

Unit 3



ESSENTIAL ELEMENTS OF A VALID CONTRACT

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Section 10 of the Indian Contract Act, 1872 provides that an agreement in order to a contract, must satisfy the following conditions:-

- 1] The parties must be **competent to contract**
- 2] It must be made by the **free consent of the parties.**
- 3] It must be made for a **lawful consideration** and with a **lawful object.**
- 4] It should **not have been expressly declared as void by law.**

* **Capacity to contract**

Meaning:- Capacity refers to the competence of the parties to make a contract.

Who is competent to contract

"Every person is competent to contract who is the age of **majority** according to the law to which he is subject, and who is of **sound mind** and **is not disqualified** from contracting **by any law to which he is subject.**"

Capacity to Contract	
Yes	No
Contract valid	Contract invalid
Major	Minor
Sound Mind	Unsound mind
Not disqualified by law	Disqualified by law

1] Age of Majority :-

In India, the age of majority is regulated by the Indian Majority Act, 1875

- Every person domiciled in India shall attain the age of majority on the completion of 18 years of age and not before.

Law relating to minor's agreement / position of Minor :-

A contract made with or by a minor is void-ab-intio :-

- A minor is not competent to contract and any agreement with or by a minor is void from the very beginning.

No Ratification after attaining majority :-

- A minor cannot ratify the agreement on attaining the majority as the original agreement is void ab intio and a void agreement can never be ratified.

A minor can be a beneficiary or can take benefit out of a contract :-

- Though a minor is not competent to contract, nothing in the Contract Act prevents the minor from making the other party bound to him.

- A minor cannot become partner in a partnership firm. However, He may with the consent of all the partners, be admitted to the benefits of partnership.

A minor can always plead minority:-

- A minor can always plead minority and is not stopped to do so even where he has taken any loan or entered into any contract by falsely representing that he was major.
- Rule of estoppel cannot be applied against a minor.

Liability for necessities:-

- A claim for necessities supplied to a minor is enforceable by law.
- There is no personal liability of the minor, but only his property is liable.
- To render minor's estate liable for necessities two conditions must be satisfied.
 - i] The contract must have already a sufficient supply of these necessities
 - ii] Necessaries [food, clothing, shelter, education, funeral ceremonies, etc] mean those things that are essentially needed by a minor
They cannot include luxuries or unnecessary articles.

Contract by guardian - how far enforceable:-

- Where the guardian makes a contract for the minor, which is within his competence and which is for the benefit of the minor, there will be a valid contract which the minor can enforce

No specific Performance:-

- A minor's agreement being absolutely void, there can be no question of the specific performance of such an agreement.

No insolvency:-

- A minor cannot be declared as insolvent as he is incapable of contracting debts and dues are payable from the personal properties of minor and he shall never be held personally liable.

Partnership:-

- A minor being incompetent to contract cannot be a partner in a partnership firm, but, he can be admitted to the benefits of partnership.

Minor can be an agent:-

- A minor can act as an agent. But he will not be liable to his principal for his acts.

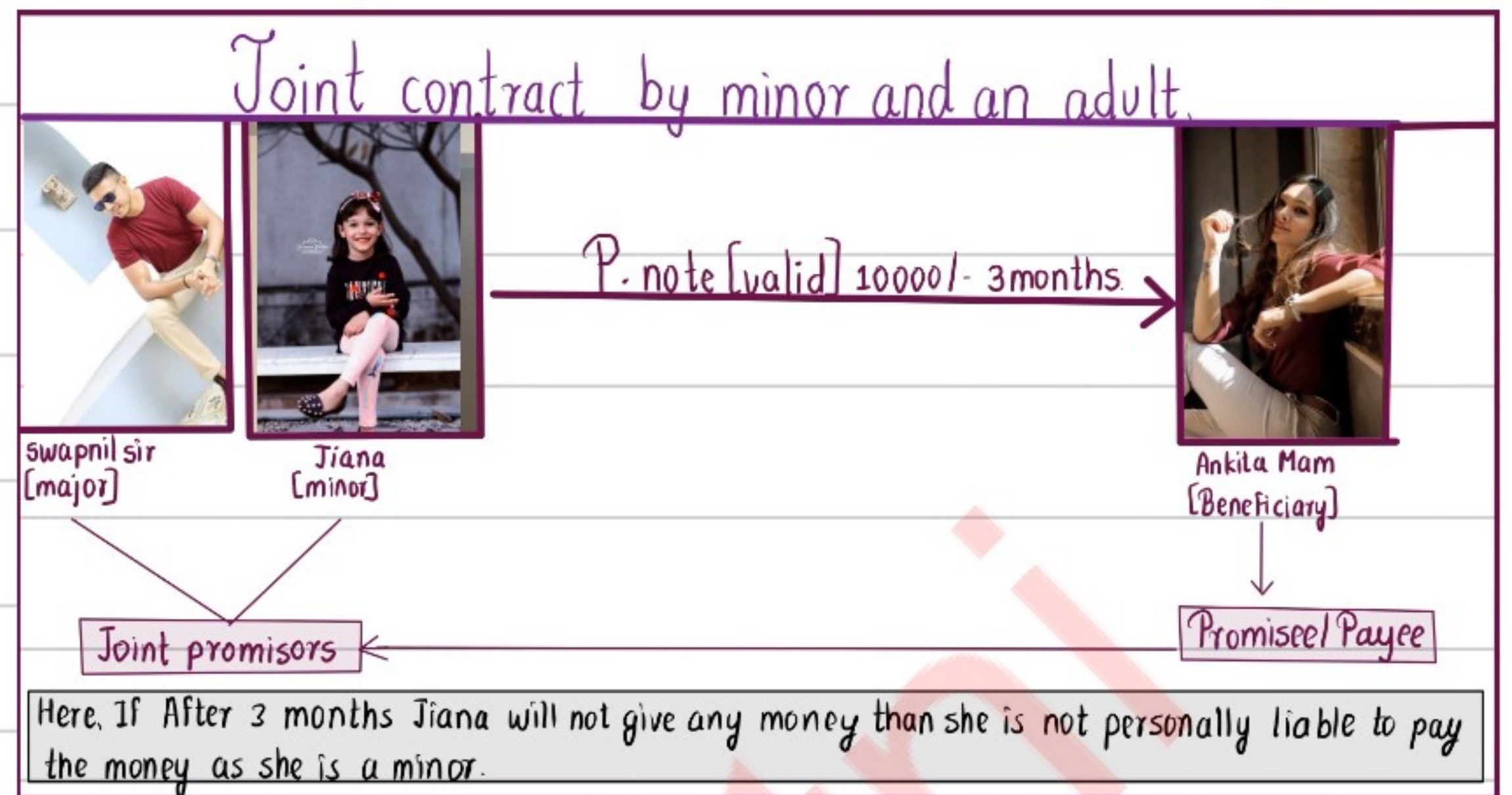
Minor cannot bind parent or guardian:-

- An infant is not capable of binding his parent or guardian even for necessaries.
- The parents will be held liable only when the child is acting as an agent for parents

Joint contract by minor and adult:-

- In such a case, The adult will be liable on the contract and not the minor

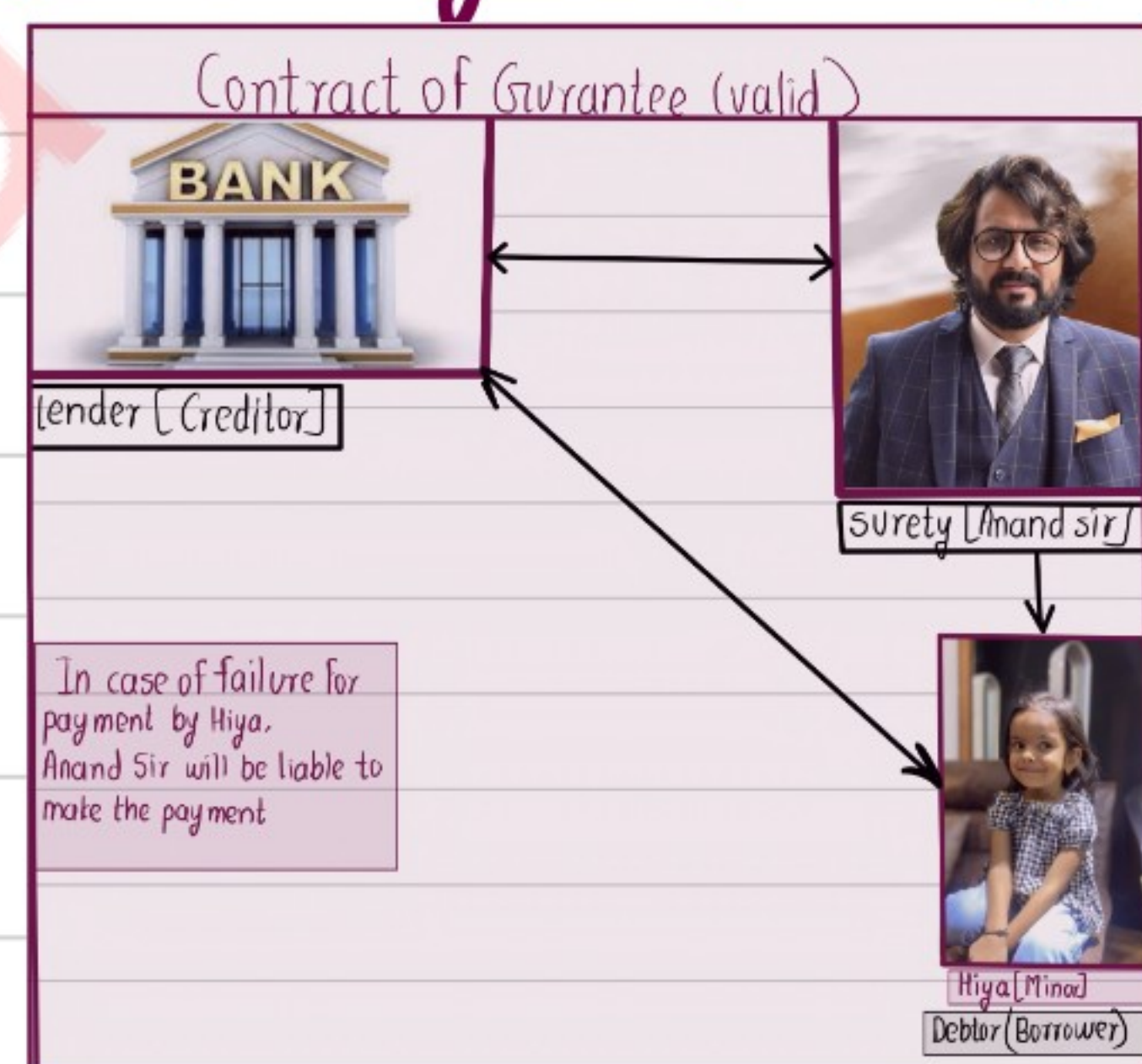
- eg:- swapnil sir and Jiana are joint promisors to Beneficiary ankita mam



Surety for a minor:-

- In a contract of gurantee when an adult stands surety for a minor then he is liable to third party as there is direct contract between the surety and third party.

- eg:- Anand sir guaranteed for the taking loan by hiya.



Minor as Shareholder:-

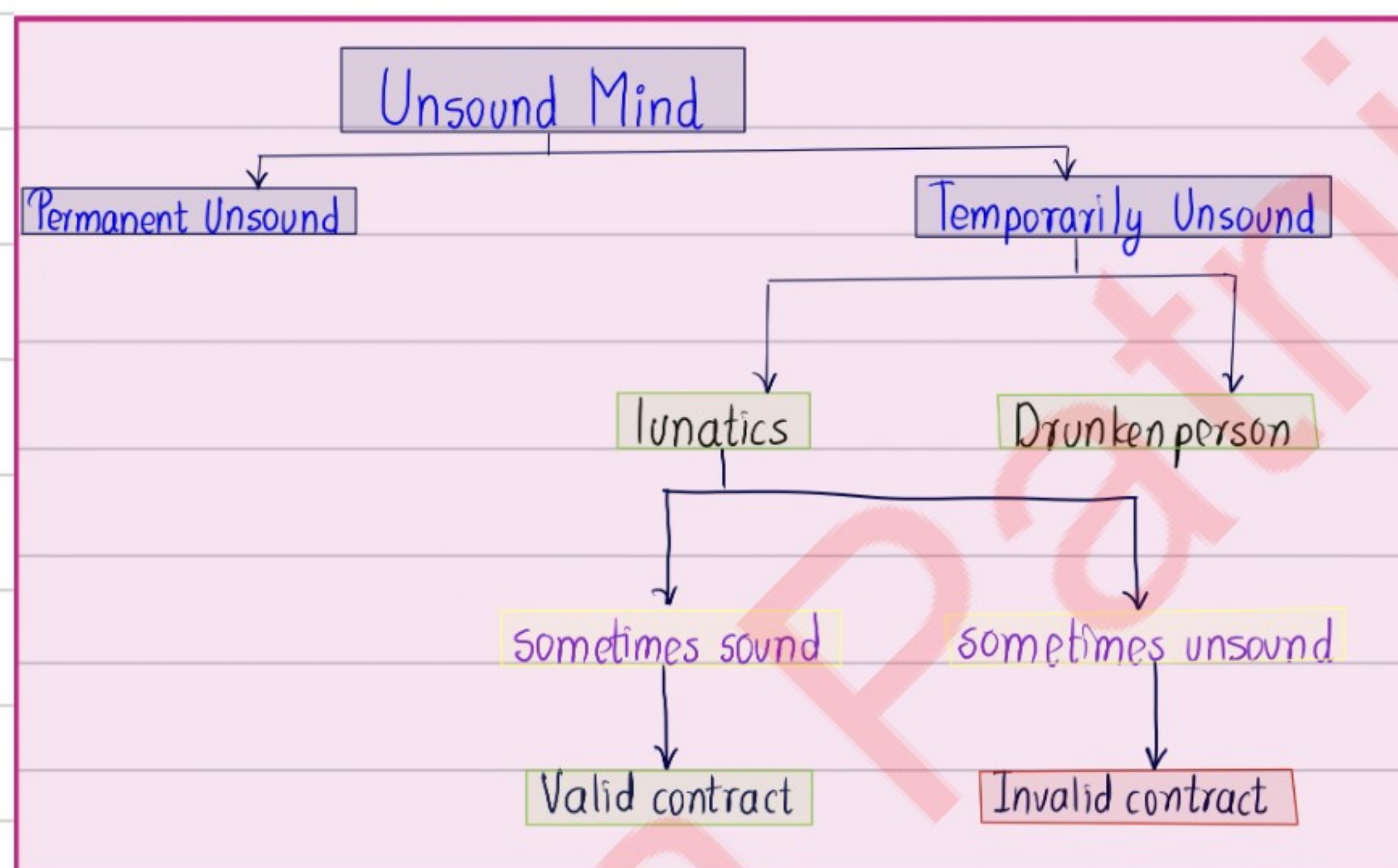
- A minor, being incompetent to contract cannot be a shareholder of the company.
- But a minor may, acting through his lawful guardian become a shareholder by transfer or transmission of fully paid shares to him

Liabilil of torts:-

- A tort is a civil wrong.
- A minor is liable in tort unless the tort in reality is a breach of a contract

II] Person of sound mind:-

"A person is said to be of sound mind for the purposes of making a contract if, at the time when he makes it is capable of understanding it and of forming a rational judgement as to its effect upon his interests"



III] Contract by disqualified person:-

- Besides minors and persons of unsound mind, there are also other persons who are disqualified from contracting, partially or wholly so that the contracts by such persons are void.

- The following persons fall in this category:- foreign sovereigns and Ambassadors, Corporations, Convicts, Insolvent, etc

Free Consent:-

- "Two or more persons are said to consent when they agree upon the same thing in the same sense"

- free consent is necessary for the validity of a contract

Consent is said to be free when it is not caused by

- ① Coercion
- ② Undue Influence
- ③ Fraud
- ④ Misrepresentation
- ⑤ Mistake

When consent to an agreement is caused by coercion, fraud, misrepresentation or undue influence, the agreement is a contract voidable at the option of the party whose consent was so caused.

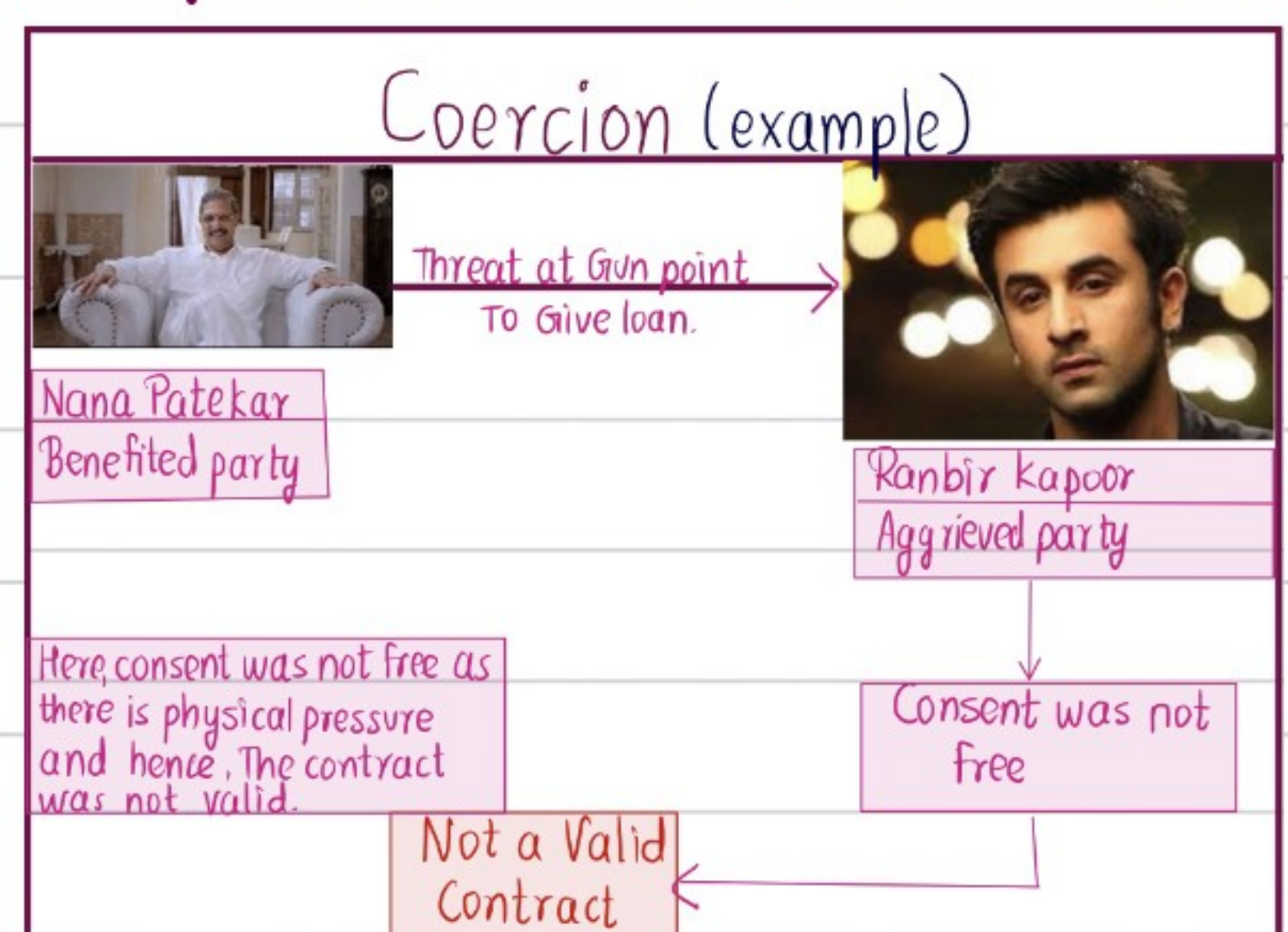
1] Coercion:-

- Coercion is the committing or threatening to commit, any act forbidden by the Indian Penal Code.
- The unlawful detaining, or threatening to detain any property to prejudice of any person whatever
- with the intention of causing any person to enter into an agreement.

* Effects of Coercion:-

a] Contract induced by coercion is voidable at the option of the party whose consent was so obtained.

b] The party rescinding a void contract should, if he has received any benefit from the other party to the contract, restore such benefit to the person from whom it was received.



II] 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 he uses that position to obtain an unfair advantage over the other.

The essential ingredients under this provisions are:-

1. Relation between the parties:-

- A person can be influenced by the other when a near relation between the two exists.

2. Relation to dominate the will:-

- Relation between the parties exist in such a manner that one of them is in a position to dominate the will of the other.

- A person is deemed to be in such position in the following circumstances:-

2A] Real and Apparent authority:-

- Master and servant, doctor and patient etc

2B] fiduciary relationship:-

- Where relation of trust and confidence exists between the parties to a contract.

- solicitor, and client, husband and wife, creditor and debtor, etc

2C] Mental distress:-

- An undue influence can be used against a person to get on a contract where the mental capacity of the person

is temporarily or permanently affected by the reason of mental or bodily distress, illness or of old age.

2D) Unconscionable bargains:-

3. The object must be to take undue advantage:-

- Where the person is in a position to influence the will of the other in getting consent, must have the object to take advantage of the other

4. Burden of proof:-

- The burden of proving the absence of the use of the dominant position to obtain the unfair advantage will lie on the party who is in a position to dominate the will of the other.

DIFFERENCE BETWEEN COERCION AND UNDUE INFLUENCE

Basis of difference	Coercion	Undue Influence
Nature of action	It involves the physical force or threat. The aggrieved party is compelled to make the contract against its will.	It involves moral or mental pressure.
Involvement of criminal action	It involves committing or threatening to commit and act forbidden by Indian Penal Code or detaining or threatening to detain property unlawfully.	No such illegal act is committed or a threat is given.
Relationship between parties	It is not necessary that there must be some sort of relationship between the parties.	Some sort of relationship between the parties is absolutely necessary.
Exercised by whom	Coercion need not proceed from the promisor nor need it be directed against the promisor. It can be used even by a stranger to the contract.	Undue influence is always exercised between parties to the contract.
Enforceability	The contract is voidable at the option of the party whose consent has been obtained by the coercion.	Where the consent is induced by undue influence, the contract is either voidable or the court may set it aside or enforce it in a modified form.
Position of benefits received	In case of coercion where the contract is rescinded by the aggrieved party, as per Section 64, any benefit received has to be restored back to the other party.	The court has the discretion to direct the aggrieved party to return the benefit in whole or in part or not to give any such directions

III] Fraud:-

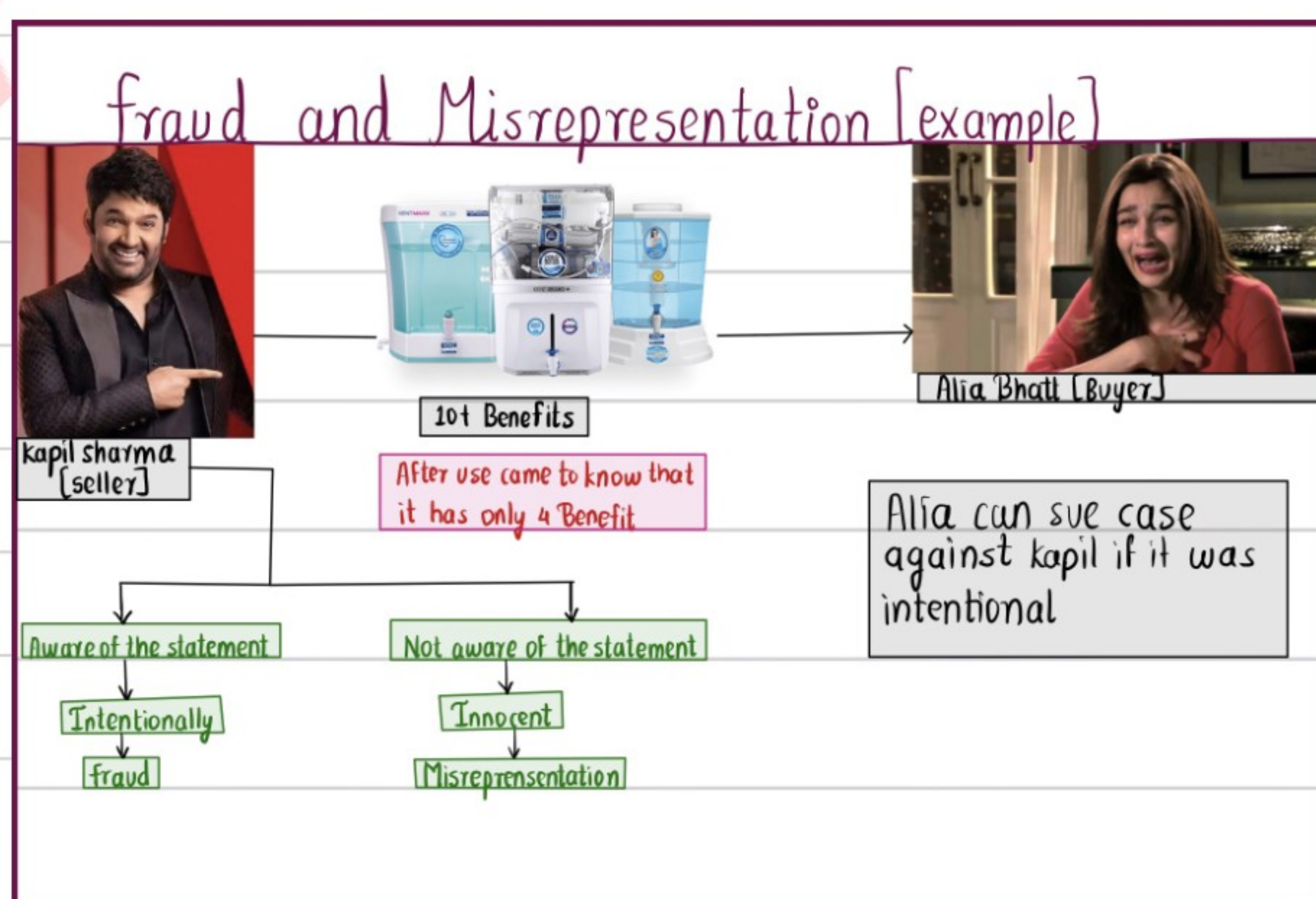
The following are the essential elements of the fraud:-

- There must be a representation and it must be false.
- The representation must be related to the fact
- The representation should be made before the conclusion of the contract with the intention to induce the other party to act upon it.
- The representation should be made with a knowledge of its falsity.
- The other party must have relied upon the representation and consequently suffered a loss

Effect of fraud upon a validity of a contract:-

When the consent to an agreement is caused by the fraud, the contract is voidable at option of the party defrauded and he has the following remedies:-

1. He can rescind the contract
2. He can sue for damages
3. He can insist on the performance of the contract on the condition that he shall be put in the position in which he would have been had the representation



Mere silence is not fraud:-

1] Where there is no duty to speak cases silence does not amount to fraud.

2] Silence is fraud when it is the duty of the person observing silence to speak.

following contracts come within this category:-

a) **Fiduciary Relationship:-**

Here the person in whom confidence is reposed is under a duty to act with utmost good faith and make full disclosure all material facts concerning the agreement known to him

b) **Contract of Insurance:-**

In contracts of marine, fire and life insurance, there is an implied condition that full disclosure of material facts shall be made, otherwise the insurer is entitled to avoid the contract.

c) **Contract of marriage:-**

Every material fact must be disclosed by the parties to a contract of marriage.

d) **Contracts of family settlement:-**

These contracts also require full disclosure of material facts within the knowledge of the parties

e) Share Allotment contracts I-

Persons issuing 'prospectus' at the time of public issue of shares / debentures by a joint stock company have to disclose all material facts within their knowledge.

3) Where the silence itself is equivalent to speech:-

For example, A says to B "If you do not deny it, I shall assume that the horse is sound" A says nothing His silence amounts to speech.

IV] Misrepresentation:-

1. statement of the fact, which of false, would constitute misrepresentation if the maker believes it to be true but which is not justified by the information he possesses.
2. When there is a breach of duty by a person without any intention to deceive which brings an advantage to him.

FRAUD V/S MISREPRESENTATION

Basis of difference	Fraud	Misrepresentation
Intention	To deceive the other party by hiding the truth.	There is no such intention to deceive the other party.
Knowledge of truth	The person making the suggestion believes that the statement as untrue.	The person making the statement believes it to be true, although it is not true.
Rescission of the contract and claim for damages	The injured party can repudiate the contract and claim damages.	The injured party is entitled to repudiate the contract or sue for restitution but cannot claim the damages.
Means to discover the truth	The party using the fraudulent act cannot secure or protect himself by saying that the injured party had means to discover the truth.	Party can always plead that the injured party had the means to discover the truth.

Legal effects of agreements without free consent-

- When consent to an agreement is caused by coercion, fraud or misrepresentation the agreement is a contract voidable at the option of the party whose consent was so caused.
- But a person who had the means of discovering the truth with ordinary diligence cannot avoid a contract on the ground that his consent was caused by misrepresentation or silence amounting to fraud.

V Mistake:-

- Mistake may be defined as innocent or erroneous belief which leads the party to misunderstand the other.
- Mistake may be either Bilateral or Unilateral.
- **Bilateral mistake** is when both the parties to a contract are under a mistake
- **Unilateral mistake** is when only one party to the contract is under a mistake

1] Mistake of law:-

- A mistake of law does not render a contract void as one cannot take excuse of ignorance of the law of his own country.
- Mistake of foreign law is excusable and is treated like a mistake of fact.

2. Mistake of fact:-

Where both the parties to an agreement are under a mistake as to a matter of fact essential to the agreement the agreement is void.

Legality of Object and consideration:-

In each of the following cases the consideration or object of an agreement is said to be unlawful:

1. When Consideration is forbidden by law:-

Acts forbidden by law are those which are punishable under any statute as well as those prohibited by regulations orders made in exercise of the authority conferred by the legislature.

2. When consideration or object defeats the provision of law:-

If the intention of the parties is to defeat the provisions of law, the court will not enforce it.

3. When it is fraudulent:-

Agreements which are entered into to promote fraud are void.

4. When consideration involves injury to the person or property of another:-

The general term 'injury' means criminal or wrongful harm.

5. **When consideration is immoral:-**

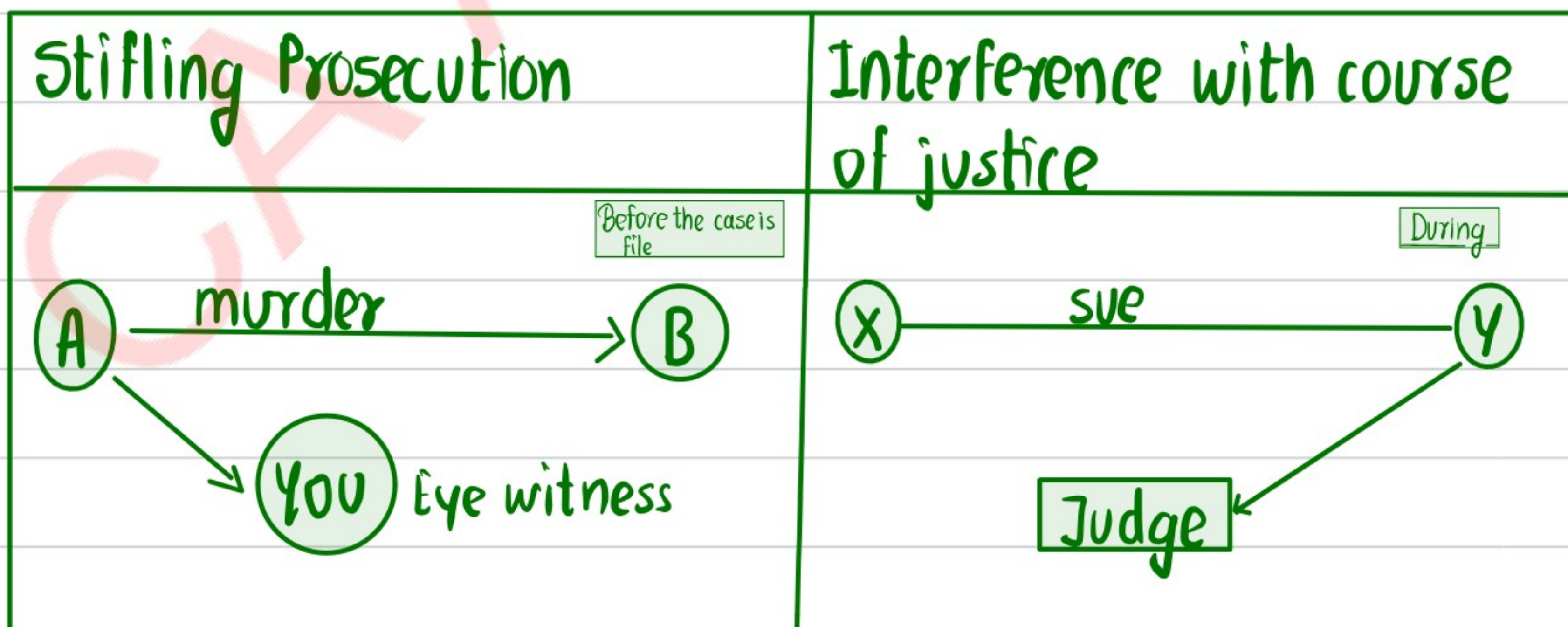
6. **When consideration is opposed to public policy:-**

Some of the agreements which are held to be opposed to public policy are-

i) **Trading with enemy -** Any trade with person owning allegiance to a government at war with India without the license of the government of India is void.

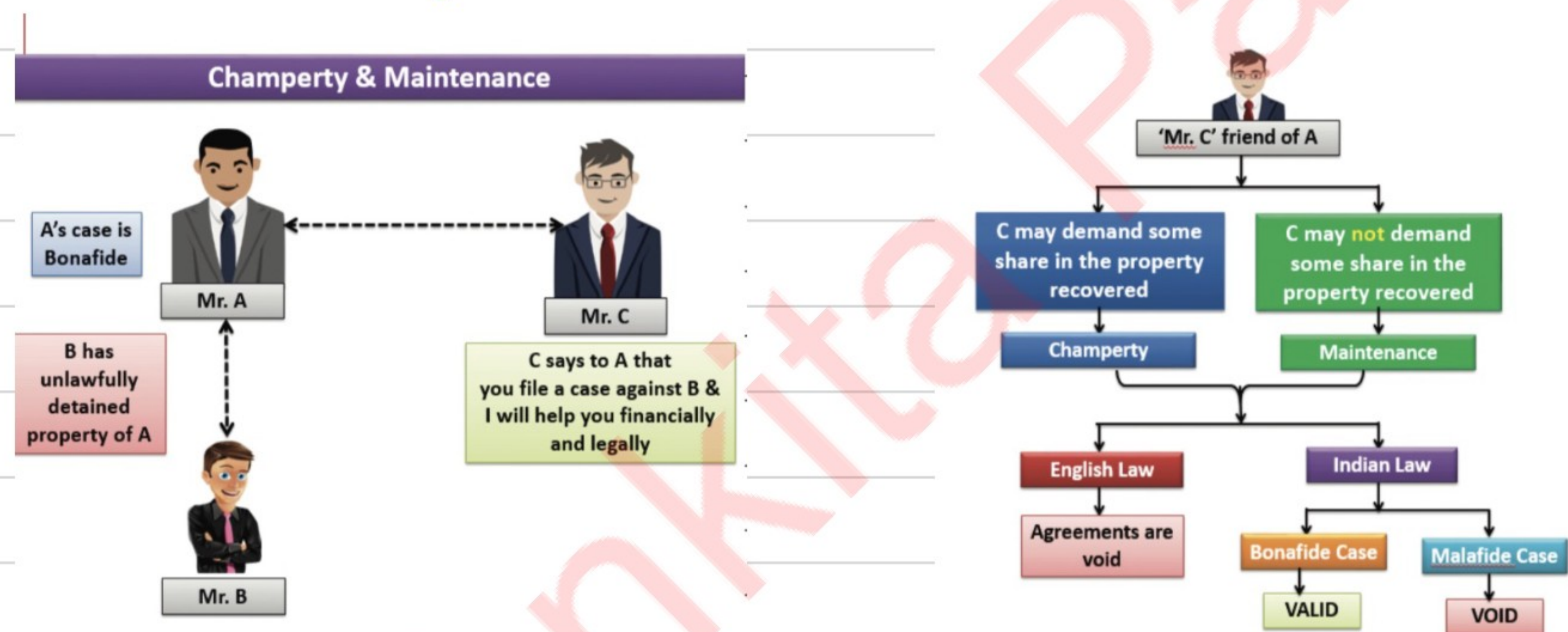
ii) **Stifling Prosecution:-** An Agreement to prevent proceedings already instituted from running their normal course using force tends to be a perversion or an abuse of justice; therefore such an agreement is void.

iii) **Interference with the course of justice:-** An Agreement whose object is to induce any judicial officer of the state to act partially or corruptly is void as it is opposed to public policy.



iv) Maintenance and Champerty:-

- Maintenance is an agreement in which a person promises to maintain suit in which he has no interest.
- Champerty is an agreement in which a person agrees to assist another in litigation in exchange of a promise to hand over a portion of the proceeds of the action.
- The agreement for supplying funds by way of Maintenance or champerty is valid unless:
 - a) It is unreasonable so as to be unjust to other party or
 - b) It is made by a malicious motive.



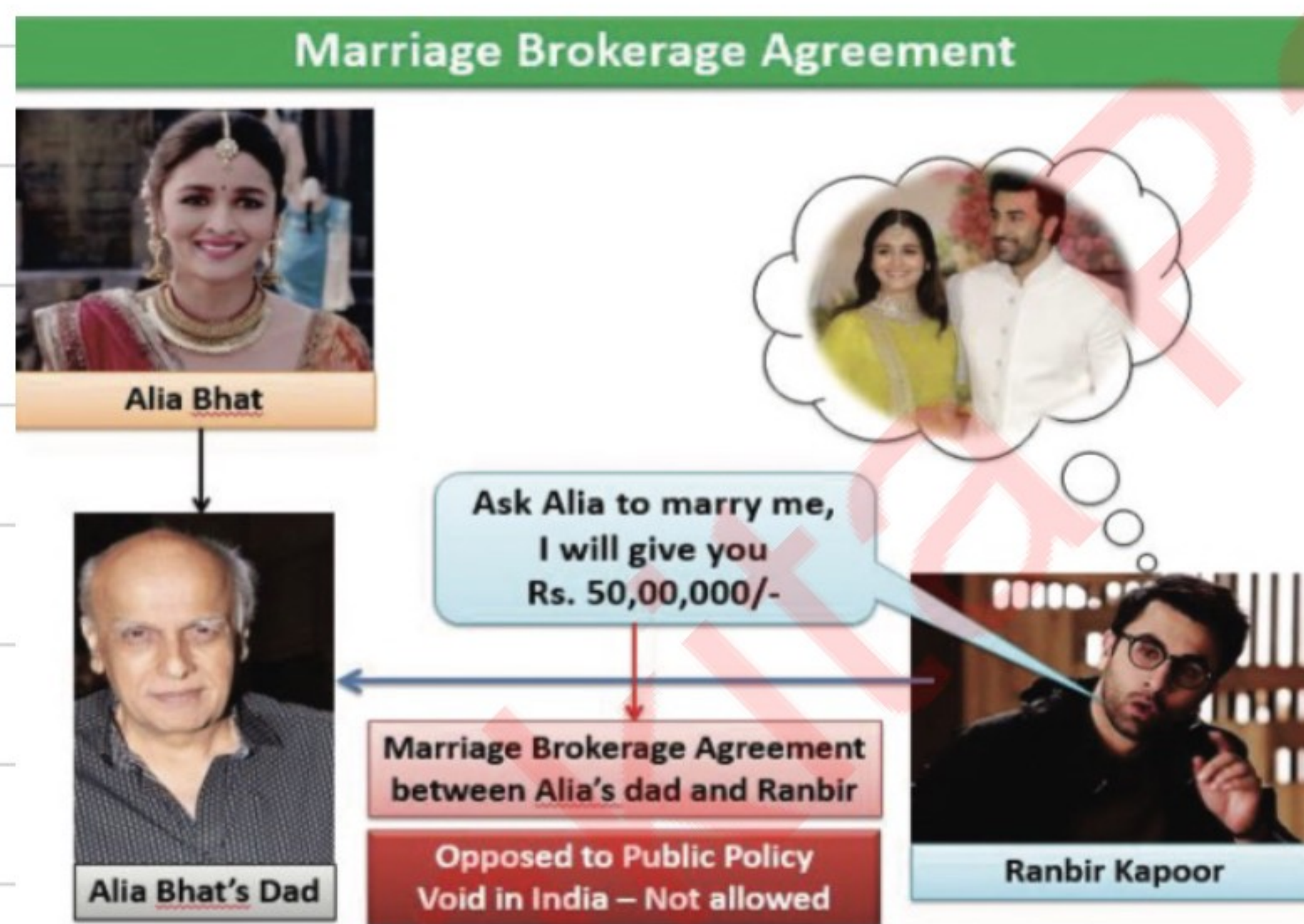
v) Trafficking relating to Public Offices and titles:-

- An Agreement to trafficking to public office is opposed to public policy, as it interferes with the appointment of a person best qualified for the service of the public.
- The following are the examples of agreements that are void. since are the amount to sale of public offices:-
 - 1] An Agreement to pay money to a public servant in order to induce him to retire from his office so that another person may secure the appointment is void.

vii] Agreements tending to create monopolies:-

- Agreements having for their object the establishment of monopolies are opposed to public policy and therefore void.

viii] Marriage Brokerage agreements:- An Agreement to negotiate marriage for reward which is known as a marriage brokerage contract is void as it is opposed to public policy.



viii] Interest against obligation:- Examples are as follows:-

1. An Agreement by an agent to receive without his principal's consent compensation from another for the performance of his agency is invalid.
2. A, who is the manager of a firm, agrees to pass a contract to X if X pays to A ₹ 20,000 privately. The agreement is void.

VOID AGREEMENTS :-

1. Agreement in restraint of marriage:-

Every agreement in restraint of marriage of any person other than a minor, is void.

2. Agreement in restraint in trade:-

An Agreement by which any person is restrained from exercising a lawful profession, trade or business of any kind, is to the extent void.

Exceptions:-

1. Sale of Goodwill:-

Where a person sells the goodwill of a business, within specified local limits, so long as the buyer or his successor in interest carries on a like business therein, such an agreement is valid.

2. Indian Partnership Act:-

If an outgoing partner makes an agreement with the continuing partners that he will not carry on any business similar to that of the firm within a specified period or within specified local limits, such an agreement, though in restraint of trade, will be valid, if the restrictions imposed are reasonable.

3 Agreement of service :-

An Agreement of service by which an employee binds himself, during the term of his agreement not to compete with his employer is not restraint in trade



3 Agreement in restraint of legal proceedings:-

An agreement in restraint of legal proceeding is the one by which any party there to is restricted absolutely from enforcing his rights under a contract through a court.

However, there are certain exceptions to the above rule:-

i) A contract by which the parties agree that any dispute between them in respect of any subject shall be referred to arbitration and that only the amount awarded in such arbitration shall be recoverable is a valid contract

4. Agreement:-

- The meaning of which is uncertain.
- An Agreement the meaning of which is not certain is void but where the meaning thereof is capable of being made certain the agreement is valid.

5 Wagering agreement:-

- An Agreement by way of a wager is void. It is an agreement involving payment of a sum of money upon the determination of an uncertain events.

Essentials of a Wager

1. There must be a promise to pay money or money's worth
2. Promise must be conditional on an event happening or not happening.
3. There must be uncertainty of event
4. There must be two parties, each party must stand to win or lose.
5. There must be common intention to bet at the timing of making such agreement.
6. Parties should have no interest in the event except for stake

Transactions similar to Wager (Gambling):-

i] Lottery Transactions:-

- A lottery is a game of chance and not of skill or knowledge where the prime motive of participant is gambling, the transaction amounts to a wager
- Even if the lottery sanctioned by the government of India it is a wagering transaction.
- The only effect of such sanction is that the person responsible for running the lottery will not be punished under the Indian Penal Code.
- Lotteries are illegal and even collateral transactions to it are tainted with illegality.

ii] Crossword Puzzles and Competitions:-

- Crossword puzzles in which prizes depend upon the correspondence of the competitor's solution with a previously prepared solution kept with the editor of a newspaper and therefore, a wagering transaction

iii] Speculative transactions:-

- An Agreement or a share market transaction where the parties intend to settle the difference between the contract price and the market price of certain goods or shares on a specified day is gambling and hence void.

iv) Horse Race Transactions:-

- A horse race competition where prize payables to the bet winner is less than ₹500, is a wager.

- Transactions resembling the wagering transaction but are not void:-

① Chit fund:- Chit fund does not come within the scope of wager

② Commercial transactions or share market transactions:-

- In these transactions in which delivery of goods or shares is intended to be given or taken, do not amount to wagers

③ Games of skill and Athletic Competition:-

- Crossword puzzles, picture competitions and athletic competitions where prizes are awarded on the basis of skill and intelligence are the games of skill and hence such competition are valid

④ A contract of insurance:-

- A contract of insurance is a type of contingent contract and is valid under law and these contracts are different from wagering agreements

	Basis	Contracts of Insurance	Wagering Agreement
1.	Meaning	It is a contract to indemnify the loss.	It is a promise to pay money or money's worth on the happening or non- happening of an uncertain event.
2.	Consideration	The crux of insurance contract is the mutual consideration (premium and compensation amount).	There is no consideration between the two parties. There is just gambling for money.

Insurable Interest	Insured party has insurable interest in the life or property sought to be insured.	There is no property in case of wagering agreement. There is betting on other's life and properties.
Contract of Indemnity	Except life insurance, the contract of insurance indemnifies the insured person against loss.	Loser has to pay the fixed amount on the happening of uncertain event.
Enforceability	It is valid and enforceable	It is void and unenforceable agreement.
Premium	Calculation of premium is based on scientific and actuarial calculation of risks.	No such logical calculations are required in case of wagering agreement.

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