2(a): Proposal - When one person signifies to another his willingness to do or to abstain from doing anything, with a view to obtaining the assent of that other to such act or abstinence, he is said to make a proposal.

2(b): Promise - When the person to whom the proposal is made signifies his assent thereto, the proposal is said to be accepted. A proposal, when accepted, becomes a promise.

2(c): Promisor and Promisee - The person making the proposal is called the "promisor", and the person accepting the proposal is called the "promisee"

2(e): Agreement - Every promise and every set of promises, forming the consideration for each other, is an agreement.

2(g): Void agreement - An agreement not enforceable by law is said to be void.

2(h): Contract - An agreement enforceable by law is a contract.

2(i): Voidable contract - An agreement which is enforceable by law at the option of one or more of the parties thereto, but not at the option of the other or others, is a voidable contract.

10: What agreements are contracts - All agreements are contracts if they are made by the 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.

Nothing herein contained shall affect any law in force in India and not hereby expressly repealed by which any contract is required to be made in writing or in the presence of witnesses, or any law relating to the registration of documents.

What is contract?

Broadly speaking, a contract is an agreement made between two or more persons to do or to abstain from doing a particular act. A contract invariably creates a legal obligation between the parties by which certain rights are given to one party and a corresponding duty is imposed on the other party. A contract has been defined by different authorities in various ways. Some of the important definitions are as follows:

> A contract is an agreement, creating and defining the obligation between parties. – Salmond
>
> A contract is an agreement enforceable at law made between two or more persons by which rights are acquired by one or more to acts or forbearances on the part of others. – Sir William Anson
>
> Every agreement and promise enforceable at law is a contract. – Sir Fredrick Pollock.

The definition as given in the Contract Act is based on Pollock's definition. **Section 2(h)** of the Act states that an agreement enforceable by law is a contract. On analysing this definition of contract, you will notice that a contract essentially consists of two elements: (i) an agreement, and (ii) its enforceability by law.

Agreement

Section 2(e) of the Contract Act defines agreement as every promise and every set of promises forming the consideration for each other. In this context a promise refer to a proposal (offer) which has been accepted. For example, Ramesh offers to sell his scooter for Rs. 8,000 to Shyam. Shyam accepts this offer. It becomes a promise and treated as an agreement between Ramesh and Shyam. In other words, an agreement consists of an offer by one party and its acceptance by the other. Thus,

Agreement = Offer + Acceptance.

From the above analysis it is clear that there must be at least two parties to an agreement, one making an offer and the other accepting it. No person can enter into agreement with himself. There is another important aspect relating to an agreement i.e., the parties to an agreement must have an identity of minds in respect of the subject matter. They must agree on the same thing in the same sense. This is also called *consensus-ad-idem.* Suppose A has two houses, one situated in South Delhi and the other in North Delhi. He offers to sell his North Delhi house to B while B is under the impression that he is buying the South Delhi house. Here, there is no identity of minds. Both the parties are thinking about different houses. Hence there is no agreement.

Legal Obligation

In order that an agreement may be regarded as a contract, it must give rise to a legal obligation i.e., it must be enforceable by law. Any obligation (duty) which is not enforceable by law is not regarded as a contract. Social, moral or religious agreements do not create any legal obligation. For example, an agreement to take lunch together or to go to a picnic is not a contract because it does not create a duty enforceable by law. Such agreements are purely of a social nature where there is no intention to create legal relationship. Hence, they do not result in contracts. In case of business agreements, however, the usual presumption is that the parties intend to create a legal relationship. For example, an agreement to sell a scooter for Rs. 8,000 is a contract because it gives rise to an obligation enforceable by law. In this agreement if there is default by either party, an action for breach of contract can be enforced through a court of law provided all the essentials of a valid contract are present in the agreement.

One must also note that every obligation which is enforceable by law is not automatically regarded as a contract. The obligations which do not arise out of agreements but from sources such as wrongful acts, judicial decisions or decree of a court, husband and wife relationship are not regarded as contracts. Thus, the law of contract is concerned with only those obligations which arise out of agreement. Salmond has rightly said about the law of contract as –

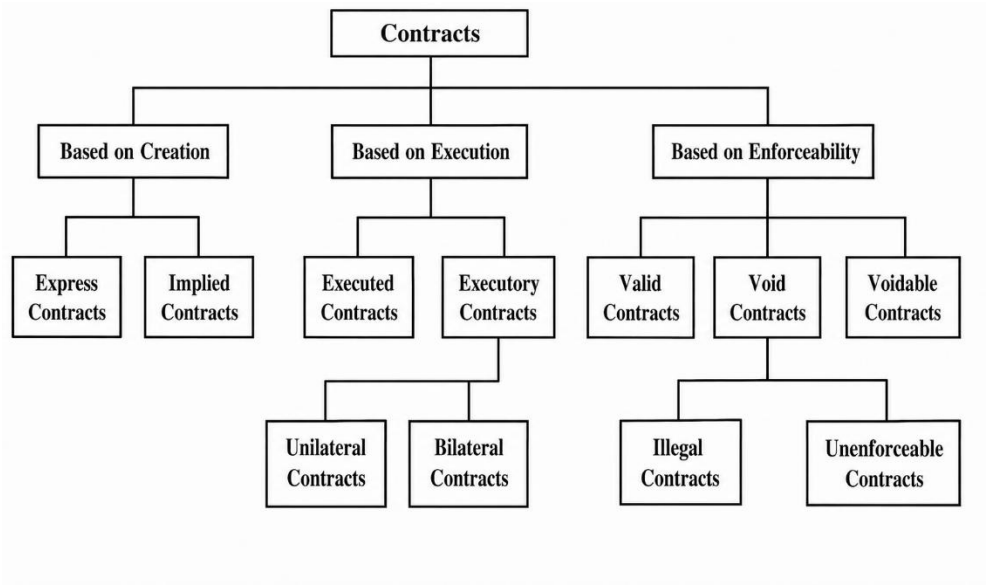
> "It is the law of those agreements which create obligations, and those obligations which have their source in agreements."

Distinction between an Agreement and a Contract

Agreement	Contract
1) Offer and its acceptance	1) Agreement and its

Agreement	Contract
constitute an agreement.	enforceability constitute a contract.
2) An agreement may not create a legal obligation.	2) A contract necessarily creates a legal obligation.
3) Every agreement may not be a contract.	3) All contracts are agreements.
4) Agreement is not a concluded or a binding contract.	4) Contract is concluded and binding on the concerned parties.

What the different classes of contract?



Contracts can be classified on a number of bases. They are:

1. On the basis of creation.
2. On the basis of execution.
3. On the basis of enforceability.

On the Basis of Creation

A contract may be (i) made in writing or by word of mouth or (ii) inferred from the conduct of the parties or circumstances of the case. The first category of contract is termed as 'express contract' and the second as 'implied contract'

i) Express Contract: An express contract is one where the terms are clearly stated in words, spoken or written. For example, A wrote a letter to B stating “I offer to sell my car for Rs. 30,000 to you”, B accepts the offer by letter sent to A. This is an express contract. Similarly, when A asks a scooter mechanic to repair his scooter and the mechanic agrees, it is an express contract made orally by spoken words.

ii) Implied Contract: A contract may be created by the conduct or acts of parties (and not by their words spoken or written). It may result from a continuing course of conduct of the parties. For example, where a coolie in uniform carries the luggage of A to be carried out of railway station without being asked by A to do so and A allows it, the law implies that A has agreed to pay for the services of the coolie. This is a case of an implied contract between A and the coolie. Similarly, when A boards a D.T.C bus, an implied contract comes into being. A is bound to pay the prescribed fare.

There is another category of implied contracts recognised by the Contract Act known as quasi-contracts (Sections 68 to 72). Strictly speaking, a quasi-contract cannot be called a contract. It is regarded as a relationship resembling that of a contract. In such a contract the rights and obligations arise not by an agreement between the parties but by operation of law. For example, A, a trader, left certain goods at B’s house by mistake. B treated the goods as his own and consumed it. In such a situation, B is bound

to pay for the goods even though he has not asked for the goods. One will learn about the quasi-contracts in detail later on.

On the Basis of Execution

On the basis of the extent to which the contracts have been performed, we may classify them as (i) executed contracts, and (ii) executory contracts.

i) Executed Contracts: It is a contract where both the parties have fulfilled their respective obligations under the contract. For example, A agrees to sell his book to B for Rs. 30. A delivers the book to B and B pays Rs. 30 to A. It is an executed contract.

ii) Executory Contracts: It is a contract where both the parties to the contract have still to perform their respective obligations. For example, A agrees to sell a book to B for Rs. 30. If the book has not been delivered by A and B has not paid the price, the contract is executory.

A contract may sometimes be partly executed and partly executory. It happens where only one of the parties has performed his obligation. In the example given above, if A has delivered the book to B but B has not paid the price, the contract is executed as to A and executory as to B.

On the basis of execution, a contract can also be classified as unilateral or bilateral. A unilateral contract is one in which only one party has to perform his obligation, the other party had fulfilled his part of the obligation at the time of the contract itself. For example, A buys a ticket from the conductor and is waiting in the queue for the bus. A contract is created as soon as the ticket is purchased. The other party is now to provide a bus wherein he could travel. A bilateral contract is one in which the

obligations on the part of both the parties are outstanding at the time of the formation of the contract.

On the Basis of Enforceability

From the point of view of enforceability, a contract may be (i) valid, (ii) void, (iii) voidable, (iv) illegal or (v) unenforceable. These terms shall be used quite frequently in this course. Hence, you must form a clear idea about their respective meanings.

i) Valid Contract: A contract which satisfies all the conditions prescribed by law is a valid contract. If one or more of these elements is/are missing, the contract is either void, voidable, illegal or unenforceable.

ii) Void Contract: According to Section 2 (j), a contract which ceases to be enforceable by law becomes void when it ceases to be enforceable. It is a contract without any legal effects and is a nullity. You should note that a contract is not void from its inception. It is valid and binding upon the parties when made, but subsequent to its formation, due to certain reasons, it becomes unenforceable and so treated as void. A contract may become void due to impossibility of performance, change of law or some other reasons. For example, A promised to marry B. Later on, B dies. This contract becomes void on the death of B. A void contract should be distinguished from void agreement. Section 2(g) says that an agreement not enforceable by law is said to be void. In the case of void agreement, no contract comes into existence. Such an agreement confers no rights on any person and creates no obligations. It is void *ab-initio* i.e., from the very beginning. For example, an agreement with a minor is void because a minor is incompetent to contract.

Now it should be clear that a void agreement is not the same thing as a void contract. A void agreement never matures into a contract; it is void from the very beginning. A void contract, on the other hand, was valid when it was entered into, but subsequently, because of one reason or the other, became void. A contract cannot be void *ab-initio*; it is only an agreement which can be void *ab-initio*.

iii) Voidable Contract: According to Section 2(i) of the Contract Act, an agreement which is enforceable by law at the option of one or more of the parties thereon, but not at the option of the other or others, is a voidable contract. Thus, a voidable contract is one which can be set aside or repudiated at the option of the aggrieved party. Until it is set aside or avoided by the party entitled to do so, it remains a valid contract. A contract is usually treated as voidable when the consent of a party has not been free i.e., it has been obtained either by coercion, undue influence, misrepresentation or fraud. The contract is voidable at the option of the party whose consent has been so caused. For example, A threatens to shoot B if he does not sell his new scooter to A for Rs. 5,000. B agrees. Here the consent of B has been obtained by coercion. Hence, the contract is voidable at the option of B, the aggrieved party. If, however, B does not exercise his option to set aside the contract within a reasonable time and if in the meanwhile a third party acquires a right in relation to the subject matter for some consideration, the contract cannot be avoided. For example, A obtains a ring by fraud. Here, B's consent is not free and therefore he can cancel this contract. But if, before this option is exercised by B, A sells the ring to C who acquires it after paying the price and in good faith, contract cannot be avoided. You should note that the option to set aside the contract on this ground is not available to the other party. Hence, if the

aggrieved party chooses to retain the contract, it remains enforceable by law. If however, the aggrieved party avoids the contract, the other party is also freed from his obligation to perform the contract and if the party avoiding the contract has received any benefit under the contract, he must restore such benefit to the person from whom it was received (Section 64).

Distinction between Void Agreement and Voidable Contracts

Void Agreement	**Voidable Contract**
1) It is void from the very beginning.	1) It remains valid till it is repudiated by the aggrieved party.
2) A contract is void if any essential element of a valid contract (other than free consent) is missing.	2) A contract is voidable if the consent of a party is not free.
3) It cannot be enforced by any party.	3) If the aggrieved party so decides, the contract may continue to be valid and enforceable.
4) Third party does not acquire any rights.	4) An innocent party in good faith and for consideration acquires good title before the contract is avoided.
5) Lapse of time will not make it a valid contract, it always remains void.	5) If it is not avoided within reasonable time, it may become valid.

Void Agreement	Voidable Contract
6) Question of damages does not arise.	6) The aggrieved party can also claim damages.

iv) Illegal or unlawful contract: The word 'illegal' means contrary to law. You know that contract is an agreement enforceable by law and therefore, it cannot be illegal. It is only the agreement which can be termed as illegal or unlawful. Hence, it is more appropriate to use the term 'illegal agreement' in place of 'illegal contract'.

An 'illegal agreement' is one which has been specifically declared to be unlawful under the provisions of the Contract Act or which goes against the provisions of any other law of the land. Such agreement cannot be enforced by law. For example, A agrees to pay Rs. 50,000 to B if B kills C. This is an illegal agreement because its object is unlawful. Even if B kills C, he cannot claim the agreed amount from A.

The term 'illegal agreement' is wider than the term 'void agreement'. All illegal agreements are void but all void agreements are not necessarily illegal. For example, an agreement to sell a scooter to the minor is void but it is not illegal because the object of this agreement is not unlawful. The other important difference between the illegal and the void agreement relates to their effect on the transactions which are collateral to the main agreement. In case of illegal agreements even the collateral agreements become void. For example, A engages B to shoot C. To pay B, A borrows Rs. 10,000 from D who is aware of the purpose of the loan. In this case, there are two agreements – one between A and B and the other between A and D. Since the

main agreement between A and B is illegal the agreement between A and D which is collateral to the main agreement is also void. D cannot recover the money from A. Take another example. A borrows money from D to pay off his wagering (betting) debts to B. Here the main agreement is void (not illegal). Hence the agreement between A and D being a collateral agreement shall not be affected even though D was aware of the purpose of the loan. From these examples, it should be clear to you that the agreements collateral to the illegal agreements are also void but the transactions collateral to void agreements are not affected in any way, they remain valid.

Difference between Void and Illegal Agreements

Void	**Illegal**
1) All void agreements are not necessarily illegal.	1) All illegal agreements are void.
2) Collateral transactions to a void agreements are not affected i.e., they do not become void.	2) Collateral transactions to an illegal agreements are also affected i.e., they also become void.
3) If a contract becomes void subsequently, the benefit received has to be restored to the other party.	3) The money advanced or thing given cannot be claimed back.

v) Unenforceable contract: It is a contract which is actually valid but cannot be enforced because of some technical defect. This may be due to non-registration of the agreement, non-payment of the requisite stamp fee, etc. Sometimes, the law

requires a particular agreement to be in writing. If such agreement has not been put in writing, it becomes unenforceable. For example, an oral agreement for arbitration are unenforceable because the law requires that an arbitration agreement must be in writing. It is important to note that in most cases, such contracts can be enforced if the technical defect involved is removed. For example, if the document which embodies a contract is under stamped, it will become enforceable if the requisite stamp is affixed.

What are the essentials of a valid contract?

We have learnt that an agreement enforceable by law is a contract. An agreement in order to be enforceable must have certain essential elements. According to **Section 10** –

> 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 hereby expressly declared to be void.

Thus, an agreement becomes a valid contract if it has the following elements.

1. Proper offer and its proper acceptance
2. Intention to create legal relationship
3. Free consent
4. Capacity of parties to contract
5. Lawful consideration
6. Lawful object
7. Agreement not expressly declared void
8. Certainty of meaning

9. Possibility of performance

10. Legal formalities

1) Proper offer and proper acceptance: In order to create a valid contract it is necessary that there must be at least two parties, one making the offer and the other accepting it. The law has prescribed certain rules for making the offer and its acceptance that must be satisfied while entering into an agreement. For example, the offer must be definite and duly communicated to the other party. Similarly, the acceptance must be unconditional and communicated to the offerer in the prescribe mode, and so on. Unless such conditions with regard to the offer and the acceptance are satisfied the agreement does not become enforceable.

2) Intention to create legal relationship: There must be an intention among the parties to create a legal relationship, If an agreement is not capable of creating a legal obligation it is not a contract. In case of social or domestic agreements, generally there is no intention to create legal relationship. For example, in an invitation to dinner there is no intention to create legal relationship and therefore, is not a contract. Similarly, certain agreements between husband and wife do not become contracts because there is no intention to create legal relationship. This point can well be illustrated by the famous case of **Balfour v. Balfour [1919] 2 KB 571 (CA)**. Mr. Balfour had promised to pay £ 30 per month to his wife living in England when she could not accompany him to Ceylon where he was employed. Mr. Balfour failed to pay the promised amount. Mrs. Balfour filed a suit against her husband for breach of this agreement, It was held that she could not recover the amount as it was a social

agreement and the parties never intended to create any legal relations.

In commercial or business transactions the usual presumption is that the parties intend to create legal relations. However, this presumption may be negatived by express terms to the contrary. The case of **Rose & Frank Co. v. J. R. Crompton & Bros. Ltd. [1925] AC 445 (HL)** is relevant here. In this case there was an agreement between Rose & Frank Company and Crompton Brothers Ltd. whereby the former was appointed as selling agents in North America. One of the clauses in the agreement read, "This agreement is not entered into as a formal or legal agreement and shall not be subject to legal jurisdiction in the law courts." It was held, that this agreement was not a legally binding contract as there was no intention to create legal relations.

One must note that whether intention to create legal relationship exists in an agreement or not is a matter for the court to decide which may look at the terms and conditions of the agreement and the circumstances under which the agreement was made.

3) Free consent: For a contract to be valid, it is essential that there must be free and genuine consent of the parties to the contract. They must have made the contract of their own free will and not under any fear or pressure. According to **Section 14**, consent is said to be free when it is not caused by (i) coercion, (ii) undue influence, (iii) fraud, (iv) misrepresentation, or (v) mistake. In case the consent is obtained by any of the first four factors, the contract would be voidable at the option of the aggrieved party. But if the agreement is induced by mutual mistake which is material to the agreement, it would be void.

4) Capacity of parties: The parties to an agreement must be competent to contract i.e., they must be capable of entering into a

contract. If any party to the contract is not competent to contract, the contract is not valid. Now the question arises as to who are competent to contract? Answer to this question is provided by **Section 11** of the Act which says that every person is competent to contract who is of 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.

From this section one will notice that in order to be competent to enter into a contract, the person should be a major (adult), should be of sound mind and he must not be declared disqualified from contracting by any law to which he is subject. Thus, the flaw in capacity may be due to minority, lunacy, idiocy, etc. If a party to a contract suffers from any of these flaws, the agreement, with a few exceptions, is not enforceable at law.

5) Lawful consideration: An agreement must be supported by consideration. Consideration means something in return. It is also defined as the price paid by one party to buy the promise of the other. However, this price need not always be in terms of money. For example, A agrees to sell his book to B for Rs. 20. Here the consideration for A is Rs. 20, and for B it is the book.

The consideration may be an act (doing something) or forbearance (not doing something) or a promise to do or not to do something, the consideration may be past, present or future, consideration must be real i.e., it must have some value in the eyes of law. However, the consideration need not be adequate. For example, A sells his car worth Rs. 50,000 to B for Rs. 10,000 only. This is a valid promise provided the consent of A is free.

For a contract to be valid, the consideration should also be lawful. The consideration is considered lawful unless it is forbidden by law, or is fraudulent, or involves or implies injury

to the person or property of another; or is immoral, or is opposed to public policy (Section 23).

6) Lawful object: The object of an agreement must be lawful. An agreement made for any act which is prohibited by law will not be valid. For example, if A rents out a house for use as a gambling den, the agreement is void because the object of the agreement is unlawful. If the object is unlawful for any of the reasons mentioned in **Section 23**, the agreement shall be void. Thus, the consideration as well as the object of the agreement should be lawful.

7) Agreement not expressly declared void: The agreement must not have been expressly declared void under Contract Act. **Sections 24 to 30** specify certain types of agreements which have been expressly declared void. They are agreement in restraint of marriage, agreement in restraint of legal proceedings, agreement in restraint of trade and agreement by way of wager.

For example, A agreed to pay Rs. 1,000 to B if he (B) does not marry throughout his life. B promised not to marry at all. This agreement shall not be valid because it is in restraint of marriage which has been expressly declared void under Section 26.

One should note that if an agreement possesses all other essential elements of a valid contract but is belongs to the category of such agreements that have been expressly declared void by the Contract Act, no power on earth can make it a valid contract.

8) Certainty of meaning: Section 29 of the Contract Act provides that agreements, the meaning of which is not certain or capable of being made certain, are void. Thus, to make a valid contract it is absolutely essential that its terms must be clear and not vague or uncertain. For example, A agreed to sell 100 tonnes

of oil to B. Here it is not clear what kind of oil is intended to be sold. Therefore, this agreement is not valid on the ground of uncertainty.

If, however, the meaning of the agreement could be made certain from the circumstances of the case, it will be treated as a valid contract. In the example given above if we know that A and B are dealers in mustard oil only, then the agreement shall be enforceable because the meaning of the agreement could be easily ascertained from the circumstances of the case.

9) Possibility of performance: The terms of the agreement must also be such as are capable of performance. An agreement to do an act impossible in itself is void. (**Section 56**). If the act is impossible of performance, physically or legally, the agreement cannot be enforced by law. The reasoning is very simple. We make an agreement with a view to perform it and if the performance is not possible, what is the fun of making such agreements? For example, A promises to B that he will enclose some area between two parallel lines or that he will run at a speed of 200 kms. per hour or that he will bring gold from the sun. All these acts are such which are impossible of performance and therefore the agreement is not treated as valid.

10) Legal formalities: We have learnt that an oral agreement is as good as is a written agreement. The Contract Act does not require that a contract must be in writing to be valid. But, in some cases the Act has specified that the agreement must be made in writing. For example, a promise to pay a time barred debt must be in writing and an agreement for a sale of immovable property must be in writing and registered under the Transfer of Property Act, 1882. In such a situation, the agreement must comply with the necessary formalities as to writing,

registration, etc. If these legal formalities are not carried out, then the contract is not enforceable by law.

After discussing the essential elements of a valid contract, it should now be clear to you that all these elements must be present in an agreement so that it becomes a valid contract. If any one of them is missing or absent, the agreement will not be enforceable by law.