

Contracting



What is a contract

CONTRACT- According to sec.2(h) of Indian Contract Act, 1872, a contract is defined as an agreement enforceable by law.

AGREEMENT - According to sec.2(e), every promise and every set of promises, forming consideration for each other, is an agreement.

PROMISE - According to sec.2(b), when a person makes a proposal to another, if proposal is assented/accepted, it becomes a promise.

OFFER - According to Sec.2(a), when a person made a proposal, he signifies to another his willingness to do or to abstain from doing something with a view to obtaining the assent of the other to such acts or abstinence.

AGREEMENT = OFFER + ACCEPTANCE

CONSENSUS - AD – IDEM-

According to Sec.13, meeting of minds or identity of minds or receiving the same thing in same sense at same time.

Essential elements of contract (Sec. 10)

- Offer & acceptance.
- Intention to create legal relationship.
- Consensus - ad - idem.
- Consideration.
- Capacity to contract.
- Free consent.
- Legality of object.
- Possibility of performance.
- Writing & registration.

OFFER

According to Sec.2(a), a person makes a proposal, when he signifies to another his willingness to do or to abstain from doing something.

TYPES OF OFFER

- Express offer
- Implied offer
- Specific offer
- General offer
- Cross offer
- Counter offer
- Standing offer

Express offer - When offer is given to another person either in writing or in oral.

Implied offer - When offer is given to another person neither in writing nor in oral. (For example, when a coolie picks up your luggage to carry it from railway platform to the taxi, it means that the coolie is offering his service for some payment)

Specific offer - When offer is given to a specific person.

General offer - When offer is given to entire world at a large. (Carlill Vs. Carbolic smoke ball Co.,)

Cross offer - When both the persons are making identical offers to each other in ignorance of other's offer.

Counter offer - When both the persons are making offers to each other which are not identical in ignorance of other's offer.

Standing offer - An offer which remains continuously enforceable for a certain period of time.

LEGAL RULES OF OFFER

- ❖ *Offer must be given with an intention to create a legal relationship.*
- ❖ *Offer must be definite.*
- ❖ *There is a clear cut difference between offer, invitation to offer, invitation to sale.*
- ❖ *Offer must be communicated.*
- ❖ *Mere statement of price is not an offer.*

ACCEPTANCE

According to sec.2(b), when a person to whom the proposal is made signifies his assent thereto, the proposal is said to be accepted.

LEGAL RULES OF ACCEPTANCE

- Acceptance must be given as per the mode prescribed by the offerer.
- Acceptance must be given before the lapse of time or within reasonable time.
- Acceptance must be unconditional.
- Acceptance may be given by any person in case of general offer.

- Acceptance has to be given by specific person in case the said person is specifically authorized.
- Acceptance must be communicated.
- Mental acceptance is no acceptance or acceptance must not be derived from silence.
- Acceptance cannot be before offer.

WITHDRAWAL OF OFFER/ACCEPTANCE

According to Sec. 5 of the Act, a proposal may be revoked at any time before communication of its acceptance is complete as against the proposer, but not afterwards.

An acceptance may be revoked at any time before the communication of the acceptance is complete as against the acceptor, but not afterwards.

CONSIDERATION

According to sec 2(d) 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 to abstain from doing, something, such an act or abstinence or promise is called a consideration for the promise .

LEGAL RULES AS TO CONSIDERATION

- *It must be at the desire of the promisor.*
- *It **may** be by the promisee .*
- *It could be past, present or future .*
- *It need not be adequate .*
- *It must be real .*
- *It must not be illegal , immoral or opposed to public policy .*

Contract without consideration is void – Exceptions (Sec-25)

- *Natural Love & affection between near relations.*
- *Compensation for voluntary service .*
- *Promise to pay a time – barred debt .*
- *For creating Agency – (sec 185) .*
- *Contract of bailment - (sec 148) .*
- *Charity .*



Competent to contract (Sec 11)

- *Should be major*
- *Should be of sound mind*
- *Should not be disqualified by any other law.*
- *Should not be insolvent*

Minor

According to sec(3) of Indian Majority Act any person under the age of 18 years is a minor.

AGREEMENT WITH MINOR

- An agreement with minor is void ab initio
- Minor can be promisee
- Minor cannot ratify his agreement on attaining the age of majority

Unsound person

- *According to sec 12, a person generally sound , occasionally unsound can enter into a contract when he is of sound mind*
- *A person generally of sound mind occasionally of unsound mind cannot enter into contract when he is of unsound mind .*

Persons of unsound mind

- 1) *Lunatic,*
- 2) *Idiots,*
- 3) *Drunken or intoxicated persons .*

FREE CONSENT

According to Sec 10 of the Indian Contract Act one of the essentials of a valid contract is “Free Consent”

Sec 13 defines “consent” as “two or more persons are said to consent when they agree upon the same thing in the same sense”.

According to Sec 14, consent is said to be free when it is not caused by:

- 1.Coercion
- 2.Undue influence
- 3.Fraud
- 4.Misrepresentation
- 5.Mistake

COERCION

According to Sec 15 coercion means “Committing or threaten to commit any act forbidden by Indian Penal Code, 1860 or unlawful detaining or threatening to detaining any other persons property with a view to enter into an agreement. It is immaterial whether the IPC is or is not in force where the coercion is employed”

The threat amounting to coercion need not necessarily be from a party to contract , it may also proceed from a stranger to the contract.

UNDUE INFLUENCE

A contract is said to be induced by “undue influence” where the relations subsisting between the parties are such that one of the parties is in a position to dominate the will of the other and uses that position to obtain an unfair advantage over the other.

Scope of undue influence between the following persons:

- Principal and agent
- Superior and subordinate
- Doctor and patient
- Father and son
- Teacher and student
- Promoter and company
- Master servant
- Spiritual advisor and devotee

Among the following relations there is no undue influence

- 1.wife and husband**
- 2.landlord and tenant**
- 3.debtor and creditor**

FRAUD

According to Sec 17, fraud means and includes any of those acts committed by a party to contract or with his connivance or by his agent with an intent to deceive or induce a person to enter a contract:

1. The suggestion that a fact is true when it is not true and the person making it does not believe in it to be true
2. The active concealment of a fact by a person having knowledge or belief of the fact
3. A promise made without any intention of performing it
4. Any other act fitted to deceive
5. Any such act or omission as the law specially declares to be fraudulent

MISREPRESENTATION

According to Sec 18 there is misrepresentation:

1. When a person positively asserts a fact is true when his information does not warrant it to be so, though he believes it to be true
2. When there is any Breach of duty by a person which brings an advantage to the person committing it by misleading another to his prejudice
3. When a party causes however innocently the other party to the agreement to make a mistake as to the substance of the thing which is the subject of the agreement

UNLAWFUL OBJECT

- If the object of an agreement is the performance of an unlawful act, the agreement is unenforceable.
- For a contract to be valid only if the object and the consideration is legal.
- The word object means purpose or design.

INDEMNITY (Sec 124)

A CONTRACT BY WHICH ONE PARTY PROMISES TO ANOTHER TO SAVE HIM FROM LOSS CAUSED TO HIM BY THE CONDUCT OF THE PROMISOR HIMSELF, OR BY THE CONDUCT OF ANY OTHER PERSON IS CALLED A CONTRACT OF INDEMNITY

ESSENTIAL FEATURES OF INDEMNITY

- ✓ There are two persons , the indemnifier the indemnified or the indemnity holder
- ✓ There must be loss either by the promisor's conduct or by any other person's conduct
- ✓ It is a contingent contract by nature
- ✓ It may be express or implied

Sec125 deals with the commencement of the indemnifier's liability. His liability commences when the event causing the loss occurs or when the event saving the indemnified from the loss becomes impossible

GUARANTEE (Sec 126)

A CONTRACT OF GUARANTEE IS A CONTRACT TO PERFORM THE PROMISE, OR DISCHARGE THE LIABILITY, OF A THIRD PERSON IN CASE OF HIS DEFAULT. THE PERSON WHO GIVES THE GUARANTEE IS KNOWN AS THE 'SURETY', THE PERSON IN RESPECT OF WHOM THE GUARANTEE IS GIVEN IS KNOWN AS THE 'PRINCIPAL DEBTOR', AND THE PERSON TO WHOM THE GUARANTEE IS GIVEN IS CALLED THE 'CREDITOR'. A GUARANTEE MAY BE EITHER ORAL OR WRITTEN.

ESSENTIAL FEATURES OF GUARANTEE

- Concurrence of three contracts
- Primary liability is that of the principal debtor
- In case the debtor is a minor , the surety's liability becomes primary
- All the essentials of a valid contract
- It may be in writing or oral
- There need not be full disclosure of facts to the surety before he gives the guarantee

TYPES OF GUARANTEE

- **SPECIFIC GUARANTEE :**

When a guarantee extends to a single transaction or debt it is known as a specific or simple guarantee

CONTINUING GUARANTEE :

When a guarantee extends to a series of transactions

It is called continuing guarantee

DISCHARGE OF A CONTRACT

- ➡ DISCHARGE BY PERFORMANCE
- ➡ DISCHARGE BY AGREEMENT OR CONSENT
- ➡ DISCHARGE BY IMPOSSIBILITY OF PERFORMANCE
- ➡ DISCHARGE BY LAPSE OF TIME
- ➡ DISCHARGE BY OPERATION OF LAW
- ➡ DISCHARGE BY BREACH OF CONTRACT

AGENT

Sec 182 defines an agent as a person employed to do any act for another , or to represent another in dealings with third persons. The person for whom such act is done is called the principal

ESSENTIALS OF RELATIONSHIP OF AGENCY

- Agreement between principal & agent
- Intention of agent to act on behalf of the principal
- Anyone can be an agent
- Anyone can employ an agent

CREATION OF AGENCY

- BY EXPRESS AGREEMENT
- BY IMPLIED AGREEMENT
 - Agency by estoppel
 - Agency by holding out
 - Agency by necessity
- AGENCY BY RATIFICATION
- AGENCY BY OPERATION OF LAW

Termination of Agency

- *By act of parties*

Agreement

Revocation by the principal

Revocation by the agent

- *By operation of law*

Performance of the contract

Expiry of time

Death of either party

Insanity of either party

Insolvency of either party

Destruction of the subject matter

Principal becoming an alien enemy

Dissolution of a company

Termination of sub-agents authority

- In the case of ***Super Poly Fabriks Ltd., vs. Commissioner Central Excise, Punjab reported in 2008 (10) STR 545***, Hon'ble Supreme Court while referring *Assam Small Scale Ind. Dev. Corp. Ltd vs. J.D. Pharmaceuticals* held that "the expression principal and agent used in a document are not decisive. The nature of transaction is required to be determined on the basis of the substance there and not by the nomenclature used. Documents are to be construed having regard to the contexts thereof.
- ***Karakattu communications vs. CCE, Cochin reported in 2007(8) STR 164, 2007*** the principal question was raised as to whether the transaction of sim cards is coming under the purview of sale or service in view of the fact that the same is subjected to sales tax. Hon'ble CESTAT, Bangalore while allowing the appeal held that, service tax is not applicable on such transactions. Subsequently, in case of ***Chetan Traders vs. CCE, Jaipur***, CESTAT, Delhi Bench while relying on the above decision has also decided the issue in favour of the assessee, treating the transaction (sale of sim cards) as a sale.

TIRUMALA VENKENTASWAR TIMBER & BAMBOO FIRM VS. CTO

- As a matter of law there is a distinction between a contract of sale and a contract of agency by which the agent is authorized to sell or buy on behalf of the principal and make over either the sale proceeds or the goods to the principal. The essence of a contract of sale is the transfer of title to the goods for a price paid or promised to be paid. The transferee in such a case is liable to the transferor as a debtor for the price to be paid and not as agent for the proceeds of the sale. The essence of agency is to sell them, not as his own property but as the property of the principal who continues to be the owner of the goods and will therefore be liable to account for the sale proceeds.

HALSBURY'S LAWS OF ENGLAND ON PRINCIPAL AND AGENT REFERRED IN BHOPAL SUGAR CASE

- A contract of agency differs from a contract of sale in as much as an agent, after taking delivery of the property, does not sell it as his own but sells it as the property of the principal under his instructions and directions. The relation of principal and agent raises by implication, a contract on the part of the principal to reimburse the agent in respect of all expenses, and to indemnify him against all liabilities, incurred in the reasonable performance of the agency provided that such implication is not excluded by the express terms of the contract between them, and provided that such expenses and liabilities are in fact occasioned by his employment.

Letter of Intent/MOU

Letter of Intent (LoI), is a document that describes a formal agreement between two parties. It is a non-committal written statement detailing the preliminary understanding of the parties who intend to enter into a contract at a future date.


The sole purpose of entering into a MoU is to record the consensus of the parties to enter into a contract in the future. The parties, through a MoU, generally do not intend to raise an obligation or create an obligation on either party. It is not a legal agreement but it helps in indicating the establishment of a business relationship that will continue and likely result in a legal agreement such as a contract in the near future.

Legal position of MoUs under Indian Law

According to Section 10 of the Act, agreements made by parties, competent to contract under the Act, of their own free will and for a lawful consideration and object are contracts


Clauses under the MoU making provision for an enforcement mechanism in case of breach by either party will confirm that the parties did intend to enter into a binding agreement.

A MoU containing preliminary terms is non-binding, unless a binding understanding between the parties can be inferred from the context.



The Courts have given mixed opinions regarding the bindingness and enforceability of Memorandums of Understanding. It can be said that the enforceability and bindingness of such Memorandums depends on the intention of the parties as seen from the terms of the agreement.

The Hon'ble Supreme Court in **Dresser Rand S.A vs Bindal Agro Chem Ltd (2006) 1 SCC 751** held that a Letter of Intent may be construed as a letter of acceptance if such intention is evident from its terms. It is not uncommon in contracts involving detailed procedure, in order to save time, to issue a letter of intent communicating the acceptance of the offer and asking the contractor to start the work with a stipulation that the detailed contract would be drawn up later



If such a letter is issued to the contractor, though it may be termed as a Letter of Intent, it may amount to acceptance of the offer resulting in a concluded contract between the parties. But the question whether the letter of intent is merely an expression of an intention to place an order in future or whether is a final acceptance of the offer thereby leading to a contract, is a matter that has to be decided with reference to the terms of the letter

In the case of Rickmers Verwaltung GmbH v. Indian Oil Corporation Ltd [1999 (1) SCC 1] it has been held by the Apex Court that whether there was any meeting of mind between the parties, which could create a binding contract between them but the Court is not empowered to create a contract for the parties by going outside the clear language used in the correspondence, except insofar as there are some appropriate implications of law to be drawn

Unless from the correspondence it can unequivocally and clearly emerge that the parties were ad idem to the terms, it cannot be said that an agreement had come into existence between them through correspondence.

Whereas in **Trimex International Fze Limited v. Vedanta Aluminium Limited** 2010 (1) SCALE 574, the Hon'ble Supreme Court took a contrary view in typical fact and circumstances of the case. *It is held that a contract is said to be **concluded** when parties **agree** as to the 'essential terms' of the contract though minor details can be left over for them to decide later, albeit subject to satisfaction of other requirements as provided by S.10: without such essential terms being decided, contract cannot be enforced by law as it is deemed to be incomplete.*