutes, by the executive through decrees and regulations, or by judges through binding precedent, normally in common law jurisdictions. Private individuals can create legally binding contracts, including arbitration agreements that may elect to accept alternative arbitration to the normal court process. The formation of laws themselves may be influenced by a constitution, written or tacit, and the rights encoded therein. The law shapes politics, economics, history and society in various ways and serves as a mediator of relations between people.

A general distinction can be made between

- ✓ Civil law jurisdictions, in which the legislature or other central body codifies and consolidates their laws
- ✓ Common law systems, where judge-made precedent is accepted as binding law.

Historically, religious laws played a significant role even in settling of secular matters, which is still the case in some religious communities, particularly Jewish, and some countries, particularly Islamic. Islamic Sharia law is the world's most widely used religious law.

1.1. Overview

The law of contract is of crucial importance in the legal management of transactions and obligations in our economic system. Essentially, a contract is an agreement between two or more parties that the law will enforce. Generally speaking, damages (that is, compensation) are payable for loss suffered by one party due to the non-performance (or poor performance) by the other party to the contract. Moreover, a party may (in appropriate circumstances) request a civil court to order performance by the other party in default.

At common law (that is, judge made law), the same legal principles generally apply to all types of contracts. Over time, the strict application of the common law has become somewhat subdued by the principles of equity, designed by the courts to restrain unconscionable contractual outcomes and promote justice. More recently, statute (that is, Parliament made law) has altered or replaced the common law in relation to various aspects of contract law, in particular contracts for consumer goods and services.

Contract law concerns enforceable promises, and can be summed up in the Latin phrase pacta sunt servanda (agreements must be kept). In common law jurisdictions, three key elements to the creation of a contract are necessary: offer and acceptance, consideration and the intention to create legal relations. In Carlill v Carbolic Smoke Ball Company a medical firm advertised that its new wonder drug, the smokeball, would cure people's flu, and if it did not, the buyers would get £100. Many people sued for their £100 when the drug did not work. Fearing bankruptcy, Carbolic argued the advert was not to be taken as a serious, legally binding offer. It was an invitation to treat, mere puffery, a gimmick. But the Court of Appeal held that to a reasonable man Carbolic had made a serious offer, accentuated by their reassuring statement, "£1000 is deposited". Equally, people had given good consideration for the offer by going to the "distinct inconvenience" of using a faulty product. "Read the advertisement how you will, and twist it about as you will", said Lord Justice Lindley, "here is a distinct promise expressed in language which is perfectly unmistakable".

"Consideration" indicates the fact that all parties to a contract have exchanged something of value. Some common law systems, including Australia, are moving away from the idea of consideration as a requirement. The idea of estoppel or culpa in contrahendo, can be used to create obligations during pre-contractual negotiations. In civil law jurisdictions, consideration is not required for a contract to be binding. In France, an ordinary contract is said to form simply on the basis of a "meeting of the minds" or a "concurrence of wills". Germany has a special approach to contracts, which ties into property law. Their 'abstraction principle' means that the personal obligation of contract forms separately from the title of property being conferred. When contracts are invalidated for some reason (e.g. a car buyer is so drunk that he lacks legal capacity to contract) the contractual obligation to pay can be invalidated separately from the proprietary title of the car. Unjust enrichment law, rather than contract law, is then used to restore title to the rightful owner.

The law relating contract in India is contained in the Indian contract Act, which came in to force on the first day of Sept 1872. The act is extended to the whole of India except the state of Jammu and Kashmir. The act as it now stands contains the general principles of contract, contract of indemnity, surety ship, Bailment, and Agency. The law of contract deals with those transactions or promises which create legal rights and obligations. In case of non performance of the promise by one party, it also provides legal remedies to an aggrieved party.

Lord Alfred Thompson Denning (1899-1999) was a populist English judge whose career spanned 37 years. Lord Denning contributed a lot in the field of Law of Contract. His contribution can be restricted to the following areas of contract.

Standard form contract

- ✓ Reasonable notice of terms
- ✓ Theory of fundamental breach

Consideration

- ✓ Privity of contract
- ✓ Promissory estoppels

1.2. Contract Definition

Generally contract may be defined as an agreement which creates rights and obligations between the parties. These obligations and right s must be of such a nature that these can be claimed in the court of law.
According to Salmond, "A contract is an agreement creating and defining obligation between the parties." Section 8(h) of the Indian Contract Act defines contract as an agreement which is enforceable by law.

From the above definitions of contract it is clear that a contract essentially consists of three elements:

- ✓ An agreement
- ✓ Obligation, and
- ✓ Enforceability

An agreement involves a valid offer by one party a valid acceptance by the other party. Enforceability means contract must be legal in nature and which can be claimed in the court of law.

For example, X invites Y to a party and Y accepts the invitation, then it is only a social agreement and not a contract. On the other hand A agrees to sell his house to B for Rs. 5, 00,000. This is a contract.

1.3. Contract Elements

An agreement to be enforced in the court has to satisfy certain conditions. On satisfying these, the agreements become a contract, and those conditions become essentials of a valid contract. The essential elements of a contract are contained in the definition of contract given in sec. 10 of the contract Act. According to this Act, "all agreements are contracts if they are made by free consent of parties competent to contract for a lawful consideration and with a lawful object and are not hereby expressly declared to be void." The essential elements of a contract include:

- ✓ Agreement: - There must be an agreement between the parties of a contract. It involves a valid offer by one party and a valid acceptance by the other party. Agreement is created by offer and acceptance. Therefore an agreement is = offer +acceptance. It is only by an agreement a contractual relation is established between the parties. For example, A sends a proposal to B to purchase a property for Rs. 10 lakhs and B accept the same, then this result into an agreement.
- ✓ Lawful consideration: Consideration means something in return. An agreement is legally enforceable only when each of the parties to it give something and gets something. It may be past, present or future and must be real and lawful. A contract without consideration is not a contract at all. The consideration must be legal, moral and not against public policy.
- ✓ Capacity of parties: The parties to an agreement must be capable of entering into a valid contract. According to sec. 11, the following persons are not competent to enter in to a contract.
    - Persons of unsound mind (Idiots, lunatic person etc.)
    - Persons disqualified by law to which they are subject.
    - Minors (Not completed the age of 18)

- ✓ Free consent: For the formation of a contract one person must give his consent to another person. The consent thus obtained must be a free consent. A consent is said to be free if it is not caused by coercion, undue influence, fraud, misrepresentation or mistake. If the consent is obtained by unfair means, the contract would be voidable.
- ✓ Consensus ad idem: It means the two parties of the contract must agree upon the subject matter of the contract in the same manner and in the same sense. That is there must be identity of minds among the parties regarding the subject matter of the contract. For example, A has two houses one at Calicut and another at Palakkad. He has offered To sell one house to B. B accepts the offer thinking to purchase the house at Palakkad, while A, when he offers; he has his mind to sell the house at Calicut. So there is no consensus ad idem.
- ✓ Lawful object: The object of an agreement must be lawful. It must not be illegal or immoral or opposed to public policy. If it is unlawful, the agreement becomes void.
- ✓ Not declared to be void: There are certain agreements which have been expressly declared void by the law. It includes
    - Wagering agreement
    - Agreement in restraint to marriage
    - Agreement in restraint of trade etc.

  Thus an agreement made by parties should not fall in the above category.
- ✓ Certainty and possibility of performance: - The terms of the contract must be precise and certain. They should not be vague. The terms of agreement must be capable of performance. For example A agrees to sell one of his houses. A has four houses. Here the terms of agreement are uncertain and the agreement is void.
- ✓ An intention to create legal relationship:- There should be an intention between the parties to create a legal relationship. Mere informal promise is not to be enforced. Social agreements are not to be enforced as they do not create any legal obligations. An oral contract is a valid contract except in those cases where writing, registration etc. is required by some statute.
- ✓ Parties – The names and addresses of all the contracting parties should be clearly stated.
- ✓ Term of contract – The length of the contract should be stated and it should also be noted whether there are any options to continue the contract. For example, 'This agreement will continue for another year unless otherwise notified to [other party] by 31 January each year'.
- ✓ Limitation of liability – This section caps the liability of either party to the contract. For example, 'Neither party shall have any liability to the other party for a claim of loss of profits...'. In an ideal world both parties would be seeking to have no liability to the other side. However, in a commercial context this is unlikely to be agreed and so both parties should try and limit their liability during the negotiation stage to appropriate levels. It is worth noting that there are statutes in force (discussed below) that forbid exclusion of liability in certain circumstances.
- ✓ Termination provisions – The circumstances under which the parties can terminate the contract should be stated clearly. The procedure for giving notice to the other party should be in the contract. For example, 'This agreement can be terminated by either party giving to the other not less than three months written notice...'.
- ✓ Change of Control – During the course of a contract one party may change the structure of their company. In these circumstances the other party may wish to terminate the contract, for example if the first party transfers a controlling interest to a competitor of the other party. The procedure for this situation should be in the contract.
- ✓ Dispute Resolution – The procedure to be followed if the parties have a dispute should be included. For example, if there is an option for arbitration or mediation where the issue cannot be resolved through internal escalation.

- ✓ Confidentiality – Some contracts deal with commercially sensitive information and the parties are likely to want to keep this information confidential. There should be confidentiality clauses drafted in the contract which identify the information being protected and the circumstances in which it can be used or disclosed.
- ✓ Intellectual Property Rights – Many commercial contracts include a clause stating who will own the intellectual property rights to any products provided under the contracts. This clause should specifically state who owns such rights. Particular attention should be given to the ownership of intellectual property rights in relation to products created specifically for or in connection with the contract.
- ✓ Warranties – It is common for the party providing goods or services under a contract to provide certain warranties in relation to the delivery of the goods or services. For example, if the contract is for provision of a licence the provider should warrant that it has the necessary rights to grant the licence. Warranties give the other party a contractual right to sue for damages if there is a breach of the warranty.
- ✓ Indemnity – Indemnity clauses are an express obligation to compensate the indemnified party by making a money payment for some defined loss or damage. They provide for an immediate right to compensation, without the need for a lengthy dispute as to the circumstances giving rise to the specified loss or damage. For this reason careful attention should be given to the agreement of any indemnities. An example of a typical indemnity is in a software contract under which the supplier indemnifies the customer against any claims made by a third party that the normal use of the software is infringing the rights of the third party.
- ✓ Force Majeure – This clause should cover situations where performance of the contract is impossible through no fault of either party. For example, if there is a natural disaster or civil unrest.
- ✓ Assignation / Assignment – If there is an option for one party to transfer their contractual rights and responsibilities to another party this should be set out in the contract along with the procedure to be followed. If there is no right to assign the contract this should also be noted.

Valid contract

A valid contract is a contract that the law will enforce and creates legal rights and obligations. A contract valid ab initio (from the beginning) contains all the three essential elements of formation:

- ✓ agreement (offer and acceptance);
- ✓ intention (to be bound by the agreement);
- ✓ consideration (for example, the promise to pay for goods or services received).

In addition, a valid contract may have to be in writing to be legally valid (although most contracts may be oral, or a combination of oral and written words).

Void contract

A void contract lacks legal validity and does not create legal rights or obligations. A contract that lacks one or more of the essential formation elements is void ab initio (from the beginning). In other words, the law says that it is not, or never was, a valid contract.

Voidable contract

A voidable contract is a valid contract that contains some defect in substance or in its manner of formation that allows one party (or sometimes both parties) to rescind it. A voidable contract

remains valid and can create legal rights and obligations until it is rescinded. The party with the right to rescind may lose that right by affirmative conduct, or undue delay, or where the rights of an innocent third party may be harmed.

Unenforceable contract

An unenforceable contract is an otherwise valid contract that contains some substantive, technical or procedural defect. Most commonly, such a contract is illegal, either in its formation or its performance, as it offends either public policy (the common law) or some statute. As a general rule, the law will not allow the enforcement of such a contract Alternatively, the law may determine that such is a contract is void (rather than unenforceable) with the consequential loss of contractual rights.

Formal contract

A formal contract is wholly in writing, usually in the form of a deed, and does not require consideration. A promise (or term) of a contract made by deed is called a covenant. A deed can be unilateral (that is, made by only one party) and this is often called a deed poll. A deed made by two or more parties is called an indenture. Some types of contracts must be in writing and must be made by deed to be effective (for example, a conveyance of non-Torrens title land).

Simple contract

A simple contract may be oral or in writing (or a combination of both). Simple contracts are made between two or more parties and require consideration.

1.4. Indian Contract Act

The main contract law in India is codified in the Indian Contract Act, which came into effect on 1 September 1872 and extends to all India except the state of Jammu and Kashmir. It governs entrance into contract, and effects of breach of contract. Indian Contract law is popularly known as mercantile law of India. Originally Indian Sales of Goods Act and Partnership Act were part of Indian Contract act, but due to needed amendment these acts were separated from Contract Act. The Contract act is the main and most used act of legal agreements in India.

The law relating to contracts in India is contained in INDIAN CONTRACT ACT, 1872. The Act was passed by British India and is based on the principles of English Common Law. It is applicable to all the states of India except the state of Jammu and Kashmir. It determines the circumstances in which promises made by the parties to a contract shall be legally binding on them. All of us enter into a number of contracts everyday knowingly or unknowingly. Each contract creates some rights and duties on the contracting parties. Hence this legislation, Indian Contract Act of 1872, being of skeletal nature, deals with the enforcement of these rights and duties on the parties in India.

The Act as enacted originally had 266 Sections, it had wide scope and included.

- ✓ General Principles of Law of Contract- Sections 01 to 75
- ✓ Contract relating to Sale of Goods- Sections 76 to 123
- ✓ Special Contracts- Indemnity, Guarantee, Bailment & Pledge- Sections 124 to 238
- ✓ Contracts relating to Partnership- Sections 239 to 266

Indian Contract Act embodied the simple and elementary rules relating to Sale of goods and Partnership. The developments of modern business world found the provisions contained in the Indian Contract Act inadequate to deal with the new regulations or give effect to the new principles. Subsequently the provisions relating to the Sale of Goods and Partnership contained in the Indian Contract Act were repealed respectively in the year 1930 and 1932 and new enactments namely Sale of Goods and Movables Act 1930 and Indian Partnership act 1932 were re-enacted.

At present the Indian Contract Act may be divided into two parts

- ✓ Part 1 : deals with the General Principles of Law of Contract Sections 1 to 75
- ✓ Part 2 : deals with Special kinds of Contracts such as Contract of Indemnity and Guarantee, Contract of Bailment and Pledge and Contract of Agency

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