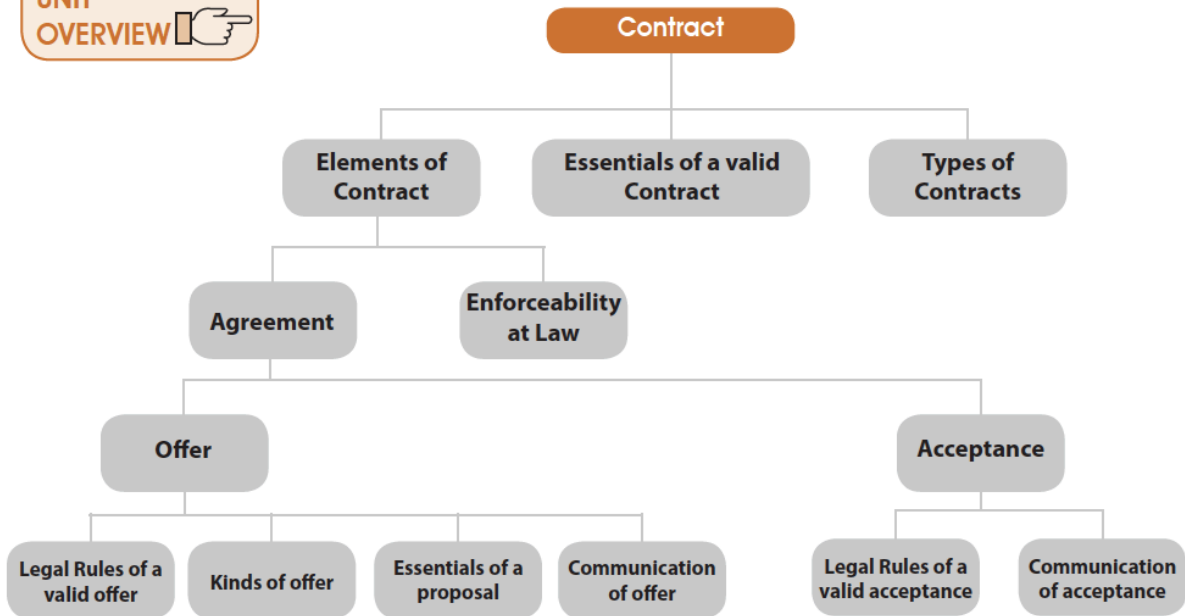


Indian Contract Act, 1872



1. What is a Contract?

The term contract is defined under section 2(h) of the Indian Contract Act, 1872 as-

“an agreement enforceable by law”.

The contract consists of two essential elements:

- (i) an agreement, and
- (ii) its enforceability by law.

(i) Agreement - The term ‘agreement’ **given in Section 2(e)** of the Act is defined as- “every promise and every set of promises, forming the consideration for each other”.

To have an insight into the definition of agreement, we need to understand promise.

Section 2 (b) defines promise as-

“when the person to whom the proposal is made signifies his assent there to, the proposal is said to be accepted. Proposal when accepted, becomes a promise”.

The following points emerge from the above definition :

1. when the person to whom the proposal is made
2. signifies his assent on that proposal which is made to him
3. the proposal becomes accepted
4. accepted proposal becomes promise

Thus we say that an agreement is the result of the proposal made by one party to the other party and that other party gives his acceptance thereto of course for mutual consideration.

Agreement = Offer/Proposal + Acceptance

(ii) Enforceability by law – An agreement to become a contract must give rise to a legal obligation which means a duly enforceable by law.

Thus from above definitions it can be concluded that –

Contract = Accepted proposal/Agreement + Enforceability by law

On elaborating the above two concepts, it is obvious that contract comprises of an agreement which is a promise or a set of reciprocal promises, that a promise is the acceptance of a proposal giving rise to a binding contract. Further, section 2(h) requires an agreement to be worthy of being enforceable by law before it is called ‘contract’. Where parties have made a binding contract, they created rights and obligations between themselves.

Example: A agrees with B to sell car for Rs. 2 lacs to B. Here A is under an obligation to give car to B and B has the right to receive the car on payment of Rs. 2 lacs and also B is under an obligation to pay Rs. 2 lacs to A and A has a right to receive Rs. 2 lacs.

So Law of Contract deals with only such legal obligations which has resulted from agreements. Such obligation must be contractual in nature. However some obligations are outside the purview of the law of contract.



Difference between Agreement and Contract

Basis of differences	Agreement	Contract
Meaning	Every promise and every set of promises, forming the consideration for each other. Offer + Acceptance	Agreement enforceable by law. Agreement + Legal enforceability
Scope	It's a wider term including both legal and social agreement.	It is used in a narrow sense with the specification that contract is only legally enforceable agreement.
Legal obligation	It may not create legal obligation. An agreement does not always grant rights to the parties	Necessarily creates a legal obligation. A contract always grants certain rights to every party.
Nature	All agreement are not contracts.	All contracts are agreements.

2. Essentials of a Valid Contract

In terms of Section 10 of the Act, "all agreements are contracts if they are made by the free consent of the parties competent to contract, for a lawful consideration and with a lawful object and are not expressly declared to be void".

Since section 10 is not complete and exhaustive, so there are certain others sections which also contains requirements for an agreement to be enforceable. Thus, in order to create a valid contract, the following elements should be present:

1. **Two Parties:** One cannot contract with himself. A contract involves at least two parties- one party making the offer and the other party accepting it. A contract may be made by natural persons and by other persons having legal existence e.g. companies, universities etc. It is necessary to remember that identity of the parties be ascertainable.

Example: To constitute a contract of sale, there must be two parties- seller and buyer. The seller and buyer must be two different persons, because a person cannot buy his own goods. In *State of Gujarat vs. Ramanlal S & Co.* when on dissolution of a partnership, the assets of the firm were divided among the partners, the sales tax officer wanted to tax this transaction. It was held that it was not a sale. The partners being joint owner of those assets cannot be both buyer and seller.

2. **Parties must intend to create legal obligations:** There must be an intention on the part of the parties to create legal relationship between them. Social or domestic type of agreements are not enforceable in court of law and hence they do not result into contracts.

Example: A husband agreed to pay to his wife certain amount as maintenance every month while he was abroad. Husband failed to pay the promised amount. Wife sued him for the recovery of the amount. Here in this case wife could not recover as it was a social agreement and the parties did not intend to create any legal relations. (*Balfour v. Balfour*)

3. **Other Formalities to be complied with in certain cases:** In case of certain contracts, the contracts must be in writing, e.g. Contract of Insurance is not valid except as a written contract. Further, in case of certain contracts, registration of contract under the laws which is in force at the time, is essential for it to be valid, e.g. in the case of immovable property.
4. **Certainty of meaning:** The agreement must be certain and not vague or indefinite. Example: A agrees to sell to B a hundred tons of oil. There is nothing certain in order to show what kind of oil was intended for.
5. **Possibility of performance of an agreement:** The terms of agreement should be capable of performance. An agreement to do an act impossible in itself cannot be enforced. Example: A agrees with B to discover treasure by magic. The agreement cannot be enforced as it is not possible to be performed.

According to Section 10 of the Indian Contract Act, 1872, the following are the essential elements of a Valid Contract:

- I. **Offer and Acceptance or an agreement:** An agreement is the first essential element of a valid contract. According to Section 2(e) of the Indian Contract Act, 1872, "Every promise and every set of promises, forming consideration for each other, is an agreement" and according to Section 2(b) "A proposal when accepted, becomes a promise". An agreement is an outcome of offer and acceptance.
- II. **Free Consent:** Two or more persons are said to consent when they agree upon the same thing in the same sense. This can also be understood as identity of minds in understanding the terms viz consensus ad idem. Further such a consent must be free. Consent would be considered as free consent if it is not caused by coercion, undue influence, fraud or, misrepresentation or mistake. When consent to an agreement is caused by coercion, undue influence, fraud or misrepresentation, the agreement is a contract voidable at the option of the party whose consent was so caused.

When consent is vitiated by mistake, the contract becomes void.

Example: A threatened to shoot B if he (B) does not lend him Rs.2000 and B agreed to it. Here the agreement is entered into under coercion and hence voidable at the option of B.

- III. **Capacity of the parties:** Capacity to contract means the legal ability of a person to enter into a valid contract. Section 11 of the Indian Contract Act specifies that every person is competent to contract who
 - (a) is of the age of majority according to the law to which he is subject and
 - (b) is of sound mind and
 - (c) is not otherwise disqualified from contracting by any law to which he is subject.

A person competent to contract must fulfil all the above three qualifications.

Qualification (a) refers to the age of the contracting person i.e. the person entering into contract must be of 18 years of age. Persons below 18 years of age are considered minor, therefore, incompetent to contract.

Qualification (b) requires a person to be of sound mind i.e. he should be in his senses so that he understands the implications of the contract at the time of entering into a contract. A lunatic, an idiot, a drunken person or under the influence of some intoxicant is not supposed to be a person of sound mind.

Qualification (c) requires that a person entering into a contract should not be disqualified by his status, in entering into such contracts. Such persons are: an alien enemy, foreign sovereigns, convicts etc. They are disqualified unless they fulfil certain formalities required by law.

Contracts entered by persons not competent to contract are not valid.

- IV. **Consideration:** It is referred to as '*quid pro quo*' i.e. 'something in return'. A valuable consideration in the sense of law may consist either in some right, interest, profit, or benefit accruing to one party, or some forbearance, detriment, loss or responsibility given, suffered or undertaken by the other.

Example:- A agrees to sell his books to B for Rs.100, B's promise to pay Rs.100 is the consideration for A's promise to sell his books and A's promise to sell the books is the consideration for B's promise to pay Rs.100.

- V. **Lawful Consideration and Object:** The consideration and object of the agreement must be lawful.

Section 23 states that consideration or object is not lawful if it is prohibited by law, or it is such as would defeat the provisions of law, if it is fraudulent or involves injury to the person or property of another or court regards it as immoral or opposed to public policy.

Example : 'A' promises to drop prosecution instituted against 'B' for robbery and 'B' promises to restore the value of the things taken. The agreement is void, as its object is unlawful.

- VI. **Not expressly declared to be void:** The agreement entered into must not be which the law declares to be either illegal or void. An illegal agreement is an agreement expressly or impliedly prohibited by law. A void agreement is one without any legal effects.

Example: Threat to commit murder or making/publishing defamatory statements or entering into agreements which are opposed to public policy are illegal in nature. Similarly any agreement in restraint of trade, marriage, legal proceedings, etc. are classic examples of void agreements.