# Directorate of Distance Education
## Centre for Distance and Online Education (CDOE)
# NALSAR University of Law, Hyderabad

**Reading Material**

## ONE YEAR ADVANCED DIPLOMA IN DRAFTING, NEGOTIATION AND ENFORCEMENT OF CONTRACTS

# 1.1 GENERAL PRINCIPLES OF LAW OF CONTRACTS

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## MODULE I

# GENERAL INTRODUCTION AND FORMATION OF CONTRACT

### HISTORY AND NATURE OF CONTRACTUAL OBLIGATION

### COMMON LAW HISTORY

The Common Law system which evolved from the Court of the King, had no intention initially to protect private agreements of people, although business would happen through verbal and written agreements, both formal and informal.[1] The early common law realm viewed the study of obligations not as a study of general principles of contract, but as the law of forms of actions.[2] Thus, courts administered by the Church, the guilds, the markets and even the ports, all understood contractual obligations in their commercial contexts.[3] The forms of recourse therefore for any breach of obligations or for seeking enforcement thus, were through various writs with their own formal and substantive requirements.

### COVENANT, DAMAGES & BONDS

There was an obvious need to ensure that important contracts would be performed. Contracts of great commercial importance, therefore, began to be authorised and authenticated by the Royal Seal, and thus began to be termed “Agreements under the Seal”.[4] This Royal Seal would ease performance, and allowed the realm of such documents (formal contracts) to occupy two broad areas – performance and breach. Thus, the multiple writs in multiple contexts could be replaced by two actions – actions which were trying to ensure that a contract was specifically performed and actions that would attempt to correct a wrong caused by breaking such a contract. These actions that sought to perform the agreements came to be called “covenants” and the actions for breaking the promise made in the covenant were actions for “damages”.

However, the covenants and their breach were restricted only to Agreements under the Seal.[5] Further, the citizens, for some reasons found using this new instrument difficult to use. It is

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[1] Glanvill, X:18.
[2] Janet Anne, O'Sullivan, and Jonathan Hilliard. *The Law of Contract*. Oxford University Press, 2011, pp. 2.
[3] Fifoot, Cecil Herbert Stuart. *History and sources of the common law: tort and contract*. Greenwood Pub Group, 1949.
[4] *Ibid.*
[5] Cheshire, pp.4.

noted that people began to use “bonds” instead of specific performance covenants. Bonds were essentially agreements where people promised each other to pay a penal sum (now called damages) unless they performed their obligations under the covenant. As a leading commentator illustrates:

*“Thus if C wished to lend D £100, D would execute a bond binding himself to pay C £200 on a certain day; the bond would have a condition that it became void (a condition of defeasance) if £100 was paid before the day, and D would hand over this bond as he received the loan of £100.*”[6]

Thus, the obligation of a contract was like that of a tort – If one committed a negligent act, one had to pay damages. Similarly, if one did not perform his covenant, one had to pay damages.[7] Justice Holmes expounds that this may be the most basic conception of a contract

– “*If you commit a contract you are liable to pay damages, unless something happens, i.e., performance, over which you may or may not have control.*”[8]

**ASSUMPSIT**

The instrument to recover the damages that were caused due to breach of an undertaking or an obligation was termed an assumpsit. Cheshire traces the history of this obligation back to the cases in *Pickering v Throughwood*[9] and *Slade's case*[10] where the Courts took a decision which had several technical implications such as moving away from deeds and instruments like the debt *sur contract*, but had one large principle implication – that an instrument could be used to protect not just the damage caused due to non-performance of contract, but also that there could be a passive transmission of the obligation to perform the contract.

Thus, in *Pinchon's case*[11], where there was a liability to pay debts, such a liability passed on to the executors of the debtors and the obligation was enforceable through an assumpsit. This laid the foundation of the simple contract as we understand. However, the assumpsit would have to undergo two major changes before assuming the form of the modern bilateral executory contract:

i. A shift of emphasis from the failure to perform a promise, as opposed to performing an actual, physical obligation

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[6] Cheshire, pp.3.
[7] Cheshire, pp.5.
[8] Holmes, Oliver Wendell. *The Common Law*. Harvard University Press, 2009, Vol. I, pp.177.
[9] *Pickering* v. *Thorough-good* (1533) B.M. MS.Harg. 388, f. 67v, 74 L.Q.R.
[10] *Slade's case* (1598) 4 Co Rep 92b, 76 ER 1074 (1602).
[11] *Pinchon's Case* (M.1611) 9 Rep. 86

ii. A nomenclature of breach or non-performance provided to the fact of going back on one's promise, with no other obligations being impugned or even conceived.

**NATURE: BILATERAL EXECUTORY CONTRACT**

While some authors may articulate several of the aforementioned instruments as contracts existing in ancient times, it must be noted that they could be conceptual pre-cursors to the current form of the contract – an instrument protecting the mutual exchange of the promises.

Law of contracts is a product of modern society. Pre-modern societies had some mechanisms to enforce promises but a pure bilateral executory contract where mere promises are exchanged and nothing else is required to be done in order to generate a binding obligation is a modern idea. The idea that one can be legally liable for making a promise provided it is accepted by the party to whom it is made is not found in pre modern societies.

The modern economy required such an idea because it required making and protecting deferred exchanges. For example A proposes to buy goods from B at a later date. The contract comes into existence the moment A accepts B's proposal and makes both of them legally liable for failure to perform their obligations. The importance of law of contracts is that it made possible to create legal liabilities just by exchange of words- without actually doing any part of the contemplated transaction.

**FORMATION OF AN AGREEMENT**

According to Section 2 (h) a contract is an agreement enforceable by law. Therefore in order to understand a contract we must understand an agreement. An agreement is formed by acceptance of an offer. Therefore first and foremost we shall understand offer and acceptance.

**1. PROPOSAL OR OFFER**

The word 'proposal' is used in the Act in the same sense as the word 'offer' is used in English law. A proposal made by one party, when accepted by another results in the formation of an agreement. It has been held that every transaction, to be recognized as a contract, must in its ultimate analysis, resolve itself into a proposal and its absolute and unconditional acceptance[12]. The making of the proposal is the first step in the process of contract formation. The interpretation clause[13] indicates that an agreement can be reached by the process of offer

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[12] Badri Prasad v. State of Madhya Pradesh, AIR 1970 SC 706 at 712; Suraj Besan and Rice Mills v. Food Corpn. of India, AIR 1988 Del 224 at 227; Deep Chandra v. Ruknuddaula Shamsher Jung Nawab Mohammad Sajjad Ali Khan, AIR 1951 All 93 at 9 (FB); Nirod Chandra Roy v. Kirtya Nanda Singh, AIR 1922 Pat 24; Dagdu v. Bhana, (1904) 28 Bom 420 at 425 (DB); Haji Mohamed Haji Jiva v. E Spinner, (1900) 24 Bom 510 at 523 (DB).

[13] Section 2 of the Indian Contracts Act 1872.

and acceptance. Section 2 (a) of the Indian Contract Act, 1872 (hereinafter, "*the Act*") defines a '*proposal*' as follows –

> *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*.

If we read the above definition in light of Section 2 ( c ) of the Act , it can be seen that the maker of the proposal is called the promisor[14] or "offeror", the person to whom it is made is called the proposee or "offeree", and when such a proposal is accepted, he is referred to as a "promisee".[15] Thus, the meaning of what constitutes a proposal can be deconstructed into two essential parts – a) It is the manifestation of the offeror's willingness to do or to abstain from doing something b) Such expression ought to be made with a view to obtaining the assent of the offeree to the proposed act or abstinence. The offeror therefore manifests or makes known his intention of doing or not doing something, and he does so with the purpose of getting the offeree to assent to it.

### 1.1 TYPES OF CONTRACT

There are two types of contracts: a unilateral contract and a bilateral contract. Unilateral contracts involve only promisor while bilateral contracts involve both a promisor and a promisee. A bilateral agreement consists of an exchange of promises, for example, A makes an offer to B to sell his car for Rs 2 lakh. B accepts to buy the car on sale for the price quoted by A. Whereas in a unilateral contract, the offerer alone makes a promise. The offer is accepted by doing what is set out in the offer. For example, A makes an offer to pay Rs 1000 to anyone who finds his lost pet. The person who finds and returns his lost pet is said to have accepted his offer by way of his 'conduct'. The distinction between a unilateral and bilateral contract becomes crucial while dealing with the following topics – a) advertisements b) revocation of offers c) communication of acceptance.

### 1.2 COMMUNICATION OF OFFER

Section 3 and 4 of the Act deals with communication of proposals, acceptances and revocation of proposals and acceptances. Section 3 specifies what is communication. Section 4 describes when it is completed. The provisions of Section 4 are applied for ascertaining whether a contract has been concluded at all; and whether rights and obligations will arise under it. A proposal is communicated when it comes to the knowledge of the offeree. Unless a proposal is communicated to the person to whom is made, it is not complete and remains inconclusive.[16]Hence, an acceptance without knowledge of the proposal is not an acceptance

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[14] Section 2 (c ) Indian Contracts Act 1872.
[15] *Ibid.*
[16] Baroda Oil Cakes Traders v Parshottam Narayandas Bagulia, AIR 1954 Bom 491.

and does not result into a contract. A proposal by letter is made not at the place where it is posted but where the offer is received or the letter delivered,[17] because a proposal is not complete unless and until it comes to the knowledge of the person to whom it is made.[18]

### 1.3 OFFER TO WHOM – CLASSIFICATION AS REGARDS PERSON(S) TO WHOM MADE

An offer may be addressed to an individual, or to a specified group of persons or to the world at large. The former is called a specific offer, and the latter general offer.

#### 1.3.1 GENERAL OFFER

An offer need not be addressed to a specific set of individuals or an ascertained person. It can be made generally, to the world at large. Merely because the offer is addressed to the world does not mean that the contract is entered into with the world. Only that person who comes forward and acts upon the conditions of the proposal can be said to have a right to enforce the contract. Therefore, for a contract to come into existence, acceptance must be made by an ascertained person, but the same logic does not extend to the making of the proposal.[19] The leading authority on this topic is the Carlill v Carbolic Smoke Ball Co.[20]

> A company offered by advertisement to pay 100 pounds to anyone '*who contracts the increasing epidemic influenza, colds or any disease caused by taking cold, after having used the ball according to printed directions'*. It was added that '*1000 pounds is deposited with the Alliance Bank showing our sincerity in the matter*'. The plaintiff used the smoke balls according to the directions but she nevertheless subsequently suffered from influenza. She was held entitled to recover the promised award.

The above mentioned case is an example of a *unilateral* offer wherein there is no strict requirement of communication of acceptance. Such proposals demand acceptance by performance. The acceptance of the offer takes place when the offeree performs the act in question. ***Section 8***[21] of the Act incorporates this principle. The offer here is said to be *unilateral* because only one party is making a promise.

Two further features of offers to be noted are that the terms of an offer must be clear and that the offer is made with the intention that it should be binding. In connection with the latter

[17] Dhanraj Mills Limited Liability Co. v. Narsingh Prasad Bodona, AIR 1949 Pat 270 (post office is an agent of the sender, not the addressee);

[18] Firm Kanhaya Lal v. Dinesh Chandra, AIR 1959 MP 234; Baroda Oil Cakes Traders v. Parshottam Narayandas Bagulia,(1954) ILR 1137, AIR 1954 Bom 491.

[19] ANSON'S LAW OF CONTRACT, 23RD Edn, 1971 ( Edited by A.G. Guest), p 40

[20] (1893) 1 QB 256 (CA)

[21] "*Section 8 – **Acceptance by performing conditions, or receiving consideration** – Performance of the conditions of a proposal, or the acceptance of any considerations for a reciprocal promise which may be offered with a proposal, is an acceptance of the proposal"*

requirement, a further defence propounded in the ***Carlill*** case was that the advertisement was a 'mere puff' and not intended to form the basis of a binding agreement. Such 'puffs' are very much part of commercial life today, particularly in the advertising industry. Clearly statements that allude to certain soap powders 'washing whiter than white' or certain types of beers working untold miracles are not intended to be taken seriously but to 'puff up' the propensities of the product to induce the all- suffering public to buy. In the ***Carlill*** case the allegation that the offer was a 'mere puff' was rejected on the basis that the advertisement also stated that the defendants had deposited £1,000 with the Alliance Bank 'to show their sincerity'. It was clear in this case that this fact indicated that *they intended* the promise to form the basis of a legal relationship.

### 1.4 OFFERS COMPARED WITH OTHER TYPES OF TRANSACTION

A proposal must be distinguished from mere statement of intention which is not intended to require acceptance. The latter may be merely a statement of intention or an invitation to make offers, or to do business. If it is not intended to be binding, it is an 'invitation to treat.

#### 1.4.1 OFFERS DISTINGUISHED FROM INVITATIONS TO OFFERS

It is important to study the classification between an offer and an invitation to offer for it holds great significance in understanding the exact point at which the contract came to be formed. It has been seen that, according to one definition, an offer is an expression of a willingness to be bound by the terms of the offer should the offer be accepted. Clearly the implication here is that the statement of offer is the final statement of an individual who wishes to be bound by those terms; it is a person's final declaration of their readiness to be bound. This becomes sufficiently clear when one looks at the definition of proposal as found in the Section 2 (a) of the Act, which emphasises on the fulfilment of the two essential parts as noted earlier. Therefore, for a statement to amount to an offer, it must require nothing more to convert it into a promise except acceptance.

It follows that if an individual is not willing to implement the terms of their promise but is merely seeking to initiate negotiations then this cannot amount to an offer, such statements being termed 'invitations to treat'. Certain examples may help in understanding the distinction. Advertisements of goods for sale in newspapers or magazines are not offers.[22] Nor are displays at the shop-window of goods with marked prices,[23]or on the shelves of a self-service shop[24], or an indication of the price of petrol at a petrol pump,[25] or

[22] Partridge v. Crittenden, [1968] 2 All ER 421, [1968] 1 WLR 1204.
[23] Timothy v. Simpson, [1834] 6 C&P 499; Fisher v. Bell, [1960] 3 All ER 731.
[24] Pharmaceutical Society of Great Britian v. Boots Cash Chemists (Southern) Ltd., [1953] 1 QB 410, [1953] 1 All ER 482(CA)
[25] Esso Petroleum Ltd. v. Commissioners of Customs and Excise, [1976] 1 All ER 117, [1976] 1 WLR 1.

advertisements announcing schemes for purchase of land, plot or houses,[26] or special offers in catalogues or brochures[27]. As a general rule, these are not offers but invitations for making offers.

The distinction between an offer and an invitation to treat is not an easy one to make since it very often revolves around that elusive concept of intention. It may be that a statement amounts to an invitation to treat even though the statement is said to make an 'offer' and vice versa. The easiest way of making the distinction is by analysing how the law deals with the problem within certain **stereotypical transactions (ex. Advertisements, Tenders, Display of Goods, Auctions etc)** bearing in mind that the courts will look at the surrounding circumstances and the intention of the parties and will not necessarily have regard to the actual wording of the statement.

### A. Advertisements

In the earlier examples cited above, it was noted as a general rule that advertisements and display of goods are statements in the nature of invitations to treat, rather than proposals as understood under Section 2 (a) of the Act. The decisions in the ***Carlill*** case stand as exceptions to this general rule. In the words of Bowen LJ:

> *It is not like cases in which you offer to negotiate or you issue advertisements that you have got a stock of books to sell, or houses to let, in which case there is no offer to be bound by any contract. Such advertisements are offers to negotiate – offers to receive offers – offers to chaffer.*

### Display of Goods for Sale

By far the most common example of the occurrence of invitations to treat is in the case of goods displayed either in shop windows or within a shop itself. The issue that arises here is that if the display of the goods in question amounts to an offer then a customer may enter the shop and purport to accept that offer, thus creating a binding obligation on the shopkeeper to sell the goods at the stated price. If, however, the display of goods only amounts to an invitation to treat then it is the customer who makes the offer to the shopkeeper, who is free to accept or reject that offer as they wish.

The general rule as regards goods displayed in shop windows is well illustrated in the case of ***Fisher* v *Bell***[28], where a price-marked flick-knife was displayed for sale in a shop window. The seller was prosecuted under the now repealed Restriction of Offensive Weapons Act 1961, which made it an offence to offer to sell such items, and was acquitted. Lord Parker stated:

[26] Adikanda Biswal v. Bhubaneswar Development Authority, AIR 2006 Ori 36.
[27] Thornton v. Shoe Lane Parking Ltd., [1971] 2 QB 163, [1971] 1 All ER 686(CA)
[28] [1961] 1 QB 394

*It is clear according to the ordinary law of contract that the display of an article with a price on it in a shop window is merely an invitation to treat. It is in no sense an offer for sale, the acceptance of which constitutes a contract.*

### B. Tenders

A request or call for tenders is normally an invitation to treat. A request for tenders for the supply of goods or for execution of works is not an offer. It is a mere attempt to ascertain whether an offer can be obtained within such a margin as the employer is willing to adopt; it is an offer to negotiate, an offer to receive offers,[29]even where the reserve price is fixed.[30] The actual tender, given in response to the call for tenders, is the offer, and if accepted, it becomes a binding contract.It was held in ***Spencer* v *Harding***[31] that a statement that goods are to be sold by tender is not normally an offer, and that thus no obligation is created to sell to the person making the highest tender. Similarly, an invitation for tenders for the supply of goods or services is not generally an offer but an invitation for offers to be submitted which can be accepted or rejected as the case may be.

But if the person inviting the tender states in the invitation that the highest offer to buy will be accepted, the invitation of tender may be regarded as an offer or an invitation to submit offers with an undertaking to accept the highest offer and the contract will be concluded as soon as the highest offer to buy is communicated.[32]Where the tenders are invited by the government or public bodies and authorities, obligations in the conduct of the procedures are imposed on the persons inviting them in the interest of fairness, preventing discrimination and natural justice, and their decisions may be subject to judicial review.[33]

## 1.5 SUMMING UP, A VALID OFFER:

A) must be communicated, so that the offeree may accept or reject it;
B) may be communicated in writing, orally, or by conduct (there is no general requirement that an agreement must be in writing. Important exceptions include contracts relating to interests in land (See rules governing specific transfers like Sale, mortgage under the Transfer of Property Act)
C) may be made to a particular person, to a group of persons, or to the whole world.
D) must be definite in substance
E) must be distinguished from an invitation to treat.

An offer may be communicated by any act or omission by which the offeror intends to communicate or has the effect of communicating it (S. 3). Its communication is complete when it comes to the knowledge of the offeree (S. 4). It can be revoked until the offeree posts

[29] SP Consolidated Engineering Co. (P) Ltd. v. Union of India, AIR 1966 Cal 259.
[30] Anil Kumar Srivastava v. State of Uttar Pradesh, AIR 2004 SC 4299.
[31] (1870) LR 5 CP 561
[32] Harvela Investments Ltd. v. Royal Trust Co. of Canada (CI) Ltd., [1986] AC 207 at 224, [1985] 2 All ER 966.
[33] Tata Cellular v. Union of India, AIR 1996 SC 11, (1994) 6 SCC 651

his acceptance (S. 5). It stands revoked by notice of revocation or by lapse of time, failure by the acceptor to accept the condition precedent to acceptance, and death or insanity of the offeror (S. 6). It may prescribe the manner of acceptance (S. 7). It may be express or implied (S. 9).

## 2. TERMINATION OF OFFER

An offer may be terminated by one of three ways – a) Revocation of Offer b) Lapse of Offer c) Rejection of Offer.

### A. Revocation (Termination by offeror)

Section 5 makes it clear that "*a proposal may be revoked at any time before the communication of its acceptance is complete as against the proposer, but not afterwards*." As against the proposer, the communication of acceptance is complete "*when it is put in a course of transmission to him, so as to be out of the power of acceptor*."[34] By logical sequence, for a communication of revocation to be effective, it must reach the offeree before he conveys his acceptance. person who has made an offer is considered as continuously making it until he has brought to the knowledge of the person to whom it was made that it is withdrawn. In other words, the revocation of a proposal is effectual if it reaches before the dispatch of the acceptance; the time of dispatching the revocation is immaterial. A revocation becomes effective only when it reaches the offeree. The rule that the revocation of proposal is effective when it reaches the offeree and not when it is posted or put into a course of transmission, applies to revocations sent through post or telegram or any other method.

In *Byrne v van Tienhoven*[35], the withdrawal of an offer sent by telegram was held to be communicated only when the telegram was received. It is also not necessary that the communication of revocation be made by the offeror himself; communication by third party will suffice. In *Dickinson v Dodds*[36], the plaintiff was told by a neighbour that a property which had been offered to him had been sold to a third party. It was held therein that the offer had been validly revoked.

### B. Lapse ( Termination by operation of law)

An offer may lapse and thus be incapable of being accepted because of passage of time. If the offer sets a certain deadline before which acceptance has to be made, and such acceptance is not received before the end of the deadline, the offer lapses. If no time is stipulated, then offer is said to lapse after a reasonable time. Offers are deemed to lapse on account of death of the offeror if the offer was in the nature of personal service or on account of death of

[34] Section 4 of the Indian Contracts Act, 1872
[35] (1880) 5 CPD 344, [1874-80] All ER Rep Ext 1432
[36] (1876) 2 Ch D 463;

offeree. Where the offer is subject to a condition precedent, non-fulfilment of such a condition results in lapse of offer.

### C. Rejection (Termination by the offerree)

A rejection may be express or implied. A counter offer is an example of an implied rejection. Traditionally, an acceptance must be a mirror image of the offer. If any alteration is made or anything added, then this will be a counter offer, and will terminate the offer. In *Hyde v Wrench*[37], the defendant offered to sell a farm for £1,000. The plaintiff said he would give £950 for it. Held—this was a counter offer which terminated the original offer which was therefore no longer open for acceptance. In *Brogden v Metropolitan Railway*[38] , the defendant sent to the plaintiff for signature a written agreement which they had negotiated. The plaintiff signed the agreement and entered in the name of an arbitrator on a space which had been left empty for this purpose. Held—the returned document was not an acceptance but a counter offer. It is important to remember that a request for further information cannot be said to amount to a counter offer. In *Stevenson v McLean*[39], the defendant offered to sell to the plaintiff iron at 40s a ton. The plaintiff telegraphed to inquire whether he could pay by instalments. Held—this was a mere inquiry for information, not a counter offer, and so the original offer was not rejected.

## 3. ACCEPTANCE

Treitel defines **acceptance** as 'a final unqualified expression of assent to all the terms of an offer'. The objective test, which was examined above in regard to offers, applies in the same manner to acceptance. In other words, evidence must be produced from which the courts can adduce an intention by the offeree to accept the offer communicated to them.

Section 2(b)[40] of the Act defines acceptance as assent to the proposal by the person to whom the proposal has been made. An unqualified, unconditional acceptance of the offer creates a contract when communicated to the offeror (see Section 7).

Under Section 3 an acceptance may be communicated by any act or omission by which the offeree intends to communicate or has the effect of communicating it. Under Section 4, its communication is complete as against the proposer when it is put into a course of transmission to him so as to be out of the reach of the acceptor, and as against the acceptor, when it reaches the proposer. Section 5 provides for revocation of acceptance. Under Section

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[37] [1974] 3 All ER 88 at p.100.
[38] (1880) 5 CPD 344, [1874-80] All ER Rep Ext 1432.
[39] [1880] 5 QBD 346.
[40] Section 2 b) - *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*.

7, acceptance must be absolute and unconditional, and of all the terms of the proposal, and in the manner, if any, prescribed by the proposal. Acceptance may be express or implied.[41]

### 3.1 ACCEPTANCE – KNOWLEDGE OF OFFER

There cannot be an acceptance of a proposal without the knowledge of the same. Thus in ***Lalman Shukla v. Gauri Dutt***,[42] the plaintiff was in the defendant's service as a *munim*. The defendant's nephew absconded, and the plaintiff volunteered his services to search for the missing boy. In his absence, the defendant issued handbills offering a reward of Rs. 501 to anyone who might find the boy. The plaintiff traced him and claimed the reward. The plaintiff did not know the handbills when he found the boy. It was held that the plaintiff was not entitled to the reward. It has been held that contractual obligations do not arise if services are rendered which in fact fulfil the terms of an offer, but are performed in ignorance of the fact that the offer exists. There cannot be assent without knowledge of the offer and reliance upon it.[43]

### 3.2 MODE OF COMMUNICATION

The general rule as regards mode of communication of acceptance can be found in Section 7 of the Act. It requires communication to be made in some '*usual and reasonable manner'* unless the proposal prescribed a specific mode to be complied with. If the mode preferred by the proposer has not been complied with by the acceptor, the proposer may, within a reasonable time after the acceptance is communicated to him, insist upon proper compliance with the mode preferred else he is deemed to have acknowledged the acceptance. Therefore, mere departure from mode prescribed by the proposer does not by itself invalidate the acceptance. The burden to avoid acceptance has been placed on the proposer within reasonable time and if he fails to do so, the contract is clinched on him and he becomes bound by the acceptance. The Indian position on this topic stands at variance with the English law, and hence English law must not be consulted on this aspect.

Where no mode is prescribed, an acceptance is not complete unless and until it is communicated to the proposer in some perceptible form which may be by speech, writing or other acts or omissions. The reason is that the proposer is entitled to know whether a contract has been concluded by acceptance, and it would be unfair to hold him bound by an acceptance of which he has no knowledge.

### 3.3 COMMUNICATION OF ACCEPTANCE

The general rule is that an acceptance must be communicated to the offeror himself. This is indicated by the use of the word 'signifies' in section 2(b). A communication to any other

[41] Section 9 of the Indian Contracts Act,1872
[42] (1913) 11 All LJ 489; Fitch v. Snedaker, (1868) 38 NY 248; Crown v. Evan Clarke, (1927) 40 CLR 227.
[43] Crown v. Evan Clarke, (1927) 40 CLR 227 (High Court of Australia).

person is as ineffectual as if no communication has been made.[44] Acceptance of the offer may be communicated either orally or in writing, or inferred from conduct. Mere mental resolve,[45] or written acceptance on a piece of paper and keeping it,[46] or inter-departmental communication proposing acceptance,[47] or mere resolution of acceptance by a company[48] would not result into a contract, unless these are communicated to the proposer. An acceptance would be effective without communication if the offeror has, expressly or impliedly, waived the requirement of communication of acceptance. Performance of the condition of an offer would amount to acceptance.[49]

The act of acceptance becomes effective so as to bind the acceptor completely when the acceptance comes to the knowledge of the proposer. In the case of a contract consisting of mutual promises, the proposer must receive intimation that the offeree has accepted his offer and has signified his willingness to perform his promise. Upon acceptance, the proposal becomes a promise. A liability under contract cannot arise unless the contract has been concluded. Whether a contract has been concluded or not is a question of fact to be determined in each case by considering all relevant facts and circumstances. A contract happens when the acceptance is signified, the question of payment of promised price is a question not of formation, but of performance.[50]

### 3.4 WHEN A CONTRACT IS CONCLUDED

When the parties are separated by distance (with no access to instantaneous mode of communication) and are contracting through postal communication, the question arises as to when the contract is said to be concluded. Does the contract arise when the acceptance is posted or when it is received?

**The postal rule**: The rule that acceptance must be communicated to the offeror is overturned when acceptance is sent via the post since here the **rule is that acceptance takes place as soon as the letter is validly posted.** In other words, acceptance takes place **when a letter is posted, not when it is received.**[51] Very simply, this rule suggests that when the proposer and acceptor are at a distance, and the acceptor posts his acceptance, it is deemed to be communicated to the proposer. This postal rule favours the offerree. While the proposer is ignorant about the actions of the offeree, the offeree is fully aware of the position of acceptance. The proposer bears the risk of the acceptance being lost or delayed in transmit.

[44] Felthouse v Bindley (1863) 7 LT 835
[45] T Linga Gowder v. State of Madras, AIR 1971 Mad 28.
[46] Brogden v. Metropolitan Railway Co., (1877) 2 App Cas 666;
[47] Gajendra Singh v. Nagarpalika Nigam Gwalior, AIR 1996 MP 10;
[48] Best's case, (1865) 2 De GJ & Sm 650, 34 LJ Ch 523
[49] Section 8 of the Indian Contracts Act, 1872
[50] Lucknow Development Authority v. MK Gupta, AIR 1994 SC 787.
[51] Note the difference between acceptance and revocation of an offer by post – Acceptance of an offer takes place when letter is posted while revocation of an offer takes place when the letter is received.

The rule is justified on the ground that the proposer can avoid this risk and protect himself by requiring actual notification of the acceptance. The rule also limits the power of the proposer to revoke the acceptance by disabling him from revoking the proposal after the offeree has acted upon the offer.

The justification for the postal rule of communication is that the offeree would not know whether his acceptance has reached the offerer and he is legally bound. This would require the offerer to send an acknowledgement to the offeree that he has received the acceptance but he would not know whether the acknowledgement has reached the offeree? This process would continue forever and a contract through postal mode can never be entered into.

The rule was laid down in *Adams v Lindsell*[52]. The defendants wrote to the plaintiffs offering to sell them a quantity of wool and requiring acceptance by post. The plaintiffs immediately posted an acceptance on 5 December. It was held—the contract was completed on 5 December. Acceptance is effective on posting, even when the letter is lost in the post. In *Household Fire Insurance Co Ltd v Grant*[53] (1879), the defendant offered to buy shares in the plaintiff's company. A letter of allotment was posted to the defendant, but it never reached him. It was held—the contract was completed when the letter was posted

1. **Unilateral Contracts** : In unilateral contracts, where only one party makes a promise, acceptance take place by conduct. The acceptance of the offer in such cases takes place when the offeree performs the act in question. ***Section 8*** of the Act incorporates this principle as noted earlier.
2. **Silence as communication** - An offeror may not stipulate that silence of the offeree is to amount to acceptance. In *Felthouse v Bindley* the plaintiff wrote to his nephew offering to buy a horse, and adding, '*If I hear no more ... I will take it that the horse is mine'*. The nephew did not reply to this letter. It was held that no contract had been concluded. Acceptance had not been communicated to the offerer. It has been suggested that **this does not mean that silence can never amount to acceptance**; for example, if, in Felthouse v Bindley[54], the offeree had relied on the offeror's statement that he need not communicate his acceptance, and wished to claim acceptance on that basis, the court could decide that the need for acceptance had been waived by the offerer

### 3.5 INSTANTANEOUS MODE OF COMMUNICATION: TELEPHONE, TELEX ETC.

The postal rule is an exception to the general principle requiring the acceptance to be communicated to the offerer. Modern technology, however, provides other methods of communication which are instantaneous in their operation to the extent that the parties are, as it were, in each other's presence. Such was the reasoning in ***Entores* v *Miles Far East***

[52] (1818) 1 B & Ald 681
[53] (1863) 7 LT 835
[54] *Ibid*

***Corporation***. Such a contract is concluded when the acceptance reaches the proposer. Where the communication is made by an 'instantaneous' mode, namely, by telephone or telex, the sender is able to know immediately whether his communication has reached, and has an opportunity of making a proper communication. In the *Entores*[55] case, the offer was made by telex in Amsterdam and notification of the acceptance was received in London also by telex; it was held that in the case of oral communication or by telex or telephone, an acceptance is communicated when it is actually received by the proposer and the contract resulting thereupon was held to be made in London. In the US and Canada, the contract in such cases is made where the acceptance is spoken. However, the rule in the Entores case has been accepted in India as applicable to acceptance by telephone,[56] and by telex.[57]

**Place of Formation of Contract and Jurisdiction of Courts**

Determining where the contract was made, i.e. the place of formation of the contract, is crucial because it aids in understanding when the contract was made, the statue that would govern the agreement in cases of cross-border contracts and which court would have jurisdiction over that particular contract.

As per Section 2(b) of the Indian Contracts Act, 1872[58] an 'offer' becomes a 'contract' once the acceptance is communicated. Consequently, the question of *where* the contract was made will then turn on when the acceptance was communicated or deemed to be communicated.

As a general rule, a contract is formed at the place where the acceptance is received, and this is the case for parties that can communicate instantaneously.[59] This rule was expounded upon in *Entores Ltd. v. Far East Corporation,*[60] . As discussed above in this case an offer was made by a party in London to a party in the Netherlands by telex. The offer was also duly accepted via telex. Since telex was an instantaneous mode of communication, much like the telephone, the court held that the contract only came into existence when the receipt of communication was notified in London. The place of formation of the contract was thus London. This principle was accepted by the India Supreme Court in the case of *Bhagwadas Kedia v. Girdharilal Parshottamdas & Co.*[61] In this case, the plaintiffs had made an offer for the supply of goods from Ahmedabad to the defendants in Khamgaon. The defendants had duly accepted the offer via the telephone. The court decided that rule in Section 4 should be confined to post, as the Act could not have possibly envisaged the use of modern technology

55 Entores Ltd. v. Miles Far East Corpn., [1955] 2 QB 327 AT 333, [1955] 2 All ER 493.
56 Bhagwandas Goverdhandas Kedia v. Girdharlal Parshottamdas, AIR 1966 SC 543, [1966] 1 SCR 656, (per majority); Firm Kanhaya Lal v. Dinesh Chandra, AIR 1959 MP 234.
57 Triveni Oil Field Service Ltd. v. Oil and Natural Gas Commission, AIR 2006 Del 331.
58 Hereinafter, the "Act".
59 *Entores Ltd. v. Miles Far East Corporation*, (1955) 2 QB 327.
60 *Supra* note 2.
61 AIR 1966 SC 543.

(like the telephone) which had not been invented then. Thus, the contract was only formed when and where the acceptance reached the offeror, i.e. in Ahmedabad.

The situation, however, gets trickier when the parties are at a distance and have to communicate using the postal method or any non-instantaneous mode of communication. Section 4 of the Act provides for the "*postal rule.*"[62] This rule provides that a binding contract is formed on the date the letter of acceptance is posted in due course. This is also the case when non-instantaneous modes of communication are utilized the parties. In these cases, the contract is considered to be validly concluded at the place where the proposal is accepted, and from where the communication of acceptance is dispatched. The court at that place would have jurisdiction to entertain a cause of action under the contract.[63] Similarly, when the parties communicate using modes like fax or other modes of instantaneous communication, the general rule applies. That is, that a binding contract is formed when and where the acceptance is received by the offeror.

To determine whether a suit on the contract is within the jurisdiction of a court will necessarily require looking at where it was formed in the light of Section 4 of the Act.[64] The place where the contract is concluded, being a part of the 'cause of action' determines the jurisdiction of the court in cases concerning a contract.[65] Section 20 of the Code of Civil Procedure provides that any suit may be filed at the plaintiff's option in the following courts where-

a. *"the defendant, or each of the defendants where there are more than one, at the time of the commencement of the suit, actually and voluntarily resides, or carries on business, or personally works for gain; or*
b. *any of the defendants, where there are more than one, at the time of the commencement of the suit actually and voluntarily resides, or carries on business, or personally works for gain, provided that in such case either the leave of the Court is given, or the defendants who do not reside, or carry on business, or personally work for gain, as aforesaid, acquiesce in such institution; or*
c. *the cause of action, wholly or in part, arises."*

The first two indicate that the suit can be filed where the defendant either resides, carries on business or personally works for gain. The third one encompasses places where the 'cause of action arises'.

[62] *Ram Das Chakarbarti v. Cotton Ginning Co Ltd.*, ILR (1887) 9 All 366.
[63] *ONGC v. Modern Construction & Co.*, (1997) 3 Guj LR 1855; *Progressive Constructions Ltd. v. Bharat Hydro Power Corpn Ltd.*, AIR 1996 Del 92.
[64] *Baroda Oil Cakes Traders v. Parshottam Narayandas Bagulia,* AIR 1954 Bom 491.
[65] Section 20, Civil Procedure Code, 1908.

“*This includes the place where the contract was made, the place where the contract as to be performed or performance thereof was to be completed or the place where in performance of the contract any money to which the suit relates was expressly or impliedly payable*.”[66]

This is an inclusive and not an exhaustive conception of where the ‘cause of action’ can be said to arise.[67] In any case, the question of *where* the contract was formed continues to form an integral part of the ‘cause of action’ of a suit, and thus a plaintiff can file a suit in a court that has jurisdiction over the place where the contract was concluded.

An interesting situation arises in cases of e-contracts, or contracts that are formed via exchange of emails. This question arose in the case of *Trimex International Fze Ltd, Dubai v. Vedanta Aluminium Ltd.*[68] In this case, the petitioner and the respondent were involved in an exchange of e-mails, in the course of which a contract was proposed and accepted on 16.10.2007. The respondent breached its obligations under the agreement, and the petitioner filed for damages. The respondent contended that no contract existed between the parties.
The court rejected this contention. It interpreted the e-mails exchanged to be sufficient to form a valid contract and proceeded to adjudge when and where the contract could be considered to be formed. The court declared-

“*10. The acceptance conveyed by the respondent, which has already been extracted supra, satisfies the requirements of Section 4 of the Indian Contract Act 1872. Section 4 reads as under:*

*"Communication when complete-The communication of an acceptance is complete.... as against the acceptor, when it comes to the knowledge of the proposer."*
*As rightly pointed out by the learned senior counsel for the petitioner, when Mr. Swaminathan of Trimex opened the email of Mr. Swayam Mishra of Vedanta at 3:06 PM on 16.10.2007, it came to his knowledge that an irrevocable contract was concluded*.”

The court thus accepted the application of the general rule to communication via e-mails.
Section 4 should be read with Section 13[69] of the Information Technology Act, 2000. When read together, the following propositions can be envisaged-

[66] *Supra* note 7.
[67] *Supra* note 7.
[68] (2010) 3 SCC 1.
[69] 13. Time and place of despatch and receipt of electronic record.—(1) Save as otherwise agreed to between the originator and the addressee, the despatch of an electronic record occurs when it enters a computer resource outside the control of the originator.
(2) Save as otherwise agreed between the originator and the addressee, the time of receipt of an electronic record shall be determined as follows, namely:—
(a) if the addressee has designated a computer resource for the purpose of receiving electronic records,—
(i) receipt occurs at the time when the electronic record enters the designated computer

(a) The communication of an offer becomes complete at the time when the electronic offer enters any information system designated by the offeree for the purpose, or, if no system is designated for the purpose, but the electronic offer is sent to some other information system, when the offeree retrieves such electronic record.

(b) The communication of an acceptance is complete when the electronic acceptance enters any information system designated by the offeror for the purpose, or, if no system is designated for the purpose, when the acceptance enters the information system of the offeror, or, if any information system has been designated, but the electronic record is sent to some other information system, when the offeror retrieves such electronic acceptance.

Consequently, the acceptance is considered communicated not when the e-mail is put into transmission, but when the same is received by the offeror.

This was also discussed by the Allahabad High Court in the case *of P.R. Transport Agency vs. Union of India.*[70] In this case, the petitioner and respondent had sent their offer and acceptance via e-mail to one another. Subsequently, the respondent sent another mail cancelling the decided e-auction due to certain unavoidable reasons. The petitioner challenged this in the Allahabad High Court, and the respondent argued that the court had no territorial jurisdiction to entertain the petition as no part of the cause of action arose in Uttar Pradesh. The principle place of business of the petitioner was in Chandauli (a district in Uttar Pradesh) and it also conducted business at Varanasi. The court interpreted Section 13(3) of the Information Technology Act, 2000 and adjudged that the acceptance of the offer by e-mail would be deemed to have been received at either of its two offices. It further stated-

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resource; or
(ii) if the electronic record is sent to a computer resource of the addressee that is not the designated computer resource, receipt occurs at the time when the electronic record is retrieved by the addressee;
(b) if the addressee has not designated a computer resource along with specified timings, if any, receipt occurs when the electronic record enters the computer resource of the addressee.
(3) Save as otherwise agreed to between the originator and the addressee, an electronic record is deemed to be dispatched at the place where the originator has his place of business, and is deemed to be received at the place where the addressee has his place of business.
(4) The provisions of sub-section (2) shall apply notwithstanding that the place where the computer resource is located may be different from the place where the electronic record is deemed to have been received under sub-section (3).
(5) For the purposes of this section,–
(a) if the originator or the addressee has more than one place of business, the principal place of business, shall be the place of business;
(b) if the originator or the addressee does not have a place of business, his usual place of residence shall be deemed to be the place of business;
(c) ―usual place of residence‖, in relation to a body corporate, means the place where it is registered.

[70] AIR 2006 All 23.

"…*the acceptance having been received by the petitioner at Chandauli/Varanasi, the contract became complete by receipt of such acceptance at Varanasi/Chandauli, both of which places are within the territorial jurisdiction of this Court. Therefore, a part of the cause of action having arisen in U.P., this Court has territorial jurisdiction to entertain the writ petition*."

Thus, it also applied the general rule and not the postal rule when e-contracts were considered.

# MODULE II

# CONSIDERATION

## 1. CONSIDERATION

The relevant sections for consideration in the Indian Contract Act, 1872 (hereunder ICA) are sections 2(d), 10, 23-25 and 63.

As a concept, consideration brings out the idea of reciprocity as the distinguishing mark; it is the gratuitous promise that is unenforceable.[71] There are two approaches to understand consideration:

a) The traditional approach is to identify consideration as a detriment to the promisee and/or a benefit to the promisor[72]
b) Second is to look at consideration as the price of the promise made.[73]

The second view has been preferred by authors such as Cheshire and Fiffot.

The ICA defines consideration, s-2(d) as :

> *"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 act or abstinence or promise is** called a consideration for the promise;"*[74]

Thus, as we notice, there are 3 parts to consideration, each of which must be satisfied for a valid consideration to arise. i.e.
Consideration must:

1. Be at the desire of the promisor,
2. May be performed by promisee or any other person,
3. Includes an act/ abstinence which can be of three kinds:
    a) has done or abstained from doing an act or abstinence,
    b) does or abstains from doing an act or abstinence,
    c) promises to do or to abstains from doingan act or abstinence.

[71] There being certain exceptions which will be noticed later.
[72] Curie v Misa (1875) LR 10 Ex 153, 162.
[73] Dunlop Pneumatic Tyre Co. Ltd v Selfridge & Co. Ltd [1915] AC 847.
[74] Section 2(d) Contract Act.

We will now look at the constituent requirements of consideration and the interpretation given to each part by the Courts.

## 2. CONSIDERATION MUST BE AT THE DESIRE OF THE PROMISOR

In Durga Prasad v Baldeo[75], on the collectors orders, 'A' built certain shops. The shops were later occupied by 'B'. B, in lieu of cost incurred by A, promised to pay 'A', a certain amount 'Rs. X'.

Later, B refused to pay A and A sued B.

A's attempt at recovering any amount failed on the ground, that though A certainly and undoubtedly incurred certain costs. In order for a contract to arise between A and B, the consideration for the contract between A and B, must be an act/abstinence **at the desire of the promisor (**i.e. B in the present case). In this case, though, by the act, practically viewed has benefitted B, it was work done under the order of the collector, thus, A was bound to do the work. There was no contract between A and B in lieu of the work done, but merely an assurance by B to pay A gratuitously.

One may try to argue that there was an agreement between A and B in the present case, however, it must be noted that there is a difference between an agreement in layman's understanding of the word agreement and agreement as understood under the ICA.
The ICA draws a distinction between agreements not enforceable by law[76] and an agreement enforceable by law is a contract.[77] Section 2(h)[78] must be read with Section 10, which states:[79]

> *"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 1[India] and not hereby expressly repealed by which any contract is required to be made in writing1 or in the presence of witnesses, or any law relating to the registration of documents."*

The ICA, thus makes only those agreements which have a lawful consideration enforceable by law.

[75]***Durga Prasad v. Baldeo***(1881)ILR3ALL221.
[76]Section 2(g) Indian Contract Act.
[77]Section 2(h) Indian Contract Act.
[78]Supra.
[79]Section 10 Indian Contract Act.

In the case above, there was no consideration between A and B, thus, no contract enforceable by law arose between the two.

In KedarnathBhatacharjee v Gorie Mohamed[80], "the plaintiff 'X', who was also Vice Chairman of the Municipality, entered into a contract with a contractor for the purpose of building the Town Hall, estimates and plans were submitted to, and approved by, the Commissioners, the original estimate amounting to Rs. 26,000. This estimate, however, was increased to Rs. 40,000, and it was found that the **subscriptions would cover this amount**, and the original plans were therefore enlarged and altered. The defendant 'Y'was a subscriber to this fund of rupees one hundred, having signed his name in the subscription book for that amount. The defendant not having paid his subscription was sued."

X was held entitled to recover the amount from the subscriber, Y.

There are a great many subscriptions that cannot be recovered. A man for some reason or other puts his name down for a subscription to some charitable object, for instance, but the amount of his subscription cannot be recovered from him because there is no consideration.
But, in the present case, persons were asked to subscribe, knowing the purpose to which the money was to be applied, and they knew that on the faith of their subscription an obligation was to be incurred to pay the contractor for the work. Put, in other words, it would be this: "In consideration of your agreeing to enter into a contract to erect or yourselves erecting this building, I undertake to supply the money to pay for it up to the amount for which I subscribe my name"

The plea that Y would not benefit by the construction of the town hall would fail, as an act in order to constitute a consideration, need not be of personal significance. The constituents of consideration, were met in the present case, i.e. X entered into the contract at the desire of Y(along with other promisors).

Thus, once the contractor entered performance, Y, could not revoke, as the act was done at the desire of Y, by the contractor.

The same must be distinguished from promises of a charitable nature, or a bare promise.

**DoraswamiIyer v Arunachala Ayyar[81]:**
Where repair of a temple was in progress, but more money was required due to increase in costs, thus subscriptions were taken. A certain "X" subscribed to the extent of Rs. 125, but later refused to pay. It was held that the amount could not be recovered, as Section 2(d)

[80]KedarnathBhattacharjivsGorieMahomed (1887) ILR 14 Cal 64
[81]DoraswamyIyervsArunachalaAyyarAndOrs. AIR 1936 Mad 135.

requires an act/abstinence at request. Whereas in the present case, action was not induced by the promise to subscribe, but was rather independent of it. While in *Kedarnath*, the work began on the faith of the subscription, presently the work began independent of the subscription.

## 2.1 CONSIDERATION MUST HAVE VALUE IN THE EYE OF LAW, BUT NEED NOT BE ADEQUATE:

If what is given in exchange for the promise has value in the eyes of the law, the court will not question whether that value is adequate and will not interfere with the fairness of the bargain made by the parties.

Thus, A may validly sell a book worth Rs. 10,000 for a mere value of Rs. 100. The Court will not enter into the adequacy of consideration. However, as explanation 2 to section 25 reads, inadequacy of consideration may be taken into account, in determining whether the consent was freely given, if it is challenged,

***White v Bluett*[82]:**

FACTS: Bluett had given his father a promissory note for money that his father had lent him. His father's executor sued Bluett on the note, and he claimed in his defence that his father had promised to discharge him from the obligation if he would stop complaining about the father's distribution of his property among his children, which he did

HELD: This is an example of illusory consideration. There appears to be some consideration but in reality, there was none whatsoever. The son had no right to complain, for the father might make what distribution of his property he liked; and the son's abstaining from doing what he had no right to do can be no consideration.
Thus, the principle is that consideration must be real and have some value in the eye of law and cannot be illusory.

## 3. EXCEPTIONS TO CONSIDERATION:

Consideration is indispensable for making an agreement to be enforceable as per section 10 of the ICA. However, Section 25 entails certain exceptions to the rule:[83]

1. Contract of natural love and affection, when it is in writing and registered.
2. When it is for compensating someone for his voluntary services for the promisor in the past.

[82]***White v Bluett*** (1853) LJ Ex 36
[83]Section 25 Contact Act.

3. When it is a promise, signed or made in writing by the person or his agent to pay whole or part of a debt which is barred by the law of limitation.

The simplest agreement which is without consideration is that which is formed out of pure gratuity. Such a promise is not enforceable. The law on this point regarding the adequacy of consideration is simple and clear that the consideration is not required being of a particular fixed value or an approximation to the promise for which it is exchanged but it must be that have some values in the eyes of the law.[84] It must change promisee's position after the consideration is acted upon or transferred from promisee to the promisor.

**3.1 NATURAL LOVE AND AFFECTION:**

Section 25(1) provides that when an agreement without consideration is expressed in writing and registered under the law and is made on account of natural love and affection between the parties, the same is valid. This is line with the English doctrine of "Solemnity of deed". Under English common law, a contract under seal is enforceable without consideration because the presence of a seal indicates an unusual solemnity in the promises made in an agreement.

However, with a different line of reasoning in different judgments on similar issues in the cases on contracts involving love and affection, the courts in India have shown that this English doctrine of has been never received as it is, in our jurisdiction. Hence, a mere formal arrangement of a promise does not result in a valid binding agreement and other factors must be considered in the cases when there is a contract without consideration, gratuitously. But, if the agreement emerges out of affection and is registered in written form, it will amount to a valid contract. In a case where a husband formed and registered an agreement with his wife that he will give his earrings to her, it was held that there was a valid agreement.[85]

On the Contrary, the existence of the near relation between the parties is not sufficient to show that there is affection between them. On this line of reasoning in *RajlukhyDabee v Bhootnath*[86], where the husband was sued for not performing his part of a promise by not giving separate residence and maintenance to his wife, it was not held to be a valid contract. The court ruled in favour of the husband stating that "the terms of the arrangement between the husband and wife clearly show that there was no affection between them and so, it was without consideration. Thus, it was void ab initio. As natural love and affection cannot be assumed every time when no other motive is known, the court presumes by considering the relation between the parties.

[84]Kulasekaraperumal v. PathakuttyThalevana, AIR 1961 Mad 405.
[85]PoonooBibee v. FyezBuksh, (1874) 15 Beng LR App 5.
[86]RajlukhyDabee v. Bhootnath, (1900) 4 Cal WN 488.

In *Vijay Ramraj v Vijay Anand*[87], the Allahabad High Court held the contract enforceable when the promisor who promised to pay a certain amount to his relative during his life died. The contract was held to be formed out of natural love and as the document of the contract was registered also, the heirs of deceased were made liable for specific performance of the terms of the contract by virtue of Sec. 25(1) and Sec. 37 of the Contract Act as it would have been done by the promisor if he had lived.

**3.2 COMPENSATION FOR VOLUNTARY SERVICES:**

This comes as another exception on the principles of English law which states that past consideration is no consideration at all unless it's a promise or an act done on promisor's request. Section 25 (2) covers this exception and there is no requirement of consideration if a person does an act or gives his service to the promisor without the knowledge of the promisor. And in turn, the promisor shows his willingness to compensate for it by an undertaking.

However, for an exception to fall under this category, some ingredients which are discussed below need to be fulfilled:

- Existence of promise to compensate in future must be there to form an exception under this section. If there is no promise, no contract arises in such a situation and thus suit for specific performance cannot be maintained.

*In Hyderabad State Bank v Ranganath Roy*[88], it was stated by the Court that "the term "voluntarily done" shows the performance of something based on one's own impulses, will and choices. There should be no constraint or pressure or suggestion from anyone".

- Thus, there should be a voluntary service to seek remedy under this section. If someone else other than the plaintiff has provided the service, such contract is not enforceable by the plaintiff. In Bachhu Ram v Chunder[89] where the defendant agreed to pay B for teaching the defendant singing and dancing at her own cost and when it was discovered that she was B's sister who had actually rendered the service, specific performance was not allowed by the court.

- Lastly, it is a prerequisite under Section 25 that the act is done or service rendered should be voluntary in nature and specifically for the promisor without his knowledge or at his request. In addition, there must be a promise by the promisor to compensate for volunteer's service in the future. It must be also kept in mind that if there is a request from the promisor to take a service, this will be directly affected by Sections 2 (a) and 2(d) and will be not entertained under Section 25.

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[87] Vijay Ramraj v. Vijay Anand, AIR 1952 1 All 564.
[88] Hyderabad State Bank v. Ranganath Roy, AIR 1958 AP 605.
[89] Bachhu Ram v. Chunder, AIR 1916 Pat 80.

### 3.3 PROMISE TO PAY TIME-BARRED DEBT:

This type of no-consideration contract falls under Section 25(3) and for invoking it, some essentials must be satisfied:

- There should be a written promise signed by a person or his appointed agent.
- A promise must be there, either to pay a whole or a part of the debt.
- The debt must have been enforced by the creditor for the limitation period.

A debtor can enter into a written agreement under Section 25 (3) for paying a part of the complete debt and a suit can lie in such cases when there is a written promise for paying it. This exception comes into picture only in cases when a promisor is a person liable for the debt and it does not extend to situations when the promise is to pay the debts of a third person.

## 4. PRIVITY OF CONTRACT:

### 4.1 PRIVITY OF CONSIDERATION

Privity of consideration means that consideration shall move from a party to the contract. This doctrine, in lieu of the clear wording of Section 2(d) of the ICA is inapplicable in India.

### 4.2 PRIVITY OF CONTRACT

The doctrine owes its origins to the classical case of Tweddle v Atkinson.[90] In this case, 'A' agreed to marry B(daughter of F). A's father and F entered into a contract that each would pay a certain amount to 'A'. F failed to pay the amount to 'A' and A sued him to recover the same. The Court held, that A had no right of recovery against F, as a stranger to a contract cannot take advantage of a contract, though the contract may be solely for his/her advantage. Thus, though the sole object of the contract was A's benefit, A was not allowed to recover the amount as it was a contract between A's father and F.

Thus, the principle enunciated is this: a contract is between parties only and a non-party to the contract cannot sue for its performance, though avowedly it is for his/her benefit. In India, the same principle has been upheld by the Supreme Court in M.C Chacko v State Bank of Travancore[91] and by the Privy Council in Jamna Das v Ram Autar[92] before that.

In M.C. Chako's case, Bank A owed money to Bank of Travancore. Manager, M of Bank 'A' and M's father had guaranteed repayment in the case. M's father gifted property to his family via a gift deed. The property under the gift deed was under the guarantee agreement, thus Bank of Travancore attempted to enforce the deed provision, however, the bank could not because of the doctrine of privity of contract.

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[90] ***Lampleigh v Braithwait*** [1615] EWHC KB J 17, (1615) Hobart 105, 80 ER 255

[91] M.C Chacko v State Bank of Travancore 1970 AIR 500 1970

[92] Jamna Das v Ram Avtar(1911) 39 IA; 21 MLJ 1158.

### 4.3 CRITICISM TO THE DOCTRINE OF PRIVITY

1. 1937 Law Commission Report in England criticized the doctrine.
2. Lord Denning criticized it in Beswick v Beswick[93]

Critiques' view is that one who is not a party to the contract shall be allowed to enforce it provided it is for such person's benefit and the defendant can take up all the defences he could have against the original party.

Courts, however, have evolved certain well-known exceptions to the rule of privity of contract:

### 4.4 EXCEPTION TO THE PRIVITY RULE

1. **Beneficiary under a Trust/ Charge:**

In Khwaja Mohammad v Hussaini Begum[94], the appellant executed an agreement with the respondent's father that in consideration to the respondent's marriage with his son(both being minors at the time) he would pay Rs 500 a month in perpetuity for the beetel-leaf expenses and charged certain properties with the payment, with power to the respondent to enforce it. The husband and wife separated on account of quarrel and the suit was brought by the plaintiff for the recovery of arrears of this amount. It was held, that though not party to the agreement, the plaintiff was clearly entitled to proceed in equity to enforce the claim.

2. **Marriage Settlement/Family Arrangement:**

In Daropti v Jaspati Rai[95], the defendants wife left him because of his cruelty. He then executed an agreement with her father promising to treat her properly and if he failed to do so, to pay her monthly maintenance and to provide her with a dwelling. Subsequently she was again ill treated by the defendant and driven out. She was held entitled to enforce the promise made by the defendant to her father.

3. **Acknowledgement/ Estoppel:**

A sold house to B. He left a part of the amount to be recovered from B, so that B could pay C, A's creditor. B pays some amount, but did not pay the rest. C, in such a case, can sue B for the same, as B acknowledged his liability to C by paying a certain amount.

4. C**ovenants running against Land:**

If A purchases land with notice/ in good faith, after complying with his duty under Transfer of Property Act, 1882 that the owner is bound by certain covenants, even A shall be bound by the same, notwithstanding that A was not party to the original contract.

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[93]Beswick v BeswickAC 58, UKHL 2

[94]Khwaja Mohammad v Hussaini Begum (1907) ILR 29 All 151

[95] Daropti v Jaspat Rai 1905) PR 171(Punjab Rec.).

## 5. PERFORMANCE OF EXISTING OBLIGATIONS

This category will further be discussed under 2 sub-headings: Pre-existing contract with promisor and pre-existing contract with third party.

### 5.1 PRE –EXISTING CONTRACT WITH PROMISOR

Consideration must be more than what promise is already bound to do. E.g. In R. Sashanahchetti v P. Ramaswami Chetti[96], 'A' was served summons, B promised to pay 'A' for the trouble taken to travel.

There is no consideration in the present case, as A is bound by law to appear before court, thus there is no consideration for the present contract.

Similarly, an agreement to pay a police officer to investigate a case or register an FIR would be devoid of consideration, just as an agreement between students and professors where the students agree to separately the professor if he teaches would be void, as in all these cases, the concerned party was duty bound to perform the acts they have been requested to perform in lieu of the consideration.

Question arises about what happens in cases where there is an agreement to do more than one's official duty?

If a person either does or promises to do what he is already legally bound to do in exchange for a promise made, then that person suffers no legal detriment and the act confers no legal benefit so that, traditionally, this has not been accepted as constituting sufficient consideration.

The device employed to avoid the rule in practice was to hold that a promisee had gone beyond the scope of his existing duty and had thereby provided the necessary consideration. E.g. Fireman beyond scope of duty to protect a person by putting his own life in danger.

### STILK VS MYRICK[97]

On a voyage from London to the Baltic, two of the seamen deserted and, because the captain could not find replacements at Cronstadt Island, he promised the remaining crew that he would divide the wages of the deserters between them if they were to sail the ship back to London. Was this promise enforceable?

[96] R. Sashanahchetti v P. RamaswamiChetti(1868) 4, 7
[97] Stilk v Myrick EWHC KB J58, 170 ER 1168.

Consideration for the ulterior pay promised to the mariners who remained with the ship. Before they sailed from London they had undertaken to do all that they could under all the emergencies of the voyage. They had sold all their services till the voyage should be completed. If they had been at liberty to quit the vessel at Cronstadt, the case would have been quite different; or if the captain had capriciously discharged the two men who were wanting, the others might not have been compellable to take the whole duty upon themselves, and their agreeing to do so might have been a sufficient consideration for the promise of an advance of wages. But the desertion of a part of the crew is to be considered an emergency of the voyage as much as their death; and those who remain are bound by the terms of their original contract to exert themselves to the utmost to bring the ship in safety to her destined port"

It has always been accepted that if a promisee has done more than he was contractually obliged to do, then the extra performance is consideration to support the promisor's promise.

**Williams v Roffey Brothers & Nicholls (Contractors) Ltd[98]**

The defendant building contractors had entered into a contract to refurbish a block of 27 flats. They subcontracted the carpentry work to the plaintiff carpenter for a price of £20,000. When the plaintiff had completed the carpentry work on the roof and only nine of the flats, and had carried out only preliminary work on the others, the plaintiff found that he was in financial difficulties, despite the fact that he had already received interim payments of £16,200. The difficulties were a result partly of the fact that he had underestimated the cost of doing the work and partly of his failure to supervise the work properly. The defendants were liable under a 'penalty clause' in the main contract if the flats were not completed on time. They were aware of the plaintiff's difficulties and that the subcontract had been underpriced. The defendants agreed to pay the plaintiff an extra £10,300 at the rate of £575 on completion of each flat. The plaintiff completed eight further flats and the defendants made one further payment of £1,500. The plaintiff stopped work and sued the defendants on their promise, which the defendants claimed was unenforceable because it was not supported by any consideration. Held: Although the plaintiff was doing no more than he was already legally obliged to do, since the defendants had obtained a benefit in making this promise, the promise was enforceable against them (in the absence of economic duress or fraud). The Court of Appeal stated that this did not overrule or contravene the principle in Stilk v Myrick[99]

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[98]Williams v Roffey Brothers & Nicholls (Contractors) Ltd  1 QB 1,, 1 All ER 512.
[99]Stilk v Myrick EWHC KB J58, 170 ER 1168.

Benefits to the defendants, which arose from their agreement to pay the additional £10,300: (i) seeking to ensure that the plaintiff continued work and did not stop in breach of the sub-contract;

(ii) avoiding the penalty for delay; and

(iii) avoiding the trouble and expense of engaging other people to complete the carpentry work.

A has entered into a contract with B to do work for, or to supply goods or services to, B in return for payment by B; → at some stage before A has completely performed his obligations under the contract B has reason to doubt whether A will, or will be able to, complete his side of the bargain; and → B thereupon promises A an additional payment in return for A's promise to perform his contractual obligations on time; and → as a result of giving his promise, B obtains in practice a benefit, or obviates a disbenefit; → B's promise is not given as a result of economic duress or fraud on the part of A; then → the benefit to B is capable of being consideration for B's promise, so that the promise will be legally binding

Does not contravene the principle of Stylk v Myrick[100] refine, and limit the application of that principle, but they leave the principle unscathed e.g. where B secures no benefit by his promise.

These were all advantages accruing to the defendants which can fairly be said to have been in consideration of their undertaking to pay the additional £10,300. True it was that the plaintiff did not undertake to do any work additional to that which he had originally undertaken to do but the terms on which he was to carry out the work were varied and, in my judgment, that variation was supported by consideration which a pragmatic approach to the true relationship between the parties readily demonstrates.

Thus, if we were to apply the principles to a case where the client promises to pay his lawyer extra money, in case they win a case. The client wins the case and then refuses to pay the lawyer, he would succeed as, the lawyer is duty bound to render his best service as a pleader. Thus, there is no fresh consideration for the special reward promised

Similarly in a case, where sailors refuse to complete a voyage due to war risks. In this case, if the captain agrees to pay extra wages, the same would be recoverable, provided, the war risks were not in the original contemplation while contracting, thus, the extra money would constitute fresh consideration in lieu of new circumstances.

Thus, the test can succinctly be stated thus:

[100] supra

PERFORMANCE OF AN EXISITING OBLIGATION MAY AMOUNT TO A GOOD CONSIDERATION PROVIDED THERE ARE PRACTICAL BENEFITS TO THE PROMISEE

So, where conditions have arisen which entitle the party to refuse to go ahead with the contract, promise to pay extra constitutes fresh consideration.[101]

**PART PAYMENT OF DEBT**

Where a creditor PROMISES to accept a smaller sum than is due from a debtor and promises not to sue for the balance, this is a promise to alter an existing contract (the debt contract). In Pinnel's Case[102] , it was held that, in such circumstances, the debtor must provide consideration for the creditor's promise to release him. Simply paying a smaller sum than that owed will not be sufficient, since the debtor has done only what he was legally obliged to do anyway under the debt contract. Traditionally, the factual benefit that might accrue to the creditor from securing some payment rather than nothing at all was not regarded as sufficient and some separate consideration was required.

However, the 'gift of a horse, hawk or robe' (property other than money) would be good consideration for a promise to forgo the balance if accepted by the creditor as full payment, since the court will not inquire into the adequacy of the consideration.

Payment before the due date is a good consideration, as is payment at a different place—as long as the change of venue is at the creditor's request and not the debtor's, since if it were at the debtor's request, there would be neither a benefit to the creditor, nor a detriment to the debtor.[103]

The principle in Pinnels case was confirmed in **Foakes v Beer.**

**Foakes v Beer[104]:** In August 1875, Julia Beer had obtained a High Court judgment against DrFoakes for £2,090 19s. It was agreed in writing, in December 1876, that if Dr Foakes were to pay £500 immediately and pay £150 on two occasions each year until the whole sum of £2,090 19s. had been paid, then Julia Beer 'would not take any proceedings whatever on the said judgment'. (As a judgment debtor, DrFoakes was liable for the interest that had accrued on the judgment debt, but the agreement had not mentioned this.) DrFoakes paid the judgment debt in accordance with the agreement, but Julia Beer then brought an action claiming the interest on the debt.

[101]Gilber Steel v University Construction.
[102]Penny v Cole(1602) 5 Co Rep 117a,
[103]Vanbergen v St Edmunds Properties Ltd. [1933] 2 KB 223.
[104]Foakes v Beer UKHL 1,, All ER Rep 106, (1884) 9 App Cas 605; 54 LJQB 130; 51 LT 833; 33 WR 233.

Held: In any event, DrFoakes had not provided any consideration for Julia Beer's promise not to take any proceedings on the judgment and therefore the promise was unenforceable. He had done only what he was legally bound to do anyway.

It cannot be legally enforced against the respondent, unless she received consideration for it from the appellant, or unless, though without consideration, it operates by way of accord and satisfaction, so as to extinguish the claim for interest. What is the consideration? On the face of the agreement none is expressed, except a present payment of £500, on account and in part of the larger debt then due and payable by law under the judgment. The appellant did not contract to pay the future instalments of £150 each, at the times therein mentioned; much less did he give any new security; in the shape of negotiable paper, or in any other form. The promise de futuro was only that of the respondent, that if the half-yearly payments of £150 each were regularly paid, she would 'take no proceedings whatever on the judgment.' No doubt if the appellant had been under no antecedent obligation to pay the whole debt, his fulfilment of the condition might have imported some consideration on his part for that promise.

As to accord and satisfaction, in point of fact there could be no complete satisfaction, so long as any future instalment remained payable; and I do not see how any mere payments on account could operate in law as a satisfaction ad interim, conditionally upon other payments being afterwards duly made, unless there was a consideration sufficient to support the agreement while still unexecuted.

What is called 'any benefit, or even any legal possibility of benefit,' . . . is not (as I conceive) that sort of benefit which a creditor may derive from getting payment of part of the money due to him from a debtor who might otherwise keep him at arm's length, or possibly become insolvent, but is some independent benefit, actual or contingent, of a kind which might in law be a good and valuable consideration for any other sort of agreement not under seal

Exceptions to Pinnels case:

1. Part payment by third party
2. Compromise agreement
3. Payment before time
4. Promissory estoppel

**PROMISSORY ESTOPPEL**

**Hughes v Metropolitan Railway Co.**[105]

On 22 October 1874, the landlord gave the tenant company six months' notice to repair the premises. However, on 28 November, negotiations began between the parties for the sale of the remainder of the lease back to the landlord. The tenant stated that the company would

[105]Hughes v Metropolitan Railway Co. (1877) 2 App Cas 439 (HL).

defer commencing the repairs until it had heard whether its proposal was acceptable. After the six months had elapsed, the landlord claimed that the lease was forfeited for breach of covenant and sought to eject the tenant. The tenant sought a stay of execution.

Held: The tenant was entitled in equity to be relieved against forfeiture of the lease because the negotiations had the effect of suspending the notice and, while they continued, the six-month period did not run. It ran again only from the time that the negotiations ended.

Reason: It is the first principle upon which all Courts of Equity proceed, that if parties who have entered into definite and distinct terms involving certain legal results—certain penalties or legal forfeiture—afterwards by their own act or with their own consent enter upon a course of negotiation which has the effect of leading one of the parties to suppose that the strict rights arising under the contract will not be enforced, or will be kept in suspense, or held in abeyance, the person who otherwise might have enforced those rights will not be allowed to enforce them where it would be inequitable having regard to the dealings which have thus taken place between the parties

Lord Blackburn, in Foakes v Beer[106] however, accepted that, in practice, agreements to accept part payment in full satisfaction often have factual benefits for the creditor. His position recognizes the practical realities.

First, that where a matter paid and accepted in satisfaction of a debt certain might by any possibility be more beneficial to the creditor than his debt, **the Court will not inquire into the adequacy of the consideration.** If the creditor, without any fraud, accepted it in satisfaction when it was not a sufficient satisfaction it was his own fault. that payment before the day might be more beneficial, and consequently that the plea was in substance good.

It is this principle which has been adopted in our contract act, under section 63.

## INDIAN POSITION ON PART-PAYMENT OF DEBT

Before considering the wording of section 63, I propose to answer, why the positions in India is better than the position in England in respect of part payment of debt. It is submitted that there is an internal contradiction in the approach taken by the Courts in England with respect to part payment of debt.

This is because the ‘gift of a horse, hawk or robe’ (property other than money) would be good consideration for a promise to forgo the balance if accepted by the creditor as full payment. This clearly signifies, the court in principle permits satisfaction and accord to one party over and above the actual amount recovered.

[106]Ibid, 32.

Such satisfaction need not be limited to object and may extend to amount in ruppees as well, for the quantum is equally less in either case, unless it is a specific object, uniquely available which satisifies the party. It would be very tough to see consistency in the courts line to permit, a robe worth Rs 100, instead of Rs 1000 actually due, but not permit complete satisfaction if the party provides Rs 200 instead.

> "63. Promise may dispense with or remit performance of promisee.—Everypromisee may dispense with or remit, wholly or in part, the performance of the promisee made to him, or may extend the time for such performance, or may accept instead of it any satisfaction which he thinks fit."[107]

Eg. A owes B 5,000 rupees. A pays to B, and B accepts, in satisfaction of the whole debt, 2,000 rupees paid at the time and place at which the 5,000 rupees were payable. The whole debt is discharged.

A owes B 5,000 rupees. C pays to B 1,000 rupees, and B accepts them, in satisfaction of his claim on A. This payment is a discharge of the whole claim2.

A owes B, under. a contract, a sum of money, the amount of which has not been ascertained. A, without ascertaining the amount, gives to B, and B, in satisfaction thereof, accepts, the sum of 2,000 rupees. This is a discharge of the whole debt, whatever may be its amount.

A owes B 2,000 rupees, and is also indebted to other creditors. A makes an arrangement with his creditors, including B, to pay them a 3[composition] of eight annas in the rupee upon their respective demands. Payment to B of 1,000 rupees is a discharge of B‟s demand.

Thus s-63 contemplates 3 kinds of alternate remedies instead of the amount actually due:
1. the promissee is entitled to dispense wholly or in part the performance
2. the promissee is entitled to extend the time of performance
3. thepromissee is entited to accept an alternate which satisfies the promissee.

## 5.2 PRE-EXISTING CONTRACT WITH THIRD PARTY

If B is already bound under a contractual promise to C, B can use that promise in favour of C (or B's performance of the promise to C) as consideration for a promise by A, e.g. involving payment for that very same performance—the assumption being that the promise or performance of the contract B/C is a benefit to A.

The leading autority on this point in English law is Shaldwell v Shaldwell[108]. We'll first look at the evolution of the concept and then observe the position in Indian law.

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[107] Section 63, Indian Contract Act
[108]Shaldwell v Shaldwell(1860) 9 CB NS 159, 142 ER 62 (Court of Common Bench).

**Shadwell v Shadwell:**[109]

After his engagement to Ellen Nicholl, the plaintiff received the following letter from his uncle:

"I am glad to hear of your intended marriage with Ellen Nicholl; and, as I promised to assist you at starting, I am happy to tell you that I will pay to you £150 yearly during my life and until your annual income derived from your profession of a Chancery barrister shall amount to 600 guineas."

The plaintiff claimed arrears in these yearly sums from the uncle's executors, alleging the consideration for the promise to be his marriage to Ellen Nicholl.

Held: (Erle CJ): The promise was binding, since it was supported by good consideration.

Reasoning: Do the facts show that the promise was in consideration either of a loss to be sustained by the plaintiff or a benefit to be derived from the plaintiff to the uncle, at his, the uncle's request?

First, do these facts show a loss sustained by the plaintiff at his uncle's request? When I answer this in the affirmative, I am aware that a man's marriage with the woman of his choice is in one sense a boon, and in that sense the reverse of a loss: yet, as between the plaintiff and the party promising to supply an income to support the marriage, it may well be also a loss. The plaintiff may have made a most material change in his position, and induced the object of his affection to do the same, and may have incurred pecuniary liabilities resulting in embarrassments which would be in every sense a loss if the income which had been promised should be withheld; and, if the promise was made in order to induce the parties to marry, the promise so made would be in legal effect a request to marry.

Secondly, do these facts show a benefit derived from the plaintiff to the uncle, at his request? In answering again in the affirmative, I am at liberty to consider the relation in which the parties stood and the interest in the settlement of his nephew which the uncle declares. The marriage primarily affects the parties thereto; but in a secondary degree it may be an object of interest to a near relative, and in that sense a benefit to him. This benefit is also derived from the plaintiff at the uncle's request. If the promise of the annuity was intended as an inducement to the marriage, and the averment that the plaintiff, relying on the promise, married, is an averment that the promise was one inducement to the marriage, this is the consideration averred in the declaration; and it appears to me to be expressed in the letter, construed with the surrounding circumstances.

The principle that performance of an existing contractual duty owed to a third party can be a good consideration has been approved by the Privy Council in two further cases—namely,

[109]Supra.

New Zealand Shipping Co. Ltd v A. M. Satterthwaite, The Eurymedon[110] and Pao On v Lau YiuLong [111].

## INDIAN POSITION

The principle of Shalwell has been follwoed in India as well. In the Madhya Pradesh HC in Gopal Co Ltd. V Hazarilal Co.[112], the following case arose:

The plaintiff was under a contract to purchase some bales of cotton from a mill, but refused to fulfill a substantial part of his contract as the price of cloth had fallen down. The defendants, who were the sole selling agents of the mill and who had guaranteed the performance of the contract, requested the plaintiff to take the whole of the quota of bales fixed for delivery in the first month and promised that they would buy from the plaintiff a part of such bales at the contract price or ay him Rs 25,000 at his option. The plaintiff elected Rs. 25,000.

The defendant contended their contract was void due to lack of consideration.

Reviewing English judgments and the interplay with Indian law, the court held that "it appears that the second agreement brings into existence a new contract between different parties and therefore a promise to do a thing which the promissee is already bound to do under a contract with a third party can be good consideration to support a contract"

Section 2(d) clearly defines that for consideration to arise, the act/abstinence must be at the desire of the promisor. In such a case, the obvious contention would be, that the party, was complying, not at the desire of the 3rd party, but due to the pre-existing contract. In such cases, it becomes tough to ascertain, at whose desire the concerned party has so acted?

Was is at the desire of the original party, the latter party, or was it a joint desire? In administrative law, the Courts try to decide on questions of composite intentions, by trying to figuring out the dominant intention. However, in contractual cases, courts have not yet tread on that line of inquiry. This is because the cases which have come up, like in Gopal Co, there was a clear change in position at the desire of the third party, i.e. the party wanted to breach, but chose not to at the desire of the third party, so there was a clear change in position at the instance of the third party. Thus, the requirement of consideration "at the desire of the promisor:" becomes easy to enquire into.

## CAPACITY TO CONTRACT

A requisite for the formation of a legally binding contract is that the parties entering into such an agreement have the capacity to do so. This is enshrined in Section 10 of the Indian

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[110] New Zealand Shipping Co. Ltd v A. M. Satterthwaite, The Eurymedon[1975] AC 154 (PC).
[111] PaoOn v Lau Yiu Long [1980] AC 614 (PC).
[112] Gopal Co Ltd. V Hazarilal Co AIR 1963 MP 37.

Contract Act, 1872[113] which requires the parties to be competent to enter into an agreement. Such agreements then are legally enforceable, provided a few other conditions are fulfilled.

These parties can be 'natural' or 'legal' persons. Natural persons are persons in fact, while legal persons are persons in law- like corporations. The former category has an unlimited capacity to enter into agreements, so to speak; while the capacity for juristic persons is limited to the purpose and object for which such personality is conferred. For example, in cases of natural persons, the question of *ultra vires* does not arise, but for corporations it is essential to ensure that the corporation had the very capacity to enter into the contract in the first place.[114]

However, not all natural persons are assumed to have the capacity to contract under the Act. Section 11 and 12 of the Act delineate two such categories of natural persons : minors and persons of unsound mind.

1. **MINORS**

   Section 11 requires that the party entering into a contract be a major, i.e. not a minor. A minor is a person younger than 18 years of age, and in case a guardian has been appointed that threshold is increased to 21 years. This definition is not given in the Act and is derived from the Indian Minority Act, 1875.

   Section 11 however does not detail the consequences of a minor entering into a contract. Is the contract *void ab initio?* Or is it voidable? And at whose option?

   This controversy was resolved in 1903 by the Privy Council in *Mohori Bibee v. Dharmodas Ghose*[115] which interpreted Section 11 as a prohibition on minors entering into agreements. Since Section 10 clearly required the parties to be competent for the contract to be legally enforceable, and Section 11 declared that minors did not possess such capacity, the effect of reading them together pointed towards a statutory prohibition. The natural consequence of this was that such agreements were *void ab initio.*

   Any alternate interpretation would allow the minor to cherry pick contracts that they could enforce or not, and would cause some level of asymmetry. This would cause hardships to adults who had dealt fairly with them.

   At the same time, it is also to protect the minors from their own poor judgments and possible fraud, as there is a level of presumed ignorance and immaturity.

   The ruling in *Mohori Bibee* has been more or less followed, in a slightly tempered form.

[113] Hereinafter, the "Act".
[114] DR. G.K KAPOOR & DR. SANJAY DHAMIJA, COMPANY LAW AND PRACTICE (22ND ED.).
[115] ILR (1903) 30 Cal 539 (PC).

The approach was changed to a more equitable one by the Privy Council in *Sirkakulam Subramanyum v. Kurra Subba Rao.*[116] The court held that contracts, as such in this case, if *both* for the benefit of the minor and entered into by the guardian who had the capacity to do so, would be binding on the minor.

a. **Estoppel against a minor**

   In case a minor misrepresents his age to induce another party into entering a contract with him/her, can he/she then be estopped from setting up a defense of his/her true age? This was settled by *Sadik Ali Khan v. Jai Kishore.*[117] Since estoppel cannot exist against a statute, there can be no plea in estoppel against a minor. Agreements entered into by them continue to be a nullity.

   Thus, even if a minor enters into an agreement by misrepresenting his/her age, it is possible for him/her to plead their true age as a defense and avoid the contract.

b. **Liability in contract or in tort arising out of the contract**

   Since the agreement with a minor remains null and void, it is devoid of all legal effect. This means that no contractual obligations can be enforced against the minor either directly or indirectly by making a claim in tort.

   In India, it is an accepted principle that if *"the tort is directly connected with the contract and is the means of effecting it…the minor is not liable in tort."*[118] However, if the action in tort and the contractual obligations are independent of each other, then it is possible to hold the minor liable in tort.

c. **Ratification**

   Even if a person ratifies a contract they had entered as a minor, the same will continue to be void *ab initio* and will not become enforceable. In the eyes of the law, the agreement had never existed in the first place.

d. **Doctrine of restitution**

   While a minor cannot be held liable for breaching contractual obligations, an equitable remedy does exist. If a minor obtains any goods or property by misrepresenting their age, the court can order them to restore the same to the other party. However, this is possible only for so long as the same is traceable in their possession. If the minor has sold or converted the goods, he/she cannot be asked to repay the value of the goods, because that is tantamount to enforcing a void agreement. Logically then, in cases where the minor has received not goods, but cash, the doctrine would not apply.[119]

e. **Beneficial contracts**

   The law laid down by the *Mohori Bibee* case has been narrowed down to cases where the minor has some obligations and the other party seeks to enforce those.

[116] ILR 1949 Mad 141 PC.
[117] AIR 1928 All PC 152.
[118] *Harimohan v. Dulu Miya,* ILR (1934) 61 Cal 1075. Further illustrations are *Radhey Shyam v. Biharilal* ILR (1918) 40 All 558; *Wali Singh v. Sohan Singh,* AIR 1954 SC 263, 265.
[119] *Leslie (R) Ltd v. Sheill,* (1914) 3 KB 607 (CA), 618.

In *Raghava Chariar v. Srinivasa,*[120] the court allowed the minor to enforce a contract which is of some benefit to him/her and under which he/she bears no obligations. Thus, if a minor has performed his/her obligations under an agreement, the court will compel the other party to perform their obligations under such an agreement. The court will not cancel the same on grounds of minority.

The Act does not prevent the minor from accepting benefits. In cases where the contract is still executory or consideration is yet to be supplied by the minor, the *Mohori Bibee* principle will be applicable.

If a minor has received consideration which fails, he/she will be entitled to restitution. However, there has to be a total failure of consideration for this principle to apply.

If a minor has paid for something and used or consumed it, the court would not allow him to recover back the money he has paid. This would be to sanction injustice towards the other party.[121]

**f. Contracts of apprenticeship and trade**

Contracts of apprenticeship are also considered to be of benefit to minors. The Indian Apprentices Act, 1850 has made provisions for contracts that may be binding on minors. These contracts are made binding to further the employability of children, especially orphans and those coming from disadvantaged backgrounds; it is in furtherance of this Act's objective of providing them with a livelihood. Section 9 requires that such contracts be made by a guardian on behalf of a minor. In England, these contracts as treated on the same footing as contracts for necessaries.[122]

Trade contracts are not considered to be beneficial for minors as such.[123]

**g. Liability for necessaries**

Section 68 of the Indian Contracts Act lays down the liability for necessaries that are provided to persons who are incompetent to contract. While the section restricts the liability to 'necessaries', this term is not defined under the Act.

A necessary article is something without which an individual cannot reasonably exist which includes, *inter alia,* food, lodging in the first instance.[124] It may also cover '*proper cultivation of the mind'*, which encompasses instruction on art and trade, or education. Then again, the 'subject and content of the contract may vary according to the state or condition of the infant himself.' Such an assessment may require taking into account, *inter alia,* his rank or the station he has to fill.[125]

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[120] (2011) 3 MWN (Civ) 1 (FB).
[121] *Valentini v. Canali,* (1889) 24 QBD 166.
[122] *Roberts v. Gray,* (1913) 1 KB 520 (CA).
[123] *Cowern v. Nield,* (1912) 2 KB 419.
[124] *Chapple v. Cooper* (1844) 13 M&W 252, 258.
[125] *Id.*

What is 'necessary' then can be seen as a relative concept to be determined in the context of and with reference to the circumstances of the minor or his/her fortune.

## 2. PERSONS OF UNSOUND MIND

Under English law, a person of unsound mind can be considered competent to enter into agreements. However, he/she can set the same aside if he proves that he was incapable of understanding the contract *and* that the other party was aware of the fact. Unless both of these are proved, the agreement will be binding on both the parties. The contract, thus, is voidable at the option of the person of unsound mind, provided both the factors are proved.

Unlike the English position, in India, such a contract is considered void. Section 12 addresses this and states as follows-

"***12. What is a sound mind for the purposes of contracting***.*—A person is said to be of sound mind for the purpose of making a contract, if, at the time when he makes it, he is capable of understanding it and of forming a rational judgment as to its effect upon his interests.*

*A person who is usually of unsound mind, but occasionally of sound mind, may make a contract*

*when he is of sound mind.*

*A person who is usually of sound mind, but occasionally of unsound mind, may not make a contract when he is of unsound mind.*

***Illustrations***

*(a) A patient in a lunatic asylum, who is at intervals of sound mind, may contract during those intervals.*

*(b) A sane man, who is delirious from fever or who is so drunk that he cannot understand the terms of a contract, or form a rational judgment as to its effect on his interests, cannot contract whilst such delirium or drunkenness lasts*."

The first part of the provision lays down the general principle of competence to contract. If a person can understand the full import of the contract, anticipate the effect of the contract on his/her interests, and exercise a rational judgment keeping in mind all circumstances, he/she can enter into agreements.

If a person is unable to understand any of the above factors, he/she can be considered to be of unsound mind jurisprudentially. The person, however, has to be suffering from this disability on the date of execution of the agreement.

Apart from these two categories, a party can be considered incompetent to contract based on legal incapacity, i.e. any other laws have imposed partial or total restrictions on the person's right to contract.

Other than natural persons, several legal persons are also capable of entering into agreements. The two relevant categories that shall be discussed here are companies and the government.

### 3. COMPANIES

A company incorporated under the Companies Act, 2013 or any other old company law possesses a separate legal personality from its shareholders. This entails that it can enter into contracts in its own name, and sue and be sued on such agreements. However, the power to enter into agreements is not absolute- it is restricted. The primary restriction lies in the Memorandum of Association of the company, under the 'objects' clause. It determines the kind of agreements that can be entered into by the company, and defines the limits of its powers more generally.

Section 4(1)(c) of the Companies Act, 2013 requires the objects of the company to be stated in the Memorandum of Association. A company cannot do anything outside or beyond its stated objects, and in case such an activity is undertaken it will be *ultra vires* and thus, void.[126] For example, in *Ashbury Railway Carriage and Iron Co. v. Riche,*[127] a contract for financing the construction of a railway in Belgium was held to be beyond the object of the company and declared void *ab initio*. The business carried on by the company was of 'Mechanical Engineers and General Contractors'. The court interpreted the sphere of sanctioned contracts to be those that were connected to the business of mechanical engineers. Consequently, the aforementioned financing contract was held to be made *ultra vires* and was thus, void.

[126] *Attorney General v. Great Eastern Railway Company*, (1880) 5 AC 473.

[127] (1875) LR 7 HL 653.

## MODULE III

# FREE CONSENT

### FREE CONSENT

It is important to understand the meaning of the term "free consent" as it is an essential requirement of a contract according to Section 10 of the Indian Contract Act, 1872. However, in order to understand free consent, one needs to first understand what "consent" means. As per Section 13, two or more persons are said to consent when they agree upon the same thing in the same sense. Commentators have opined that the language of this section is largely a judicial construction rather than a legislative one.[128] As an authoritative definition of consent, Section 13 does not seem to define very much. However, the words "same thing" and "same sense", which appear in the scheme of Section 13, have been subject to widespread debate as to how should they be interpreted. The words "same thing" have been understood to not only refer to corporeal property, but also to the whole content of the agreement.[129] Henceforth, no contract can be said to be formed unless parties are *ad idem* on all the essential terms of the transaction.

Furthermore, a valid contract can only come into existence, when acceptance of an offer must be in the "same sense" in which the offer was made.[130] In *Raffles v. Wichelhaus*[131], one of the parties contracted to buy a cargo of cotton which was to be transported from Bombay via a ship named Peerless. However, there were two ships by the name of Peerless which sailed from Bombay. One left in October, while the other in December. Herein, both the parties had different ships in mind. The court was unable to determine which ship was referred to in the contract. Henceforth, it ruled that there was no contract as the offer and acceptance did not coincide because the parties had different things in mind.

The Act goes a step further and defines "free consent". According to Section 14, consent is said to be free when it is not caused by;

1. Coercion, as defined in Section 15
2. Undue Influence, as defined in Section 16
3. Fraud, as defined in Section 17
4. Misrepresentation, as defined in Section 18
5. Mistake, as defined in Section 20, 21 and 22.

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[128] NILIMA BHADBADE, POLLOCK AND MULLA ON THE INDIAN CONTRACT AND SPECIFIC RELIEF ACTS 307 (14th ed., Lexis Nexis 2013).
[129] *Id.*
[130] Bhagwandas Goverdhandas Kedia v. GIrdharilal Parshottamdas, AIR 1966 SC 543.
[131] (1864) 2 H&C 906.

In the absence of free consent, the contract is generally voidable at the instance of the party whose consent was not freely obtained.[132] However, a generic assertion that consent was not free is not enough. It is necessary to prove that consent was vitiated by at least one of the factors enumerated in Section 14.

According to Section 19, if consent is vitiated by coercion, fraud or misrepresentation, then the contract is voidable at the option of the party whose consent was so obtained. In other words, he can either avoid the contract or affirm it. He can exercise the option only once. If the contact is affirmed, it becomes enforceable by both parties and, if it is avoided, it becomes void against both parties who are to be restored to their original position. Similarly, according to Section 19-A, if consent is obtained by undue influence, the contract is voidable at the option of the party who consent was obtained. He can avoid the contract provided he returns any benefits he received in pursuance of the contract. Lastly, Section 20 and 21 prescribes that any mistake as to an essential fact by both the parties renders a contract void.

## COERCION

### 1. 'COERCION' DEFINED UNDER INDIAN LAW

Coercion is defined under Section 15 of the Contract Act, 1872. It is defined as the commission of any of the following acts, with an intention to induce the conclusion of a contract:

i. Committing or threatening to commit any offence under the Indian Penal Code (1860);
ii. Unlawful detention or the threat of detention of any property to the prejudice of any person.

Consent is caused by coercion if it is caused by the pressure exerted by either of the techniques mentioned above. The explanation to Section 15 further states that it is immaterial whether the Indian Penal Code (IPC) is or is not in force at the place where such coercive tactics are employed. Section 15 is clearly intended to have global reach, whenever Indian Contract Law is applicable. The burden of proof shouldered by the plaintiff is therefore only that the alleged act is prohibited by the IPC, and not the applicability of the IPC at the place of coercion. The illustration provided to Section 15, clarifies that Indian courts can admit a suit pleading the absence of free consent, even if the place of coercion would ordinarily be beyond the normal jurisdiction of Indian courts.

[132] Deo Nandan v Chhote, AIR 1983 Cal 186.

## 2. TECHNIQUES OF CAUSING COERCION

### 2.1 ACTS PROHIBITED BY THE INDIAN PENAL CODE

The first technique of coercion that is defined in Section 15 is the commission or threat to commit an act that is contrary to the penal law. For example, consent obtained at gunpoint would satisfy this definition. To amount to coercion, the pressure exerted must be unlawful. Therefore it has been observed: "To threaten criminal prosecution is not per se an act forbidden by the Indian Penal Code. Such an act would only be one forbidden by the Indian Penal Code if it amounted to a threat to file a false charge."[133]

### 2.2 DETENTION OF PROPERTY

The second technique of causing coercion as defined under Section 15 is related to the unlawful detention or the threat of unlawful detention of property. Here the threat to one's property is understood to be the 'pressure' that vitiates the parties' free consent. An illustration of the detention of property is found in *Astley v Reynolds*,[134] where the Plaintiff had pledged his plate against the defendant for £20. When he attempted to recover it against that sum, the pledgee insisted that an additional £10 in interest was also owed to him. The plaintiff paid this to redeem the plate and then sued for recovery. He succeeded in his claim because the act of refusing to deliver the good without the payment of an additional sum amounted to a detention of property.

## 3. DISTINGUISHING COERCION FROM DURESS UNDER COMMON LAW

The Madras High Court has compared the positions in English and Indian law, as follows:

"What the Indian Law calls 'coercion' is called in English Law 'Duress or Menace'. Duress is said to consist in actual or threatened violence or imprisonment of the contracting party or his wife, parent or child by the other party or by anyone acting with his knowledge and for his advantage. But coercion as defined under Section 15 is much wider and includes the unlawful detention of property also. Further, coercion may be committed by any person, not necessarily by a party to the contract. Again, it need not be directed against the contracting party, or his parent, wife or child. It may be directed against any person, even if he is a stranger. While in English Law, duress must be such as will cause immediate violence and also unnerve a person of ordinary firmness of mind, these requisites are not necessary in Indian Law."[135]

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[133] Askari Mirza v. Bibi Jai Kishori, (1912)16 IC 344.
[134] Astley v. Reynolds, (1731) 2 STR 915.
[135] Karuppayee Ammal v. Karuppiah Pillai, (1987) 1 MLJ 138.

Coercion as defined under Indian Law therefore does not require that the coercion cause immediate violence. However, it would appear incorrect to interpret the decision of the court as meaning that unnerving a person of ordinary firmness of mind does not amount to coercion. The pressure that unnerves the firmness of mind is the very basis of the rule on coercion under Section 15. It is noteworthy however that Section 15 only defines coercion in terms of the IPC and the unlawful detention of property.

Additionally, the Madras High Court pronounces a somewhat narrow construction of duress. According to Anson's Law of Contract, a contract is voidable when its conclusion is "induced by unlawful or illegitimate forms of pressure".[136] In *Rookes v Bernard*, Lord Devlin commented on the nature of duress that: "[a]ll that matters to the plaintiff is that, metaphorically speaking, a club has been used. It does not matter to the plaintiff what the club is made of – whether it is a physical club, a tortious club or an otherwise illegal club."[137] The modern construction of duress encompasses not just threats to person and property, but also threats of economic harm.[138] Consequently, duress cannot be read restrictively to cover only actual or threatened violence to person and immediate family. The remedy for duress is rescission of contract.

## UNDUE INFLUENCE

### 1. 'Undue Influence' Defined

Section 16 of the Contract Act, 1872 stipulates that a contract is said to be induced by undue influence where the relations that subsist between the parties are such that one party is in a position to dominate the will of the other and uses that position to obtain an unfair advantage over the other. In Anson's Law of Contracts, the editors draw a distinction between 'duress' and 'undue influence'. The distinction made is that duress is concerned with the process by which the contract was made and the manner in which consent was perfected. It does not concern itself with the harshness of the terms of the contract. Undue influence on the other hand is "also said to be primarily concerned with procedural unfairness" but is "more complicated" because of its role in protecting excessively vulnerable parties, and has "significant substantive aspects."[139]

### 1.1 ABILITY TO DOMINATE WILL OF THE OTHER

Any relationship where the ability to dominate the will of the other party is used to obtain an unfair advantage will satisfy the requirement under Section 16(1). The test is a 'but for'test

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[136] BEATSON ET AL, ANSON'S LAW OF CONTRACT, 350 (2010). [*Hereinafter* ANSON].
[137] Rookes v. Bernard, [1964] AC 1129, 1209.
[138] ANSON, *supra* note 9 at 351. (The 'club' referenced by Lord Devlin is a metaphorical one that is intended to signify any form of unlawful or illegitimate pressure. When it comes to duress, this pressure (read 'club') may manifest in many ways whether through physical threat or injury, or even other harms such as economic harms.)
[139] ANSON, *supra* note 9 at 349.

whereby it can be said that the contract would not have been entered into but for the undue influence exerted by the party in a superior position.

## 1.2 RELATIONS INVOLVING DOMINATION

One party can be said to dominate the will of another in all cases where the relationship involves active trust and confidence, or where the parties are not at an equal footing. Consequently, it is understood that buyers and sellers in ordinary trade, for example, are placed at an equal footing.[140] However, it is apparent that there are infinite varieties of relationships where this may arise. While this position retains its generality in India, Section 16(2) of the Contract Act identifies two instances in which a person will be presumed to be in a position to dominate the will of another:

i. Where one party holds real or apparent authority over another, or stands in a fiduciary relation to the other;
ii. Where a contract is made with a person whose mental capacity is temporarily or permanently affected by reason of age, illness, or mental or bodily distress.

### *1.2.1 Real or Apparent Authority*

A person in authority is presumed to be able to dominate the will of the person over whom such authority is held. Authority may be either real or apparent. This may include an Income Tax Official vis-à-vis an assessee, a police official vis-à-vis an accused person. Apparent authority includes cases where there is no real authority, but where the person is able to approach the other with the colour of authority.

### *1.2.2 Fiduciary Relation*

Every relationship of trust and confidence is a fiduciary relation.[141] Since confidence rests at the base of many transactions, this becomes a wide category of relations. It includes a solicitor and her client,[142] trustee and *cestui que trust*,[143] spiritual advisor and devotee,[144] doctor and patient, woman and confidential managing agent,[145] parent and child,[146] and creditor and debtor.[147] Generally speaking, these are relationships where confidence is reposed by one party and influence is exercised by the other.

[140] Devki Nandan v. Gokli Bai, (1886) 90 PLR 325 (P&H).
[141] Subhas Chandra Das Mushib v. Ganga Prasad Das Mushib, AIR 1967 SC 878.
[142] Pushong v. Mania Halwani, 1868 BLR AC 95.
[143] Raghunath v. Varjivandas, (1906) 30 Bom 579.
[144] Mannu Singh v. Umadat Pande, ILR (1888-90) 12 All 523.
[145] Wajid Khan v. Raja Ewaz Ali Khan, (1890-91) 18 IA 144.
[146] Lakshmi Doss v. Roop Laul, ILR (1906-08) 30 Mad 169.
[147] Diala Ram v. Sarga, AIR 1927 Lah 536.

### *1.2.3 Mental Capacity*

Temporary or permanent impairment of mental capacity is another reason for undue influence to be presumed. This impairment may be through age, illness, or mental or bodily distress. The term 'mental distress' warrants closer inspection because of the possibility that such a person may be easily persuaded to give consent to an unfavourable contract. Such contracts are therefore voidable. In *Rannee Annapuri Nachiar v Swaminatha Chettiar*,a poor Hindu widow who sought to establish her right to maintenance was persuaded by a moneylender to pay 100 per cent interest. This is a clear instance of undue influence exerted upon a person in distress.

An urgent need for money alone, however, does not meet the standard of mental distress. In *Raghunath Prasad Sahu v Sarju Prasad Sahu*, a person who borrowed exorbitant amounts of money from moneylenders to fight a criminal prosecution brought by his father was not found to be in a position where the moneylender could have dominated his will.[148] Further, a contract under statutory compulsion cannot be said to cause mental distress.[149] This is because though the contract is compelled by law, it is viewed as being freely consented to in the law.

## 2. Burden of Proof & Presumption of Undue Influence

There are two key points that a plaintiff must prove in an action for undue influence under Section 16. First, it must be shown that the other party had the ability to dominate the will of the other. Second, it must be shown that this ability to exercise influence was actually used to induce the plaintiff's consent. It is insufficient to demonstrate that one party *could* influence decisions without demonstrating that it *used* this influence. Notwithstanding the generality of this position, there are circumstances in which the burden of proof is reversed and shifted to the other party, in relationships that raise a presumption of undue influence. The effect of such a presumption is that once it is shown that a person was in a position to dominate the will of the other, it will be assumed that this position was used to gain an unfair advantage, unless otherwise proven. The following cases illustrate where such a presumption arises:

### 2.1 UNCONSCIONABLE BARGAINS

When one party is in a position to dominate the will of the other, and the terms of the contract executed are apparently unconscionable and unfair, the law presumes that consent must have been secured by undue influence. The term 'unconscionable' was defined by the Supreme Court of Indian in *Central Inland Water Transport Corporation v Brojo Nath Ganguly* as something that shows no regard for conscience and is irreconcilable with what is

[148] Raghunath Prasad Sahu v. Sarju Prasad Sahu, (1924) 19 LW 470.
[149] Andhra Sugars Ltd. v. State of AP, AIR 1968 SC 599.

right or reasonable.[150] Once the presumption of undue influence arises, the dominating party bears the burden to demonstrate the transaction to be free from undue influence.

The Privy Council's decision in *Wajid Khan v Ewaz Ali Khan* is a useful illustration.[151] Here, an elderly and illiterate woman who was incapable of any business conferred an important pecuniary benefit under the guise of a trust to her managing agent, without any valuable consideration. The Privy Council ruled that since all signs pointed to an active undue influence, "the onus was on the grantee to show conclusively that the transaction is honest, bona-fide, the subject of independent advice free from undue influence."

It is noteworthy that the presumption of undue influence arises for unconscionableness only when one party is in a position to dominate the will of the other. This presumption does not arise with parties at an equal footing based on unconscionableness alone.[152] However, influence must be distinguished from persuasion because if a party is persuaded and thereby voluntarily enters into a transaction, it will be legitimate in the eyes of the law.[153] The following instances also serve as illustrations for when the presumption of undue influence arises:

i. Unconscionable bargains are more frequently witnessed in moneylending transactions and gifts. The Courts have taken this a step further. In *Bhimbha v Yeshwantrao*,[154] a farmer, unable to repay a loan within a fixed time period, executed a sale deed in favour of the creditor. The Bombay High Court set aside this sale, allowing repayment in a fixed period.
ii. Inequality of bargaining power between the parties, such that one may cause economic duress to the other, may also give rise to the presumption of undue influence. In *Lloyd's Bank v Bundy*, Lord Denning MR, speaking for the Court of Appeals ruled that where a contractor, unable to repay a loan, had executed a mortgage with the creditor bank, he was entitled to set aside the mortgage with unfair terms.
iii. Exploitation of the needy has also been used as grounds to presume undue influence. This has been seen in cases concerning songwriters and music publishing companies where the terms have been unfavourable to the songwriters not allowing them the right to terminate the agreement unlike the company,[155] or restricting the songwriter's publishing rights while retaining the right to reject the publication of his songs.[156]

### 2.2 CONTRACTS WITH A PARDANASHIN WOMAN

[150] Central Inland Water Transport Corporation v. Brojo Nath Ganguly, (1986) 3 SCC 156.
[151] Wajid Khan v. Ewaz Ali Khan (1890-91) 18 IA 144.
[152] (1924) 19 LW 470.
[153] Shrimati v. Sudhakar R. Bhatkar, AIR 1998 Bom 122.
[154] ILR (1900) 25 Bom 126.
[155] A. Schroeder Music Publishing Company v. Macaulay, (1974) 1 WLR 1308.
[156] Clifford Dav Management Limited v. W.E.A. Records, (1975) 1 WLR 61.

Contracts with *pardanashin* women are presumed to have been induced by undue influence. This presumption arises because a *pardanashin* woman is understood to be altogether secluded from social intercourse.[157] She may avoid the contract unless the other party can demonstrate that it was her "intelligent and voluntary" act,[158] and that the terms of the contract were fully explained to her causing her to freely consent. The extent of this burden has been clarified by the Privy Council.[159] It is not sufficient that the woman simply endorsed the contract and that there was some alleged consideration. The burden went further than that, to show that the transaction was bona-fide and fully consented to.

### 3. Remedy

The remedy for undue influence is found under Section 19-A of the Contract Act, 1872. Undue influence causes the contract to be voidable at the option of the party whose consent was so obtained. Such a contract may be set aside entirely in absolute terms, or in instances where the party seeking to avoid has received any benefit under the contract, upon conditions that the Court deems fit.

## MISREPRESENTATION

### 1. Misrepresentation in Common Law

According to Anson's Law of Contracts an operative misrepresentation "consists in a *false statement* of existing or past *fact* or *law* made by one party (the 'representor') *before or at the time* of making the contract, which is addressed to the other party (the 'representee') and which *induces* the other party to enter into the contract."[160]

There are certain exception where statement, though untrue do not amount to a misrepresentation. For instance, the expression of an opinion is generally insufficient to amount to a misrepresentation.[161] This holds for mere commendatory expressions or 'puffs' as well such as deodorant commercials which claim that the product being advertised is irresistibly attractive to members of the opposite sex.

In modern law, misrepresentation may be further categorised as 'fraudulent', 'negligent' and 'innocent' misrepresentations. The distinction between the three lies in the remedies available as a consequence. Fraudulent misrepresentations not only allowed the representee to seek rescission of the contract but also entitled the representee to an action for damages in respect of the deceit.[162] For negligent misrepresentations the representee has to elect whether to continue

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[157] Hondes v. Delhi & London Bank Ltd., (1899-1900) 27 IA 168, 175-76.
[158] Bellachi v. Pakeeran, (2009) 12 SCC 95.
[159] Moonshe Buzloor Raheem v. Shumsoonisa Begum, 1867 MIA 551 (PC).
[160] ANSON, *supra* note 9 at 301.
[161] Bisset v. Wilkinson, [1927] AC 177.
[162] ANSON, *supra* note 9 at 310.

with the contract and seek damages for losses suffered for the tort of misrepresentation. Or to rescind the contract and claim damages for any losses suffered after rescission. A party induced to contract by innocent misrepresentation has the right to rescind the contract, but is not entitled to claim damages, only an indemnity.[163]

## 1.1 FALSE REPRESENTATION

Generally, to constitute an operative misrepresentation, there must be a positive statement, or some conduct from which a statement can be implied. Mere silence does not amount to a misrepresentation.[164] Conduct that may amount to a statement could illustratively include 'a nod or a wink, or a shake of the head or a smile'.[165]

When assessing if a complex pre-contractual document contains a misrepresentation it is suggested to look at the matter more broadly and to assess whether the overall statements in the document are substantially correct. As compared to focussing 'more and more microscopically so as to concentrate on each sentence, phrase or word.'[166]

## 1.2 PARTIAL NON-DISCLOSURE OR ACTIVE CONCEALMENT

Notwithstanding the general position that mere silence does not amount to a misrepresentation, a partial non-disclosure may constitute misrepresentation. This is because the suppression of material facts can render facts already stated to be false. The determinative question is whether the representor's words or actions have misled the representee and have induced the conclusion of the contract. An important case to consider on this point is *R v Kylsant*,[167] where the prospectus of a company stated that it was regularly paying dividends. This created the impression that it was making profits. The truth was that the company had been making losses for several years. Dividends were being paid only out of wartime accumulated profits. The suppression of this fact was held to be a misrepresentation.

## 1.3 CHANGE IN FACTS

To constitute a misrepresentation a statement must be false before or at the time when the representee relies upon it to enter into the contract. If the representation is true at the time it is made but becomes false subsequently, before the contract is concluded, it becomes a

[163] *Id.* at 311.
[164] Keates v. Lord Cardogan (1851) 10 CB 591.
[165] Walters v. Morgan (1861) 3 De GF & J 718, 724 (Lord Campbell).
[166] Avon Insurance plc v. Swire Fraser Ltd [2000] 1 All ER (Comm) 573,632 (Rix J).
[167] (1932) 1 K.B. 442.

misrepresentation at the time at which the representor knows it to be false. Courts treat such cases as cases of continuing representations.[168]

### 1.4 REPRESENTATIONS OF LAW

A misrepresentation of law was not held to constitute a misrepresentation in common law until recently.[169] Distinguishing between representations of law and those of fact can prove a tricky exercise because some statements of law contain statements of fact and vice versa. For instance questions on whether a dwelling-house is 'new' for the purposes of the rents act. Misrepresentations of foreign law have also been treated as misrepresentations of fact.[170] Anson's Law of Contract argues that there is no reason for wilful misrepresentation of the law, should not be viewed as a representation of opinion.[171] The position of law has now changed and misrepresentations of law are now capable of securing the same remedy as misrepresentations of fact.

## 2. Misrepresentation in Indian Law

### 2.1 'MISREPRESENTATION' DEFINED

Section 18 of the Indian Contract Act, 1872 defines 'Misrepresentation' to mean and include:

1. Unwarranted Positive Assertions
2. Breach of Duty
3. Inducing Mistake over subject-matter of contract

#### *2.1.1 Unwarranted Positive Assertions*

Any positive assertion that something is true, may amount to the truth even when the speaker believes it to be the truth. Misrepresentation is established when the speaker's information does not warrant such an assertion. A statement is warranted when the person making it receives such information from a reliable and trustworthy source.[172] Mere hearsay does not meet this requirement.

When a representation acquires the status of a term of a contract and is proven to be untrue, the aggrieved party can both sue for damages for such breach, and avoid the contract. The falsity of a statement alone is relevant to determine it to be a misrepresentation, not the intention behind such a statement, howsoever innocent. An illustration of this is found in the Canadian case

[168] Davies v. London & Provincial Marine Insurance Co., (1878) 8 Ch D 469, 475.
[169] Goff v. Gauthier, (1991) 62 P & CR 388.
[170] Laurence v. Lexcourt Holidngs Ltd [1978]
[171] ANSON, *supra* note 9 at 304; Beatti v. Lord Ebury, (1872) LR 7 Ch App 777.
[172] AVTAR SINGH, CONTRACT AND SPECIFIC RELIEF, 194 (2013).

*Alessio v Jovica*.[173] The buyer in this case purchased a plot of land specifically for the construction of a duplex. The seller represented that he saw no difficulty in such a use of the land. Permission to build such a complex was refused unless sewage costing 3000 dollars was provided. The court allowed the buyer to avoid the contract, though the misrepresentation was innocent.

### *2.1.2 Breach of Duty*

Any breach of duty which brings an advantage to the person committing it, by misleading another person to her prejudice. The intention to deceive is not relevant in this case as well. Such misrepresentation is also termed 'constructive fraud' because even if there is no intention to deceive, the party breaching such a duty is held equally answerable in effect as someone acting on motives of fraud or deceit.[174]

Notwithstanding the broad nature of the duty of care described above, the Madras High Court has stated 'as a matter of sound reasoning' that it is no defence for persons of full age who were literate and sign a document to say that they affixed their signatures to a blank document or that they signed a contract without appraising themselves of the recitals.[175] On the other hand, in *Oriental Bank Corporation v John Fleming*,[176] the plaintiff signed a deed without having the time to read its contents based on the impression created by the defendant that the deed contained nothing but matters already settled. The deed contained a release in favour of the defendant. The court allowed

### *2.1.3 Inducing Mistake about the Subject-matter of Contract*

Causing, however innocently, another party to an agreement to make a mistake regarding the subject matter of an agreement is misrepresentation. Parties enter into contracts because they deem the subject-matter of the contract to possess some value or quality. If one party causes another to make a mistake as to the nature or quality of the subject matter, howsoever innocently, then it amounts to a misrepresentation.

## 2.2 SUPPRESSION OF VITAL AND MATERIAL FACTS

Misrepresentation may arise from suppression of vital facts. Where such a suppression of fact amounts to a breach of duty it will be misrepresentation under Section 18(2) of the Contract Act. Where such a suppression of fact leads to a mistake as to the subject matter of the contract it will constitute misrepresentation under Section 18(3) of the Contract Act.

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[173] Alessio v. Jovica, (1973) 42 DLR (3d) 242, Canada.
[174] Oriental Bank Corporation v. John Fleming, ILR (1879) 3 Bom 242, per Sargent LJ at p. 287.
[175] Chokkammal v. K. Balraj, (2008) 5 CTC 690.
[176] Khandu Charan Polley v. Chanchala Bhuiyan, AIR 2003 Cal 213.

Misrepresentation must pertain to facts material to the contract. A fact may be said to be material if it would affect the judgement of a reasonable person in concluding the contract. For example, if a car was represented to be 5 years younger than it really was, this would amount to a misrepresentation of a material fact. The age of the car is material because it determines the price a buyer is willing to pay.[177]

Just as in common law, a mere ‘commendatory expression’ or ‘puff’ is an insufficient ground for avoiding the agreement. A statement that land was ‘fertile and improvable’ would not amount to a misrepresentation when it was later found that parts of it were abandoned and useless.[178] On the other hand, the description of a tenant as being ‘most desirable’ would not be considered a mere puff, when in reality his rent was in arrears.[179] Similarly, a mere expression of opinion cannot be regarded as a misrepresentation even if the opinion subsequently turns out to be wrong.

### 2.3 MEANS OF DISCOVERING TRUTH

A party cannot claim misrepresentation if she had the means of discovering the truth with ordinary diligence. This principle is enshrined in Section 19 by way of an exception, which reads:

“If such consent was caused by misrepresentation or by silence, fraudulent within the meaning of Section 17, the contract nevertheless is not voidable, if the party whose consent was so caused had the means of discovering the truth with ordinary diligence.”

This exception becomes complicated when considering whether a person has the means of discovering the truth, but does not use them, relying upon the representations made instead. Where reliance is placed on the representations made and not upon the means available to discover the truth, then the contract may be avoided. The English Court of Appeal’s decision in *Redgrave v Hurd*[180] captures this principle:

“If a man is induced to enter into a contract by false representation, it is not sufficient for him to say: ‘If you had used due diligence you would have found out that the report was untrue. You had the means afforded you of discovering its falsity, which you did not choose to avail yourself of.’”

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[177] Baker v. Asia Motor Co. Ltd., 1962 MLJ 425.
[178] Dimmock v. Hallett, (1866) 2 Ch App 21.
[179] Smith v. Land & House Property Corpn, (1884) 28 Ch D 7 (CA).
[180] (1881) 20 Ch D 1.

This principle finds its application in modern company law when a prospectus containing false statements is issued. Those who accept such statements are not deprived of a remedy for failure to exercise their due diligence.

## FRAUD

An intentional misrepresentation of facts can be used to broadly explain "fraud".[181] Broadly speaking, fraud ensues from the application of the "writ of deceit" in tort law to a contractual setting. Section 17 exhaustively defines fraud. However, the section is only concerned with the effect of fraud, so far as it is material in procuring the consent of either party. It would not apply to fraudulent actions committed in the course of the performance of the contract.[182] A bare reading of Section 17(1) reveals the following constituent elements required to establish fraud;

a. There should be a suggestion as to a fact;
b. The fact suggested should not be true;
c. The suggestion should have been made by a person who does not believe it to be true; and
d. The suggestion should be made with intent either to deceive or to induce the other party to enter into the contract.[183]

### 1. Essential Ingredients of Fraud

Firstly, there should be a representation by one of the parties. This representation is nothing but a statement of fact. However, it is distinct from a statement of opinion[184], though in certain circumstances, a statement of opinion may be regarded as a statement of fact. Moreover, this representation has to be material to the extent that it may influence a reasonable man in deciding whether to enter into a contract or not.[185]

Secondly, the representation should be nothing but a false assertion made with intent to deceive the party or induce him to enter into the contract. Lord Herschell in *Derry v. Peek*[186] laid down the common law principles that capture the essence of fraud. Accordingly, fraud can only be proved when it is shown that a false representation has been made (i) knowingly; or (ii) without belief in its truth; or (iii) recklessly careless, whether it be true or false. *In R.C.*

[181] AVTAR SINGH, CONTRACT & SPECIFIC RELIEF 210 (12th ed., EBC 2017)
[182] Jamsetji Nassarwanji v. Hirjibjai Naoroji, (1913) 37 Bom 158; Fazal D Allana v. Mangaldas M Pakvasa, AIR 1922 Bom 303.
[183] R.C. Thakkar v. Gujarat Housing Board, AIR 1973 Guj 34 at 44.
[184] Bissett v. Wilkinson, [1927] AC 177.
[185] Bhagwan Bai v. Life Insurance Corporation of India, AIR 1984 MP 126.
[186] [1886-90] All ER 1 at 22.

*Thakkar v. Gujarat Housing Board,*[187] a public authority had invited tenders and had mentioned the cost estimates in the tender notices. However, the estimates turned out to be incorrect. It was held that mention of the cost estimates amounted to making a representation to the interested bidders that the concerned public works would cost a particular amount. Hence, it was related to material facts, as bidders would be led to believe in the cost estimates given by the public authority. Moreover, it was held that "a man making any representation, which he intends other to act upon, must be taken to warrant his belief in its truth." In other words, it is the actual and honest belief in the truth of the representation that matters. If a person, making a statement believes it to be untrue or has knowledge of its falsehood, the he is guilty of fraud.

Statements made without any belief in their truth include statements made recklessly. They show indifference on part of person making the representation as to the truth or falsehood of his representation. In fact, even mere ignorance as to the truth or falsehood of an assertion is equivalent to the knowledge of its falsehood, if it turns out to be untrue.[188] Lastly, it is unnecessary to prove motive when a false statement is knowingly made.[189]

**2. Active Concealment**

The essential ingredients required to establish active concealment have been laid down in Section 17(2). It is fraud where a person who knows or believes a fact to be truth, but actively conceals it from the other party with an intention to induce that person to enter into a contract. Section 17(2) has to be read along with the Explanation which postulates that mere silence does not amount to fraud.

**3. Where Silence is Fraud**

However, it should be noted that the Explanation does not lay down that silence *per se* is fraud. But then how far silence may go? Silence may amount to fraud, if 1) there is a duty to disclose; 2) silence is equivalent to speech; 3) there is a change in circumstances; 4) half-truths.

**3.1 DUTY TO DISCLOSE**

There does not exist any general duty to disclose. In other words, it does not require the disclosure of facts which could be discovered by parties through ordinary means. In *Bell v. Lever Bros Ltd,*[190] the parent company had agreed to pay a large compensation to directors of

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[187] *Supra*, note 56..
[188] Bhadbade, *supra* note 1, at 391.
[189] United Motor Finance v. Addison & Co. Ltd., AIR 1937 PC 21.
[190] [1931] All ER Rep 1.

its subsidiary company, whose services were being terminated. After payment of compensation, the company discovered that the directors had committed breaches of duty that would lead their dismissal without compensation. The House of Lords held that the directors were under no duty to disclose the breaches committed by them.

The principle that there is no duty to disclose during the negotiations for an ordinary commercial contract stems from the view that each party is under an obligation to obtain the necessary information by himself and cannot expect the same to be, supplied by the other party, even when that other is aware of his ignorance.[191] However, this common law principle has been severely criticized, because it seems to be only suitable for transactions between knowledgeable businessmen. It cannot be effectively applied to dealings between private persons.

The duty referred to in the Explanation is legal duty and not a moral one.[192] This duty generally arises in particular classes of contracts where one of the parties is utterly without any means of discovering the truth and has to depend on the good sense of the other party. Such classes of contracts include contracts between an insurer and insured etc., or where one party stands in a fiduciary relationship with the other. In a contract of insurance, the insurer does not possess any knowledge of the life or circumstances of the insured. Henceforth, a duty is cast on the insured to disclose to the insurer all the material facts which affect the risk covered under the insurance contract with candour and completeness. A contract for insurance, for this reason, is called a contract *uberrima fides* or contracts of absolute good faith. A duty to disclose, of a particular defect in goods may exist because of trade usage. In such cases, omission to disclose particular defects amounts to an assertion that they do not exist.[193]

### 3.2 SILENCE IS EQUIVALENT TO SPEECH

Silence may become deceptive when it amounts to speech. A person who chooses to remain silent, knowing very well that his silence may be deceptive, is guilty of fraud. Illustration (d) of Section 17 stipulates that a buyer who has more knowledge about the value of the property which is subject to sale, but prefers to keep the information from the seller, the latter may avoid the sale.

### 3.3 CHANGE OF CIRCUMSTANCES

Sometimes a factual assertion is true, when made, but, it may, on account of a change in circumstances, become false when actually acted upon by the other party. In such cases, it is

[191] Banque Financiere de la Cite SA v. Westgate Insurance Co. Ltd, [1990] 2 All ER 947.
[192] Sher Khan v. Akhtar Din, AIR 1937 Lah 598.
[193] Jones v. Bowden, (1813) 4 Taunt 847.

the duty of the person who made the assertion to disclose the change in circumstances. For example, the prospectus of a company contained a statement certifying that certain persons were the directors of the company. On the basis of this statement, which was true when made, certain persons applied for allotment of shares. However, before such allotment could took place, certain directors retired from the company. This change in circumstances was not communicated to the applicants. The Madras High Court held that they were entitled to avoid the allotment.[194]

### 3.4 HALF-TRUTHS

A person, who is under no duty to disclose, may become guilty of fraud by suppression of facts if he voluntarily discloses a part of the facts and then stops half –way. In such a case, the statement is false in substance and the wilful suppression makes it fraudulent. Lord Macnaughtan in *Gluckstein v. Barnes*[195]stated that "everybody knows that sometimes half a truth is no better than a downright falsehood."

### 4. Promise Made Without Intention of Performing

Section 17(3) includes a third type of fraud where a promise made with no intention of performing it at the time of making such promise amounts to fraud. Any subsequent conduct or representation is immaterial. A purchase of goods without any intention of paying the price is a fraud which entitles the seller to rescind the contract.[196] It is a fraud to obtain or use property, under a contract by professing to use it for some lawful purpose when the real intention is to use it for an unlawful purpose.[197]

### 5. Any Other Act Fitted to Deceive

The mention of 'any other act fitted to deceive' as a fourth type of fraud in Section 17(4) is merely for the sake of abundant caution. A person who signed an agreement with the knowledge that the other party had recorded it erroneously, did so, fraudulently as he sought to take advantage of the error, is guilty of fraud.[198]

### 6. Any Act or Omission Declared Fraudulent by Law

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[194] T.S. Rajagopala Iyer v. South Indian Rubber Works, (1942) 2 MLJ 228.
[195] 1900 AC 240 at 250.
[196] Clough v. London North Western Rail Co., (1871) LR 7 Ex 26; Whitaker, *ex p*, (1875) LR 10 Ch 446 at 449.
[197] Feret v. Hill, (1854) 15 CB 207.
[198] William Charles Binnus v. W&T Avery Ltd, AIR 1934 Cal 778.

Section 17(5) deals with this special category of fraud where certain factual disclosures are especially required by law, and non-compliance with the same is expressly declared as amounting to fraud. Section 17(5) intends to cover all acts or omissions which are regarded fraudulent under any other branch of law. A pertinent example would be Section 55 of the Transfer of Property Act, 1882 which requires the seller of the immovable property to disclose to the buyer any material defect in the property itself or the seller's title to the property, which the buyer is not aware of, and which he could not with ordinary care discover.

## MISTAKE

As discussed earlier, the foundation of any contract is consent i.e. parties agree upon the same thing in the same sense. Unlike other vitiating factors of consent such as coercion, undue influence, misrepresentation, fraud, mistake attacks this very foundation. In *Bell v. Lever Bros Ltd,*[199] it was held that "if mistake operates at all, it operates so as to negate or in some cases nullify consent. When parties are prevented by virtue of mistake from reaching an agreement where one party intends to contract about a particular thing and the other about another, there is no real consensus. This lack of real consensus negatives consent. When parties agree on the same thing, but their agreement is based on mistaken beliefs as to the terms of the contract, it can be said that such mistakes nullify consent. Section 20 deals with mistake that nullifies consent.[200]. On the other hand, mistakes which negative consent are largely dealt under Section 13 as they go to the root of the contract.

### 1. Mistakes Going to the Root of the Contract

A contract may be void where the parties contract under a false and fundamental assumption, going to the root of the contract, and which both of them must be taken to have in mind at the time they entered into it as the basis of their agreement. This form of mistake is not distinct from other forms of mistake which are discussed in subsequent sections. Instead, it provides a general test that can be applied to mistakes as to non-existence of subject-matter, its quality or substance etc. This test is based on 'fundamental assumptions' and received approval in *Bell v. Lever Bros Ltd,* although some concerns were raised regarding the applicability of this test owing to its vague formulation by the judges. This test is based on the impossibility of performance, although this must be interpreted as not limited to physical impossibility but extending to commercial impossibility: the shared purpose of the contract cannot be fulfilled, through no fault of the either party and where neither party has undertaken the risk of non-performance.

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199 [1932] AC 161.

200 ITC Ltd., v. George Joseph Fernandes, AIR 1989 SC 839.

In *Bell v. Lever Bros Ltd,* an agreement of service between the parent company and two directors of its subsidiary company was terminated after payment of compensation by virtue of a compensation agreement. Later, it was found out that the directors had engaged in misconduct which resulted in them earning secret profits. This would have entitled the parent company to immediately terminate their services without payment of compensation. Subsequently, the company brought an action for repayment of money on the ground that it was paid under a mutual mistake of fact. The action failed as the House of Lords held that the mistake was related to the quality of service rather than the subject matter of employment contract as the directors did not have in their mind breaches of duty while they entered into the agreement for compensation nor had the parent company contemplated that they had the right to terminate the contract of service of the directors without payment of compensation. Lord Thankerton held that: "*The phrase 'underlying assumption by the parties', as applied the subject-matter of the contract.....can only properly relate to something which both must have necessarily accepted in their minds as an essential and integral element of the subject-matter*."[201] In the present, this requirement was not fulfilled. On its true construction, the compensation agreement applied notwithstanding the termination of the agreement of service.

## 2. Mistake under Section 20

The Indian law on mistake is captured by Section 20. According to this section, the essential ingredients required to establish mistake are as follows;

1. It has to be the mistake of both parties
2. It must be a mistake of fact, and
3. The fact must be essential and not incidental or subsidiary to the agreement.

Thus, any agreement that contains the aforementioned ingredients would be void. Moreover an Explanation is appended to this Section. It provides that an erroneous opinion regarding the value of the subject-matter is not deemed to be a mistake of fact.

### 2.1 MISTAKE OF BOTH THE PARTIES

In order to render a contract void under Section 20, the mistake must have been committed by both the parties. In India, a mistake by a single party or a unilateral mistake would not only suffice because of Section 22 which states that if one party is alone under a mistake of fact, the contract is not rendered merely voidable on that ground. However, the language of Section 22 does not preclude the operation of other vitiating factors such as

[201] *Supra* note 72, at 235.

misrepresentation, fraud etc. alongside mistake so as to render the contract voidable.[202] It means that if unilateral mistake is compounded by some other vitiating factors, unilateral mistake may also become a ground of nullity.

## 2.2 MISTAKE OF FACT AND NOT LAW

According to Section 21, a mistake as to any law which is in force in India does not render a contract voidable at the hand of parties. However, the section distinguishes between mistake of Indian law and a mistake of the law of any foreign country. Mistake of foreign law is considered as a mistake of fact and allows parties to avoid the agreement. On several issues, it becomes very difficult to separate mistakes of law from mistakes of fact. For example, in a liquidation case the liability of the bank to clear the dues of the creditors depends upon capacity in which the bank holds the funds. More often than not, this is a question of both fact and law. If the agreement between the banker and the debtor clearly defines the status of the bank, then it should be regarded as a matter of fact.

## 2.3 MISTAKE OF ESSENTIAL FACT

Broadly speaking, there are certain facts which are essential to every agreement. They can broadly be divided into the following three categories;

1. The identity of the contracting parties
2. The identity and nature of the subject matter of the contract, and
3. The nature and content of the promise.

### 2.3.1 Mistake as to the Identity of Contracting Parties

Mistake as to identity generally occurs where one of the parties represents himself to be some person other than who he really is. In view of the fact that Indian decisions are scanty in this regard, English judgements have been considered for analysis.

In *Hardman v Boothe,*[203] the plaintiffs were meaning to deal with Thomas, Gandell & Sons, went to their office and took an order from a man who represented himself to be Edward Gandell, a partner in the firm. He received the goods and sold them to the defendant, a *bona fide* buyer. The plaintiff sued the defendants to recover their goods. It was held that although a contract was made personally with Edward Gandell, but what the plaintiffs intended to do was enter into a contract Gandell & Co. The facts were such that Edward Gandell was neither a member of the firm, nor had any authority to act as the agent of Gandell & Co. Therefore,

[202]Bhadbade, *supra* note 1,at 480.
[203] (1862) 27 LJ 117 [118-19].

Gandell & Co. were not the buyers, and at no time were there consenting minds drawn together to the same agreement.

This operative scope of mistake as to identity was further reduced when the parties contract in each other's presence. In *Philipps v. Brooks*,[204] a man, called North, entered the plaintiff shop and selected some jewellery. While signing a cheque for the amount he said "You see who I am, I am Sir George Bullough." The plaintiff let him have some the jewellery after finding a reference in the directory that a certain Sir George Bullough lived at the address mentioned by the man called North. He promised to return for the rest of the jewellery once the cheque was cleared. However, before the fraud could be discovered, he pledged the jewellery in his possession with the defendants who advanced money *bona fide* and without notice. Later the plaintiff sued the defendants for the value of the pledged jewellery. Horridge J. held that although the plaintiff believed the person to whom he handed the jewellery was Sir George Bullough, he in fact had contracted to sell the jewellery to the person who had come to his shop whom he identified by sight and hearing. Henceforth, the contract was not void on the ground of mistake, but only voidable on the ground of fraud, and therefore the defendants had acquired good title to the ring. This decision created an impression there cannot be a mistake as to the identity of the contracting parties when they are face to face as it would lead to an inference that each one of them intended to contract with the other and not with someone else.

However, Court of Appeal in *Ingram v. Little*[205] differed from *Phillips v. Brooks.* Herein, three ladies, joint owners of a car posted an advertisement for its sale. An interested person contacted them and offered to pay a reasonable price. He chose to pay through a cheque. However, the ladies refused to accept a cheque. He was able to convince them that he was Hutchinson, a leading businessman. He produced an address and a telephone number to buttress his claim. After verification of the particulars from the directory, the ladies accepted the cheque and gave him the car. The impostor resold the car to the defendants and absconded. Later, the cheque also proved worthless and the plaintiff sued the defendants for the recovery of the car or its value. It was held that the plaintiffs in their minds had exclusively made an offer to the real Hutchinson. The physical presence of the impostor did not dictate the identity of the real party which the ladies intended to contract with in the first place. Hence, the imposter did not acquire a good title to the car which he could convey to the defendant. In his dissenting opinion, Devlin J. emphasized the need for a more practical approach where the title of an innocent party is not dependent on the contractual relationships of third parties.

This approach was later adopted by the Court of Appeal in *Lewis v.* Avery.[206] A man, named Lewis had a car to sell. A person, who described himself as Richard Greene wanted to buy

[204] (1919) 2 KB 243.
[205] (1960) 3 All ER 332.
[206] (1971) 3 All ER 907.

the car and offered a cheque. Lewis was reluctant to hand over the car till the cheque was cleared. In order to prove his identity, the impostor produce a special pass of admission to a film studio. The plaintiff got convinced and allowed him to take away the car. The impostor resold the car to the defendant. Later, the plaintiff sued the defendant for recovery of the car. Lord Denning, after analysing the previous cases, held that it would be unjust to allow an innocent purchaser to suffer because the seller was mistaken as to the identity of a person whom he had contracted with. The innocent buyer had acted in good faith and knew nothing about the dealings between the seller and the rogue. Hence, his title cannot be negated just because the seller let the rogue have the goods by virtue of a mistake as to his identity. Moreover, he was of the view that a mistake as to the identity of a contracting party and mistake as to his attributes are one and the same thing as it is difficult to objectively separate them. He refused to accept that mistake as to identity is capable of rendering a contract void.

In *Shogun Finance Ltd. v. Hudson,*[207] the majority preferred to hold a hire purchase agreement for a car between a rogue and a finance company void. Thus, the innocent buyer was left without any recourse but to return the car to the finance company. This approach reflects the current position in common law. It links the passage of title to an innocent party with the validity of an earlier contract. The minority in *Shogun* adopted the practical approach advocated by Lord Denning and called for a radical reconsideration of the existing position as theoretical considerations such as the status of a contract should not come in the way of doing practical justice.

### 2.3.2 Mistake as to the Nature of Subject Matter

A mistake as to the subject-matter of the contract negatives the presence of *consensus ad idem* between parties as to the subject matter in question. This usually revolves around the existence of the subject-matter and its substance.

#### 2.3.2.1 Non-existent Subject Matter

A mistake of this type occurs usually when the subject-matter may have ceased to exist before the contract was made. In *Gustavus Couturier v. Robert Hastie*,[208] the defendant was hired by the plaintiffs to sell a cargo of Indian corn to a third person. After the defendant had entered in a contract for sale with a third party, it was discovered that a fortnight before the contract was made, the cargo had to be sold at an intermediate port as it was damaged due to bad weather. Consequently, the third party buyer repudiated the contract. The court held that the contract was void *ab initio* as none of the parties were aware that the goods had been destroyed at the time of entering into the contract. Hence, the contract was vitiated by mistake as to the existence of subject-matter.

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[207] [2004] 1 AC 919.
[208] (1856) 10 ER 1065.

### 2.3.2.2 Substance of the Subject Matter

In *Seikh Bros Ltd. v. Ochener*,[209] the appellants granted a license to the respondent to cut and process sisal trees in a forest. The respondents undertook to process and deliver 50 tons of sisal fibre every month. But it turned out that the leaves of the sisal trees did not have the potential to produce the stipulated quantity of fibre. The respondent was sued for breach. It was held that the contract was void as both parties were mistaken as to an essential fact (the fibre-producing potential of the sisal tree leaves) which formed the substance of the contract.

However, a mistake as to the quality of the subject-matter as distinguished from its substance may not render the agreement void. In *Smith v. Hughes*,[210] the defendant wanted to purchase old oats for his horses. The plaintiff gave him some samples of oats he had, but said nothing about their age. The defendants eventually placed an order. After a portion of the oats was delivered, he found out that the oats were new. He rejected them on the ground that he was mistaken about their quality. The court held that there was consensus *ad idem* between the parties for sale and purchase of oats. Henceforth, the substance of the agreement was the sale, rather than the quality of oats. The quality of the goods would not be relevant in the present case. Hence, a mistake as to quality would not render an agreement void unless it forms the substance of an agreement.

### 2.3.2.3 Different Subject-matters

At times, parties may also have completely different subject matters in mind due to a reasonable mistake of fact. This would render an agreement void for want of true consensus *ad idem.* In *Raffles v. Wichelhaus,*[211] the parties had in mind different ships which went by the same name. The court held that there was no binding contract as parties had different subject-matters in mind.

### 2.3.3 Mistake as to the Nature of Promise

It is a well-established principle that when a deed of a particular character is executed under the mistaken impression that it is of a different character, such a deed is void.[212] For example, where a gift deed was signed under a mistaken impression that it was a power of attorney, it was held to be void.[213] A mistake of this kind is generally brought about by fraud of one party. One of the parties owes a duty to disclose the true nature of the document but fails to do so. This induces the other party to sign the document under the belief that he is signing some instrument of a different nature. Moreover, the Supreme Court has held that a

[209] 1957 AC 136.
[210] (1871) LR 6 QB 597 at 609.
[211] *Supra* note 4.
[212] Appanna v. Jami Venkatapaddu, AIR 1953 Mad 611; Mandakini Pundalik Salker v. Chandrasen Raiker, AIR 1986 Bom 172.
[213] Sarat Chandra v. Kanailal, AIR 1929 Cal 786.

distinction must be made between a fraudulent misrepresentation as to the character of a document and a fraudulent misrepresentation as to its contents.[214]

### 2.3.3.1 Non-est Factum

The defence of *non-est factum* allows a party who has signed a document to plead that it is not his document because he signed it under a mistake. This doctrine was originally developed for the benefit of blind and illiterate people to relieve themselves from the effect of a contract which they could not have read and which was also not explained to them properly.[215] In *Foster v. Mackinnon*[216], a person was induced to sign on the back of a paper. The true face of the paper which captured its contents was not shown to him. He was verbally told that it was an ordinary guarantee the likes of which he had executed in the past. The paper turned out to be a bill of exchange. The holder of the bill sued that person as an endorser of the bill. The court held that the mind of the signor never accompanied the signature. He never intended to sign an instrument which was negotiable.

It must be emphasized that *non-est factum* offers a very narrow defence. It is not available to a person of full understanding and capacity who carelessly omits to read a document before signing it. If a document signed is fundamentally different from what the signor intended it to be, he will not be entitled to disown his signature as against a third part unless he can prove that he exercised reasonable care.[217]

At one time, the common law position was that the defence of *non-est factum* would not be available if the mistake was as to the contents of the document, as opposed to its character.[218] However, the common law position later changed. The difference between character and contents was now not considered to be very intelligible, for a document takes its character from its contents. In *Saunders v. Anglia Building* Society[219], this distinction was rejected by the House of Lords in favour of a more flexible approach: that there must be a 'radical' or 'essential' or 'fundamental' or 'very substantial difference' between the document signed and the document the person intended to sign.

As discussed earlier, the Indian position differs from the common law position as it recognizes the distinction between the character and contents of a document.[220] In another case of the same kind, an illiterate woman was asked by her son-in-law and his brothers to put her thumb impression upon two stamp-papers which meant that she was gifting her land to her daughter. However, one of the stamp-papers contained a sale-deed by which the son-in-law and his brothers became registered owners of the land. The Supreme Court held that

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[214] Ningawawa v. Byrappa Shiddappa Hireknrabar, AIR 1968 SC 956 [958].
[215] Bhadbade, *supra* note 1, at 317.
[216] [1861-73] All ER Rep 1913.
[217] Saunders v Anglia Building Society, [1971] AC 1004 at 1025.
[218] Howatson v Webb, [1907] 1 Ch 537.
[219] *Supra* note 90, at 1017-19.
[220] *Supra* note 90.

the documents were void due to a mistake as its character induced by fraudulent misrepresentation.[221]

[221] Dularia Singh v. Janardan Singh, AIR 1990 SC 1173.

## MODULE IV

# LIMITATIONS ON FREEDOM OF CONTRACT

### PRINCIPLE OF FREEDOM OF CONTRACT

Freedom of contract means "Right of an adult to make a legally binding mutual agreement with one or more other persons, without governmental interference as to what type of obligations he or she can take upon himself or herself." But there are certain limitations on the said freedom of an adult and the agreements which violate these limitations are void.

### VOID AND VALID AGREEMENTS

**Void Agreements:** The Act defines void agreements under Section 2(g) as "an agreement not enforceable by law is void". A void agreement therefore does not give rise to any legal consequences, is void from very beginning and is a nullity in eyes of law. The following types of agreements are expressly declared to be void under the Act:

1) Agreements of which consideration and objects are unlawful in part (Sec 24)
2) Agreements without consideration (Sec 25)
3) Agreements in restraint of marriage, (Sec 26)
4) Agreements in restraint of trade, (Sec 27)
5) Agreements in restraint of legal proceedings, (Sec 28)
6) Unmeaning Agreements, (Sec 29)
7) Wagering Agreements, (Sec 30) and
8) Agreements to do impossible acts. (Sec 56)

**Valid Agreements:** These are agreements enforceable by law. They satisfy all the essentials of a valid contract laid down under Section 10 of the Act. Valid agreements are defined under Section 2(h) as "an agreement enforceable by law is a contract." The things necessary to establish a valid contract include: Capacity, Consideration, Lawful object and consideration and free consent.

### UNLAWFUL CONSIDERATION OR OBJECT

An agreement is a contract only if it is supported by lawful consideration for a lawful object as under Section 10.[222] Section 23[223] of the Indian Contract Act, 1872, elucidates circumstances wherein considerations or objects can be deemed unlawful. It reads as follows,

[222] Section 10, Indian Contract Act, 1872.
[223] Section 23, Indian Contract Act, 1872.

The consideration or object of an agreement is lawful, *unless*-

a) it is forbidden by law; or is of such nature that, if permitted, it would defeat the provisions of any law; or
b) is fraudulent; or
c) involves or implies injury to the person or property of another or;
d) the Court regards it as immoral, or opposed to public policy.

Every agreement of which the object or consideration is unlawful is void. Thus, the rights of the person entering into contract are subject to limitations founded in overriding considerations of public policy, statutory illegality and others enunciated under it.

The term *'object'* under section 23 connotes the purpose or design of the contract[224]. Consideration received in furtherance of the contract is thus different from the object or purpose driving the contract. Thus, even though the consideration received may be lawful, a contract could still be deemed illegal and hence void due to an unlawful object. This illegality is assessed along the standard laid down in section 23 and judicial pronouncements that have clarified the scope of these limitations on contractual freedom. In determining the validity of the contract, the object of the agreement and not action actually taken under the agreement should be considered.

## I. FORBIDDEN BY LAW OR DEFEAT PROVISIONS OF ANY LAW

The term "*forbidden by law*" marks the first limit to contractual autonomy. All considerations and objects that are expressly forbidden by law or defeat the provisions of law would thus render the contract void. A bare possibility of the transgression of the provisions of any law does not invalidate the agreement. 'Law' in this case means judicial law enacted by the government, whether criminal law, special legislative enactments, regulations or orders. In the event that there is no express prohibition by the law, the imposition of penalties is sufficient to imply a prohibition, for instance a contract in contravention of provisions of the Motor Vehicles Act. Whether the object or consideration violates these provisions will depend on the intention that can be gathered from the Act said to be violated.

"*If permitted, it would defeat the provisions of law*" refers to the *performance* of an agreement which would necessarily entail a transgression of provisions of the law. The general rule followed by courts is in case the express provisions of any law is violated by a contract, the interests of the parties or of third parties, would be injuriously affected by its fulfillment. The general rule of law is that facts showing illegality must be pleaded, and if one of the contracting parties challenges an agreement as being unenforceable, the burden

[224] Pollock and Mulla, Indian Contracts Act, 1872 (8th Edn.).

lies on him to show the circumstances that made it so.[225] The laws in question are legislative enactments in India, provisions of Hindu or Muslim law or any other law in force at the time. For example, if A, B and C enter into an agreement for the division among them of gains acquired by them by fraud. The agreement is void, as its object is unlawful.

Thus, an agreement or contract is rendered unenforceable or void if, *first,* the purpose is the commission of an illegal act, *second,* if it is expressly or impliedly prohibited by any law and *third,* if its performance is not possible without disobedience of any law. According to Anson[226], "*The law may either forbid an agreement to be made, or it may merely say that if it is made, the courts will not enforce it. In the former case, it is illegal, in the latter only void, but in as much as illegal contracts are also void, though void contracts are not necessarily, the distinction is for most purposes not important and even judges seem to treat the two as inter-changeable*". The Court in the case of *Rajat Kumar Rath vs Government of India*[227] reiterated this distinction, highlighting how an illegal agreement taints the transactions collateral to it, though a contract that is void though not by virtue of illegality does not have the same effect on collateral transactions.

## II. FRAUDULENT

When the object of an agreement is to cheat the other party by concealment of any material fact or otherwise, it is said to be fraudulent.[228] For instance, A, being agent for a landed proprietor, agrees for money, without the knowledge of his principal, to obtain for B a lease of land belonging to his principal. The agreement between A and B is void. as it implies a fraud by concealment, by A, on his principal. When the object of an agreement between A and B was to obtain a contract from the Commissairate Department for the benefit of both, which could not be obtained for both of them without practicing fraud on the Department. The agreement being fraudulent, is thus void.

## III. INJURY TO PERSON OR PROPERTY OF ANOTHER

As per the provisions of section 23, an agreement which involves causing injury to a person or property of third party is void and cannot be enforced by court and therefore, no claim is sustainable for the breach of such an unlawful agreement. So, an agreement which compels a debtor to do manual labor for the creditor as long as the debt is not repaid in full is void. Similarly, an agreement to destroy the residence of another is void under the Act.

## IV. IMMORAL OR OPPOSED TO PUBLIC POLICY

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[225] B.V.R. Sarma, Lawful objects and considerations under Section 23 of Indian Contract Act 1872 – An analysis. (Manupatra 2016).

[226] ***Principles of the English Law of Contract, 22nd edn.***

[227] Rajat Kumar Rath v Government of India, ***AIR 2000 Ori 32, 34-35***

[228] Harsimran Singh, Section 23 Of Indian Contract Act – Lawful Considerations and Objects (Mondaq 2015).

The understanding of objects and considerations that amount to *immoral* in the eyes of the court must be assessed on *standards of morality prevailing at a particular time* and approved by courts. For example, A agrees to let her daughter to hire to B for concubinage, this constitutes an agreement void on the ground of immorality.

The Act also fails to define what is meant by "public policy". It could be taken to represent issues concerning public interest or benefit the public at large. The Supreme Court in *Gherulal Parekh v. Mahadevdas Maiya*[229] had observed how Public policy is an illustrative concept, rather like an unruly horse. The court observed "*the primary duty of a court of law is to enforce a promise which the parties have made and to uphold the sanctity of contract which forms the basis of society but in certain cases, the court may relieve them of their duty of a rule founded on what is called the public policy*." Lord Atkin describes that something done contrary to public policy is a harmful thing; but the doctrine is extended not only to harmful cases; but also, to harmful tendencies as is governed by precedents. The law relating to public policy is not a fixed and immutable matter; rather it is alterable by the passage of time. Broad areas that come under the scope of violating public policy include trading with an enemy nation, shifting prosecution, interference with the course of justice etc.

Thus, the provisions of section 23 provide the circumstances under which the court can limit the party's freedom to contract, invoking a higher rule of law standard that is meant to be complied with.

## DISTINGUISHING VOID AND VOIDABLE AGREEMENTS

Void agreements have been defined and briefly explained in the previous section. To appreciate the differences between void and voidable agreements, it is necessary to understand legal implications of such an agreement. The word void means something isn't valid and it isn't legally binding. When we say a contract is void, it implies it's null, void, and that it is not backed by the force of law. That makes it unenforceable, and if anyone breaches an unenforceable contract, the other party to the contract has no legal recourse against them. Further, a contract can be valid when formed and later become void. This happens when the contract fulfils all the necessary conditions of a valid contract when it's formed, but the laws change later or something changes to make fulfilling the contract impossible and beyond the capacity of imagination or beyond the control of the involved parties. Then, at that time, it becomes void.

A voidable agreement has been defined under Section 2(i) of the Act, as "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", thereby such agreements binds one party and the other party has the option to change their mind. This means they can cancel the contract anytime they want. The party that isn't bound by the contract has the control in this type of contract. A

[229] Gherulal Parekh v Mahadevdas Maiya, ***AIR 1959 SC 781***

mutual mistake on the part of both parties to a contract makes it voidable. If one or more pieces of material information are omitted from the contract, that also makes it voidable.

A contract involving a minor is one example of a voidable agreement. Minors can enter contracts, but if minors decide to breach the terms of a contract there isn't any form of legal action that can be taken against them. This makes minors unbound parties in the contract. Another example of an unbound party in a contract is someone who's either under the influence or someone who isn't mentally capable of entering into a contractual agreement.

To summarize the discussion, these are the key distinguishing factors between void and voidable agreements:

- Both void contracts and voidable contracts are forms of legal contracts. A void contract, however, is invalid from the very beginning because it regards an illegal act. A voidable contract becomes invalid when one of parties involved cancels it for legal reasons.
- Because a void contract is holding against the law, neither party can enforce it. The voidable contract is both legal and valid until cancelled or revoked.
- While no law is in place to support a void contract as a valid, existing contract, at least one party involved can be bound by a voidable contract.
- Neither obligations nor rights are associated with a void contract. With the voidable contract, which is covered under the law, only one party has the option of whether to continue it or rescind it. Legal liability can't be assessed on either party to the contract if it's void, but the voidable contract is upheld until the unbendable party chooses to rescind it.
- A contract that is void can't be made into a valid contract by two parties agreeing to the contract because you can't legally agree to do something that's illegal. A voidable contract, however, can be made valid by the party who isn't bound, if they agree to give up the right to rescind the contract.
- Lastly, when a contract is ruled void, the court treats it as if it never existed. When a contract is ruled voidable, it can become a void contract based on the conditions that were in place when the contract was formed or it can be avoided under the law.

## ILLEGAL AND UNLAWFUL AGREEMENTS - EFFECT OF ILLEGAL AND UNLAWFUL AGREEMENTS

**Unlawful agreements:** As has already been discussed, Section 23 of the Act lays down plethora of circumstances wherein object or consideration of an agreement is unlawful. An agreement hit by Section 23 is *void ab initio* and thereby in no circumstances enforceable.

**Illegal agreements:** Illegal agreements are those agreements which are: 1. void. 2. punishable by criminal law of the country or by any special legislation/regulation. Such agreements are not enforced by court of law relying on the principle of *ex turpi causa.* It refers to cause of action arising from the transgression of positive laws of a country. Resultantly, no court will lend its aid to a man who founds his cause of action upon an immoral or illegal act.[230]

There are two general principles; *First,* a contract that is entered into with the object of committing an illegal act is unenforceable. If the intent is mutual, it is not enforceable at all and if it is on part of one party, he cannot enforce the contract. *Second,* the court will not enforce a contract which is expressly or impliedly prohibited by the statute and it does not matter what the intent of the parties was, the agreement is unenforceable.[231] This classic position has undergone some changes over the course of time. A strict application of the principle illegality may cause injustice in some cases because of unjust enrichment; henceforth the courts adopt an approach of concerning various factors when it comes to enforcement of these contracts. These factors are:-

**INTENTION OF PARTIES**: The effect of illegality depends upon the intention of the parties at the time of making the contract, to do an act forbidden by law. The rights and remedies will depend upon whether they knew of, or participated in, the illegal intention. While a party who enters into the contract with an unlawful purpose or with the intention to perform the contract unlawfully, he is not entitled to remedies, though remedies may be granted to the party who is innocent of the illegality.[232] Further, if such party becomes aware of the illegality before the performance, it may refuse to perform the contract. For e.g. If a party who is to furnish a property does not know of the unlawful intention, the contract is voidable at his option when he discovers the other party's intent.[233]

**IN PARI DELICTO**: The true meaning of the maxim *'in pari delicto potior est conditio posidentis'* is that where circumstances are such that the court will refuse to assist either party, the consequence, must in fact follow that the party in possession should not be disturbed. It must not be understood to mean that where a transaction is vitiated by illegality, the person left in possession of goods after its completion is always and of necessity entitled to keep them. As no person can found a cause of action upon his immoral or illegal act, therefore despite there being a failure of consideration, no claim can lie on restitutionary principles. To put simply the consideration that has flown from the party for execution of an illegal agreement cannot be claimed back in cases of *in pari delicto (for equal fault).*

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[230] Nair Service Society v. K C Alexander, AIR 1986 SC 1165.
[231] In Re an arbitration between Mahmoud and Ispahani, (1921) 2 KB 716.
[232] Cowan v. Milbourn (1867) LR 2 Ex 230.
[233] Pragilal Kanhaiya Lal v. Ratan Lal Mathra Prasad, AIR 1931 All 458.

**Possibility of Restitution**: However, these are the few exceptions where courts have admitted claims and provided relief to the party, relieving it of the consequences of an illegal agreement. These are:

a) Where the illegal purpose has not yet been substantially carried out and before it is sought to recover the money paid or goods delivered in furtherance of it[234];

b) Where the plaintiff is not *in pari delicto* with the defendant[235];

c) Where the plaintiff does not have to rely upon the illegality to make his claim.[236]

**Collateral Transactions**: If an agreement is merely collateral to another or constitutes an aid facilitating the carrying out of the object of the other agreement, though void, is not in itself prohibited, within the meaning of Section 23 or any of the laws in the country, it may be enforced as a collateral agreement. The courts employ severability in dealing with questions of enforcement of such collateral agreements. The question adjudicated upon is whether the illegal or void parts may be separated or severed from the contract and the rest of the contract can be enforced without them. When severable, regardless of illegality being created by statute or by common law, bad parts can be rejected and good ones can be retained. When not severable, the contract is altogether void. This is mandated in terms of Section 24 of the Act. For e.g. In a transaction for sale of goods supplied in black market payable by black money, payment for the goods supplied can be enforced because the transaction involved purchase of goods against the price payable, which was not in itself illegal or opposed to public policy.[237]

**Effects of illegal agreements**: From the discussion undertaken above, the following points can be drawn out:

1. The collateral transactions to an illegal agreement also becomes illegal and hence cannot be enforced.

2. No action can be taken for the recovery of the money or property transferred under an illegal agreement.

**VOID AGREEMENTS - AGREEMENTS WITHOUT CONSIDERATION**

Section 25 declares consideration to be a necessary element of a binding contract. While, this has already been assumed under Section 10, Section 25 expressly provides for it. An agreement without consideration is void under this section, which further provides for

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[234] K Tirupati Mudali v. T Lakshmana Mudali, AIR 1953 Mad 545.
[235] Chettiar v. Chettiar, (1962) 1 All ER 494 (PC).
[236] Supra Note 2.
[237] Anand Prakash Om Prakash v. Oswal Trading Agency, AIR 1976 Del 24.

exceptional cases in which consideration may be dispensed with. The section is exhaustive and therefore an agreement made without consideration is either enforceable under this section or not enforceable at all.
Further the section reads "Agreements without consideration, void, unless it is writing and registered or is a promise to compensate for something or is a promise to pay a debt barred by limitation law".

**AGREEMENTS IN RESTRAINT OF TRADE**

Section 27 prohibits formation and operation of agreements by which anyone is restrained from exercising a lawful profession, trade or business of any kind. Part XIII of the Constitution of India contains provisions relating to the freedom of trade, commerce and intercourse within the territory of India. The provisions are laid down in Articles 301 to 307. Just as the Legislature cannot take away individual freedom of trade, wise versa the individual cannot barter it away by agreement. The Principle of law being that public policy requires that every man shall be at liberty to work for his own good, and shall not be at liberty to deprive himself, skill or talent, by any contract that he enters into. So plain meaning of the section is that every agreement by which any one is restrained from exercising a lawful profession, trade or business of any kind, is, to that extent, void.

In India it will be valid if it falls within any of the statutory or judicially created exceptions. Indian law is rigid in that sense, it invalidates all restraints whether general or partial and neither the test of reasonableness nor the restraint being partial apply to a case governed by Section 27, unless they fall within the exception provided in that section.

**THESE AGREEMENTS CAN BE BROADLY DIVIDED INTO THREE CATEGORIES:**

a) Contracts imposing restraints on a vendor of business, where the vendor of goodwill of a business agrees that in future he will not be carrying on a similar business competing with that of a purchaser.
b) Contracts of employment where an employee agrees that he will not during the course of employment or after leaving the employment compete against his employer either by entering the service of a rival trader or by setting up a rival business on his own account.
c) Combinations for regulation of trade, where manufacturers and merchants form a combination to regulate their trade relations.

**HARMONIZING INDIAN AND UK COURTS' APPROACH**

Courts in India have adapted to different approaches while dealing with these different types of agreements. Previously, the distinction between general and partial restraint, that a general restraint was void in cases of contracts of both employment and of sale of business but a partial restraint was valid and enforceable was the law in UK. This was done away with through the later pronouncement in *Nordenfelt's case.*[238] Lord Macnaghten formulated two propositions: 1) All covenants in restraint of trade, partial as well as general are prima facie void and cannot be enforced unless the test of reasonableness is satisfied. 2) Reasonableness will vary in cases of sale of business and contracts of service.

The Indian courts have since then followed these principles in adjudicating upon Section 27 cases. The absence of requirement of reasonability as provided by the terms of the section has been done away with. In *Niranjan Shankar Golikari*[239], the Supreme Court held that a restraint on trade, whether partial or general, may be good if shown to be reasonably necessary for freedom of trade. A restraint reasonably necessary for the protection of covenantee must prevail unless some specific ground of public policy can be established against it.

## STATUTORY EXCEPTIONS

### I. SALE OF GOODWILL

The only exception mentioned in the proviso to Section 27 of the contract act is that relating to sale of goodwill. It is thus stated:

"One who sells goodwill of a business with a buyer to refrain from carrying on a similar business, within specified local limits so long as the buyer, or any person deriving title to the goodwill from him, carries on a like business therein provided that such limits appear to the Court reasonable, regard being had to the nature of business." Provided that such limits appear to the court reasonable, regard being had to the nature of business. Apparently the object is to protect the interest of a purchaser of goodwill. It is difficult to imagine that when the goodwill and trade of a retail shop were sold, the vendor might the next day set up a shop within a few doors and draw off all the customers. Therefore, some restrictions on the liberty of the seller become necessary. Indeed, the restriction is the only "means by which a saleable value is given to the goodwill of a business". Far from being adverse to public interest, the restriction, by giving a real marketable value to the goodwill of a business, operates as an additional inducement to individuals to employ their skills and capital in trade and thus tend to the advantage of public interest.
Goodwill is an intangible asset of a firm, that is, it exists, yet it is not material or physical. It essentially means the reputation or status of the firm in society. Goodwill has its origin in

[238] Nordenfelt v. Maxim Nordenfelt Guns and Ammunition Co. Ltd., (1894) AC 535.
[239] Niranjan Shankar Golikari v. Century Spinning & Manufacturing Co Ltd., (1967) 2 SCR 367.

brand value, employee morale, reputation, customer advantage etc. It is an important asset because a customer is expected to engage with the same favourable firm, that he was engaged with earlier, because of its name and reputation. This is why Goodwill of a firm holds a value.
Like other assets of the firm, the goodwill of the firm can also be sold. Once the goodwill of a firm is sold, the buyer acquires some rights like: He/she can use the firm's name; He/she can represent the firm; He/she can restrain the seller of the goodwill from being in contact with the previous customers of the firm. After a sale of goodwill, the seller continues to enjoy the right to carry out a competing business. But, in case, it is agreed upon through a contract that the seller will not enter into any such agreement, such rights extinguish.

There are certain conditions that make a restraint on trade during a sale of goodwill valid, these are:

1. The seller can be restrained only from carrying out a *similar* business.
2. The restraint can be applied only to certain *local limits.*
3. The limits/restraint should appear to be reasonable.[240]

## II. RESTRICTIONS UNDER PARTNERSHIP ACT

There are various provisions in the Partnership act which validate agreements in restraint of trade. Section 11(2) enables partners during the continuance of the firm to restrict their mutual liberty by agreeing that none of them shall carry on any business other than that of the firm. Section 36(2) enables them to restrain an outgoing partner from carrying on a similar business within a specified period or within specified local limits. Such agreement shall be valid if the restrictions imposed are reasonable. A similar agreement may be made by partners upon or in anticipation of dissolution by which they may restrain each other from carrying on business similar to that of the partnership firm they have already worked.

It is necessary for the validity of a restraint under Section 36 that:

1. The Agreement should specify the local limits or the period of restraint, and
2. The restrictions imposed must be reasonable.

An agreement by a retiring partner not to carry on similar business on the land belonging to him and adjoining the factory of the firm, has been held to be reasonable and binding on the persons buying the land from him. In a case, two similar business owners, in a partnership, came to an agreement that only one of their factories would work at a time and the profit will be shared between them. This restraint was held to be valid.

[240] Chandra Kanta Das v. Parasullah Mullick, (1921) 48 IA 508.

## UNDER JUDICIAL INTERPRETATIONS

### I. TRADE COMBINATIONS

It is now almost a universal practice for traders or manufacturers in the same line of business to carry on their trade in an organised way. Thus, there are combinations of equipment manufacturers, grain merchants, sugar producers, etc. The primary object of such associations is to regulate business and not to restrain it. Combinations of this kind are often desirable in the interest of trade itself and also for the promotion of public interest. They bring about Standardised goods, fixed prices and eliminate ruinous competition. Thus, agreements to the effect of giving backing to the regulations as to the opening and closing of business in the market, licensing of traders, supervision and control of dealers and the mode of dealing are not illegal, even if there is incidental deprivation of trade liberty.

But the courts would not allow a restraint to be imposed disguised as trade regulations. An agreement between certain persons to carry on business with the members of their caste only, and an agreement to restrict the business of sugar mill within zone allotted to it, have been held void. Similarly, an agreement between two companies that one would not employ the former employees of the other has been held to be void by reason of its generality. Rules framed for regulating the market would amount to restraint of trade, if they are unreasonable and stifle trade. The restraint is adjudged reasonable if it affords fair protection to the parties and does not interfere with public interest.

The question whether an agreement whereby manufacturers agree with one another to carry their work under special conditions, or traders agree amongst themselves to sell their wares at a fixed price, is in restraint of trade has frequently arisen before courts in UK and India. Such agreements have been upheld valid in India subject to nature of restraint being reasonably sufficient to protect the interests of the party concerned.[241] Such agreements do not play foul of Section 27 of the Act.

### II. EXCLUSIVE DEALING AGREEMENTS

Another business practice in vogue is that a producer or manufacturer likes to market his goods through a sole agent or distributor and the latter agrees in turn not to deal with the goods of any other manufacturer. A producer may, for example, agree to sell all his outputs to one consumer who, in turn, agrees not to buy his requirements from any other source. As long as the negative stipulation is nothing but an ordinary incident of or ancillary to the positive covenant, there is hardly anything obnoxious to Section 27. Such negative

[241] Bholanath Shankar Das v Lachmi Narain, (1930) 53 All 316.

stipulations do not have the effect of restraining the manufacturer. On the contrary, he is encouraged to exercise his business because he is assured of a certain market for the products of his labour.

However, where a manufacturer or supplier after meeting all the requirements of a buyer, has surplus to sell to others, he cannot be restrained from doing so. The buyer cannot restrain the seller from dealing with others unless he can acquire the whole stock during the period of the agreement. The court may not countenance the agreement particularly where the buyers intend to corner or monopolise the commodity so that he may resell at his own price or where he binds the seller for an unreasonable period of time.

In a case, a seller of combs entered into an agreement with all the manufacturers of combs in the city of Patna whereby the latter undertook during their lifetime to sell all their products to him. Holding the agreement void under Section 27, the court that the contract bound the manufacturers from generation to generation; it was unrestricted both as to time and place; it was oppressive; it was intended to create monopoly. In the case of *M/s Gujarat bottling Co. Ltd.*[242] Supreme court laid down the test to adjudge the validity of such agreements in terms of- "If the negative stipulation is confined in its application to the period of subsistence of the agreement and the restriction imposed therein is operative only during the period the agreement is subsisting, the said stipulation cannot be held to be in restraint of trade so as to attract the bar of Section 27 of the Contract Act."

## RESTRAINTS ON EMPLOYEES UNDER AGREEMENT OF SERVICE

The employer-employee relationship is, and has always been, in a constant state of evolution. As the nature of this relationship evolves and changes, so does the nature of disputes that arise as a result of diverging interests, which the employer and employee seek to protect in their interaction with each other and the society in general. Several laws and legislations have been drafted to create an appropriate framework to address these concerns with an objective to reasonably balance the interests of employers and employees. Such employment laws have a broad ambit and include within their scope all areas of the employer-employee relationship and are not merely restricted to contractual issues and/or workplace discrimination.

While an increasingly liberalized market has promoted healthy competition between businesses, it has also resulted in accordance of significant importance to protection of innovative ideas, proprietary information, internal workings and mechanisms which lend firms the 'competitive edge' to thrive in the present economic environment. The objective to protect the 'competitive advantage' has in turn resulted in concerns of potential misuse of

[242] M/s. Gujarat bottling Co. Ltd. & Ors v. The Coca Cola Co. & Ors., AIR 1995 SC 2372.

confidential and proprietary information of employers by employees, especially before hiring, during, and post termination of, their employment.

Incorporation and subsequent enforcement of ‘restrictive covenants’ such as confidentiality, non-disclosure and non-solicitation in employment contracts, intended to restrict the employees from disseminating confidential and other important information exclusively available with an employer, are often amongst contentious issues in India because such provisions seemingly conflict with Section 27 of the Contract Act.

Further, Article 19 (g) of the Constitution of India clearly provides every citizen, the right to practice any profession, trade or business. This is not an absolute right, and reasonable restrictions can be placed on this right in the interest of the public. The courts have always been weary of upholding such restrictions and have kept the interpretation of this provision flexible to ensure that the principles of justice, morality. The types of restrictions can be divided into:

**I. Non-Competition Restrictions**

Non-Competition restrictions are imposed through incorporation of non-compete clauses in the employment contract entered into between the employer and the employee. Non-compete clause restrains an employee from practicing a similar profession that requires him to perform similar duties so that the trade secrets of the employer are not divulged.

To determine whether a restrictive covenant in employment contract would be reasonable/ valid or not, the courts have paid due regard to bargaining power of each party, reasonableness of restrictions set out in the covenant, time, place and manner of restriction etc. In India, due to the heavy bargaining power of the employers, the trend is for the courts to protect the rights of the employees and adopt an interpretation favourable to them. While it is a settled position of law that restrictive agreements bind current employees in lawful employment of the employers throughout the duration of the contract, the position of laws regarding validity of such restraints on employees after termination of contract is more contentious and adjudicated before courts.

The Supreme Court in *Niranjan Shankar Golikari v. Century Spinning & Mfg Co. Ltd*[243] enumerated the test to determine the validity of ‘restrictive’ agreements in terms of Section 27 of the Contract Act. In this case, a foreign producer collaborated with a company manufacturing tyre cord yarn by an agreement which stated that the company would maintain secrecy of all technical information. In pursuance of the agreement, the company signed a non-disclosure agreement with the appellant, at the time of his/her employment. The test laid down by this case focuses on the time period during which the restriction is sought to operate. A distinction with respect to covenant being in operation ‘during the employment’

[243] Supra Note 245

and 'post the employment' was created. The Supreme Court observed, "…Considerations against restrictive covenants are different in cases where the restriction is to apply during the period after the termination of the contract than those in cases where it is to operate during the period of the contract. Negative covenants operative during the period of the contract of employment when the employee is bound to serve his employer exclusively are generally not regarded as a restraint of trade and therefore do not fall under section 27 of the Contract Act." Such covenants were thus held to be valid during the course of employment.

On this basis, the Court held that the contractual restraints under consideration did not play foul of section 27, since they acted only during the subsistence of the contract. However, the decision was silent on when post-contractual restraints are valid, restricting itself to the statement that they are to be treated differently from restraints during the contract.

This issue was next considered in *Superintendence Co. of India Pvt. Ltd. v. Krishan Murgai*[244] wherein the employing company carried on business as valuers and surveyors and had established a reputation and earned goodwill in its business by developing its own techniques for quality testing and control. It possessed trade secrets in the form of these techniques and its clientele. The terms and conditions of employment contained a post-service restraint preventing the employee from serving any competitive firm, or carrying on a business himself in the same line as that of the appellant company. His employment was terminated, after which the employee started his own business, which was in competition with that of the employer. The employer sought a permanent injunction against the employee to prevent breach of the terms of the employment, and claimed damages. Thus, the issue before the Court was two-fold- (a) whether the contract was in restraint of trade and hence invalid; and (b) whether the non-compete clause applied only when the employee left voluntarily, or also when his services were terminated.

The Supreme Court held all post contractual restraints as barred by Section 27 and thereby doesn't permit the reasonableness enquiry. Further holding that an employer is not entitled to protect himself against competition per se against an employee after the employment has ceased, but he is entitled to protection of his proprietary interest and his trade secrets. A contract of restraint of trade is prima facie void, but is becomes binding upon proof that the restriction is justifiable in the circumstances as being reasonable from the point of view of the parties themselves and also of the community.

This jurisprudence was further entrenched through the case of *Percept D'Mark (India) Pvt. Ltd. v. Zaheer Khan & Anr*[245] where It was held by the Supreme Court that "… a restrictive covenant extending beyond the term of the contract is void and not enforceable". The

[244] Superintendence Co. of India Pvt. Ltd. v. Krishan Murgai, AIR 1980 SC 1717.
[245] Percept D'Mark (India) Pvt. Ltd. V. Zaheer Khan & Anr., AIR 2006 SC 3426.

Supreme Court also held that the doctrine of restraint of trade does not apply during the continuance of the contract of employment and it applies only when the contract comes to end. The Supreme Court further went on to observe that the doctrine of restraint of trade is not confined to contracts of employment, but is also applicable to all other contracts.

Further in a recent case of *Ozone Spa Pvt. Ltd. v. Pure Fitness & Ors.*[246] The Delhi High court restricted the defendants from establishing, running or setting up any competing business in any area that falls within a range of four kilometers from the premises of the plaintiff. Although, Section 27 states that all agreements in restraint of any profession, are void, so long as an employee does not have the motive to cheat, mistrust or cause irreparable loss to the company, trade or business. Hence, reasonable restraints are permitted and they do not render the contract void. We thus see, In India, due to the heavy bargaining power of the employers, the trend is for the courts to protect the rights of the employees and adopt an interpretation favourable to them.

**II. Non-Solicitation of Employees and Customers**

A non-solicitation clause prevents an employee or a former employee from indulging in business with the company's employees or customers against the interest of the company. For example, an employee agrees not to solicit the employees or clients of the company for his own benefit during or after his employment. Non-solicitation obligations have been enforced in some circumstances, albeit on a case to case basis. On the question what amounts to solicitation, it has been that "solicitation is essentially a question of fact. The appellants should prove that the respondents approached their erstwhile customers and only on account of such solicitation, customers placed orders with the respondents. Mere production of quotation would not serve the purpose."

In *Desiccant Rotors International Pvt. Ltd v Bappaditya Sarkar & Anr.*[247], the Delhi High Court allowed an injunction against the manager prohibiting him/her from soliciting Desiccant's customers and suppliers to stand in effect. It is pertinent to note, however, that the Delhi High Court held that a marketing manager could not be deemed to possess confidential information and that his written declaration to that effect in his employment agreement was also meaningless and thus the Court rejected Desiccant's claim to enforce the confidentiality obligations on the manager.

Further, in *FL Smidth Pvt. Ltd. v M/s. Secan Invescast (India) Pvt.Ltd.*[248] *(Secan Invescast Case)* the Madras High Court ventured into the question of what amounts to 'solicitation'. It was held that merely approaching customers of a previous employer does not amount to

[246] Ozone Spa Pvt. Ltd. v. Pure Fitness & Ors., 2015 SCC Online Del 10768 : 2015 222 DLT 372.
[247] Desiccant Rotors International Pvt Ltd v Bappaditya Sarkar & Anr., Delhi HC, CS (OS) No. 337/2008 (decided on July 14, 2009).
[248] M/s. FLSmidth Pvt.Ltd. v. M/s. Secan Invescast (India) Pvt.Ltd., (2013) 1 CTC 886.

solicitation until orders have been placed by such customers based on such approach. The court observed, "….solicitation is essentially a question of fact. The appellants should prove that the respondents approached their erstwhile customers and only on account of such solicitation, customers placed orders with the respondents. Mere production of quotation would not serve the purpose. It is not that the appellant is left without any remedy. In case the Court ultimately holds that the appellant has got a case on merits, they can be compensated by awarding damages." The judgment further states that such clauses may be valid if reasonable restrictions such as distance, time limit (reasonable time frame), protection and non-usage of trade secrets and goodwill are imposed on former employees.

It is to be noted that like any other restrictive clause, non-solicitation clauses are also considered to be playing foul of Section 27 of the Contract Act, subject to reasonability. However there are certain non-solicitation clauses that do not amount to restraint of trade, business or profession and would not be subject to Section 27 of the Act, as held by the Delhi High Court in *Wipro Ltd. v. Beckman Coulter International SA.*[249] In this case, Wipro worked as a sole and exclusive canvassing representative/ distributor for Beckman Coulter International, S.A., for 17 years. Beckman Coulter decided to undertake direct operations in India and issued advertisement seeking employment from people and giving preference to candidates having experience in having handled respondent's product or similar products. Wipro Limited alleged that such advertisement was in violation of non-solicitation clause and approached the court for prohibiting solicitation and claimed damages. It was held that since the restrictions had not been imposed on the employees but on Wipro and Beckman Coulter, Section 27 would not be attracted and thus the agreement was held not to be in restraint of trade.

India being a services oriented economy, there are sectors in which people switch jobs frequently, as they always are looking for better opportunities to grab, such as the IT Services Sector. Many at times it so happens that some documents concerning ex-employer end up the employee who has now joined a marker rival of such ex-employer. Therefore companies today are incorporating necessary provisions with respect to treatment of such documents. *Crowson Fabrics Ltd. v. Rider*[250], where it was held that even though the act of retaining various documents belonging to the ex-employer concerning customer and supplier contact details by the employees during employment did not amount to a breach of confidentiality, such 'illegitimate' actions constituted a breach of employees' duty of fidelity.

### III. Non-disclosure of Confidential information and trade secrets

The employee is mandated to take reasonable steps to keep all the confidential information in confidence except and to the extent when disclosure is mandatory under any law in force.

[249] Wipro Ltd. v. Beckman Coulter International SA, 2006 (3) ARBLR 118 (Delhi).
[250] Crowson Fabrics Ltd. v. Rider, [2007] EWHC 2942.

The employee further agrees that he/she shall not discuss or disclose the confidential information of the company to any person or business unrelated to the company.

In a case at hand, the defendant, an advocate, was working at the plaintiff's law firm. On termination of employment, the defendant took away important confidential business data, such as client lists and proprietary drafts, belonging to the plaintiff. The defendant contended that, he was the owner of the copyright work as it was done by him during his employment since the relation between parties was not that of an employer and employee. The Delhi High Court rejected this contention and ruled that the plaintiff had a clear right on the material taken away by the defendant. Accordingly, the Delhi High Court restrained the defendant from using the information taken away illegally.[251] It should be noted that the Court did not prohibit the defendant from carrying on a similar service. The defendant was only restrained from using the information he took, as this was necessary to protect the interests of the plaintiff.

In *Hi Tech Systems and Services Ltd. v. Suprabhat Ray*[252], the Supreme Court restrained the respondents from acting as sales agent of other companies, saying that they had acted in breach and they were in process of utilizing trade secrets and confidential information.
Further, *In American Express Bank Limited v. Priya Puri*[253] the defendant was working as the Head of Wealth Management for the plaintiff bank for the North India region. Upon the defendant serving her notice for termination of employment, the plaintiff bank instituted allegations of sharing trade secrets, confidential information and possessing intellectual property of the plaintiff. The plaintiff consequently filed a plea for injunction against the defendant. The Delhi High Court rejected this plea on the ground that "The inconvenience caused to the defendant shall be much more in case the injunction as prayed by the plaintiff to be granted in his favour."

In cases concerning intellectual property rights over the vital information, it has been held in order to claim copyrights, the plaintiff should have abridged, arranged and/or done something 'which would show that they have done something with the material which is available in public domain so as to claim exclusive rights on that'.

In addition to restraining employees from using such confidential information post termination, by way of seeking injunction or claiming damages, the criminal legislation also comes to the aid of employers and provides them with an opportunity to take criminal action against the employees in addition to seeking civil remedies. Several provisions of the Indian

[251] Diljeet Titus v. Mr. Alfred A. Adebare and Others, (2006) 32 PTC 609, Delhi.
[252] Hi Tech Systems and Services Ltd. v. Suprabhat Ray, 2015 SCC Online Cal 1192: AIR 2015 Cal 261
[253] American Express Bank Limited v. Ms. Priya Puri 2006 (110) FLR 2061.

Penal Code (IPC)[254] and Information Technology Act, 2000 are also attracted in case of breach of confidentiality and disclosure provisions and allow criminal prosecution and imprisonment or fine or both as required.

## IV. Garden Leave Clauses

The uncertainty of the judicial decisions over the non-compete clauses has resulted in the development and taking recourse to a concept called "Garden Leave" in the corporate industry, having its genesis in England, under which, employees are paid their full salary during the period in which they are restrained from competing. However, when the validity of "garden leave" clauses came for consideration before the Bombay High Court, it was argued that the Garden Leave Clause is prima facie in restraint of trade and is hit by Section 27 of the Contract Act. The effect of the clause is to prohibit the employee from taking up any employment during the period of three months upon the cessation of the employment. The Bombay High Court, accepting the argument, held that obstructing "an employee who has left service from obtaining gainful employment elsewhere is not fair or proper".[255] However the concept of garden leave has gained popularity recently in India and practiced across various companies.

Garden leave clause has its origin in UK in the case *Standard Co. Ltd. v. Henderson*[256] where the court held that the defendant should not be violating the obligation to the effect of which the contract was executed, i.e. to work for a competitor or any other business concern while the contract was in effect. This clause has not been widely accepted by the Indian courts. It has not received much appreciation since it puts a disguised restraint of trade which goes deep into the root of freedom of contract, which is fundamental to the validity of a contract.
When this clause came for consideration before the Bombay High Court in the case of *VFS Global Services Private Limited v. Mr. Suprit Roy*[257] the contention raised was that the Garden Leave concept is not a clause that is independent of section 27. The clause, prima facie is in restraint of trade and it explicitly prohibits the employee from taking up any other employment for a certain period. The Court had accepted this contention and held that "to obstruct an employee who has left service from obtaining gainful employment elsewhere is not fair or proper"

## V. Non-poaching agreements

Whilst non-compete, non-solicitation and non-disclosure agreements deal with the employer-employee relationship, a fourth class of restrictive agreement which are often signed by the parties is the non-poaching agreement which is executed between two employers. In an age

[254] IPC provisions like Section 381: Theft by clerk or servant that is punishable with imprisonment which may extend to 7 years and fine.
[255] VFS Global Services Private Limited v. Mr. Suprit Roy, (2008) 2 Bom. CR 446.
[256] Standard Co. Ltd. v. Henderson [1987] I.R.L.R. 64.
[257] Supra Note 261.

of constantly evolving specialized industries and niche talent pools, employers often tend to invest a very large amount of human capital into their employees. If these employees subsequently join direct competitors, it can result in substantial economic loss for the ex-employer. A non-poaching agreement therefore enforces guidelines to be followed in cases of lateral hiring.

This type of agreement essentially considers the case wherein two organizations/companies agree not to solicit or 'poach' the employees of their direct competitors. Non-poaching agreement per se does not contravene section 27 of the Contract Act as it does not restraint an employee from seeking and/or applying for any job/employment. What this class of agreement does instead is, it simply mandates that one competitor should seek the consent of the other before hiring those other competitors' employees. The issue of non-poaching agreements now also comes within the ambit of the Competition Act, 2002. Whilst no cases have been considered exclusively in connection with non-poaching agreements under the Competition Act so far, Section 3 of the Competition Act expressly states that agreements which are anti-competitive in nature are banned.

### VI. Training Bonds

The employer in order to protect and safeguard its interest often executes a training bond with its employees for training imparted and/or provided during the course of their employment or specifically provided prior to their joining, to ensure that they work for a particular duration. These bonds specify the minimum period for which the employee shall serve the employer, though such clauses may not be enforceable in the Indian context. If the employee acts in breach of such an agreement, the employer can seek compensation, at times which are limited to the expenses incurred for training the employees. However, the compensation demanded should be reasonable and not imposed by way of a penalty.

In *Satyam Computer Services Limited v. Ladella Ravichander*[258], the defendant was an employee who had abruptly left the company and as per terms of employment bond, was required to pay liquidated damages of Rs. 200,000 along with stipend charges and additional expenses incurred by the company for the defendant. However, the Andhra Pradesh High Court held that such action by the defendant did not cause any damage or loss to the company and it would be unreasonable to acquire such an amount from the defendant. An amount of Rs. 100,000 was fixed by the court as reasonable damages taking into consideration the period of work and the fact that no actual loss was caused to the Company.

In *Toshnial Brothers (Pvt.) Ltd. v. E. Eswarprasad & Ors.*[259] the Madras High Court dealt with a situation where an employee working as sales engineer in breach of his undertaking left his services within 14 months as against the contractually agreed period of three years. The Madras High Court held that the employer was entitled to recover the stipulated

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[258] Satyam Computer Services Limited v. Ladella Ravichander, MANU/AP/0416/2011.

[259] Toshnial Brothers (Pvt.) Ltd. v. E. Eswarprasad & Ors., 1997 LLR 500.

damages, which is a genuine pre-estimate by the parties of the damages incurred. There is no requirement to prove separately any post-breach damages. The employer is required to establish that the employee was the beneficiary of special favour or concession or training at the cost and expense wholly or on the part of the employer and there had been a breach of the undertaking by the beneficiary of the same. In such cases, the breach would per se constitute the required legal injury resulting for the employer due to breach of the contract.

## AGREEMENTS IN RESTRAINT OF LEGAL PROCEEDINGS

It is a well-known rule of the English law that "an agreement purporting to oust the jurisdiction of the courts is illegal and void on grounds of public policy." Thus, any clause in an agreement providing that neither party shall have the right to enforce the agreement by legal proceedings is void. Agreements stipulating no intention to contract or a gentleman's agreement which is an agreement that relies upon the honour of the parties for its fulfilment, rather than being in anyway enforceable by law is not in violation of Section 28.

Section 28 of the Indian Contract Act renders void two kinds of agreement, namely:

1. An agreement by which a party is restricted absolutely from enforcing his legal rights arising under a contract by the usual legal proceedings in the ordinary tribunals.
2. An agreement which limits the time within which the contract rights may be enforced.

An agreement having for its object the restrain of an individual from enjoying the fundamental right of resorting to a court of law for redress and relief is invalid. Section 28 applies to agreements that wholly or partially restrain this right of the parties. A contract having a clause that no action should be brought up on it is void since it restricts both parties from enforcing their rights under the contract in a court of law. In a case it was held that a special agreement between an advocate and his client that the latter would not be sued for fees has been held void under this section. Similarly, an agreement by a servant not to sue for wrongful dismissal is invalid; so is a condition restraining a transferee from enforcing his rights under the transfer in anyway.

It should be noted that an agreement, whereby the parties to a suit bind themselves before the judgement is passed in the court of first instance, to abide by the decree of that court and forego their right to appeal, is valid and binding.

### I. Agreements on Limitation of Time

An agreement which provides that a suit should be brought for the breach of any terms or agreement within a time shorter than the period of limitation prescribed by law is void. The effect of such an agreement is absolutely necessary to restrict the parties from enforcing their rights after the expiration of the stipulated period, though it may be within the period of the limitation. According to the Limitation Act, 1963, an action for breach of contract may be brought within three years from the date of the breach. In a case, a clause in a policy of life insurance declaring that "no suit to recover under this policy of life insurance shall be brought after one year from the death of the assured" was held void.

Cases sometimes occur where parties agree to extend the period of limitation. No provision is made the section for agreements extending period of limitation for enforcing rights under it. There is no restriction imposed upon the right to sue; on the contrary, it seeks to keep the right to sue subsisting even after the period of limitation. It would, however be void under Section 23, as tending to defeat the provisions of the Limitation Act 1908, Section 3 which provides that every suit instituted after the period of limitation prescribed by the act shall be dismissed, although limitation has not been set up as a defence.

### II. Agreements prescribing Jurisdiction

Section 28 makes void only those agreements which absolutely restrict a party to a contract from enforcing the rights under that contract in ordinary tribunals. But this section has no application when a party agrees not to restrict his right of enforcing his rights in the ordinary tribunals but only agrees to a selection of one of those ordinary tribunals in which ordinarily a suit would be tried. Parties cannot by agreement confer jurisdiction on courts to try suits not cognizable under the ordinary law. The principle that the parties cannot by consent confer jurisdiction on a court or deprive a court of jurisdiction has been stated to apply to cases of inherent jurisdiction of a court over the subject matter of the suit, and the question of territorial jurisdiction as not being a question of inherent jurisdiction.

If such contract is clear, unambiguous and explicit and not vague, it is not hit by this section. But an agreement however cannot confer jurisdiction on the court which has no jurisdiction at all to entertain the suit; and if the court mentioned in the contract has no jurisdiction at all, the jurisdiction of other courts is not barred. The choice regarding the jurisdiction of courts should be clearly unambiguous and explicit. The party invoking the clause must strictly prove that the restriction applies to the proceedings under consideration. It is also necessary that important terms of this nature must be specifically brought to the notice of the parties whose rights are sought to be curtailed.

## UNCERTAIN AND AMBIGUOUS AGREEMENTS

An agreement is void under Section 29 when its terms are vague and uncertain and thus cannot be made certain. An agreement may be uncertain either because the terms in it are ambiguous or vague or because it is incomplete. The general rule is that if the terms of an agreement are vague or indefinite which cannot be ascertained with reasonable certainty of the intention of the parties, then there is no contract enforceable by law.

Section 29 provides the meaning of an agreement that should be clear on the face of it, so also effect can be provided to the contract if its meaning is found with reasonable clearness. If this is not possible then the contract would not be enforceable. Merely difficulty in interpretation will not be considered as vague. The principle can be formulated as a party who seeks remedy from court for breach of a contract; the obligation must be able to identify the obligation with sufficient precision to justify the remedy. The law thus stated is more flexible, and recognizes that different levels of certainty may be needed for the remedies.

It has been held that a contract is not void if its terms are capable of being made certain. The meaning of the contract should not be uncertain and further, it needs to be shown that it is not capable of being made certain. Mere vagueness or uncertainty which can be easily removed by proper interpretation does not make a contract void.[260] Even oral agreements will not be considered vague if its terms are ascertainable with precision.

A contract out of which more than one meaning, when constructed, can produce in its application more than one result will not be void for uncertainty. A contract will be void for uncertainty only if it's essential terms are uncertain or incomplete unless the uncertain part being not essential is severed, leaving the balance of the agreement intact. To ascertain what is essential and what is not, one must look into the intention of the parties.

The courts will not undertake to supply defects or remove ambiguities according to its own notions of what is reasonable as it would not be to enforce a contract by parties but to make a new contract for them. It has also been observed that courts often use severability when it comes to enforcement of uncertain agreements. That is to say where there is agreement on all substantial terms, the court may disregard a subsidiary term on the grounds that it is meaningless.

To sum up the discussion, it is important to remember that agreements whose meaning is not certain or is incapable of being made certain are void in nature. An agreement can be unsure either because it contains ambiguous or vague terms or because it is incomplete. The general rule is that if the terms of an agreement are vague or indefinite, which can't be ascertained with reasonable certainty of the parties ‘ intention, then the law does not enforce a contract.

[260] Bahadur Singh v Fuleshar Singh, AIR 1969 Pat 114.

## MODULE V

# DISCHARGE OF A CONTRACT AND ITS VARIOUS MODES

### DISCHARGE OF A CONTRACT

Discharge is the process whereby the primary obligations under a validly formed contract come to an end. The primary obligations under a contract are those that determine performance by the parties.[261] In many cases, secondary obligations such as the payment of damages also come to an end upon discharge.[262] A contract may be discharged through performance, an agreement, frustration or a breach. Each of these modes of discharge have a differing effect on the resulting rights and obligations of the parties.

### DISCHARGE BY PERFORMANCE

When a contract is discharged by performance it is said to have been discharged 'fully' since the mutual rights and obligations of the parties are completely extinguished with no new legal ties arising from this mode of discharge. It is the principal and most usual mode of discharge[263] and has been dealt with in Sections 31 – 67 of the Indian Contract Act, 1872 (*hereinafter,* "the Act").

#### Performance

Performance occurs when the promisor fulfils the obligations he/she has undertaken under Section 37 of the Act. This performance must be 'exact' in the sense that the party must perform within the specified time and the agreed upon standard. This standard of obligation often varies according to the type of the contract. For example, contracts for the supply of goods have a strict standard.[264] Whether the actual performance rendered satisfies the contractually prescribed standard is a mixed question of law and fact.[265]

Contracts may be classified into two general categories with respect to performance: (1) **absolute contracts** and (2) **contingent contracts**. In an **absolute contract**, the promisor binds himself/herself to perform without any condition external to the contract. However, there may be a condition internal to the contract such as making the performance of one party

[261] *Photo Production Ltd. v. Securicor Transport Ltd.*, [1980] AC 827.
[262] JILL POOLE, TEXTBOOK ON CONTRACT LAW 323 (2008).
[263] POLLOCK & MULLA, INDIAN CONTRACT & SPECIFIC RELIEF ACTS 942 (2004).
[264] *Kurt A. Becher GMBH & Co. v. Roplak Enterprises SA (The World Navigator*, [1991] 2 Lloyd's Rep 23.
[265] CHITTY ON CONTRACTS 1097 (1999).

conditional on the willingness to perform of the other party. On the other hand, in a **contingent contract**, the condition precedent for performance is external to the contract. The definition of 'contingent contract' in Section 31 of the Act makes it clear that this condition must be collateral to the contract. For the contract to be truly contingent, the condition must also be of an uncertain nature. Examples of contingent contracts include contracts of indemnity, contracts of guarantee and contracts of insurance. A wager is also a contingent agreement, but it is unlawful.

A contract will be regarded as contingent even if the occurrence of the contingency depends on the will of a party to perform an act. For example, a contract to purchase shares on the condition of being appointed the sole agent of the company is contingent on the company so appointing the person.[266] It is important to note that there is no promise, and consequently no contract, if performance is dependent on the mere will and pleasure of the promisor. In *Roberts v. Smith*,[267] it was held that there was no contract at all when a promise was made to pay whatever the promisor himself thinks right or reasonable for a certain service.

The Act classifies contingent contracts as follows:

(i) contingent on an event happening (S. 32);
(ii) contingent on an event not happening (S. 33);
(iii) contingent on the future conduct of a living person (S. 34);
(iv) contingent on the happening/not happening of a specified event within a fixed time period (S. 35); and
(v) contingent on an impossible event (S. 36).

In all of these classifications, the moment the happening of the event becomes impossible, the contract is void. It logically follows that contracts of type (v) are void ab initio.

**Tender of Performance**

An attempted performance will also result in a discharge as it is the legitimate attempt on the part of the promisor to perform his/her contractual obligations unconditionally at the agreed upon time and place. If the promisee unjustifiably does not accept the performance, this attempted performance or tender would amount to actual performance and, according to Section 38 of the Act, the contract is deemed to be discharged. Any rights that would accrue to the promisor under the contract would not be prejudiced by such a discharge.

The word 'tender' is used interchangeably with 'attempted performance.' This is because of the word's English law association with the actual payment of money by the debtor to the creditor in a contract of debt. In order to determine whether such tender is valid, we must

[266] *Re Jaunpur Sugar Factory Ltd*., AIR 1925 All 658.
[267] *Roberts v. Smith*, 118 RR 462.

look into the questions relating to by whom it must be offered, who may demand enforcement of the contract, where and when performance must occur and in what manner must it be made.

The first two are the preliminary questions relating to performance. Section 40 of the Act answers the question of by whom a promise must be performed. In most cases tender must be made by the promisor, or by his/her agent, unless it was otherwise intended. For instance, tender for payment of shares by the purchaser's attorney was held to be sufficient proof of readiness and willingness to perform.[268] There may also be joint promisors and such a situation is governed by Sections 42 – 44 of the Act. Indian law is in slight variance with English law on this point. In India, all joint promisors are jointly and severally liable, whereas under English law, there is a difference between a 'joint promise' and a 'joint and several promises'.

It is primarily the promisee who may claim for enforcement of the contract as the promise is for his/her benefit. AS per S. 54, the promise may also be made for the benefit of more than one person jointly and these 'joint promisees' may together enforce the contract.

The time and place for performance is often explicitly mentioned in the agreement between the parties. If the time has been left unspecified and the promisee need not apply for the performance of the promise, the Act states in Section 46 that performance must be rendered within a reasonable time. The determination of the meaning of a 'reasonable time' is a question of fact. Sections 47 – 49 elucidate the general rules for time and place of performance.

Section 49 is of particular note as it places a duty on the promisor to apply to the promisee to appoint a reasonable place for performance. This encapsulates the common law principle that a debtor must seek out the creditor and ensure repayment at that place.[269] Such appropriation of payment is a mixed question involving both time and place of performance and the general rules for the same have been laid down in Sections 59- 61 of the Act.

Section 50 of the Act grants the promisee wide discretion in specifying any time and any manner in which performance must be rendered. For a tender to be valid, it must be unconditional [S. 38(1)] meaning that performance must be offered in the exact manner in

[268] *Sohanlal Pachisia v. Bilasray Khemani*, AIR 1954 Cal 179.
[269] *L.N. Gupta v. Taramani*, AIR 1984 Del 49.

which was agreed upon. It must also be an offer to perform the whole of the promise.[270] With respect to payment, the whole amount must be tendered, and it must be in the *"current coin of the country."*[271] Moreover, a tender of a debt before the due date is not valid and will not prevent the accrual of interest on the loan.

A creditor is not bound to accept payment in a form other than what was agreed upon. If the creditor accepts payment by a negotiable instrument like a bill of exchange or a cheque, it is a question of fact to be determined on a case-by-case basis as to whether the payment has been received in absolute satisfaction of the debt or its satisfaction is *conditional* upon the realization of the instrument.[272] With respect to payment by credit card, it has been similarly held that there is no general presumption that when a payment was agreed to be made through a third party (the issuer of the credit card), the acceptance by the seller (the creditor accepting the credit card payment) is conditional upon the third party actually making the payment to the seller.[273]

**Performance of Reciprocal Promises**

When an agreement consists of an exchange of promises, they are known as 'reciprocal promises'.[274] The term has been defined in Section 2(f) of the Act. In *Jones v. Barkley*,[275] Lord Masfield observed that these promises may be classified as being mutual and dependent, mutual and independent and mutual and concurrent. Sections 51 to 54, 57 and 58 of the Act govern issues related to reciprocal promises such as the required order of performance.

According to Section 52, the order of performance of the reciprocal promises may be fixed in the contract itself, and if it is not so fixed, the order will be determined by the nature of the transaction. The courts have laid down the general principle that *"in the ordinary course of business, work is not usually paid for before it is done."*[276] If the reciprocal promises are to be performed simultaneously (mutual and concurrent), the promisor need not perform until and unless the promisee demonstrates that he/she is 'ready and willing' to perform the reciprocal promise [as per S. 51]. For instance, in a contract for the sale of goods, the seller need not deliver the goods until the buyer is able and willing to pay for the goods on

[270] POLLOCK & MULLA, INDIAN CONTRACT & SPECIFIC RELIEF ACTS 976 (2004).
[271] *Salik Ram Upadhia v. B. Jai Gopal Singh*, AIR 1955 All 350.
[272] POLLOCK & MULLA, INDIAN CONTRACT & SPECIFIC RELIEF ACTS 984 (2004).
[273] *Re Charge Card Services Ltd.*, [1988] 3 All ER 702 (CA).
[274] AVTAR SINGH, LAW OF CONTRACT & SPECIFIC RELIEF 371 (2017).
[275] *Jones v. Barkley*, 4 Douglas 659.
[276] *Hashman v. Lucknow Improvement Trust*, (1927) 101 IC 847.

delivery.[277] Whether the promisee is so 'ready and willing' is a question of fact that is determined on a case-by-case basis.

If one of the parties prevents the other from performing their respective reciprocal promise, Section 53 provides that the contract becomes voidable at the option of the party so prevented. This obstruction to performance may be caused by even the inadequacy of material or machinery supplied by a party.[278] If the reciprocal promises are mutual and dependent to the extent that if the promise cannot be performed till after the other promise has been, the promisor cannot claim performance of the reciprocal promise if he fails to perform his own first. This is the principle behind Section 54. For instance, the Supreme Court in *Nathulal v. Phoolchand*[279] held that the nature of the contract required the seller to have had his own name recorded as the owner and have obtained the requisite permission from the State government for the transfer of agricultural land before he could ask for the final payment.

There may also be situations wherein the reciprocal promises comprise of both legal and illegal parts. Section 57 states that if persons reciprocally promise to first do legal acts and under certain circumstances subsequently do other acts that are illegal, the first set of promises is a contract while the second set is void. This provision applies only when the void part can be properly separated from the rest of the agreement.[280] Similarly, Section 58 provides that if there are alternatives promises wherein one branch is legal and the other illegal, the legal branch may alone be enforced.

**Time as the Essence of a Contract**

As noted earlier, parties may stipulate a time by which performance must be completed. The question arises as to what the effect on the contract would be if performance is not rendered within the specified time. Section 55 states that the answer depends on whether the intention of the parties was to make time the essence of the contract. If such an intention is shown, the contract becomes voidable at the option of the promisee. It is only when time is not essential as per the intention of the parties that the contract remains enforceable despite a delay.

However, the promisee would be entitled to compensation for any loss caused due to the failure to perform within the specified time. Moreover, even in the case of time being deemed to be of the essence, if the promisee accepts performance at any time other than what

[277] AVTAR SINGH, LAW OF CONTRACT & SPECIFIC RELIEF 371 (2017).
[278] *Kleinert v. Abosso Gold Mining Co*., (1913) 59 Sol Jo 45; *Uberoi Mohinder Singh v. State of Haryana*, (1991) 2 SCC 362; *Ramachandra Narayan Nayak v. Karnataka Nerravari Nigam Ltd.*, (2013) 15 SCC 140.
[279] *Nathulal v. Phoolchand,* AIR 1970 SC 546.
[280] AVTAR SINGH, LAW OF CONTRACT & SPECIFIC RELIEF 376 (2017).

was expressly agreed upon, then the promisee cannot claim compensation for any losses caused unless at the time of acceptance he notifies his intention to claim the losses.

Whether time is of the essence is a mixed question of fact and law.[281] Time is generally considered to be of the essence in the following three cases: (i) where the parties have expressly agreed to treat it as the essence of the contract; (ii) where delay operates as an injury; and (iii) where the nature and necessity of the contract requires it to be so construed.[282] An example for situation (iii) is the well-known authority of *Bhudra Chand v. Betts*.[283] Here, the plaintiff wished to engage the defendant's elephant. The contract provided that the elephant would be delivered on October 1st, but the defendant got an extension of time till the 6th. The elephant was not delivered till October 11th. The plaintiff refused to accept it and sued for damages. The court held that time was of the essence of the contract as is evidenced from the fact that the defendant felt the need to ask for an extension of time.

In the case of commercial contracts specifically, time is presumed to be of the essence.[284] This is due to the fact that the business world requires certainty.[285] It has also been held that *"merchants are not in the habit of placing upon their contracts stipulations to which they do not attach some value and importance."*[286] A time schedule in a construction contract is of essence since construction is a commercial service.[287] In a contract of sale of goods, the time of shipment has been held to be of essence.[288] However, in the case of contracts for the sale of land or other forms of immovable property, it is presumed that time is not of essence and the mere incorporation of a penalty clause for a default does not by itself evidence an intention to make time of the essence in such contracts.[289]

It is important to note that time may be made of the essence even by a subsequent notice. This notice ought to fix the longest time that could reasonably be required for performance of the remaining acts to be done.[290]

**Assignment**

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281 *Municipal Corporation of Delhi v. Jagan Nath Ashok Kumar*, (1987) 4 SCC 497.
282 *Orissa Textile Mills Ltd. v. Ganesh Das*, AIR 1961 Pat 107.
283 *Bhudra Chand v. Betts*, (1915) 22 Cal LJ 566.
284 *China Cotton Exporters v. Beharilal Ramcharan Cotton Mills Ltd.*, AIR 1961 SC 1295.
285 *Hitkari Motors v. Attar Singh*, AIR 1962 J&K 10.
286 *Bowes v. Shand*, (1877) LR 2 AC 455, 463.
287 AVTAR SINGH, LAW OF CONTRACT & SPECIFIC RELIEF 380 (2017).
288 *Bowes v. Shand*, (1877) LR 2 AC 455, 463.
289 *Gomathinayagam Pillai v. Palaniswami Nadar*, AIR 1967 SC 868, 871.
290 *Crawford v. Tooqwood*, 13 Ch. 153.

Normally, the persons entitled to claim performance are either the promisees or their respective legal representatives. This is in line with the general rule that a stranger to the contract cannot enforce performance (doctrine of privity of contract). However, contractual rights and obligations can be transferred or 'assigned', and the assignees may ask for performance from the promisors.

The question arises as to whether a promisor may assign his/her contractual liability to another person. Under both Indian and English law, there can be no such assignment without the consent of the promisee.[291] This is because the promisor has the right to insist that performance shall be the responsibility of the promisor especially if the engagement is of a personal nature. If the consent of the promisee is obtained, a new contract is created as what occurs in such a situation is really *"a novation resulting in substitution of liabilities"*.[292] Assignment of contractual rights may also occur by operation of law, such as in the cases of insolvency or death, as opposed to an act of the parties.

However, vicarious performance under Section 40 is not to be confused with assignment since the liability of the promisor subsists – he/she is responsible for the performance by his/her agent. In *Davies v. Collins*,[293] Lord Greene MR observed that this is true of most contracts in his statement that *"In many contracts all that is stipulated for is that the work shall be done and the actual hand to do it need not be that of the contracting party himself; the other party will be will be bound to accept performance carried out by somebody else. The contracting party, of course, is the only party who remains liable."*

There are three primary conditions for an effective assignment. Firstly, an assignment requires some consideration between the assignor and assignee unless the assignment has been made as a gift. In the absence of such consideration, the assignment is revocable at the option of the assignor.[294] Secondly, the title of the assignee is subject to all equities that existed at the time between the assignee and assignor and those that arise upto the time that the notice of assignment is given to the debtor. For instance, if the assignor had induced the other party to contract with him by fraud, the other party will have the same right of recission against the assignee as he would have had against the assignor. However, an assignee is not affected by any equity of a personal nature between the assignor and the assignee. For example, the right to claim damages for the fraud committed by the assignor cannot be used

[291] *Robson & Sharpe v. Drummond*, (1831) 109 ER 1156.
[292] *Khardah Co. Ltd. v. Raymon & Co. Ltd*., (1963) 3 SCR 183.
[293] *Davies v. Collins*, (1945) 1 All ER 247.
[294] *Gleg v. Bromley*, (1912) 3 KB 474.

to defeat the right of the assignee.[295] Thirdly, a notice of assignment should be given to the other party.

**Death & Bankruptcy**

In the case of death of the promisor prior to performance, his/her legal representatives are bound by the promise as per Section 37 of the Act. With respect to a contract involving a joint promise, if any of the joint promisors dies, his/her representatives must jointly fulfil the promise along with the surviving joint promisors as per Section 42. Upon the death of the last survivor, the representatives of all of them must fulfil the promise jointly. The devolution of joint rights follows a principle similar to that which governs such joint liabilities. According to Section 45, if one of the joint promisees dies, the right to claim performance rests with his/her legal representative who may exercise it jointly along with the survivors. Upon the death of the last joint promisee, all their legal representatives may claim performance jointly.

The question arises as to what amounts to a valid tender to the executor of a deceased promisee. In *Pandurang v. Dadabhoy*, the creditor had died and before taking out the probate, the executors called upon a mortgagor to whom the deceased had lent money on mortgage to pay the amount due. The money for repayment was made available before the notice expired, but the probate was not obtained till after that date. The debtor offered to pay the debt on a proper release being executed. The court held that the actual tender by production of money was not necessary since there was no legally constituted representative to whom it could be made.[296] It was further held that interest on the mortgage debt should stop on the expiration of the notice in light of the fact that the executors could have behaved more diligently by obtaining the probate before the relevant date. It was sufficient that the debtor was able to pay the debt and had made money available for this purpose.

A contrasting view was taken in the case of *Ismail Bhai Rahim v. Adam Osman*,[297] wherein the court held that a debtor must either tender performance to a legally constituted representative or take the risk of tendering to a person not legally entitled to receive the debt, or wait until someone has obtained probate and incur liability to pay the additional interest that accrues in the meanwhile. Pollock & Mulla submit that this is the correct view since a debtor may escape this situation by taking advantage of Sections 9-11 of the Administrator-General's Act, 1913.[298]

[295] *Stoddart v. Union Trust Ltd.*, [1912] 1 KB 181 (CA).
[296] *Pandurang Krishnaji v. Dadabhoy Nowraji*, (1902) 26 Bom 643.
[297] *Ismail Bhai Rahim v. Adam Osman,* AIR 1939 Cal 131.
[298] POLLOCK & MULLA, INDIAN CONTRACT & SPECIFIC RELIEF ACTS 986 (2004).

To a debtor, the biggest benefit of filing for bankruptcy is the discharge of debts. Bankruptcy prioritizes debts and manages the debtor's assets so as to pay creditors in an orderly fashion. Once these assets have been so exhausted, any debt not yet paid is discharged. The creditor may no longer pursue the collection of such debts as the debtor is no longer legally bound to pay them. However, it must be kept in mind that some debts may not be discharged at all.

**DISCHARGE BY BREACH**

When a contract is said to have been 'discharged by breach', it is broken by the promisor through non-performance. Although this does result in an extinguishment of the original rights and obligations, the legal relationship between the parties does not end since this mode of discharge results in the creation of remedial rights (of damages or specific performance) and their corresponding obligations.

A breach of contract is said to occur when a party renounces his/her liabilities under it or by his/her own act makes it impossible for him/her to perform his/her obligations, or totally or partially fails to perform such obligations.[299] Breach can be classified into two kinds, namely present breach and anticipatory breach, based on whether the failure to perform or renunciation takes place when the time for performance has arrived or even prior to that.

The occurrence of an anticipatory repudiation through an announcement by the party of his/her intention not to fulfill the contract and that he/she will no longer be bound by it has certain effects on the rights of the parties. First and foremost, the innocent party which is not in breach is excused from performance or from further performance. The injured party now has the option to either sue immediately or wait till the time of performance. This immediate right of action was recognized as early as in 1853 in *Hochester v. De La Tour*.[300] Anticipatory breach may occur even in the case of a contingent contract. An immediate action for damages would lie as long as the promisor disabled himself/herself from performance prior to the happening of the contingency.[301]

It is important to note that if the injured party chooses to wait for performance despite the notice of anticipatory breach, he/she keeps the contract alive for not only his/her benefit (such as being able to claim a greater amount in damages) but also for that of the party in breach. This means that the other party may not only fulfill their obligations notwithstanding

[299] *Associated Cinemas of America, Inc. v. World Amusement Co.*, (1937) 201 Minn 94.
[300] *Hochester v. De La Tour*, 118 ER 922.
[301] *Frost v. Knight*, (1872) LR 7 Exch 111.

their earlier notice of repudiation, but also may take advantage of any supervening circumstance, such as frustration, that permits the party to decline performance.[302]

The above principle applies to premature termination of employment contracts as well. If the employee does not accept the repudiation, the contract remains alive irrespective of whether he/she is permitted to perform his/her duties.[303] In general, courts do not direct reinstatement of a dismissed employee in order to specifically enforce the contract. However, it is well-settled that courts may forbid the infringement of a negative stipulation even if it is necessary to a positive covenant for the performance of personal services as per another contract. For instance, where the defendant had agreed that she would sing at the plaintiff's theatre for three months and would not sing elsewhere for that time period, the negative part of the covenant was enforced.[304]

If the anticipatory breach is accepted prior to the date of performance, the damages for the breach must be assessed according to the loss suffered at the time of repudiation.[305] If the promisee does not so accept the repudiation, damages will be assessed at the time that was fixed for performance which ordinarily leads to a greater monetary claim. However, the promisee would have to undertake the risk of the market falling and would also have to take all reasonable measures to mitigate his losses.[306]

The question arises as to what amounts to repudiation. This drastic conclusion of repudiation may be reached only when it is a clear case of refusal to perform in a manner going to the root of the contract.[307] An agreement may stand repudiated either by words expressing an intention to not perform or by the conduct from which such intention can be gathered.[308] An example to illustrate the latter situation is a refusal by the buyer to accept documents in a CIF contract. This was held to amount to repudiation.[309]

The whole conduct of the party has to be assessed objectively in order to see whether there is an intention to abandon and refuse performance. Every minor irregularity will not result in a premature termination of the contract. Thus, in an agreement for the supply of 100 tons of flock to be delivered in installments where the 16th delivery was below the standard agreed upon and the buyer attempted to treat this as a repudiation, the court held that the seller's

[302] *Jhandoo Mal Jagan Nath v. Phul Chand Fatesh Chand*, AIR 1925 Lah 217; *Avery v. Bowden*, 119 ER 647.
[303] *Thomas Marshall (Export) Ltd. v. Guinle*, 1979 Ch 227.
[304] *Warner Bros Pictures Inc. v. Nelson*, (1937) 1 KB 209.
[305] *Ramgopal v. Dhanji Jadhavji Bhatia*, AIR 1928 PC 200.
[306] *Mackertich v. Nobo Coomar Roy*, ILR (1903) 30 Cal 477.
[307] *Woodar Investment Devp. Ltd. v. Wimpey Construction UK Ltd*., (1980) 1 WLR 277 (HL).
[308] POLLOCK & MULLA, INDIAN CONTRACT & SPECIFIC RELIEF ACTS 995 (2004).
[309] *M. Gulamali Abdul Hussain & Co. v. APMS Mohamed Yusuf*, AIR 1954 Mad 268.

conduct did not indicate that he wanted to throw away the contract in its entirety and the buyer should be content with damages for the defective goods.[310]

The acceptance of such repudiation must be clear and unequivocal. Thus, silence and inaction cannot constitute a valid acceptance of repudiation. This principle was laid down in *Vitol SA v. Norelf Ltd.*[311] wherein the buyer had refused to accept the cargo because of a delay in loading and the seller remained silent on the matter. Such silence did not amount to an acceptance of repudiation.

Section 39 of the Act encapsulates the above doctrine of anticipatory breach. The language of the provision stresses upon a refusal to perform. The courts have interpreted the same by adding the qualification that such refusal must go to the whole of the contract.[312] This position seems contrary to the illustrations to the section which indicate that a singer willfully absenting herself on one day from singing at a theatre where she has contracted to perform at amounts to repudiation. However, this is a misapprehension as the act of willfully absenting herself, though on one night only, did amount to an altogether refusal to perform an integral part of her contract.[313]

Whether a partial failure goes to the root of the contract or not is a question of fact that must be decided on a case-by-case basis. It is undisputed that when a party abandons a contract prior to its completion, he/she is liable to pay the cost for completion. Conversely, whether the party is entitled to recover anything for the partial work done depends on several factors. One of the factors for consideration is whether the aggrieved party had an option to reject the work but nevertheless accepted it in its partial state. In such a scenario, the aggrieved party would be bound to pay an amount worked out on the basis of *quantum meruit*. It has been held that in a contract for work and labour where the completion of the work is not a condition precedent, payment would have to be made for the amount of work actually done.[314]

After putting an end to the contract, the aggrieved party may bring an action for damages in lieu of the breach, but he/she will be bound by the stipulations in Section 64 in that he/she must restore to the other party the benefits received under the contract.[315]

[310] *Maple Flock Co. Ltd. v. Universal Furniture Products (Wembley) Ltd.*, (1934) 1 KB 148 (CA).
[311] *Vitol SA v. Norelf Ltd.*, 1996 AC 800.
[312] *PC Rajput v. State of MP*, AIR 1993 MP 107.
[313] *Schiller v. Sooltan Chand*, ILR (1878) 4 Cal 252, 256.
[314] *Hoenig v. Isaacs*, (1952) 2 All ER 176 (CA).
[315] *Muralidhar Chatterjee v. International Film Co. Ltd*., AIR 1943 PC 34.

## SUPERVENING IMPOSSIBILITY OF PERFORMANCE

Performance may be deemed impossible when such impossibility is apparent on the very face of the contract. Such a situation is termed as intrinsic or absolute impossibility and these agreements are void ab initio. For example, an agreement to perform black magic. The more material form of impossibility is that which arises subsequent to the formation of the contract. This is termed as supervening or subsequent impossibility. Both forms of impossibility are governed by Section 56 which states that the agreement would be void in either scenario.

The doctrine of supervening impossibility was not always accepted in English law. The old rule laid down in *Paradine v. Jane*[316] was that there is no excuse for non-performance as a contract creates a duty which a promisor is bound by irrespective of any subsequent events. This was labelled as the 'do or die' theory. In *Taylor v. Caldwell*,[317] Blackburn J. laid down that this rule is only applicable when the contract is positive and absolute and not subject to any conditions whether express or implied. These two decisions signified the struggle between the following two principles – the principle of sanctity of contract which supports absolute liability and the principle that a contract is discharged when the shared contractual assumption has been destroyed by a change in circumstances.

'Frustration' of a contract occurs when either performance becomes physically impossible or when the object that the parties had in mind has failed to materialize. An example to illustrate the latter is as follows: a defendant had hired a flat from the plaintiff for the purpose of viewing a coronation procession. This procession was cancelled, and the defendant refused to pay the balance amount due. It was held that the object of the contract was frustrated by the non-happening of the coronation and the plaintiff was not entitled to recover the balance.[318]

### Specific Grounds of Frustration

The principle of frustration is applicable to a great variety of contracts, and it is thus not possible to lay down an exhaustive list of situations where the doctrine may be applied.[319] Nevertheless, there are certain grounds that have become well-established and have been elucidated below.

[316] *Paradine v. Jane*, 82 ER 897.
[317] *Taylor v. Caldwell*, 122 ER 309.
[318] *Krell v. Henry*, (1903) 2 KB 740 (CA).
[319] AVTAR SINGH, LAW OF CONTRACT & SPECIFIC RELIEF 397 (2017).

The doctrine applies with full force where there has been destruction of the subject matter of the contract.[320] *Taylor v. Cadwell* is a prime example for this specific ground as the promise to let out a music hall was held to be frustrated on the destruction of the hall by a fire. Another ground for frustration is a change in circumstances which makes performance of the contract impossible in the manner and time agreed upon. Such a change in circumstances must be unanticipated and affect performance so as to make it virtually impossible or even extremely difficult or hazardous. If this change in circumstances is not brought about by the fault of either party, the courts will not enforce the contract.[321]

Non-occurrence of an event contemplated by the parties in the contract is a ground for frustration as was exemplified in *Krell v. Henry*. Death or incapacity of a party is also a ground for frustration where the nature of the contract requires personal performance by the promisor. In *Robinson v. Davison*,[322] there was a contract between the plaintiff and the defendant's wife that she should play the piano at the plaintiff's concert. On the day of the concert, she fell ill, and the concert had to be postponed leading to losses. The court held that the contract was clearly subject to the condition of her being well enough to perform, and hence it was held to be frustrated. The foundation of the contract failed, and thus damages were not payable.

A contract will be dissolved when there is an administrative or legislative intervention that affects the fulfillment of a contract for a specific work so as to transform the contemplated conditions of performance. Therefore, where a vendor of a piece of land could not execute the sale-deed as he ceased to be the owner by operation of law, the contract was held to be frustrated.[323]

The intervention of war or warlike conditions in the performance of a contractual obligation has posed several difficult questions. For example, the closure of the Suez Canal following the Anglo-French war with Egypt interrupted the performance of numerous contracts. One contract so affected was that considered in the case of *Tsakiorglou & Co. Ltd. v. Noblee & Thorl GMBH*. The party responsible for delivery argued that it was an implied term of the contract that shipment would be via the Suez Canal. It was held that since the customary route via the Suez Canal was closed, the party was bound to ship the goods via a reasonable

[320] *Blackburn Bobbin Co. v. T.W. Allen & Sons*, (1918) 2 KB 467 (CA).
[321] *Pameshwari Das Mehra v. Ram Chand Om Prakash*, AIR 1952 Punj. 34.
[322] *Robinson v. Davison*, (1871) LR 6 Exch 269.
[323] *Shiam Sunder v. Durga*, AIR 1966 All 185.

and practical route. Even if the use of this route requires greater expenditure, this does not render the contract fundamentally or radically different.[324]

**Application of the Doctrine of Frustration to Leases**

The question of whether the doctrine of frustration is applicable to leases is one that is not yet finally settled in English law. In the landmark case of *Crickelwood Property & Investment Trust Ltd. v. Leighton's Investment Trust Ltd.*,[325] the House of Lords unanimously held that frustration was not applicable to the facts of the case since a lease for 99 years cannot be said to have been upset by a few years' disturbance. However, it is important to note that the judges were not willing to accept the argument that a lease is more than a contract and amounts to an estate meaning that it can never end prematurely by frustration even if the subject-matter of the lease is buried in the depth of the sea or swallowed by a vast concussion of nature.

It was held erroneous to presume that there is an authority to the effect that a lease cannot be ended by frustration under any circumstances. A lease shall be determined absolutely on the happening of an event which in an ordinary contract works as a frustration.[326] For instance, if a legislation is passed which prohibits private building in the leased area, then this would end the currency of a building lease whose object would be so defeated. However, it is important to note that the English courts have held the position to be that although the doctrine of frustration is in principle applicable to leases, the cases in which it may be properly applied are rare.[327]

In India, the question was considered in the case of *Raja Dhruv Dev Chand v. Raja Harmohinder Singh*[328] wherein the Supreme Court held that the general view is that Section 56 of the Act is not applicable where the rights and obligations of the parties arise under a lease. The Punjab High Court held that where on account of an event beyond the parties' control the lessor is not able to transfer possession, the lessee would be entitled to take back the rent paid.[329] While the Supreme Court affirmed the decision, it categorically disagreed with the observation of the High Court that the broad principle of frustration is generally applicable to leases. The avoidance of the lease was upheld on the reasoning that a lease implies the transfer of a right to enjoy that land and where any material part of the property is

[324] *Tsakiorglou & Co. Ltd. v. Noblee & Thorl GMBH*, 1962 AC 93.
[325] *Crickelwood Property & Investment Trust Ltd. v. Leighton's Investment Trust Ltd.*, 1945 AC 221 (HL).
[326] *Matthey v. Curling*, (1922) 2 AC 180 (HL).
[327] *National Carriers Ltd. v. Panalpina (Northern) Ltd*., 1981 AC 675.
[328] *Raja Dhruv Dev Chand v. Raja Harmohinder Singh*, AIR 1968 SC 1024.
[329] *Gurdashan Singh v. Bishen Singh*, (1962) 2 Punj. 5 (FB).

destroyed or rendered unfit for the purpose for which it was let out, Section 108(c) of the Transfer of Property Act gives the lessee the option to avoid the lease.

**Effect of Frustration**

It is well-settled that when there is frustration, the dissolution of the contract occurs automatically. This dissolution does not depend on the ground of repudiation or on the election of either party.[330] For this dissolution to occur, the essence of the principle of frustration must not be violated, namely that it is not self-induced.[331] This means that the impossibility of performance should not have been caused by the act or omission of either party.

Another principle that must be kept in mind is that frustration automatically discharges the contract *"irrespective of the individuals concerned, their temperaments and failings, their interest and circumstances."*[332] The belief, knowledge and intention of the parties are evidence to be considered only to the extent that they may form the basis of the court's conclusion as to whether the altered circumstances destroyed altogether the basis of the contract and its underlying object.[333] The language of Section 56 affirms this statement as it lays down a rule of positive law and does not leave any room for the matter to be determined according to the intention of the parties.

**Frustration & Restitution**

Frustration results in a contract being deemed void, and this may result in a disproportionate alteration to the parties' rights. Such a situation warrants that the parties' rights be adjusted in order to preserve an equitable balance. Section 65 of the Act provides for such adjustment as it stipulates that when an agreement is discovered to be void, any person who has received any advantage under the said agreement is bound to restore it or to compensate the person from whom he/she received the benefit. It is important to note that this section applies only when the agreement is found to be void subsequent to the formation of the contract, and not a situation wherein the contract was void at the time of making it.[334]

This section also is not applicable to a scenario wherein the benefits are passed at a time when the contract has, though unknown to the parties, already ceased to be enforceable. In

[330] *Denny, Mott & Dickson Ltd. v. James B. Fraser & Co. Ltd*., 1944 AC 265 (HL).
[331] *Maritime National Fish Ltd. v. Ocean Trawlers Ltd.*, 1935 AC 524 (PC).
[332] *Davis Contractors Ltd. v. Fareham Urban Distt. Council*, 1956 AC 696, 715.
[333] *Satyabrata Ghose v. Mugneeram Bangur & Co*., AIR 1954 SC 44.
[334] *Joginder Singh v. Registrar of Coop Societies*, AIR 1965 J&K 39.

*Jagadish Prosad Pannalal v. Produce Exchange Corpn. Ltd.*,[335] the court held that for the section to apply, the advantage must be received 'under' the contract whereas in the facts of this case, the excess price was paid after the contract had already become void and ceased to be enforceable.

In cases of frustration, the principle of restitution operates by ensuring that any benefits which may have passed under the contract, which subsequently becomes impossible to perform or unlawful, from one party to another must be restored. In English law, the two coronation cases of *Krell v. Henry*[336] and *Chandler v. Webster*,[337] led to an inequitable position that frustration deems a contract to be *void ab initio* and any rights acquired by the parties must not be disturbed. Within a year after these two judgments being passed, the Law Reform (Frustrated Contracts) Act, 1943 was passed in England in order to adjust the rights of parties whose contract has ended by frustration. It essentially provided that all sums of money which have been paid under such a contract must be refunded and all those payments which are still due shall cease to be payable. The same principle applies to benefits other than money. The rationale behind this English legislation has been incorporated into Indian law via Section 65 as illustrated above.

## DISCHARGE BY EXPIRY OF LIMITATION

The law of limitation is a procedural filter to determine what actions can be litigated before a court of law vis-à-vis the temporal origin of their cause of action. It seeks to achieve repose, peace, and harmony in the social order by seeking to extinguish uncertainty of claims. It does so by raising a presumption that a "*right not exercised for a long period of time*" must have been deemed to be settled in favour of the *status quo*. Socially, it seeks to ensure that the rights of parties should not be in a state of "*constant doubt, dispute or uncertainty*".[338] Simply put, in so far as the law of contracts is concerned, the law of limitation extinguishes a claim arising out of a contract after the lapse of a certain period of time. The Limitation Act, 1963 consolidates the "*law for the limitation of suits and other proceedings and for purposes connected therewith" in India*.[339] It seeks to achieve two purposes expressed best in the legal maxims "*interest republicae ut sit finis litium*" (that it is in the interest of the state to put an end to litigation) and "*vigilantibus non dormientibus jura subveniunt*" (that the law assists the vigilant and not one who sleeps over his rights).

[335] *Jagadish Prosad Pannalal v. Produce Exchange Corpn. Ltd.,* ILR (1945) 2 Cal 41.
[336] *Krell v. Henry*, (1903) 2 KB 740 (CA).
[337] *Chandler v. Webster*, (1904) 1 KB 493.
[338] CK TAKWANI, CIVIL PROCEDURE WITH LIMITATION ACT 782 (2013).
[339] Preamble to the Limitation Act, 1963.

According to Avtar Singh, the expiry of a "period of limitation"[340] is not a mode of discharge recognised by the Indian Contract Act. Since the particular Limitation Act, 1963 and the general concept of limitation are merely procedural in nature, they do not extinguish or put an end to the parties' rights and obligations (under the contract) and only prohibit the respective remedies that they may avail of so as to implement the terms of their contract.[341]

However, for all practical purposes (disregarding mere academic distinction between a right and a remedy), one may conveniently say that a contract may stand practically discharged (if not theoretically) when a party with a contractual right sleeps over the same and fails to exercise a remedy (suit for declaratory relief, damages, specific performance, injunction, restitution) within the stipulated period of three years. Section 3 (1) of the Limitation Act, 1963 sets up the "bar" of limitation whereby a suit instituted by a promisee in a contractual relationship against the promisor in breach "*after the period prescribed*" will be liable to be "*dismissed*" unless otherwise provided. Part II of Schedule I to the Limitation Act, 1963 prescribes a period of three years from the date from the arising of the cause of action in a

suit relating to contracts.

For instance, some of the instances covered by Part II of Schedule I to the Limitation Act are reproduced as follows:

| **Description of suit** | **Period of limitation** | **Time from which period begins to run** |
|---|---|---|
| For specific performance of a contract. | Three years | The date fixed for the performance, or, if no such date is fixed, when the plaintiff has notice that performance is refused. |
| For compensation for the breach of any contract, express or implied not herein specially provided for. | Three years | When the contract is broken or (where there are successive breaches) when the breach in respect of which the suit is instituted occurs or (where the breach is |

[340] Section 2 (j) of the Limitation Act, 1963 defines the "*period of limitation*" as the period of limitation prescribed for any suit, appeal or application by the Schedule, and prescribed period means the period of limitation computed in accordance with the provisions of this Act" (internal quotation marks omitted).
[341] AVTAR SINGH, CONTRACT AND SPECIFIC RELIEF 339 (2013).

| | | |
|---|---|---|
| | | continuing) when it ceases. |
| Against a carrier for compensation for losing or injuring goods. | Three years | When the loss or injury occurs. |
| By a surety against the principal debtor. | Three years | When the surety pays the creditor. |

Therefore, practically one may say, that a contract may stand discharged when the remedy to enforce rights and liabilities stand exhausted after a period of limitation.

**DISCHARGE BY AGREEMENT AND NOVATION**

A contract is a creation of the will of the parties. Therefore, the law permits such parties to redefine their contractual relationship by way of a new contract. Section 62 of the Indian Contract Act, 1872 provides that "*if the parties to a contract agree to substitute a new contract for it, or to rescind or alter it, the original contract need not be performed*".

**NOVATION**

Novation is when the parties to a contract agree to "*substitute*" the existing contract with a new contract. In the case of *Scarf v. Jardine*[342] Lord Selborne explained novation as when "*there being a contract in existence, some new contract is substituted for it either between the same parties or between different parties, the consideration mutually being the discharge of the old contract*." Such novation may happen in two ways: either (a) novation involving change of parties; or (b) novation involving substitution of a new contract in place of the old.

An example of the former will be a situation where A owes money to B under a contract, it may be agreed between A, B and C that B shall thenceforth accept C as his debtor, instead of a. The old debt of A to B is at an end, and a new debt from C to B has been contracted.[343] Such novation may also take place when a new partner is admitted into an existing firm or when a partner retires from a firm and the new firm as constituted after admission or retirement accepts the liabilities of the old firm and this is approved by the persons dealing with the firm. Concurrent of all the parties is considered necessary; whereby all the parties even to the erstwhile contract have to tender their consent.

[342] (1882) 7 AC 345.
[343] Illustration (a) to Section 62, Indian Contract Act, 1872.

In the latter way, parties to a subsisting contract may agree to substitute a new contract for it, thereby discharging the original contract which now need not be performed. A necessary condition for a contract to stand novated is a valid and unbroken subsisting contract. Novation is impossible where the original contract has been breached. In *Manohur Koyal v. Thakur Das Naskar*[344] the plaintiff had filed a suit in order to recover the sum due on a bond. After the due date of the bond, the plaintiff agreed to accept part payment due on such bond. The Calcutta High Court held that the contract had been discharged, not by novation but by breach. This was because the defendant had reneged on its promise of performance as in the original contract itself, thus committing breach. Such breached contract could not then be novated. The new agreement should be valid and enforceable. In a case where an existing mortgage was replaced by a new contract of mortgage which was not registered. Such new mortgage being unregistered in its form was unenforceable and hence there was no valid novation and the parties were held to be still bound by the original mortgage.[345] Where the rights under the old contract are kept alive even after the second agreement, then there is no substitution of the contract and hence no novation in law.

Novation between the same and the new parties often takes place in reconstitution of partnership firms where often a new partner may be admitted into an existing firm. According to the Partnership Act, 1932, a firm is reconstituted by admission of a new partner, retirement, expulsion, insolvency or death of an existing partner or transfer of a partner's share. Except in the case of dissolution, in all other cases there is a reconstitution of a firm which involves an express or implied novation.

*In Re European Assurance Society*[346] a person had entered into a contract of life-insurance with X Co.. Later, this X Co. amalgamated with Y Co. Through this process, an endorsement was made on the policy that from thence onwards, Y Co. would be liable for the policy. It was held that there was novation and the policy money could be recovered from Y Co.

**RESCISSION**

Section 62 of the Indian Contract Act, 1872 not only provides for novation of a subsisting contractual relationship, but also enables parties thereto either "*to rescind or alter it*".

A contractual relationship may stand discharged when the parties may rescind (revoke or repeal) it by mutual consent thus cancelling all or any of the terms of the contract between

[344] ILR (1887-88) 15 Cal 319.
[345] *See Shanker Lal Damodhar v. Ambalal Ajaipal,* AIR 1946 Nag 260.
[346] (1867) 3 ChD 391.

them. If some of the terms are rescinded, they may be replaced or substituted by new terms. In that case, the contract will stand novated. A party to a contract may also rescind it without prejudice to its right to claim compensation for a breach when the other party fails to perform it when the contract lends itself to such a rescission. For example, where S agrees to supply certain goods to B by the 15th, and B agrees to pay the price on the 30th but however S fails to fulfil his promise on the 15th, B need not pay the price and may also procure the goods even the very next day (i.e. 16th) and claim compensation for any loss that he may have sustained.

In *Syed Israr Masood v. State of Madhya Pradesh*[347] there was a contract for the sale of forest coupes through auction. However, on the date of supply, the plaintiff found there to be substantial variation vis-à-vis the quality of timber in comparison to such that was shown on the date of auction. The Supreme Court allowed rescission under Section 62 allowing refund of the deposit.

Section 67 provides that if a promise neglects or refuses to afford the promisor reasonable facilities for the performance of his promise, the promisor thereby is excused by such neglect or refusal as to any non-performance. An illustration is where A agreed to repair B's house, but B refuses to point out to such aspects of the house which needed such repair, then A stands excused for such non-performance as may have been caused by or attributable to such refusal or neglect on the part of A. This will allow A to rescind the contract.

The Specific Relief Act, 1963 contemplates another form of rescission. When a contract is breached by one party, the other party may have the right to rescind the contract and treat itself as absolved from its countervailing obligations and hold the other party liable in damages. The remedy of rescission is also available in cases where the contract is voidable at the option of one of the parties. This remedy is available under Section 27 (1) of the Specific Relief Act, 1963 which provides that a contract may be rescinded either (a) "*where the contract is voidable or terminable by the plaintiff"; or* (b) "*where the contract is unlawful for causes not apparent on its face and the defendant is more to blame than the plaintiff."*

Thus, a contract may be rescinded at the option of such party who is entitled to get it rescinded where the contract may be unlawful and the plaintiff and defendant are not in *pari delicto.* However, the existence of some facts such as the following may preclude a plaintiff from seeking to rescind the contract:

1. Where the plaintiff has expressly or impliedly ratified the contract

[347] (1981) 4 SCC 289.

2. Where restoration to original circumstances is not possible. For example, where the goods which were the subject matter of the contract have been consumed or resold.
3. Where third parties have, during the subsistence of the contact, acquired rights in good faith for value without notice. For example, a *bonafide* buyer.
4. Where, only a part of the contract is sought to be rescinded and such part is not severable from the rest of the contract.

Section 30 states that on the rescission of a contract, the court may require the party to whom the relief is granted to restore, so far as may be, any benefit which it may be received from the other party and to make any compensation in this regard which justice may require. This provision effectuates the principle that those who seek equity must do equity.[348]

## ALTERATION

Parties to a contract also possess the power to alter its terms. However, they may do so only by way of mutual consent and no party can unilaterally alter contractual terms. In *Magnum Films v. Golcha Properties Ltd.*[349] the parties had fixed the rates for the leasing of a cinema hall. If any one party unilaterally alters any *material* contractual term, then the effect would be that of the other party being discharged with respect to such contract. This harsh consequence does not follow from all unilateral alterations but only from such alterations as may relate to material terms. Materiality of an alteration implies that alteration should be one which alters the legal effect of the contract. In another case where the date of a bond was altered, the Calcutta High Court held that the bond would stand discharged. Section 87 of the Negotiable Instruments Act holds that a material alteration of a negotiable instrument will discharge persons who became or were parties to such negotiable instrument prior to the time of such alteration.

## REMISSION

Section 63 of the Indian Contract Act, 1872 provides that "*every promisee may dispense with or remit, wholly or in part, the performance of the promise made to him, or may extend the time for such performance, or may accept instead of it any satisfaction which he thinks fit.*" [350] Thus, it is a promisee who may remit the contract.

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[348] *See* Section 64, Indian Contract Act, 1872.

[349] AIR 1984 Del 162.

[350] The simplest explanation of this provision is illustration (a) appended to it in the Act itself. Where A promises to paint a picture for B and B thereafter forbids him to do so, A will no longer be bound to perform the promise earlier made. Another illustration, *inter alia* is (b) where "A owes B 5,000 rupees. A pays to B, and B accepts, in satisfaction of the whole debt, 2,000 rupees paid at the time and place at which the 5,000 rupees were payable. The whole debt is discharged."

Therefore, a contract can be said to have been discharged by way of remission when a party who had the right to demand performance of the contract:

1. remit or dispense with it, wholly or in part; or
2. extend the time for its performance; or
3. accept any other satisfaction thereof, instead of performance.

Factual possibilities that may signify a remission of a contract include where a party may accept lesser sum than what was due, or may waive its right under a contract or may extend the time for performance. In *Kapurchand Godha v. Mir Nawab Himayatalikhan Azamjah*,[351] the Supreme Court was concerned with a situation where "*the liability was above twenty seven lakhs of rupees, and a committee…offered twenty lakhs to the creditor in full satisfaction and he accepted it*." Justice SK Das of the Court held that the facts of the case squarely fell within the scope of Section 63 and closely mirrored those of illustration (c) appended thereto. It was held that where the appellant accepted the payment in full satisfaction of his claim, he was not entitled to further file a suit for seeking the remainder of the sum. The material inquiry thus becomes as to whether the acceptance of such lesser sum was "*in full satisfaction*" of the contractual right and if the answer is in the affirmative, only then will the contract stand discharged by way of remission. In *Union of India v. Gangaram Bhagwandas*,[352] where the Railways had sent a cheque in favour of the defendant and he had neither issued any receipt that he was accepting it in full and final satisfaction and nor did he stopped from pursuing his matter, it was held that there was no agreement to remit the contract by way of acceptance of a lesser sum.

In *Manohur Koyal v. Thakur Das Naskar*[353] the Calcutta High Court held that Section 63 not only modifies but is in direct contrast to the law of remission in England. This was because in as early a case as *Foeakes v. Beer*[354] where facts similar to illustration (a) as discussed above led to a different conclusion as reference to Section 63 would make one reach. In that case, A owed B a sum of five hundred pounds and even if B unilaterally consents to take just two hundred pounds in payment of such debt, such arrangement would be *nudum pactum* and B could still legally claim the unpaid sum of three hundred Pounds. The position contained in Indian law (i.e. Section 63) is very different from that in English law. In the latter, consideration is necessary not only for the formation of a contract but as well as for the discharge of a contract. Therefore, in English law, where a promisee seeks to discharge a promisor from performance, consideration must be there from the other side so as to balance this promise to waive. If such consideration is found absent, then the waiver will not be effective and such promisee may hold the promisor liable for non-performance. This meant

[351] AIR 1963 SC 250.
[352] AIR 1977 MP 215.
[353] ILR (1887-88) 15 Cal 319.
[354] LR 9 AC 605.

that a contract could be discharged by remission only when the party remitted does something else in return. However, such requirement for consideration to a waiver is absent in Indian law.

## ACCORD AND SATISFACTION

When a contractual promise stands breached, the remedy to redress such breach may instead be substituted by a new agreement. This new agreement, which is an arrangement entered into between the parties after a breach is called an accord. Here, the party not at fault can accepted a substituted consideration. The liability arising out of a contractual breach, thus may be discharged not by the exercise of a judicial remedy by the promisee but by accord and satisfaction. The validity of such new arrangement must be judged by the general law of contract quite apart from the provisions of Sections 62 and 63.[355] The legal effect of accord and satisfaction is best spelt out in the following judgment of the Privy Council in the case of *Payana Reena Layana Saminathan Chetty v. Pana Lana Pana Lana Palaniappa Chetty*:[356]

> "*The receipt given by the appellants and accepted by the respondents and acted upon by both proves conclusively that all the parties agreed to a settlement of all their existing disputes by the arrangement formulated in the 'receipt'. It is a clear example of what used to be well-known in common law pleading as 'accord and satisfaction by a substituted agreement'. No matter what were the respective rights of parties inter se, they are abandoned in consideration of the acceptance by all of a new agreement. The consequence is that when such an accord and satisfaction takes place the prior rights of the parties are extinguished. They have, in effect, been extinguished by the new rights; and the new agreement becomes a new departure and the rights of all the parties are fully represented by it.*"

Such wronged party, which accepts such accord, can no more exercise its remedies for contractual breach, which it otherwise could have as a consequence of such breach (for example, damages).

In *P.K. Ramaiah & Co. v. NTPC*[357] the Supreme Court of India held that where there was a full and final settlement of the claim, there came into being an accord and satisfaction, thus leaving no 'breach' as per the new arrangement. In this case, there was an arbitration clause in the contract that provided for arbitration as the mode of dispute resolution. However, the Court held that there no more existed an arbitrable dispute in lieu of, and because of this accord and satisfaction.

What sets apart the concept of accord and satisfaction as a mode of discharging a former contractual relationship is that it takes place after such former contract has been breached by

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[355] AVTAR SINGH, CONTRACT AND SPECIFIC RELIEF 430 (2013).
[356] (1913-14) 41 IA 142: 18 CWN 617 (PC)
[357] 1994 Supp (3) SCC 126.

the promisor. Such breach of the previous contractual arrangement is not necessary to be there in case the parties agree to remit or alter or novate upon it. However, where a novation occurs post the breach of the previous contract, the phenomenon or mode of discharge is that of accord and satisfaction. However, an illegal contract cannot support an accord and satisfaction.[358]

**EFFECT OF DISCHARGE BY AGREEMENT AND NOVATION ON ARBITRATION AGREEMENTS**

Where a contact contained a clause providing for arbitration as the chosen method of dispute-resolution, and such agreement has been discharged by way of agreement and novation; a question arises as to the force and validity of the arbitration clause (which forms a separate arbitration agreement by itself) contained in such discharged contract.

Under Section 62 of the Indian Contract Act, 1872 when a main agreement stands novated, rescinded or altered, it is said to lose its validity and hence the arbitration agreement incorporated as one of the clauses of such agreement may also be thought to have been avoided. This misunderstanding might be based on a principle that if a contract is superseded by another, the arbitration clause, being a component part of such earlier contract, falls along with it.

However, this common-sense notion is displaced by the doctrine of severability. As per the doctrine of severability, an arbitration clause in a main contract, stands as a separate agreement on its own footing and with a life and tenure of its own which runs beyond the force and vigour of the main contract. Therefore, in the case of *Delhi Airport Metro Express Pvt. Ltd. v. CAF India Pvt. Ltd.*[359] the High Court of Delhi (although reached a factual conclusion that there was no novation in that case yet) explained the position as to the effect of novation on the arbitration clause/agreement as follows:

> "…*the arbitration clause which is a dispute resolution clause as per the well settled principle of law is a collateral term in the contract and cannot perish on account of the change or alteration in the performance as per the well settled principle of law…if there is a dispute resolution clause, which would include the disputes of diverse nature including the claims arising out of the obligations and breaches prior to the termination and post termination of the agreements between the parties and the matters incidental thereto and more importantly the dispute as to whether there exists a novation of the agreement or not which in the prima facie view of this court, it is*

[358] *Union Carbide Corporation. v. Union of India*, (1991) 4 SCC 584.
[359] 215 (2014) DLT 112; 2014 (4) Arb LR 273 (Delhi).

> *not, the arbitration clause in such a case cannot be said to be come to an end or for that matter altered merely because there is exchange of the performances or obligations from one hand to another…*"[360]

Therefore, the effect of the doctrine of severability is to immunise or insulate the arbitration agreement enshrined in the main contract from any vicissitudes and vagaries of frustration, novation, rescission, remission that may govern the main contract. This means that even if the main contract stands novated or altered or frustrated, the parties thereto will still be able to get the arbitration agreement enforced and therefore attain the resolution of their dispute by their chosen method of arbitration.

Section 16 of the Arbitration and Conciliation Act, 1996 enacts the principle of severability in its sub-section (1) (a) as follows:

> "*…an arbitration clause which forms part of a contract shall be treated as an agreement independent of the other terms of the contract…*"

Therefore, there will be no effect on an arbitration agreement contained in a clause of the main contract even where such main contract may be said to have been discharged by agreement or novation.

**REMEDIES FOR BREACH OF CONTRACT**

One of the ways in which a contract may be discharged is breach, which is an "antithesis of performance". Simply put, breach of a contract occurs when the parties thereto do not perform their part of the promise. Unlike performance, which as a form of discharge concludes the legal relationship that the contract effected, breach on the other hand, opens new doors and signals the dawn of new rights and liabilities for the parties. Breach of a contract would amount to enabling the wronged party to legally enforce its contractual rights. The legal enforceability of "contract" as in the case of a breach is what distinguishes it from moral or non-legally enforceable or legally unenforceable "agreements". The law recognizes that since a wronged party has suffered injustice as a consequence of the breach of the other party, it must have a remedy. This is the principle of "*ubi jus ibi remedium*,"[361] which means that where there is a right, there must be a remedy in order to avail that right. In *Associated*

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[360] To state this, the Court relied on the Supreme Court of India's judgments in the following cases: *National Agricultural Co-Op. Marketing Federation India Ltd. v. Gains Trading Ltd*, (2007) 5 SCC 692 and *P. Manohar Reddy & Bros. v. Maharashtra Krishna Valley Development Corporation and Ors*, (2009) 2 SCC 494.

[361] *Ashby v. White* (1703) 14 St Tr 695, 92 ER 126.

*Cinemas of America Inc. v World Amusement Co.*[362], an American court defined "breach" as a situation where "*a party thereto renounces his liability under it, or by his own act makes it impossible that he should perform his obligations under it or totally or partially fails to perform such obligations*". Therefore, a breach giving rise to discharge may occur in three ways:

1. When a party renounces its obligations under the contract,
2. When a party by its own conduct makes it impossible for itself to fulfil its contractual obligations; and
3. When a party fails to perform its promise.

While the first two scenarios occur in the course or process of performance or where the performance may not yet be due on the part of the party; and hence it is only in anticipation of foreseeable future that it seems that the party will be unable to perform. This is the case of an "*anticipatory*" breach. On the other hand, the third way is one where the party stands in "*actual*" breach of its contractual obligation.

Where a contract stands breached, either *actually* or in *anticipation*, the primary obligations of the party in breach are accounted for by its secondary obligation to compensate the wronged or injured party. Such compensation may take effect either in money or in non-money terms. The consequences of breach (exercisable remedies) may either be found in the contract itself or in the law of contracts. Sometimes the parties to the contract specified within the terms of the contract as to what will be the consequences of the breach; mostly providing for a sum of damages payable by the party in breach. In the United States this is mostly the case and such pre-decided damages are called double quotes begin double "*liquidated damages*". However, in India, the parties entering into the contract are said to be in the "*honeymoon stage*" where they do not contemplate that their contract may come to be discharged by way of breach and not by way of performance; they hate to think about breach of contract and keep lawyers away from the scene. This leads to a situation where injured parties often end up in court, asking it to compute the damages payable by the party in breach. However, since litigation (or any other form of dispute resolution) is usually inefficient and costly, it may be prudent to have terms of the contract dealing with the consequences of any breach committed by either party.

However, if the terms of the contract are silent or inadequate to guide the parties as the consequences of the breach, the injured party may knock at the court's doors for relief. While the Common Law courts in England used to only award "*damages*" in cases of contractual breaches, later the Courts of Equity gave birth to what came to be known as equitable

[362] (1937) 201 Minnesota 94.

remedies of "*specific performance*" and "*injunction*". As happened in England in 1873,[363] which was transplanted in India later, the divergent systems of common law and equity were synthesized and came to be administered by one set of courts alone. Therefore, today, all law courts can award both common law and equitable reliefs. In India, the Indian Contract Act, 1872 provides for the awarding of damages, and the Specific Relief Act, 1963 (replacing the earlier Specific Relief Act of 1877) provides for the equitable reliefs. Taking a holistic perspective of the law of remedies in cases of contractual breaches, the authors of Anson's Law of Contract put forth the following:

> *"These remedies fall under three heads:*
>
> *(1) Every breach of contract entitles the injured party to damages. Damages are primarily concerned to compensate the injured party for the loss he or she has suffered.*
> *(2) In certain circumstances the injured party may obtain the enforcement of the promise by an order for specific performance of the contract, an injunction to restrain its breach or for the payment of the sum due under the contract.*
> *(3) In certain circumstances the parties to a contract that has been broken may be entitled to the return of money paid or restitution of the value of services rendered or goods transferred. These are restitutionary remedies for the independent cause of action of unjust enrichment. They are not remedies for the breach of contract. Exceptionally an injured party may be granted an award reflecting the gain made by the contract-breaker from the breach of contract. This is a restitutionary remedy for the breach of contract.*"[364]

**DAMAGES**

Damages are in the nature of monetary compensation that is paid by the party in breach to the injured party. The origin of this remedy is traceable to common law. The fundamental principles to compute damages were exhaustively first considered by the Court of Exchequer in England in the case of *Hadley v. Baxendale*.[365] Overtime, different courts have affirmed what was held in this case, and from these judicial pronouncements was the content of Section 73 (relating to awarding damages for breach) in the Indian Contract Act, 1872 finalized. Since damages were also awarded in cases of tortious liability, many courts deemed appropriate in the 19th century to distinguish those cases with the award of damages in cases of contractual liability.

In *Hadley v. Baxendale*, the work in Hadley's (plaintiff) mill suffered cessation due to a broken crank shaft. To get the mill back working, the broken shaft was to be sent to its

[363] The Judicature Act of 1873.
[364] SIR JACK BEATSON ET.AL., ANSON'S LAW OF CONTRACT, 53 (2010)., which further cites TREITEL, REMEDIES FOR BREACH OF CONTRACT (1988).
[365] (1854) 9 Ex 341.

makers at Greenwich. The defendant who was a common goods carrier and transporter, promised to deliver this shaft at Greenwich within a day's time. The defendant was informed about the broken shaft and the nature of the plaintiff's business activity carried out in the mill. However, Baxendale was negligent and thus unduly delayed the transit. The consequence of this was that the mill remained idle for such longer time duration than it would have been if the contractual promise would have been performed as promised (i.e. in a day's time). Due to this, the plaintiff lost profits for which he sued Baxendale for damages. The Court of Exchequer laid down that the damages payable on account of contractual breaches should be such as may "*fairly and reasonably*" be considered either arising naturally according to the usual course of things from such breach or such as may be supposed to have been in the contemplation of both parties at the time they made the contract, as the probable result of its breach. These have become the golden words that define the law relating to payment of unliquidated damages in cases of contractual breaches, acquiring for themselves the sobriquet "*the rule in Hadley v. Baxendale*".

The *ratio* in this case was incorporated as the general rule in Section 73 of the Indian Contract Act, 1872 which provides as follows:

> *"**Section 73 - Compensation for loss or damage caused by breach of contract***
>
> *When a contract has been broken, the party who suffers by such breach is entitled to receive, from the party who has broken the contract, compensation for any loss or damage caused to him thereby, which naturally arose in the usual course of things from such breach, or which the parties knew, when they made the contract, to be likely to result from the breach of it.*
>
> *Such compensation is not to be given for any remote and indirect loss or damage sustained by reason of the breach.*
>
> *Compensation for failure to discharge obligation resembling those created by contract*
>
> *When an obligation resembling those created by contract has been incurred and has not been discharged, any person injured by the failure to discharge it is entitled to receive the same compensation from the party in default, as if such person had contracted to discharge it and had broken his contract.*
>
> *Explanation. - In estimating the loss or damage arising from a breach of contract, the means which existed of remedying the inconvenience caused by the non-performance of the contract must be taken into account."*

Thus, there are two types of damages: ordinary and special. While the former are awarded for the breach *per se* ("*compensation for any loss or damage caused to him thereby, which* *naturally arose in the usual course of things from such breach*”), the latter may only be awarded where the special foreseen or contemplated consequences (“*which the parties knew, when they made the contract, to be likely to result from the breach of it*”) of the breach have occasioned as a result of the breach.

This legal position in Section 73 is supplemented by way of exemplification in as many as eighteen illustrations from *(a)* to *(r)* in the Act, to which one must refer so as to understand the provision better.

Baron Alderson of the Court of Exchequer went on to observe and lay down that in a situation where there was little or no informational asymmetry between the contractual parties as to the foreseeability of the effects of a breach, then the damages to be awarded would be such as was the foreseeable injury so known and communicated between the parties. However, in a case of informational asymmetry, where the defendant was not aware or was not made aware of the effective consequences of a breach (such as loss to the plaintiff due to cessation of his mill), then he could not be said to have in his mind or contemplation those effective consequences if he chose or the circumstances made him to breach his promise. Applying these principles, Alderson denied the loss of profits in this case to be paid as damages.

Thus, in the case of *Simpson v. London and North Western Railway Co.*,[366] where the plaintiff had consigned certain of his goods for dispatch to a place to be displayed at an agricultural fair, and had written “must be at Newcastle Monday certain” it was held that the defendant railway company must be said to be possessing the knowledge of special circumstance thus exposing it to payment of special damages when it delayed the performance of its promise to deliver such goods.

**Remoteness of damages**

The authors of the Anson’s Law of Contract before treading upon the subject of remoteness of damages, allude to the concept of “*causation*” and propose as follows:

> “*In order to establish a right to damages for a loss the claimant must show that the breach of contract caused the loss. Establishing ‘but for’ causation (i.e., that but for the breach of contract, the loss would not have been suffered) is not enough. Rather*

[366] (1876) 1 QB 274.

*the breach of contract must be the 'effective' cause of the loss, as opposed to an event which merely gives the opportunity for the claimant to sustain the loss*."[367]

Once the test for causation has been established, the courts account for whether the damages sought are too remote to be awarded by the court. If they are remote, they may not be awarded by the court. Alderson's exposition of the principle of damages is understood to also lay down the doctrine of remoteness of damages. Such clarity to the Baxendale rule was rendered by Lord Justice Asquith in *Victoria Laundry (Windsor) Ltd. v. Newman Industries Ltd.*[368] who held that if the loss actually resulting from the breach was "*reasonably foreseeable*" at the time of the entering into the contract, then it would be recoverable. If it was not so foreseeable, then it would be too remote to be recoverable through a court of law. To determine as to what can be reasonably foreseeable at the time of entering into the contract, one must assess the knowledge then possessed by such party who is later found to be in breach. In law, such knowledge may be possessed by a party either *actually* (for instance, where there was express communication between the contracting parties) or *imputably*. The latter will be a case with such knowledge as must be assumed to be available with all reasonable persons who are ordinarily taken to know "*what loss may be likely to result in the ordinary course of things*". However, Asquith further went on to hold that if there were some special circumstances likely to cause more loss to the plaintiff which the defendant may be aware of, in addition to this general knowledge, then the plaintiff may sue for such extra sum of damages.

The facts of the case in *Victoria Laundry* were such that an engineering firm delivered a boiler on 8 November which they otherwise contractually ought to have delivered on 5 June. The facts further showed that the engineering firm was fully made aware that such boilers played a central role in the expansion prospects of the plaintiff which carried the potential of generating high profits. The Court of Appeal held that the defendants, with their knowledge of the industry and of the special facts, could not escape the conclusion that the loss of potential profits was beyond their foresight. Hence, Asquith LJ awarded higher damages on account of "*reasonable foreseeability*" on the part of the defendants of such higher economic injuries.

However, as we now know, the liability under contracts is essentially different from that under torts; as in the former it is the intention of the parties which reigns supreme. The decision in *Victoria Laundry* came to be criticized and hence modified by the House of Lords

[367] SIR JACK BEATSON ET.AL., ANSON'S LAW OF CONTRACT, 543 (2010).
[368] (1949) 2 KB 528.

in *Heron II, Koufus v. Czarnikov Ltd.*[369] where a general test of reasonable foreseeability on the part of the defendant was replaced with a more nuanced test of whether the foreseeability of such damages was in the reasonable contemplation of *both the parties* at the time of entering into the contract. Therefore, if either of the parties could not be said to possess knowledge so as to form an opinion about the reasonable foreseeability of damages on account of loss of profits, a suit to seek such extra damages would be held to be remote to the contract and hence denied. In this case, a ship-owner was held to be presumably supposed to be aware of price-fluctuations in markets of the goods that he was contractually made bound to deliver and transport. In a different case, Lord Wright[370] distinguish the payments of damages in a form of a continuum of a straight line where remarked that while *firstly* damages may be payable on account of breach of contract (i.e. first or primary consequence), in situations, they could *secondly* be payable for such "*consequences of the consequence* [first consequence of breach simpliciter]" as were reasonably foreseeable by both the parties. Therefore, payment of damages hence came to be distinguished into the two components of:

1. Ordinary damages, and
2. Special damages.

In some cases, contractual damages may also be recoverable for "*substantial physical inconveniences*" or mental distress caused by a contractual breach. For example, where a family were transported by a railway company to the wrong railway station, forcing them to walk several kilometers home on a raining wet night, in *Hobbs v London & South Western Railway*[371] they were awarded damages for such physical inconvenience caused. The authors of the Anson's Law of Contract have identified two scenarios where such damages for mental distress may be awarded:

> "*Damages for mental distress can be awarded where the claimant's distress is directly consequential on physical inconvenience caused by the breach of contract. They can also be awarded where an important purpose of the contract is to provide enjoyment or peace of mind, or to prevent distress.*"[372]

Another qualifier in this context is that although damages cannot be recovered in a contractual action for injury to reputation *per se*, but they may be where the loss of reputation caused by the breach of contract causes financial loss. [373]

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[369] (1969) 1 AC 350.
[370] (1933) AC 449.
[371] (1875) LR 10 QB 111.

[372] SIR JACK BEATSON ET.AL., ANSON'S LAW OF CONTRACT, 536 (2010), citing *Perry v. Sidney Phillips & Sons*, [1982] 1 WLR 1297 and *Jarvis v. Swans Tours Ltd*, [1973] QB 233.
[373] *Malik v. Bank of Credit & Commerce International SA*, [1998] 1 AC 20.

**Ascertainment of Damages**

Once it has been determined by a court on an *in-principle* level as to whether or not damages (both ordinary and special) would be payable, then the next step in a suit seeking remedy for breach would have to assess and ascertain the actual sum of money that should be paid to the plaintiff. If on the other hand, it is decided that no damages have to be paid to the plaintiff, then the court need not progress to this stage of determination.

In order to find out how much money ought to be awarded as damages to a plaintiff in order to remedy the contractual injury suffered by him as a result of the breach, the principle of *restitutio in integrum* provides guidance. Judicially first pronounced in the case of *Sunley Ltd. v. Cunward White Store Ltd*.[374], the principle dictates that so far as monetary damages can, they should always restore the plaintiff to such a point as if he would have been at, had he did not suffer the contractual injury. Thus, damages should be quantified at such value that "*where a party sustains loss by reason of breach of a contract, he is, so far as money can do it, to be placed in the same situation with respect to damages, as if the contract has been performed*".[375]

One way of breaking up the two components of damages would be to provide for (a) expectation loss and (b) reliance loss. While the former is what the plaintiff would have received had the contract been performed, the latter is the loss caused to the plaintiff on account of relying on the contractual promise of the defendant. In *Anglia Television v. Ried*[376], the Queen's Bench laid down that reliance losses would be payable as damages as were sought by the plaintiff. In this case, the plaintiff had contractually engaged an American actor to appear for a television show. However, the actor (defendant) declined to make the television appearance at the very last moment, leaving the plaintiff with no time to find a replacement. The plaintiff in this case, did not mount a case seeking damages on account of expected profits that it would have made had the show been broadcasted with the actor, but on account of all preparations made by it to host the actor: such as engaging a script writer, hiring other actors, rent for the location etc. The Court upheld plaintiff's suit and awarded him such damages as were based on its reliance of the defendant actor's promise.

Thus, damages are awarded on account of the loss suffered by the plaintiff as a result of the breach. If no loss is suffered as a result of breach, the plaintiff may still obtain a court judgment in his favor, but the damages awarded in this case will only be nominal or notional.

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[374] (1940) 1 KB 740.
[375] *Robinson v Harman*, (1848) 1 Exch 850, 855.
[376] (1972) 1 QB 60.

Damages are only meant to compensate the plaintiff for his loss, and it is not the court's job, hearing a suit arising out of contractual breach, to punish a defendant for a contractual breach. Therefore, damages must not be calculated with a motive to penalize or punish the defendant party in breach. Even vindictive or exemplary damages have no place in the law of remedies for contractual breach. In Judge Hawthrone's words:

> "*the primary aim or principle of the law of damages for a breach-of-contract is to place the plaintiff in the same position he would be in if the contract had been fulfilled, or to place the plaintiff in the position he would have occupied had the breach of contract not occurred*."[377]

Once this purpose stands fulfilled, that is where the line must be drawn in the awarding damages. In *Ruxley Electronics and Construction ltd. v. Forsyth*[378] the defendant had committed a breach of the nature that in a contract for the construction of a swimming pool, the depth of the pool so constructed happened to be lesser than what was stipulated in the contract. The pool being otherwise useful to the plaintiff, the court only allowed the difference in value of the pool as provided and its value as it should have been provided. The Court refrained from allowing the cost of setting right the pool because that would have given the plaintiff "*windfall profits*" which are impermissible in the law of contractual damages as the purpose here is only to compensate the claimant and not to punish the defendant. Even where a defendant's conduct was outrageous, contractual awarded cannot be used to inflict punitive force. In *Addis v. Gramophone Co.*[379] where the defendant had wrongfully dismissed his salaried agent in Calcutta without giving the contractually required six-months' notice, there was nothing more than salary and estimated commission that the court awarded as damages. Limiting the quantum of damages to compensatory purposes, the House of Lords held that such "*employers were not to be penalized in damages for the humiliating and oppressive manner in which they*" might have dismissed their contracted employed.

**Mitigation of damages**

While ascertaining the amount of damages that it will ask the defendant to pay to the plaintiff, the court must also ascertain whether or not the plaintiff took any reasonable steps available to him in order to reduce or mitigate the extent of injuries suffered by him as a consequence of the contractual breach. What must be ascertained is whether the plaintiff

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[377] *Firiedman Iron & Supply Co. v. J.B. Bearid & Co.,* (1952) 63 SO 2d 144 (Supreme Court of Louisiana).
[378] 1996 AC 344.
[379] [1909] AC 488.

acted reasonably post actual or anticipatory breach and took steps which were possible to take, in order to minimize his injuries as a consequence of the breach. This is a question of fact and the defendant may induce evidence in order to show that the plaintiff did not take reasonable steps in order to mitigate his injuries.

This principle is another manifestation of the principle against remoteness of damages, as expressed by Lord Haldane in *British Westing House Electric & Manufacturing Co. v. Underground Electric Railway Co. of London*[380] where the first principle of compensation for pecuniary loss naturally flowing from the breach was qualified by a secondary principle which imposed a duty of taking all reasonable steps to mitigate the loss. The duty to mitigate damages makes those possible claims of damages remote which may occasion due to the plaintiff's neglect to take reasonable steps in this regard. This principle finds expression in the Explanation to Section 73 of the Indian Contract Act, 1872 which states that "[in] *estimating the loss or damage arising from a breach of contract, the means which existed of remedying the inconvenience caused by the non-performance of the contract must be taken into account*". Some scholars have pointed out that the explanation does not create a duty to mitigate, but only provides a consideration that a court must keep in mind while adjudicating a suit for damages.

The concept of mitigation often has application in breaches of contracts of sale and purchase of goods.[381] Where a buyer refuses to take delivery as promised, the seller should resell the goods at the market price and may thereafter sue to recover the difference between the contractual price at which he had agreed to sell the goods to the defendant and the market price at which he eventually sold the goods. Avtar Singh comments that if a seller does not resell the goods and therefore aggravated loss is borne by him due to the falling market prices, such seller cannot recover such enhanced loss that is attributable to his negligence. A leading case on the point is Privy Council's judgment in *A.K.A.S. Jamal v. Molla Dawood Sons & Co.*[382] where the defendants had refused to pay as per their promise in the contract to buy shares from the plaintiff on a particular date in December. The plaintiffs did not sell the shares to some other party on that day at a loss of Rupees 1,09,218 as the market rate on that date had fallen from what had been mentioned in the contract when the market was on the rise. They waited and sold the shares only when the market price had again risen in February, thus fetching them a price which was only Rupees 79,862 lesser than the contractual price. The defendants from the original contract contended that they should be made liable only to pay Rupees 79,862 and not the earlier differential amount as stood on the (December) date of their decline to accept delivery of shares. Lord Wrenbury held that the loss incurred by the

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[380] (1912) AC 673.
[381] *P.S.N.S Ambalavana Chettiar v. Express Newspapers Ltd*., AIR 1968 SC 741.
[382] (1915-1916) 43 IA 6.

plaintiff must be ascertained as it stood on the date of the breach (December) and not as it was ultimately borne by the plaintiff in February, and hence awarded to the plaintiff Rupees 1,09,218 as damages. Mitigation is not taken to prejudice a plaintiff in such a scenario, as if a seller "*retained the shares after the breach, he cannot recover from the buyer any further loss, nor he is liable to have the damages reduced if the market rises*".

However, the concept of mitigation must not be read to impose unreasonable or unusual burden on the part of the wronged party. Where the damage was avoidable and not avoided by the plaintiff, there such damages as may ultimately be awarded be reduced by such avoidable quantum that could and ought to have been mitigated.

**PENALTY AND LIQUIDATED DAMAGES**

Liquidated damages are such which are stipulated in the terms of the contract at the very occasion of entering into the contract or otherwise agreed to between the parties which a party undertakes to pay to the other in case of breach of their promise under such contract. The proof of a contractual breach is essential for such a contractual cause to be triggered.[383] Section 74 of the Indian Contract Act, 1872 reads as follows:

> *"When a contract has been broken, if a sum is named in the contract as the amount to be paid in case of such breach, or if the contract contains any other stipulation by way of penalty, the party complaining of the breach is entitled, whether or not actual damage or loss is proved to have been caused thereby, to receive from the party who has broken the contract reasonable compensation not exceeding the amount so named or, as the case may be, the penalty stipulated for."*

The legal content in the Section is supplemented and exemplified by way of seven (a to g) illustrations appended thereto. The essence of the provision is that a wronged or an injured party may seek "*reasonable compensation*" not exceeding the contractually stipulated amount from the party in breach. In Indian law, there is a distinction between liquidated damages and penalty: where reasonable damages fall short of the stipulated sum, the sum payable will be reduced to that extent as penalty.

Another facet of Section 74 is the meaning conveyed by the expression "*whether or not actual damage or loss is proved to have been caused thereby*" which may mislead a reader to believe that actual loss may not be necessary. In this regard, Section 74 must be read along

[383] *FACT Engg Works v. Kerala Industries*, AIR 2001 Ker 326.

with the preceding Section 73 and in light of the Supreme Court of India's decision in *Maula Bax v. Union of India*. [384] The court held that where no loss was proved, neither Section 73 nor Section 74 would be attracted. The phrase only applies to a situation where it may be impossible for a plaintiff to prove the monetary value of the loss suffered by him. Where however, the loss in money is capable of being determined, it must be so proved.

The explanation appended to the provision states that "*a stipulation for increased interest from the date of default may be a stipulation by way of penalty*". This clarifies that parties, may, in addition to the sum of damages, may also provide for payment of interest on such sum, payable in case of delay from the date of default/breach.

The courts have come down heavily against agreements which stipulate/liquidate a sum of damages either unconscionably or extravagantly.[385] While adjudicating a suit seeking the awarding of liquidated damages, Indian courts have the latitude to reduce the amount stipulated by the parties to a reasonable level. According the position in English law, the court must either accept the liquidated sum in whole or reject it in whole.[386]

The sum so stipulated in a contract, must be "liquidated" which means that it should not be an unascertained sum of money that one party may reserve the right to quantify at the point of the breach of contract. This came up before the Supreme Court of India in *State of Karnataka v. Shree Rameshwara Rice Mills*[387] where the court held a contractual clause according one of the parties such autonomy as void as it held that a "*party to a contract cannot be an arbiter in his own cause*".

**INJUNCTIONS**

An injunction is an equitable remedy where a defendant may be ordered to refrain and abstain from doing a particular act. Injunctions can only be granted where damages may be an appropriate remedy or where the contract may be capable of being specifically enforced (specific performance). The remedy only attracts to the *person*, thus applicable only *in personam*, and not *in rem*. This means that it does not run with the subject matter or the property where a person was injuncted from doing something with such subject matter or such property. It is a remedy which the court may grant in its discretion.[388] In India, the law relating to the grant of injunctions is contained in the Specific Relief Act, 1963 and is supplemented by some provisions contained in the Code of Civil Procedure, 1908.

[384] (1969) 2 SCC 544.
[385] AVTAR SINGH, CONTRACT LAW AND SPECIFIC RELIEF 520 (2013).
[386] *Fateh Chand v. Balkishan Dass*, AIR 1963 SC 1405.
[387] AIR 1987 SC 1359.
[388] Section 36, Specific Relief Act, 1963.

Temporally (in the sense of their effect in time), injunctions may be either (1) *temporary* or (2) *perpetual*. Instrumentally (in the sense of what they do), they may be either (1) *prohibitive* or (2) *mandatory*. The authors of Anson's Law of Contract explain the distinction between the latter types as follows:

> "*Injunctions are either prohibitory or mandatory. A prohibitory injunction may be granted to restrain the breach of a negative contract or of a negative stipulation in a contract. A mandatory injunction compels the positive performance of an act and may be used to restore the situation to what it was before the breach of contract*."[389]

Chapter VII of the Specific Relief Act, 1963 deals with injunctions, where Section 37 temporally distinguishes injunctions:

> **"*Section 37 - Temporary and perpetual injunctions***
>
> *(1) Temporary injunctions are such as are to continue until a specific time, or until the further order of the court, and they may be granted at any stage of a suit, and are regulated by the Code of Civil Procedure, 1908 (5 of 1908).*
>
> *(2) A perpetual injunction can only be granted by the decree made at the hearing and upon the merits of the suit; the defendant is thereby perpetually enjoined from the assertion of a right, or from the commission of an act, which would be contrary to the rights of the plaintiff*."

Rule 2 of Order XXXIX of the Code of Civil Procedure, 1908 provides that in a suit for restraining a defendant from committing a breach of contract, the plaintiff may at any time after the commencement of the suit apply to the court for a temporary injunction to restrain such defendant from committing the breach of contract.

In *Lumley v. Wagner*[390] the defendant had contractually agreed to sing at plaintiff's theater for a particular time duration and to sing nowhere else during such contractual period. But soon the defendant not only refused to not perform his *positive* part of the contract to sing at the plaintiff's theater, but also entered into a different contract with a different theater to perform over there, thus breaching also his *negative* promise not to perform at any theater other than that of the plaintiff. The court injuncted the defendant from performing at the other theater, rationalizing that the same may induce him to perform his positive promise.[391]

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389 SIR JACK BEATSON ET.AL., ANSON'S LAW OF CONTRACT, 581 (2010).

390 (1852) 5 De GM&G 604.

391 Note that the contract being one of personal skill, the defendant could not have been ordered particularly to perform at the plaintiff's theatre (i.e. it could not have specifically enforced). For further clarity, one may refer to Section 42 of the Specific Relief Act, 1963 which permits this to happen which reads as follows: "*Notwithstanding anything contained in clause (e) of section 41, where a contract comprises an affirmative agreement to do a certain act, coupled with a negative agreement, express or implied, not to do a certain act, the circumstances that the court is unable to compel specific performance of the affirmative agreement shall not*

Similar facts made the King's Bench reach a similar decision in *Warner Bros. v. Mrs. Nelson*.[392] Thus, awarding of a preventive injunction to enforce a negative term may have the indirect effect of leaving a defendant without any alternate course of action but to perform out the positive term. The authors of Anson's Law of Contract have termed this possibility as providing for "*indirect specific performance*".[393]

An injunction what commands or mandates the defendant to do something is called a mandatory injunction. According to Salmond, a mandatory injunction is sought to command the defendant to do a positive act for the purpose of putting an end to a wrongful state of things created by him, or otherwise fulfil his legal obligations. For example, a court may order a defendant to demolish a building or a construction which the defendant may have erected in violation of a contractual term. Section 39 of the Specific Relief Act, 1963 defines a mandatory injunction as follows:

> "***Section 39 - Mandatory injunctions***
>
> *When, to prevent the breach of an obligation, it is necessary to compel the performance of certain acts which the court is capable of enforcing, the court may in its discretion grant an injunction to prevent the breach complained of, and also to compel performance of the requisite acts*."

Section 41 of the Act provides as to when a court would refuse granting a perpetual injunction:

> **"*41. Injunction when refused***
>
> *An injunction cannot be granted--*
>
> *(a) to restrain any person from prosecuting a judicial proceeding pending at the institution of the suit in which the injunction is sought, unless such restraint is necessary to prevent a multiplicity of proceedings;*
> *(b) to restrain any person from instituting or prosecuting any proceeding in a court not subordinate to that from which the injunction is sought;*
> *(c) to restrain any person from applying to any legislative body;*
> *(d) to restrain any person from instituting or prosecuting any proceeding in a criminal matter;*
> *(e) to prevent the breach of a contract the performance of which would not be specifically enforced;*
> *(f) to prevent, on the ground of nuisance, an act of which it is not reasonably clear that it will be a nuisance;*

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*preclude it from granting an injunction to perform the negative agreement: Provided that the plaintiff has not failed to perform the contract so far as it is binding on him*."

[392] (1937) 1 KB 209.

[393] SIR JACK BEATSON ET.AL., ANSON'S LAW OF CONTRACT, 587 (2010).

*(g) to prevent a continuing breach in which the plaintiff has acquiesced;*
*(h) when equally efficacious relief can certainly be obtained by any other usual mode of proceeding except in case of breach of trust;*
*(ha) if it would impede or delay the progress or completion of any infrastructure project or interfere with the continued provision of relevant facility related thereto or services being the subject matter of such project.*

*(i) when the conduct of the plaintiff or his agents has been such as to disentitle him to the assistance of the court;*
*(j) when the plaintiff has a no personal interest in the matter.*"

Section 40[394] is an important clarificatory provision as per which a plaintiff may also seek damages either in addition to or in substitution of a claim for a mandatory or a perpetual injunction. For instance, in *Tilok Chand v. Dhundiraj*[395], the Court awarded damages to a plaintiff neighbor instead or injunction the defendant to demolish to encroaching construction.

**REFUND AND RESTITUTION**

The authors of Anson's Law of Contract begin their chapter on restitutionary remedies with the following words:

> "*A person who pays money or renders services or supplies goods to the defendant pursuant to a contract which is discharged by breach may be entitled to restitution of the money paid or to restitution in the form of a reasonable remuneration for the services rendered (quantum meruit) or a reasonable price for the goods supplied (quantum valebat). These restitutionary remedies may be available not only to an innocent party but also, in certain situations, to a contract-breaker. These remedies may also be available in respect of money paid or non-money benefits rendered under other ineffective agreements including those that are void, illegal, discharged for frustration, or too uncertain to amount to contracts: such claims, which are outside the scope of this part of the book, since they do not follow a breach of contract, have been briefly considered in the chapters on ineffective contracts.*"

It must be noted that the cause of action enabling a party to claim for refund or restitution lies in the concept of unjust enrichment. Broadly, there may be three situations where a claim

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394 It reads as follows: *"(1) The plaintiff in a suit for perpetual injunction under section 38, or mandatory injunction under section 39, may claim damages either in addition to, or in substitution for, such injunction and the court may, if it thinks fit, award such damages. (2) No relief for damages shall be granted under this section unless the plaintiff has claimed such relief in his plaint: Provided that where no such damages have been claimed in the plaint, the court shall, at any stage of the proceedings, allow the plaintiff to amend the plaint on such terms as may be just for including such claim. (3) The dismissal of a suit to prevent the breach of an obligation existing in favour of the plaintiff shall bar his right to sue for damages for such breach."*
395 AIR 1957 Nag 2.

seeking restitution may arise: recovery of money paid during the contractual relationship, seeking return of goods provided or seeking an account of profits measured by benefits to the contract-breaker.[396]

The principle of *quantum meriut* states that where a party has in the performance of his or her contractual obligation rendered some service and any further performance has been made futile or useless by the other party thereto, he may recover reasonable compensation for such work or service.[397] In *Craven Ellis v. Canons Ltd.*[398] a restitutive recovery was allowed when a person had rendered services under a supposed contract which was later found out to be a nullity.

Section 65 of the Indian Contract Act, 1872 provides for the remedy of restitution as an obligation casted on a "*person who has received advantage under void agreement, or contract that becomes void*" and reads as follows:

> "*When an agreement is discovered to be void, or when a contract becomes void, any person who has received any advantage under such agreement or contract is bound to restore it, or to make compensation for it to the person from whom he received it*."

For example, as a matter of illustration, where A pays B 1,000 rupees in consideration of B's promising to marry C, A's daughter but C (i.e. the daughter) is dead at the time of the promise. Therefore, since the agreement is void, therefore under Section 65 B must repay A the 1,000 rupees.[399]

**SPECIFIC PERFORMANCE**

Specific performance is another equitable remedy available to a plaintiff in case of a contractual breach where the court may direct the defendant to actually perform his contractual promise or a part thereof. On the relationship between the award of damages and specific performance, the revising authors of Anson's Law of Contract have commented that "[i]*f the claimant's interest in the performance of the contractual obligations cannot*

[396] SIR JACK BEATSON ET.AL., ANSON'S LAW OF CONTRACT, 587 (2010).
[397] AVTAR SINGH, CONTRACT AND SPECIFIC RELIEF 568 (2013).
[398] (1936) KB 403.
[399] Another illustration is appended to the Section in the bare act which illustrates that: "A, a singer, contracts with B, the manager of a theatre, to sing at his theatre for two nights in every week during the next two months, and B engages to pay her a hundred rupees for each night's performance. On the sixth night, A willfully absents herself from the theatre, and B, in consequence, rescinds the contract. B must pay A for the five nights on which she had sung."

*adequately be protected by an award of damages, there has been greater willingness to order that the contract be specifically performed where this is possible and practicable*."[400]

Section 10 of the Specific Relief Act, 1963 was recently amended in 2018 to make all contracts capable of specific performance unless they are incapable of such specific performance by virtue of the provisions contained in Section 11 (2), Section 14 or Section 16 of the Act. Previously (i.e. before 2018) the position as per the old Section 10 was that only those cases of contractual breaches where either there was no standard for ascertaining the actual damage caused by non-performance or where compensation in money would not afford adequate relief would be capable of being specifically enforced by a court. This position has undergone a radical shift in 2018 where all contracts unless falling within the radar of Sections 11 (2) or 14 or 16 would be capable of being specifically enforced. This policy-shift suggests an inclination and a legislative preference in favor of specific performance as a form of remedy to address contractual breaches.

Yet reference to the older provisions of Section 10 may be made in order to get an insight into the rationale and purpose of specific performance. The older Section carved a scope for specific performance in cases where there was either no standard available to compute a contractual injury in monetary terms or where the nature of the contractual promise could not be compensated solely in money-terms. But after the 2018 amendment, these conditions *do not limit* the scope of contracts capable of specific enforcement but can only *explain* the ambit of the remedy of specific relief. For example, an explanation appended to the older Section 10 as an example provided that unless otherwise proved, the "*breach of a contract to transfer immovable property*" would not be capable of being "*adequately relieved by compensation in money*".

Now to understand when shall a court be precluded from awarding specific performance of a contract, reference may be made to the following provisions:

**Section 11 (2)**:

> "*A contract made by a trustee in excess of his powers or in breach of trust cannot be specifically enforced.*"

**Section 14**:

> "*The following contracts cannot be specifically enforced, namely: --*
>
> *(a) where a party to the contract has obtained substituted performance of contract in accordance with the provisions of section 20;*

[400] SIR JACK BEATSON ET.AL., ANSON'S LAW OF CONTRACT, 534 (2010).

(b) *a contract, the performance of which involves the performance of a continuous duty which the court cannot supervise;*

(c) *a contract which is so dependent on the personal qualifications of the parties that the court cannot enforce specific performance of its material terms; and*

(d) *a contract which is in its nature determinable.*"

**Section 16:**

"*Specific performance of a contract cannot be enforced in favour of a person--*

(a) *who has obtained substituted performance of contract under section 20; or*

(b) *who has become incapable of performing, or violates any essential term of, the contract that on his part remains to be performed, or acts in fraud of the contract, or willfully acts at variance with, or in subversion of, the relation intended to be established by the contract; or*

(c) *who fails to prove that he has performed or has always been ready and willing to perform the essential terms of the contract which are to be performed by him, other than terms of the performance of which has been prevented or waived by the defendant.*

*Explanation. -- For the purposes of clause(c), --*

(i) *where a contract involves the payment of money, it is not essential for the plaintiff to actually tender to the defendant or to deposit in court any money except when so directed by the court;*

(ii) *the plaintiff must prove performance of, or readiness and willingness to perform, the contract according to its true construction.*"

In all other cases (except as those covered by the aforementioned provisions of Sections 11 (2), 14 and 16) would be capable of being specifically enforced against a defendant as per the Specific Relief Act, 1963.

Therefore, as per the proscriptions contained in Section 14, contracts such as those of marriage, employment, personal service, skill, cannot be specifically enforced. In *Scott v. Rayment*[401] the contract of partnership was held to be not capable of determination in nature as either of the partners could at will dissolve the partnership. In *Dowty Boulten Paul Ltd. v. Walver Rampton Corporation*,[402] it was observed that a contract to have a "*an airfield in constant operation*" would require constant supervision of the court, and hence would not be amenable to specific enforcement.

If a contract has a number of terms which the defendant has to perform, whether or not such contractual terms may be ordered to be specifically performed as against other terms is a question which is answered by Section 12 of the Act. Sub-Section 1 of Section 12 lays down

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[401] (1868) LR Equ. 1912.

[402] (1971) WLR 204.

a general rule that a court "*shall not direct the specific performance of a part of a contra*ct". However, Sub-Section (2) provides that where the unperformed part is only a small proportion to the whole contractual promise in value and admits of payment of damages, the court may direct the specific performance of so much of the contract as can be performed and award compensation for the remaining deficient t performance. Sub-Section (3) provides that where the unperformed part forms a considerable part of the whole or such that does not admit of compensation in money, the court may direct the party in default to perform specifically so much of the part which is capable of performance. However, this is subjected to the conditions contained in the very same sub-section. Sub-Section 4 provides that when a part of the contract can be specifically performed stands on a "*a separate and independent footing from another part of the same contract which cannot or ought not to be specifically performed*", the court may award specific performance of the former specifically enforceable part.

Section 21 clarifies that even in a suit for specific performance, a plaintiff "*may also claim compensation for its breach, in addition to, such performance".* The amount of such compensation shall be determined as per the principles specified in Section 73 of the Indian Contract Act, 1872. For instance, if A sues for specific performance of a resolution passed by the directors of a public company under which he is entitled to have certain shares allotted to him. But all the shares have already been allotted to others. In such a scenario, where the plaintiff had either originally pleaded for compensation in lieu of specific performance or later amended his plaint to such effect, the court may go ahead and award damages as a form of compensation.

Section 23 further provides that even in a situation where a contract envisaged the payment of liquidated damages in cases of breach, and the party in breach is willing to pay such sum as stipulated; the court retains its power to grant specific performance if it is of the opinion that such stipulation of liquidated damages was done "*only for the purpose of securing performance of the contract and not for the purpose of giving to the party in default an option of paying money in lieu of specific performance*". However, if the court decides to order specific performance, it shall not, in the same decree the payment of "*sum* [of liquidated damages] *so named*" in the contract.

# MODULE VI

# STANDARD FORM CONTRACTS

## WHAT IS A STANDARD FORM CONTRACT?

A standard form contract also referred to as an 'adhesion contract' or a 'boilerplate contract' is a standardized contract between two parties that does not offer the opportunity for any realistic negotiation. Such a contract, often drafted in advance by a supplier of goods and services presents itself as a 'take it or leave it' opportunity before the customer, whereby the customer can only obtain the desired product or service when she agrees to the pre-drafted terms of the contract. This standardized contract, once it has been finally drafted by a party (most often a large organisation), is then used in every bargain dealing with the same good or service.[403] The following characteristics can be looked at to identify standard form contracts:[404]

- They contain boilerplate and standardized language and are based on printed forms
- They are used to cater to a mass demand for goods or services
- They are drafted without keeping any one person in mind. The contract is drafted for mass consumption, a large number of people, and no single person.
- They are drafted by, or on behalf of, one of the parties to the transaction.

Thus the terms of these contracts of adhesion, or contracts that are to be adhered to *in toto*, are drafted unilaterally and forced on the other party (customer), who has to either accept the contract *en bloc* or walk away from the good or service sought totally. By setting the stage for a contract which only functions under the garb of free will, these pre-printed contracts have often been criticised to be contracts in name, alone.[405]

This, however, does not mean that standard form contracts are unenforceable or of no use, or even that they are to be seen as tools of exploitation, alone. Standard form contracts are legally binding agreements between the two parties which have entered into the contract. The difference that puts them at a dissimilar footing from the traditional contract is that they are pre-written by one party which has all the bargaining power, giving the other party no space

[403] F Kessler, *Contract of Adhesion-Some Thoughts about Freedom of Contract*, 43 Columbia LR 629, 631 (1943).
[404] Arthur Lenhoff, *Contracts of Adhesion and Freedom of Contract*, 36 Tul. L. R. 481 (1962); *see also* Todd D Rakoff, *Contracts of Adhesion: An Essay in Reconstruction*, 96(6) Harvard Law Review, 1173, 1177(Apr. 1983).
[405] 199th Law Commission Report, p. 55.

to keep her own interests in mind. To provide remedies for the injustice that could result of such transaction, where the party with all the bargaining power tries to exploit the 'weaker' party, remedies have been created in the common law, which shall be discussed slightly later.

First what needs to be examined is the circumstance that led to the development and popularisation of these 'take it or leave it' contracts.

### HISTORICAL CONTEXTS: THE BIRTH AND GROWTH OF STANDARD FORM CONTRACTS

> "*As the nineteenth century waned it became ever clearer that private enterprise predicated some degree of economic equality if it was to operate without injustice. The very freedom to contract with its corollary, the freedom to compete, was merging into the freedom to combine; and in the last resort competition and combination were incompatible. Individualism was yielding to monopoly, where strange things might well be done in the name of liberty. The twentieth century has seen its progressive erosion on the one hand by opposed theory and on the other by conflicting practice. The background of the law, social, political and economic, has changed. Laissez-faire as an ideal has been supplanted by 'social security'; and social security suggests status rather than contract*"[406]

Borne out of the needs of the commercial world, the field of contract law has witnessed developments in its discipline to meet the ever changing dynamics of commerce and business. The 20th century economic environment saw the development of mass production and distribution, and of giant corporations with vast infrastructural organisation. Organisations that were doing business at such a large scale gravitated towards standard templates for contracts that they needed at fairly regular levels to conduct their normal business.

While the initial idea behind these standard form contracts would have been that of ease, it became a fairly logical conclusion that the contracts that were formed by the producers of large scale goods and services contained terms that were most often one sided, giving no space to the interest of the consumer. On the other side of powerful organisations, to avail a service or buy the desired good, a consumer could do nothing but comply with all the conditions put before her.

However, the origin of standard form contracts does not lie in settings that sought a profit at the altar of equal bargaining power. The ancient origins of standard form contracts, as of the entire body of contract law, can be traced to mercantile law.[407] In order to facilitate business, some standard terms were established and settled for common occurrences that would be

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[406] MP Furmston, CHESHIRE, FIFOOT AND FURMSTON'S LAW OF CONTRACT, p. 25 (Oxford University Press, 16th ed.).
[407] *Schroeder Music Publishing Co v. Macaulay* (1974) 1 WLR 1308.

carried out in all these transactions. Some examples of pre-prepared templates of contracts in the field of mercantile law are charter parties, bills of lading, policies of insurance, etc. These standard terms and contracts are prevalent till date.

The standard clauses in these templates were not a product of attempts to exploit a party, or make a profit. In fact, they were the product of years of negotiation by representative stakeholders, who had, over time, adopted certain standard ways of carrying out their practices. Reducing to paper, that which was an established, standard and time-tested way of conducting business was thus a means to streamline and ease the conduct of trade.

By formalising these practices into standard clauses in mercantile contracts, not only were the two parties to the mercantile transaction benefitted, but so were other third parties who had commercial interests in the transaction. These could be the buyers or sellers of the goods, the charterers, the ship owner, insurers, bankers etc. Being aware of what would be expected of a transaction, while the agreement was still in the motion, the parties to the mercantile transaction, as also the parties allied to it, would already be aware of the standards of reasonableness, care, due diligence, and general functioning of business that would follow.

In these cases, since the standard clauses were not a product of unequal dynamics of power, but a result of years of usage by parties who have fairly equal bargaining power, there is greater presumption of reasonableness and fairness that can be lent to these standard terms.

> "*The same presumption, however, does not apply to the other kind of standard form of contract. This is of comparatively modern origin. It is the result of the concentration of particular kind of business in relatively few hands… The terms of this kind of standard form of contract have not been the subject of negotiation between the parties to it, or approved by any organization representing the interests of the weaker party. They have been dictated by that party whose bargaining power, either exercised alone or in conjunction with others providing similar goods or services, enables him to say: 'If you want these goods or services at all, these are the only terms on which they are obtainable. Take it or leave it.*'"[408]

Even in the present day, one is confronted with two different sets of circumstances that result in the use of standard form contracts. They have been succinctly reproduced in ***British Fermentation Products Ltd v Compair Reavell Ltd.***,[409]

> "*Broadly speaking, standard form contracts are of two different types. One type is exemplified by forms which may be adopted in commercial transactions of a particular type or for dealings in a particular commodity, such as the different*

[408] Lord Diplock, *Schroeder Music Publishing Co v. Macaulay* (1974) 1 WLR 1308.
[409] [1999] BLR 352.

*forms of sale contracts used by the Grain and Feed Trade Association or the forms for building and engineering contracts sponsored by the Royal Institute of British Architects, the Institution of Civil Engineers and the Federation of Associations of Specialists and Sub-contractors. Such forms may be drawn up by representative bodies with the intention of taking into account the conflicting interests of the different parties and producing a document acceptable to all. The other type is the form produced by, or on behalf of, one of the parties to an intended transaction for incorporation into a number of contracts of that type without negotiation. Examples include a multitude of printed documents setting out conditions of various kinds, terms found in catalogues and price lists, and terms set out or referred to in quotations, notices and tickets. Although it is the second type of standard form contract that has attracted most criticism, both types have in common the fact that they were not drafted with any particular transaction between particular parties in mind and are often entered into without much, if any, thought being given to the wisdom of the standard terms in the individual circumstances*."

### STANDARD FORM CONTRACTS IN THE MODERN CONTEXT

The next question that arises is, where do we see standard form contracts in our every-day lives? The short answer is, almost everywhere. The most prominent example of standard form contracts, which in fact is thought to be the starting point of standard form contracts of the 'second kind', that is, of comparatively modern origin, is the tickets we buy for transportation purposes.[410] Any form of travel is supported by a standard form contract, setting in place all the terms that are to be followed by the consumer- the mode of transport, the price, the particulars of the carriage transporting you, and even the dimensions of the luggage you carry!

Standard form contracts also form the backbone of the construction and building, insurance, engineering and carriage business. They are found in almost every branch of business- employment contracts, hire-purchase contracts, courier services, residential leases, software agreements etc. In fact, e-commerce is sustained on standard form contracts.

The widespread use of standard form contracts begs the question, what are the advantages of these contracts of adhesion.

[410] MP Furmston, CHESHIRE, FIFOOT AND FURMSTON'S LAW OF CONTRACT, p. 27 (Oxford University Press, 16th ed.).

**ADVANTAGES OF STANDARD FORM CONTRACTS**

"Preoccupation with the evils of standardised contracts from the point of view of the offeree must not allow their admitted virtues to be overlooked."[411]

If one were to put aside the issues typically raised against standard form contracts, or assume that a standard form contract has been so drafted that it does not take advantage of unequal bargaining powers, one would be confronted with the several advantages offered by this kind of contract. It is in fact these benefits that have popularised the usage of these forms of contracts in this industrialised world that depends on quick ways of conducting any business. In fact, with large scale economic activity becoming the norm in the twentieth century, the widespread use of standard form contracts was almost inevitable[412] owing to the practical and efficient solution they provides to businesses.

Firstly, they allow for **uniformity** in business transactions. This facilitates the calculation and allocation of risks, protection against unforeseeable contingencies, etc. in the contractual relationship.[413] For example, often when we download or purchase some software, in the end we need to agree to the terms and conditions for using the software. Once the 'I agree' button has been pressed, we have electronically agreed to a standard form contract. We can be rest assured that if our friend or neighbour downloaded the same software, they would be agreeing to the same conditions as ourselves. In this way the software company has ensured that it has uniform obligations and duties towards its customers downloading that software.

Owing to this advantage of uniformity, standard form contract ensure **certainty** in transactional relationships. At the first level, both the parties are aware of the kind of terms they will be looking at when entering into a standard form contract. But, even beyond that, an interpretation of the terms of the contract becomes easier when there is precedent regarding its application.

An example is the charter parties entered into between ship owners and charterers, to 'hire' the ship. Typically, the contractual relationship between the parties is based on standardized templates of charter parties. Due to the age-old presence of these standard form contracts, there are several commentaries and judicial precedents interpreting various clauses of these charter parties. Hence, when parties are to enter into a shipping transaction of such nature, they have various sources to rely upon to understand the import of each clause. With such certainty prevailing, the prospect of litigation is drastically reduced.[414] Furthermore, even if, ultimately, there is any dispute of any kind, its resolution, too is aided by the presence of such commentaries and judgments.

[411] NS Wilson "Freedom of contract and adhesion contracts" (1965) 14 ICLQ 172, 176.
[412] JR Harker "Imposed terms in standard form contracts" (1981) 98 SALJ 15, 16.
[413] D Yates, EXCLUSIONS CLAUSES IN CONTRACTS, 4 (2nd ed, 1982) .
[414] E Kahn et al, 1 CONTRACT AND MERCANTILE LAW: A SOURCE BOOK 34 (2nd ed., 1988).

Irrespective of the circumstance that witnesses the use of a standard form contract, the ultimate reason of its continued use is the **benefit of familiarity**. The contract that the adhering party is being asked to sign, whether fair or unfair, is known to all. The drafting time for such contracts is almost *nil* especially when the standard form contract is between a big corporation and an individual (most often powerless) customer. Since no lawyer is needed to draft each contract, the cost of entering into the contractual transaction is negligible for the party that has drafted the contract.

In this way, standard form contracts provide a **temporally and financially efficient** way of conducting business. Further, the use of these contracts in big corporations comes in handy also from the perspective that often the contracts are being entered into by subordinate sales staff, for example, in the insurance sector. In such cases, the senior management is still able to retain control over the contractual arrangement that is being entered into, with each customer, without personally bargaining with them.[415]

An argument is also made that the use of standard form contracts in a competitive market need not be exploitative since the adherent has the option to shop for a producer that provides better terms and conditions, more suited the needs of the customer (adherent).[416] However, that could be perceived as an immense reduction of the criticisms mounted against standard form contracts. This is because often, even in competitive markets, the terms and conditions provided by different producers of goods and services in their standard form contracts are more or less the same.

It is thus essential to have a detailed understanding of the 'threats' that standard form contracts can hold.

### DISADVANTAGES OF STANDARD FORM CONTRACTS

*Consensus ad idem* or the "meeting of minds"[417] is the basis of contractual obligations.[418] Both the parties to a contract, after agreeing with all the terms and conditions of an agreement, in the same sense, are to enter into a contract. The idea is the parties themselves have agreed upon the duties that are to be imposed upon them, the rights that they consequently enjoy and the liabilities they may incur if they deviate from their promise. The duty of the law is to just ensure that later, one party does not run away from what it agreed to do, disadvantaging the other party which relied upon the former's promise while performing reciprocal obligations under the contract.

[415] *Barkuizen v Napier* (2007) 5 SA 323 (CC), para139.

[416] Todd D Rakoff, *Contracts of Adhesion: An Essay in Reconstruction*, 96(6) Harvard Law Review, 1179 (Apr. 1983).

[417] Black's Law Dictionary, 919 ($8^{th}$ ed. 2004)

[418] David M. Walker, PRINCIPLES OF SCOTTISH PRIVATE LAW, 11 (4th ed. 1988).

However, it is difficult to understand and prove what goes on in the minds of people, and whether or not two parties agreed to the same terms in the same sense. The law of contracts, and consequently, the Courts, thus look at tangible expressions of such agreement- witnessed in the signature on the contract by the two parties involved, etc. It is at this juncture that critics argue that the threshold of looking at external circumstances to see whether the terms of a standard form contract have been agreed to by the contracting parties should be much higher.

It is a popularly held notion that while signing a contract of adhesion, the adhering party is most likely to not have read the terms and conditions of the contract. As Lord Denning fittingly states, "No customer in a thousand years ever read the conditions. If he had stopped to do so, he would have missed the train or the boat".[419] Further, most often the terms and conditions are written in such a manner that no customer would think of reading it. It could be drafted in legal language that is incomprehensible to lay persons.[420] Or, for example in train tickets and the like, the terms could be presented illegibly, in very small print or perhaps could be even hidden.[421]

Furthermore, since the customer knows that she does not have the opportunity to bargain with the other party (with greater power) she may not even try reading the terms of the contract since she can do nothing about it! "*He cannot alter those terms or even discuss them; they are there for him to take or leave. He therefore does not undertake the laborious and pointless task of discovering what the terms are*."[422]

It is thus this unequal bargaining power that then forms the centre of the critique against standard form contract. As has been discussed previously, the contract is drafted by legal advisors of one party, who are seeking to protect the interests of only that one party. Since the typical example is of the contract being drafted by a business venture, or a large organisation, it is the interest of the venture that will be looked out for, over the interest of the consumer, in the standard form contract.[423]

In the extreme scenarios, this translates into the exploitation of the customer, who is faced with a 'take it or leave it' scenario. With no bargaining power, the customer can do nothing but suffer the consequences of a contract drafted keeping in mind only the ease of the bigger organisation that she has entered into a contract with. Critics of this form of contract particularly argue against the unfair terms worked into such contracts, which no party would have otherwise willingly agreed to.

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[419] *Thornton v Shoe Lane Parking Ltd.* (1971) 1 All ER 686 (CA).
[420] Joseph Chitty, 1 CHITTY ON CONTRACTS: GENERAL PRINCIPLES, para 12.097 (27th Ed, 1994).
[421] *Henderson v Stenvenson*, (1875) 32 LT 709 (HL).
[422] F Kessler, *Contract of Adhesion-Some Thoughts about Freedom of Contract*, 43 Columbia LR 629 (1943).
[423] K Hopkins, *Standard Form Contracts and the Evolving Idea of Private Law Justice: A Case of Democratic Capitalist Justice versus Natural Justice*, (2003) 1 TSAR 150, 154.

Questions are raised about the very foundation of free consent being given to such a contract. This is especially because the idea that the consumer is free to enter into a contract is used very loosely in such contracts. As mentioned above, whether in a competitive or a non-competitive market, a consumer might be faced with the same exploitative terms and conditions while purchasing a good or service. While in some cases the consumer might actually have the freedom to refuse the good or service that is being received pursuant to the standard form contract, that may not always be the case.

A most apt example to show the actual lack of freedom in these cases is that of insurance covers. It is quite moot to say that a customer has the freedom to contract if she is being offered similar terms for insurance covers by all insurance companies. However, it is equally impossible for an individual to live without insurance cover. Thus, the freedom really does not rest in the hands of the individual, even if the contrary appears to be the case!

## PROTECTIVE DEVICES

"*The battle against abuse has fallen to the courts*."[424] However, the judiciary cannot take upon itself the mantel of nullifying each standard form contract. The Courts have most often been bound to uphold standard form contracts where an individual has signed the documents involved.[425]

> *"It would be absurd to say that this document, which is partly in writing and partly in print, and which was filled up, signed, and made sensible by the plaintiff, was not binding upon him. A person who signs a paper like this must know that he signs it for some purpose, and when he gives it to the Company must understand that it is to regulate the rights which it explains. I do not say that there may not be cases where a person may sign a paper, and yet be at liberty to say, "I did not mean to be bound by this," as if the party signing were blind, and he was not informed of its contents. But where the party does not pretend that he was deceived, he should never be allowed to set up such a defence."*[426]

The mere fact that a party did not have equal bargaining power does not invalidate the contract. Nor can an adhering party be given reprieve if the party refused to acquaint itself with the terms and conditions of the standard form contract. "*Where a document containing contractual terms is signed, then, in the absence of fraud, or misrepresentation, the party*

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[424] Avatar Singh, CONTRACT AND SPECIFIC RELIEF, 67 (Eastern Book Company, 11th ed, 2013).
[425] *L'Estrange v. F Graucob Ltd*., (1934) 2 KB 394.
[426] *Henrioulle v. Marin Ventures, Inc.*, 20 Cal. 3d 512.

*signing it is bound, and it is wholly immaterial whether he has read the document of not*."[427] The result may have been different, had the complaining party not signed the contract.

The importance given to such external attributes as the signature of the parties is because, as mentioned above, it is impossible to prove that the adhering party did not pay heed to the terms and conditions of the contract. If the courts, then, blindly start invalidating contracts where an adhering party signs the contract and later claims that it did not read the terms and conditions of the contract, it would bring to a complete standstill the way most enterprises conduct business.[428]

It is in this light that we need to look at the judicial tools that have been crafted to analyse a standard form contract and nullify it when the contractual obligation can just not be given legal sanction. This, of course, is over and above the existing grounds in contract law to invalidate contracts. However, even these judicial tools designed over time, to check the excessed that can be committed in the execution of standard form contracts do often base their logic in the traditional grounds of contractual invalidation. We shall now turn to the manner in which the judiciary has sought to balance the interests of the weaker party in such contracts, while keeping the "elementary rules" of the law of contracts intact.

### ***Reasonable Notice***

The Courts, over time have tried to enforce that there should be at least reasonable notice of the terms and conditions that standard form contracts seek to impose. This seeks to eliminate the first level barrier on the adhering party, of finding the terms and conditions that are to be imposed upon her, when she signs a contract over which she has no bargaining power. Hence, it has been declared to be the duty of the party that has drafted the standard form contract to give proper notice of the terms and conditions of the contract, otherwise the acceptor shall not be bound by it.

This proposition was laid down in the case of *Henderson v. Stevenson*.[429] The facts of that case are as such. The document in question was a steamer ticket, which, on the front side had only the words, 'Dublin to White Haven' printed. This ticket was given to a passenger by a steam packet company. The passenger did not read the ticket at all, just paid the money and boarded the steamer. Unfortunately, the steamer got shipwrecked, and in the chaos, the luggage of the passenger got lost. As a result, the passenger brought an action against the steam packet company.

[427] *L'Estrange v. F Graucob Ltd*., (1934) 2 KB 394.
[428] *S. Manuel Raj and Co. v. J. Manilal And Co.*, AIR 1963 Guj 148.
[429] (1875) 32 LT 709 (HL).

In their defense, the company referred to the terms and conditions found on the back of the steamer ticket. This condition stated that the ticket was being issued on the condition that the company would incur no liability for any delay, loss or injury caused to the passenger or his luggage. Even if such loss arose out of a negligent act of the company or its agents, it was still stated that the company would not be liable.

In a historic judgement, the House of Lords found against the steam packet company, laying the foundational stone of the need for 'reasonable notice' in standard form contracts. It was stated by the Lord Chancellor, Lord Cairns that,

> "*It seems to me that it would be extremely dangerous, not merely with regard to contracts of this description, but with regard to all contracts, if it were to be held that a document complete upon the face of it can be exhibited as between two contracting parties, and, without any knowledge of anything beside, from the mere circumstance that upon the back of that document there is something else printed which has not actually been brought to and has not come to the notice of one of the contracting parties, that contracting party is to be held to have assented to that which he has not seen, of which he knows nothing, and which is not in any way ostensibly connected with that which is printed or written upon the face of the contract presented to him.*"

These observations reflect that in cases where the front side of the ticket was sufficient to be classified as a complete contract, and there was no indication that the passenger should look elsewhere to find yet more conditions, the conditions on the back could not limit the rights of the passenger.

The question of what reasonable notice is, was further lent clarity in the case of *Richardson, Spence and Co. and Lord Gough S.S. Co. v. Minnie Rowntree*[430]. In this case, Ms. Rowntree bought a steamer ticket from the former company for a voyage. That ticket was handed over to her in a folded manner by the ticket clerk. No writing on the ticket was visible in this manner. No one sought to bring her attention to any terms and conditions on the ticket. Ms. Rowntree did not even try reading any of the writing on the ticket and got on to the steamer. Over the course of the voyage, Ms. Rowntree suffered personal injuries and brought an action against the steam packet company. It was at this stage that the company referred to the numerous conditions found on the ticket, one of which read that "*The company is not under any circumstances liable to an amount exceeding 100 dollars for loss of or injury to the passenger or his luggage*".

The judgement found in favour of Ms. Rowntree, stating that no attention was sought to be brought to the conditions imposed upon Ms. Rowntree, especially when, in the folded

[430] (1894) AC 217.

form that she was given the ticket in, no writing could be seen on the paper. Lord Ashbourne in his judgement went on to state that "*The ticket in question in this case was for a steerage passenger—a class of people of the humblest description, many of whom have little education and some of them none. I think, having regard to the facts here, the smallness of the type in which the alleged conditions were printed, the absence of any calling of attention to the alleged conditions, and the stamping in red ink across them…*"

Thus, from these observations it can be inferred that the lack of reasonable notice can also be attributed to practical aspects like the small font in which the terms and conditions are presented, or the stamping in red over them, in addition to the lack of calling any attention to them.

Another important aspect that is covered by this judgement is the reasonable expectation that can be had, of an acceptor of such contracts actually understanding the terms and conditions written on them. It was noted that passengers of such steamers would be from the 'humble classes', having little education. To expect that conditions printed in terse legal language would be understood by the masses was unreasonable. In such cases, thus, it has been held that no reasonable notice of the onerous terms and conditions was actually provided to the acceptor of the contract.

Such principle finds resonance in the Indian jurisprudence as well. In the case of M/s. Prakash Road Lines (P) Ltd. & Anr. v. H.M.T. Bearing Limited,[431] one party entered a contract with another to carry a consignment of goods. The latter party accepted this consignment and issued a lorry receipt. Due to a fire accident, the goods got burnt. As a result, an action was brought in a court in Andhra Pradesh. This action was challenged on two grounds. Firstly, that the lorry receipt specified that delivery was at the risk of the good owners and secondly that this receipt also specified that any disputes would be subject to 'Bangalore jurisdiction only'.

In this case it was held that since there was no evidence that the condition on the lorry receipt was brought to the attention of the owner of the goods, this could not be considered to be part of the contract between the two parties. It was held that,

> "*It must be remembered that people often sign order forms containing lot of printed material without caring to read or knowing what is printed and if everything that is printed on such form is taken as part of the contract, without anything further, it would be reading more terms into the contract for which there had been no consensus ad idem between the parties. Therefore, it is always necessary that the Courts should insist that the*

[431] 2001 ACJ 40 (AP).

*printed material or the note made thereunder should be made known to the parties before the same is read into the contract as one of its integral terms. Therefore, we are of the view that mere presence of a printed note at the bottom of the lorry receipt docs not form part of the contract, which can be enforced in a Court of law, in the absence of a proof that the same was brought to the notice of the plaintiff and that it has accepted it is a term of the contract.*"[432]

**The corollary** to these cases is the situation where a company brings to attention the specific terms and conditions of the standard form contract to the consumer. In the case of *Parker v South Eastern Railway Co*.[433] this is exactly what happened. The plaintiff deposited his articles at the cloak room at a railway station. He received a ticket which laid out some conditions on the front side. But along with it, the front side of the ticket also contained the words, '*See Back*'. On the other side of the ticket, it was clearly specified that the company would not be responsible for any package exceeding the value of 10*l*. A placard stating similar information was also publicly exhibited the cloak room. The bag that was deposited by the plaintiff of this case far exceeded this value. It got lost or stolen. As a result, an action was brought in Court seeking compensation.

Asserting that he did not think that the ticket would have any conditions and put it directly in his pocket, without seeing it, the plaintiff tried to claim that he did not have reasonable notice of the conditions. However, in this case, it was held that sufficient notice was given to the plaintiff, and thus the railway company could not be held liable in this case.

In fact, it has been held that in similar cases, sufficient notice would be considered to have been given if the front of the ticket asked the customer to look at the other side, which did not expressly mention terms, but incorporated them by reference to another (railway) time table.[434]

The standard of bringing notice to conditions that are not found on the front side of a ticket, with specific instructions on the front side directing a customer to look elsewhere has been upheld in India, too.[435]

The onus on the offeror of a standard form of contract is higher when a more onerous or **unusual condition** is sought to be imposed. In such cases, "clear, fair and reasonable effort"[436] to bring such onerous conditions to the attention of the party is required. In the

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[432] *Prakash Road Lines (P) Ltd. & Anr. v. H.M.T. Bearing Limited*, 2001 ACJ 40.
[433] (1877) 2 CPD 416.
[434] *Thompson v. L.M. and S. Ry. Co.* (1930) 1 KB 41.
[435] *Singhal Transport v. Jesaram*, AIR 1968 Rajasthan 89.
[436] *Interfoto Picture Library Limited v. Stiletto Visual Programmes Limited* (1988) 1 All ER 348 (CA).

famous words of Denning LJ, "*The more startling a clause is, the greater the notice which must be given of it. Some clauses would need to be printed in red ink with a red hand pointing to it before the notice could be held to be sufficient*."[437]

There is another question that arises when terms of contract are sought to be enforced when they are found on tickets, order forms, etc. The question is whether such tickets and other similar documents are to be treated as **receipts or contractual documents**. The simple answer is that each case is to be appreciated for its own facts, to arrive at a decision.

The broad proposition to differentiate between mere receipts and vouchers from contractual documents has been laid out in the abovementioned case of *Parker v South Eastern Railway Co*.[438] in the following terms

> " *I think there may be cases in which a paper containing writing is delivered by one party to another in the course of a business transaction, where it would be quite reasonable that the party receiving it should assume that the writing contained in it no condition, and should put it in his pocket unread. For instance, if a person driving through a turnpike-gate received a ticket upon paying the toll, he might reasonably assume that the object of the ticket was that by producing it he might be free from paying toll at some turnpike-gate, and might put it in his pocket unread…*"[439]

In India too, there are a few cases which deal with the argument seeking to exclude terms found on documents that do not fall within the strictest notions of 'contractual documents.' Clauses found in order forms signed by the acceptor that specify the jurisdiction of courts for dispute resolution have been upheld by the Courts.[440] In fact, in the discussion of such a legal dispute, it has been commented that, "*It is not open to a person who signs an order form of the opposite party containing the printed words to say that the printed words are not part of the contract*." To take such a view, it has been held, would "*upset the commercial practice of India, and unless such a position is necessary in view of the wording of any particular section, I am not prepared to take that view. I am not prepared to upset the commercial practice of India unless the law requires me to do so*."[441]

In India, the biggest signifier of agreement and *consensus ad idem* with respect to these additional documents is the physical act of signature by an acceptor. Thus, a signed order form which states that disputes can be resolved before a Court will be held to be enforceable.

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[437] *Spruling (j.) Ltd. V. Bradshaw* (1956) 2 All ER 121 (CA).
[438] *Supra*
[439] (1877) 2 CPD 416.
[440] *S. Manuel Raj and Co. v. J. Manilal and Co.* AIR 1963 Guj 148
[441] *Ibid.*

Unsigned bills seeking to incorporate such terms and conditions are not given such weightage and validity.[442]

### *Notice should be Contemporaneous*

A key component to the protective device of reasonable notice of specific terms is that such notice should be contemporaneous to the forming of the contract. This has been offered as another protective device by the Courts. It has been made explicit that conditions that seek exemption from liability, or enforce other unusual terms, should be given reasonable notice of to the acceptor at the time the contract is being accepted by her. That is, at the time of assenting to the standard form contract, the acceptor should be aware of such terms. If that is not the case, then it will be considered that such term or condition was not assented to.

The application of this protective device can be understood with the help of the case of *Olley v Marlborough Court Ltd*.[443] Here, a man and his wife rented a hotel room by paying some money in advance. It was only later that they found that the hotel exempted itself from any liability arising out of the theft or loss of any articles of the guests from their rooms. The couple in question here received notice of this term when they saw it printed on one of the walls of their hotel rooms. Subsequently due to the negligence of the hotel, some articles of the couple were stolen. In the action that followed in the Court, it was held that the hotel could not exempt itself from liability since it had not given notice of such terms to the couple at the time they entered into the contract of renting the room.

### *Strict Construction*

Given the power dynamics in question in adhesion contracts, where one party seeks to incorporate terms completely in its favour, without giving the other party opportunity to negotiate, courts have devised the protective device of 'strict construction', too.[444] Per this protective device, it has been held that clauses in standard form contracts that seek to exempt liability of the offeror of a standard form contract must be construed in the strictest sense. Thus, the narrowest reading is to be given to such terms. This is especially held to be the case where an exemption clause seeks to cover the widest ambit possible.

In the light of such a protective device, the case of *Lee (John) & Sons (Grantham) Ltd. V. Railway Executive*[445] can be analysed. In this case, a railway warehouse was leased to a tenant, who had stored goods in the same. These goods got damaged in a fire and the tenant

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[442] *Jaishree Luxury House, Kota and Ors. v. Kathotia Sons*, AIR 1980 Raj 42.
[443] (1949) 1 All ER 127 (CA).
[444] Avatar Singh, CONTRACT AND SPECIFIC RELIEF, 83 (Eastern Book Company, 11th ed, 2013).
[445] (1949) 2 All ER 581 (CA).

brought an action against the railway executive, claiming that the damage was a result of negligence. In defense, attention was brought to a clause that exempted the railway company from "*loss, damage, costs, and expenses, however caused… (whether by act or neglect of the company or their servants or agents or not) which but for the tenancy hereby created… would not have arisen*."

Such an exemption clause is a perfect example of a broadly worded exemption clause. In this case, the Court held that the exemption clause was to be construed to exempt liability of lessors only from those activities that arose out of the relationship of tenancy. The fire did not arise out of that relationship and was a product of negligence. Hence liability was placed on the landlords.

Based on the rationale behind the rule of strict construction is the notion that when a clause in a standard form contract is ambiguous, and open to two constructions, then that interpretation is to be given which favours the weaker party. A formalization of this notion is in the **rule of *contra proferentem***. Per this rule, in cases of ambiguity, when two meanings of a clause can stand on their feet, that reading should be taken which goes against the party who inserted the clause. In the context of an insurance contract, the rule and its rationale are encapsulated well in the following words, as reproduced in the case of *Industrial Promotion and Investment Corporation of Orissa Ltd. v. New India Assurance Company Ltd. and Ors.*[446]:

> "*Quite apart from contradictory clauses in policies, ambiguities are common in them and it is often very uncertain what the parties to them mean. In such cases the Rule is that the policy, being drafted in language chosen by the insurers, must be taken most strongly against them. It is construed contra proferentem, against those who offer it. In a doubtful case the turn of the scale ought to be given against the speaker, because he has not clearly and fully expressed himself. Nothing is easier than for the insurers to express themselves in plain terms. The assured cannot put his own meaning upon a policy, but, where it is ambiguous, it is to be construed in the sense in which he might reasonably have understood it. If the insurers wish to escape liability under given circumstances, they must use words admitting of no possible doubt.*
>
> *But a Clause is only to be contra proferentem in cases of real ambiguity. One must not use the Rule to create an ambiguity. On must find the ambiguity first. Even where a Clause by itself is ambiguous if, by looking at the whole policy, its meaning becomes clear, there is no room for the application of the doctrine. So*

[446] AIR 2016 SC 3908

*also where if one meaning is given to a clause, the rest of the policy becomes clear, the policy should be construed accordingly.*"[447]

Thus, an application of the principle requires there to be an ambiguity in the interpretation of clauses of the contract. As can be gleaned from a catena of cases, first the attempt is made to find a coherent meaning in the words of the terms itself.[448] In fact, such meaning is to be derived not only from the words of the text, but also from the conduct of parties.[449] Especially in recent times, primary effort of the Courts are dedicated towards giving meaning to the terms of the contract, itself, in the first instance.[450]

So, when is it that ambiguities arise in a contract, and how is the rule applied then? For that, reference can be made to the case of *Bharti AXA General Insurance Co. Ltd. v. Priya Paul and Ors*.[451] In this case, the respondent had gone on vacation to Canada, where during a sight-seeing flight tour, the glider plane of her son exploded, killing him. The respondent filed a claim with the petitioner company based on the Smart-Personal Accident-Individual Insurance Policy taken by her son. This claim was denied by the company on the basis that the insurance policy was to only extend to accidents in standard flights and not to those in motorized gliders for sightseeing.

The Court perused the various policies and rules applicable to seek a meaning for what would be a 'standard aircraft'. It was acknowledged that "*accidental death or permanent disablement suffered by the insured while mounting into, dismounting from, or travelling in any aircraft or balloon, while engaging in aviation or ballooning…*" was excluded. However, '*accidents suffered during aerial activities*' was a very broadly worded clause. Along with listing the various factors that would enable a motorized glider to be understood as a 'standard aircraft', the Court also referred to the rule of *contra proferentem*. It stated:

> "*The usage of as vague a phrase as "standard type of aircraft" in the Policy, thus, suggests to us that the same must be construed in a liberal manner so as to benefit the insured... In the instant case, we agree with the conclusion of the National Commission that had the insurer really intended to exclude gliding activity from the purview of the Policy, it could have done so expressly, similar to the manner in which hang-gliding and para-gliding were excluded in Clause 7(xiii) of the Policy. Similarly, the insurer could have also defined the phrase "standard type of*

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[447] Colinvaux's Law of Insurance, 42 (6th ed., 1990) (Robert and Merkin, eds.).
[448] *Sushilaben Indravadan Gandhi and Ors. v. The New India Assurance Company Limited and Ors.* AIR 2020 SC 1977; *BHS Industries v. Export Credit Guarantee Corpn. Ltd.*, (2015) 9 SCC 414; *Export Credit Guarantee Corporation of India Ltd. v. Garg Sons International* (2014) 1 SCC 686.
[449] *Udaipur Sahkari Upbhokta Thok Bhandar Ltd v. CIT* (2009) 8 SCC 393; this case deals with the question of statutory, compulsory sales and the need to interpret the terms of the contract dependent upon the conduct of the parties.
[450] *Assistant General Manager and Ors. v. Radhey Shyam Pandey* 2020 (2) SCT 305 (SC); *New India Assurance Company Limited and Ors. v. Rajeshwar Sharma and Ors* (2019) 2 SCC 671.
[451] (2020) 1 ACC 391 (SC).

*aircraft" for the purpose of the Policy, but it chose not to do so. In these circumstances, it is not open to the insurer to reject a claim arising out of a glider accident by now arguing that a glider is not a standard aircraft by virtue of not principally being a powered aircraft.*"

Thus, in this case, using the *contra proferentem* rule, the ambiguity in interpretation was resolved in favour of the insured.

Similarly, in a case where a building was insured against damage caused by "*Impact by any rail/road vehicle or animal*", the impact caused by the vibration of a bull dozer that went from nearby the building was considered to be covered under the policy.[452] In this case, it was noticed that even though there was no ambiguity in the insurance policy, and in the ordinary course of events, too, the impact of a bull dozer would be covered under the policy, even if there had been an ambiguity, the same would be resolved *contra proferentem*.

***THEORY OF FUNDAMENTAL BREACH***

Following the rationale of the previous protective device, the theory of fundamental breach, too, seeks to protect the 'weaker party' in a standard form contract. It does so by controlling exemption clauses that have a wide sweep. This protective device holds unenforceable those exemption clauses incorporated in a contract, which if given effect, would not hold the offeror of the contract liable for even a fundamental breach of the contract.

The basic thing to understand for the application of this protective device is what is a fundamental breach? It is the breach of something that is fundamental, or at the core of the contract. What would be at the core of contract? It would be those objectives and very terms for which two parties came together in the transaction. The use of this idea in standard form contracts is that breach in discharge of fundamental duty cannot be protected under an exemption clause.

The use of this principle originated over a course of three cases adjudicated in the UK,[453] of which *Alexander v Railway Executive*[454]is one. This case will lend understanding to the theory of fundamental breach. In this case, the plaintiff had bought the service of safe keeping of his luggage at the railway parcel office, where he deposited his baggage. The ticket which he received for this contained an exemption clause that defendants would be exempt from any liability for mis-delivery or loss of any article exceeding 5 pounds, unless a special charge was paid for the same. Plaintiff did not pay any special charge. The luggage of plaintiff was given to another person who did not even produce a ticket.

[452] *United India Insurance Co. Ltd. v. Pushpalaya Printers*. (2004) 3 SCC 694.
[453] Professor Brian Coote, *The Second Rise And Fall Of Fundamental Breach*, available at http://www.nzlii.org/nz/journals/NZLRFSP/1980/6.pdf .
[454] (1951) 2 KB 882.

The plaintiff sued the parcel office. The defendant claimed protection against the exemption clause. Such protection was not given. It was stated that,

> "*an essential part of the executive's duty was to take care of the deposited goods; that they had committed a fundamental breach of the contract in allowing unauthorized person to have access to the goods and to take them away and, therefore, they could not rely on the exemption clause to shield them from liability*."[455]

This concept was given weightage as a substantive principle of law by Denning, LJ in the case of *Karsales v Wallis*.[456] The facts of the case are as such. Wallis was interested in buying a car which was in excellent condition, for 600 pounds. To arrange financing of the car, he went through a hire-purchase company, Karsales. The company purchased the car and finally supplied it to Wallis. When Wallis received the car now, it was not the same as before. Many parts were broken or worn out. He brought an action against Karsales, which relied on an exclusion to the following effect. "*No condition or warranty that the vehicle is roadworthy or as to its age, condition or fitness for any purpose is given by the owner or implied herein.*"

This exemption clause was not allowed to be applied in this case, on the basis of the theory of fundamental breach. Famously, Denning, LJ. stated,

> "*Notwithstanding earlier cases which might suggest the contrary it is now settled that exempting clauses of this kind, no matter how widely they are expressed, only avail the party when he is carrying out the contract in its essential respects. He is not allowed to use them as cover for misconduct or indifference or to enable him to turn a blind eye to his obligations. They do not avail him when he is guilty of a breach which goes to the root of the contract. It is necessary to look at the contract apart from the exempting clauses to see what are the terms express or implied which impose an obligation on the party. If he has been guilty of a breach of these obligations in a respect which goes to the very root of the contract he cannot rely on the exempting clauses…*
>
> *The principle is sometimes said to be that a party cannot rely on an exempting clause when he delivers something 'different in kind' from that contracted for, or has broken a 'fundamental term' or a 'fundamental contractual obligation'. However, I think they are all comprehended by the general principle that a breach which goes to the root of the contract disentitles the party from relying on the exempting clause.*"

[455] *Ibid*.
[456] (1956) 1 WLR 936.

However, this doctrine faced backlash in the House of Lords. The rule of strict construction is what was preferred over such theories that allowed for the 'freedom of contract' to be infringed by judicial tools. The position of 'fundamental breach' as a theory of law was questioned in the *Suisse Atlantique* case,[457] where, while the theory of fundamental breach was not done away with totally, it was confined to be a rule of construction, rather than a stand-alone rule of law.[458]

> "*In my view, it is not right to say that the law prohibits and nullifies a clause exempting or limiting liability for a fundamental breach or breach of a fundamental term. Such a rule of law would involve a restriction on freedom of contract and in the older cases I can find no trace of it…*
>
> *… Accordingly, it is now said that there is a rule of construction that normally an exceptions clause should be construed as not applying to a fundamental breach. There is no category of breach of contract known as "fundamental breach" in English law. In determining the rights of parties the courts must apply certain rules of construction and certain rules of law and all the cases are merely applications of these rules.*"[459]

This case further reproduced excerpts from *U. G. S. Finance Ltd. v. National Mortgage Bank of Greece and National Bank of Greece*[460] to properly express the difference between the theory of fundamental breach as a rule of construction, rather than a rule of theory,

> "*As to the question of 'fundamental breach,' I think there is a rule of construction that normally an exception or exclusion clause or similar provision in a contract should be construed as not applying to a situation created by a fundamental breach of contract. This is not an independent rule of law imposed by the court on the parties willy-nilly in disregard of their contractual intention. On the contrary it is a rule of construction based on the presumed intention of the contracting parties. It involves the implication of a term to give to the contract that business efficacy which the parties as reasonable men must have intended it to have. This rule of construction is not new in principle but it has become prominent in recent years in consequence of the tendency to have standard forms of contract containing exceptions clauses drawn in extravagantly wide terms, which would produce absurd results if applied literally.*"

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[457] *Supra*.

[458] Professor Brian Coote, *The Second Rise And Fall Of Fundamental Breach*, available at http://www.nzlii.org/nz/journals/NZLRFSP/1980/6.pdf .

[459] *Suisse Atlantique Societe D'Armement Maritime SA v. NV Rotterdamsche Kolen Centrale* (1967) 1 AC 361.

[460] S.A. [1964] 1 Lloyd's Rep. 446.

This refusal to adopt the theory of fundamental breach as a rule of law was briefly disturbed in *Harbutts Plasticine Limited v. Wayne Tank and Fuel Company Limited*,[461] which trend continued for a brief period of time.[462] However, a more categoric end to the use of the theory of fundamental breach in judicial decisions came with the case of *Photo Production Ltd. v Securicor (Transport) Ltd.*[463]

This was a case where the defendants entered into a contractual relationship with the plaintiffs to provide a night- patrol service at the latter's factory. There was a clause exempting liability in this contract, which excluded liability on the defendants' part for "*any injurious act or default of any employee of the (defendants) unless such act or default could have been foreseen and avoided by the exercise of due diligence on the part of the employer; nor in any event shall the company be held responsible for any loss suffered through fire or any other cause except in so far as is solely attributable to the negligence of the company's employees acting within the cause of their employment*." As it turns out, one of the employees of the defendant started a fire deliberately, resulting in an actionable claim.

The dispute rested on the interpretation of the exemption clause. Relying upon the *Suisse Atlantique* case,[464] it stated that,

> "*(1) There is no suggestion in any of the speeches cited that,*[465] *after the affirmation of a contract by the innocent party, exclusion clauses are somehow excised from the continuing contract. (2) None of their Lordships said that on the acceptance of repudiation by fundamental breach, an exclusion clause necessarily ceased to apply, whatever its terms. The development of this branch of the law has been bedevilled by well meaning concessions made by counsel in the reported cases which do not bind the courts. The decision in the present case cannot be supported on the grounds in any of the judgments in the Court of Appeal.*

But, this case went one step ahead and stated that if the language of the exemption clause did not allow for it, the clause could not be read in a manner that would allow the offeror of the contract to be liable for a fundamental breach of the contract.

> "*In commercial contracts negotiated between business-men capable of looking after their own interests and of deciding how risks inherent in the performance of various kinds of contract can be most economically borne (generally by*

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461 (1970) 1 All ER 225.

462 Professor Brian Coote, *The Second Rise And Fall Of Fundamental Breach*, available at http://www.nzlii.org/nz/journals/NZLRFSP/1980/6.pdf .

463 (1980) 2 WLR 283.

464 *Supra*

465 In the *Suisse Atlantique* case (*supra*).

*insurance), it is, in my view, wrong to place a strained construction upon words in an exclusion clause which are clear and fairly susceptible of one meaning only even after due allowance has been made for the presumption in favour of the implied primary and secondary obligations.*"

However, while the judiciary exempted itself from using this tool to interpret standard form contracts, the UK legislature promulgated the Unfair Contract Terms Act, 1977, and more recently, the Consumer Rights Act, 2015, which put in place tools to tackle with unfair terms in the standard form contract.

### *UNREASONABLE TERMS OF THE CONTRACT*

Another protective device used for protecting a party in a standard form contract relation is by excluding the enforcement of unreasonable terms in the contract. While it has been felt that freedom of contract is important, statutory and judicial interventions have been considered necessary to protect parties against terms that would completely fall outside the contours of reasonableness.[466] As Lord Denning LJ remarks, "*There is the vigilance of the common law which, while allowing freedom of contract, watched to see that it is not abused*"[467]

So, what is the threshold of unreasonableness in a contract?

The essence of unreasonableness in a contract is captured in these following words,

> "*One may safely say that the parties cannot, in a contract, have contemplated that a clause shall have so wide an ambit as in effect to deprive one party's stipulations of all contractual force: to do so would be to reduce the contract to a mere declaration of intent*."[468]

Thus, this tool is to be used to protect a party against a term that would render null the entire benefit received by it in the contract.

In 1977, with the promulgation of the Unfair Contract Terms Act, the test of reasonableness was introduced by the UK legislature as well, to ensure that such unreasonable terms cannot be enforced in standard form contracts. So, what is unreasonable per the Act? The Act provides that any exemption clause restricting liability arising due to a breach of contract should be void unless it meets the test of reasonableness.[469] And the reasonableness test seeks to answer the question whether a term would be fairly and reasonably included, "*having*

[466] Joseph Chitty, 1 CHITTY ON CONTRACTS: GENERAL PRINCIPLES, para 4 (25th ed).
[467] *Lee (John) & Sons (Grantham) Ltd. v. Railway Executive*, (1949) 2 All ER581.
[468] *Suisse Atlantique Societe D'Armement Maritime SA v. NV Rotterdamsche Kolen Centrale* (1967) 1 AC 361.
[469] Ss. 2(2), 3(2), 6(1A), 7(1A), 1977 Act.

*regard to the circumstances which were, or ought reasonably to have been, known to or in the contemplation of the parties when the contract was made*."[470] As is evident this test does not lay down an objective, straitjacket answer that would indicate the same answer for all contracts.[471] Each contract would need independent deliberation and an analysis of surrounding factors to understand whether the terms were reasonable or not.

However, guidelines have been found present in the Act itself to provide a general understanding of relevant circumstances that could assist with an assessment of the reasonableness of terms.[472] These are obviously not exhaustive guidelines. The guidelines for relevant factors in understanding the reasonableness of a term are as follows:

1. The bargaining power dynamics of the parties, including the effective alternative with a customer to avail of the same product or service elsewhere.
2. Whether a customer entered a contract due to an inducement, or whether the customer had a real opportunity to enter into a similar contract with someone else, without having to accept the 'unreasonable' term in question.
3. Whether the customer had relevant knowledge of the extent and scope of the term in question, including implied knowledge of relevant customary practices.
4. Whether a term excluding, or restricting liability was reasonable at the time the contract was entered into.
5. Whether the goods were manufactured or adapted in a manner to meet the specific stipulations of a customer.

Using these contours mentioned, in the case of *St. Albans City and District Council v. International Computers*,[473] an exemption clause, limiting the liability of the seller of a computer software owing to an error in the software, to 100,000 pounds, was held to be unreasonable, and was thus not enforced.

### REPUGNANCY TO PUBLIC POLICY

Another aspect of understanding unreasonableness in a contract is looking at terms which could be repugnant to public policy.[474] This is the standard that is most typically used in India.

An analysis of the case which determined the justiciability of 'unconscionable terms' in a contract of employment entered with a Government Company helps understand the test of 'repugnancy to public policy'.[475] In this case, the help of Section 23 of the Indian Contract

[470] S. 11(1), 1977 Act
[471] *Smith v. Eric S Bush*, (1990) 1 AC 831.
[472] S. 11(2), Schedule II, 1977 Act
[473] (1996) 4 All ER 481.
[474] *L.I.C. of India & Anr. v. Consumer Education & Research Centre & ors. etc.* (1995) 5 SCC 482.
[475] *Central Inland Water Transport Corporation Limited and Ors. v. Brojo Nath Ganguly and Ors.* 1986 AIR SC 1571.

Act was taken for holding unreasonable terms of the contract void on the ground of public policy.[476] A reference to Section 23 of the Indian Contract Act is helpful in this context:

> "***Section 23 - What considerations and objects are lawful and what not:***
>
> *The consideration or object of an agreement is lawful, unless-*
>
> *It is forbidden by law; or is of such a nature that, if permitted, it would defeat the provisions of any law; or is fraudulent; or involves or implies injury to the person or property of another; or the Court regards it as immoral, or opposed to public policy.*
>
> *In each of these cases, the consideration or object of an agreement said to be unlawful. Every agreement of which the object or consideration is unlawful is void.*"

But how is 'public policy' to be understood when adjudicating claims of unreasonable terms in standard form contracts. The aforementioned judgement clarified the same in the following terms:

> "*Public policy, however, is not the policy of a particular government. It connotes some matter which concerns the public good and the public interest. The concept of what is for the public good or in the public interest or what would be injurious or harmful to the public good or the public interest has varied from time to time. As new concepts take the place of old, transactions which were once considered against public policy are now being upheld by the courts and similarly where there has been a well-recognized head of public policy, the courts have not shirked from extending it to new transactions and changed circumstances and have at times not even flinched from inventing a new head of public policy…*
>
> *… It is thus clear that the principles governing public policy must be and are capable, on proper occasion, of expansion or modification. Practices which were considered perfectly normal at one time have today become obnoxious and oppressive to public conscience. If there is no head of public policy which covers a case, then the court must in consonance with public conscience and in keeping with public good and public interest declare such practice to be opposed to public policy.*"

Thus, the threshold that has developed is that if such terms are contained in standard form contracts that are unreasonable to the extent that they shock the conscience of the court, then they shall be held void.

[476] *Ibid*.

In this aforementioned case, it was finally held that the term of service of employees of the aforementioned Company which allowed for their dismissal without even giving them the right to an enquiry would be considered to unconscionable. Such a term was found to be contrary to Section 23 of the Indian Contract Act and thus declared null and void.

Similarly, the case of *Lilly White v. R. Munuswami*[477] provides us with another good example of the adjudication upon what can be understood as unreasonable terms in a contract. The genesis of the dispute lay in a laundry receipt which contained a condition that if a customer's article got lost, she or he would be entitled only up to 50% of the market value or price of the item. A customer's new sari was lost. When the matter reached Court, it was held that such a term could not be enforced. If it were done, the laundry owner would have incentive to misappropriate articles at half price! This was considered against public policy and public interest, and hence the condition was not enforced.

***LIABILITY IN TORT***

The interaction of individuals in society is not governed by contract law, alone. The law of tort is another field that seeks to regulate interactions of people at an individual, private level. It is in this field that we find the next protective device. As per this protective device, even if an exemption clause of a standard form contract is so wide that all forms of liability have been excluded, it is not that an acceptor will be without any remedy. In such cases, the Court awards the acceptor a relief in the field of torts.

This is best exemplified in the case of *White v John Warwick*.[478] The defendant leased a cycle to the plaintiff. The lease deed stated that the defendants would maintain the cycle, but "*nothing in this agreement shall render the owners liable for any personal injuries*…". Due to negligence on the part of defendants in maintaining the cycle properly, the plaintiff got injured. An action was brought before the Court. Even though the exemption clause in the standard form contract sought to exclude all liability that could arise from the transaction, the Court used the tort of negligence to hold the plaintiff liable. Thus, to place liability, the law of tort was taken support of.

The caveat in these cases was that some standard form contracts could even exempt liability in the field of tort law. Thus, specific terms could be incorporated to exempt the offeror of a standard form contract from liability even under tort law. Initially such exemption clauses were upheld since the plain language of the contract could not be re-written by the Courts.[479] In UK this stance changed with the promulgation of the Unfair Contract Terms Act, 1977 which specifically prohibits incorporation of terms that exclude liability under tort law.[480] In India, while there is no legislation that occupies this field, the analysis above on the

[477] AIR 1966 Mad 13.
[478] (1953) 2 All ER 1021.
[479] *Rutther v. Palmer* 1922 2 KB 87.
[480] 199th Law Commission Report, p. 103.

incorporation of unreasonable terms, and concurrent protective devices, indicates that such terms excluding liability even in tort law could fall foul of S. 23 of the Indian Contract Act.[481]

### *EXEMPTION CLAUSES AND THIRD PARTIES*

The way exemption clauses operate vis-à-vis third parties in standard form contracts is not a protective device unique to these forms of contracts, as such. Per the principle of privity of contract, the terms of a contract are meant to bind the parties to a contract, and not any third party. Similarly, even with standard form contracts, a similar treatment prevails. Any third party to the standard form contract is not subject to the liabilities arising from the contract, nor can it enjoy any of the benefits. What this also means is that any exemption clause protecting the offeror of a standard form contract, does not automatically extend such protection to another third party.

How does this work out, though? There are two specific consequences of such different treatment of a third party. Firstly, a good or service provided pursuant to a standard form contract, where the offeror exempts herself from any liability will protect the offeror only with respect to the person who is offered the good or service. That is, if someone else, a third party, gets affected by it, the offeror of the good or service will not be safe from any liability arising in tort law.

This is what happened in the case of *Haseldine v. CA Daw & Son Ltd.*[482] In this case, an owner of a building entered into a contract with an engineering company to maintain a lift in the building. As per this contract, the engineering company had inserted an exemption clause, preventing itself from any liability that could arise in the maintenance of the lift. The owner had also rented apartments in the building to various tenants. During a monthly inspection of the lift, a workman of the engineering company had repacked its cylinder glands in a faulty manner, which led to an accident in the lift. The tenant who got injured in the lift brought an action against the engineering company and the owner.

With respect to the liability against the engineering company, it was held that while the company had clauses protecting itself from liability vis-à-vis the owner of the building, the same would not apply against the tenants. Thus, the engineering company would be liable for negligence against the tenant.

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[481] In this light the case of *Central Inland Water Transport Corporation Limited and Ors. v. Brojo Nath Ganguly and Ors.* 1986 AIR SC 1571 (paras 79 and 89) may be perused as it agrees with the practice in UK and in common law of holding null standard terms that exclude liability in tort law.
[482] (1941) 2 KB 343.

The other consequence of the exemption clause not applying vis-à-vis third parties is that if the offeror of the standard form contract outsources its work to a third party, the acceptor of the contract will be within her right to hold such third party liable. In the case of *Scruttons Ltd. v. Midland Silicones Ltd.*,[483] some cargo was being shipped from one place to another. The shipping company had limited its liability to 500 USD for any loss caused to the goods. The stevedores at England agreed to help with the handling of the cargo, subject to the same liability limiting condition. However, no such contract was entered into with the owners of the cargo, now were they made aware of any such condition. When the cargo got lost because of the negligence of the stevedores, an action was brought against them. The Court held that since the stevedores were a third party to the contract which limited liability, the owners of the cargo would not be limited by the amount of 500 USD while claiming relief from the stevedores. In other words, since the owners of the cargo did not enter into an agreement with the stevedores which limited the latter party's liability, such exemption would be of no benefit to the stevedores.

[483] 1962 AC 446.