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## UNIT 5 GENERAL PRINCIPLES OF CONTRACTS

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### Objectives

After studying this Unit, you should be able to:

- Identify different Sources of Mercantile Law
- Understand the process of Formation of Contracts
- Explain the completion of Contracts and Jurisdiction
- Appreciate essentials of Valid Contract and Performance of the Contracts
- Describe the consequences of Breach of Contract

### Structure

- 5.1 Introduction
- 5.2 Sources of Mercantile Law
- 5.3 Formation of Contracts
- 5.4 Completion of Contracts and Jurisdiction
- 5.5 Essentials of Valid Contract
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- 5.7 Doctrine of Frustration or Agreement to do an Impossible Act
- 5.8 Appropriation of Payments
- 5.9 Consequences of Breach of Contract
- 5.10 Summary
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### 5.1 INTRODUCTION

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Every human being owes certain obligations to his family members and society. These obligations fall under the Law of obligations that covers rights and duties arising between the individuals which are collateral in nature. The concept of obligations existed since the ancient period where the word of mouth was considered to create a bond. In other words, people will never leave from their words i.e., promises. The concept of primary obligations is one of humanity's greatest moral inventions. Wherever the promises are breached they will be brought before the panch system for resolving the dispute between the parties.

The law that is applicable to mercantile transactions is called the mercantile law which includes General Contracts, Special Contracts and the law of Insolvency and Bankruptcy. This law relates to the rights and obligations arising out of mercantile transactions between traders or merchants. The movable property connected with mercantile is of two types namely **Choose in possession** and **Choose in action**. If person 'A' had a ring on his hand which is stolen by a thief, 'A' is a person having **choose in possession**. In other words, it means an Individual who had legal possession of any property of movable nature and physically visible.

Person 'A' can resist the thief from snatching and recover it in a court of law. Recovering the amount due on a promissory note is considered as **choose in action**. This right of the payee or holder is not visible as compared to the ring. Further, it must also be noted that the law of Contracts is applicable even to non-mercantile transactions.

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## 5.2 SOURCES OF MERCANTILE LAW

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The main sources of Mercantile Law in England are: The Law of Merchant or *Lex Mercatoria*; Acts of Parliament or Statutes; Common Law of England and Principles of Equity. *Lex Mercatoria* is the set of customs and usages which are recognised and enforced between merchants and part of the *Common Law of England*. The second one is the sanction of the State and most superior and powerful source and it overrides any rule of Common Law of Equity. The phrase common law is used to denote the law that can be based on judicial pronouncements delivered from generations. King Henry II in 12<sup>th</sup> Century established the Common Law Courts or King's Courts which were also known as Chancery or Equity Courts. Equity courts were not bound to grant relief in every case, as it was always a matter in discretion and governed by certain maxims. There are two maxims which the courts of Equity act: "*he who seeks equity must do equity*" and "*he who comes to Equity must come with clean hands.*"

Prior to the Indian Contract Act, 1872, the English Common Law with some modifications suited to Indian conditions for some time in the British India Courts. After the Establishment of courts at Madras, Bombay and Calcutta the Hindu Law and Mohammedan law and the law of defendants are to be considered for the application of law.

The introduction of judicial system during the British India paved the way to introduce a legislation to recognize and legalize the concept of obligations and the practices among the people by the Contract Act, 1872. The principles of Law of contract are divided into four categories namely ***the formation of the contracts, content of contracts, excuses for non-performance, and enforcement of contracts.***<sup>1</sup>

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## 5.3 FORMATION OF CONTRACTS

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A contract is an **agreement** enforceable in a court of law. An agreement is a set of reciprocal promises between the parties to the contract. These set of promises arises from an **offer** and **acceptance** from the parties to the contract.

The contract may be express or implied i.e., it may be oral words or in writing and even inferred from the conduct of the parties.<sup>2</sup> It may be bilateral or unilateral contract. The former one refers to the involvement of two parties and the latter refers one party alone can perform without the other.

**Agreements:** Two or more persons agree mutually to undertake to do or not do certain things through an agreement, for example, to deliver goods and to pay for them. This is not through a process of offer and acceptance.

**Offer:** The offer is a proposal by the offeror to undertake to do or abstains from doing something provided the offeree will also undertake to do or abstains from doing something.<sup>3</sup> The offer contains two things namely '*an expression of a*

willingness to be bound' and 'a statement of what each party to the proposed agreement must do or not to do.' The person making the proposal is said to be called as 'Promisor', 'Offeror,' or 'Proposer.'<sup>4</sup> The offer is of two types namely *specific offer* and *General offer*. An offer to a specific person is specific offer and the offer to public at large is general offer. 'A's offer to sell his watch to 'B' is specific and 'X' offer to pay Rs.1,000/- to one who finds his lost dog is the example of general offer.

**Acceptance:** The person to whom the proposal is made signifies his assent thereto, the offer/proposal has been accepted and which raises a promise.<sup>5</sup> The person to whom the proposal is made or the person from whom the promisor seeks the assent is said to be called as 'Promisee' or 'Acceptor.'<sup>6</sup>

*Example: When 'A' signifies his willingness to sell his motor cycle for Rs.55,000/- to B, and B express his willingness to purchase for the said price, A is the proposer/promisor or offeror and B is the promisee/acceptor.*

The proposal/offer/promise must possess the following characteristics:

- 1) **It must be intended and capable of creating legal relationship between the parties to give rise to legal consequences:** The set of promises rise between the parties must create legal relations. In the above example, if A does not deliver the vehicle after receiving the price or if B does not pay the price, the other party having right for breach of promise/obligation undertaken by the party in the offer/acceptance as the case may be. The set of promises between parties which are not capable of giving rise to legal relationship or those which are not enforceable in a court of law are called as social obligations/agreement. If a person makes a promise to his friend to take him to dinner at a restaurant and the other agrees and if the promisor failed to perform his obligation, the promise could not be enforceable in a court of law as it was a social obligation. In other words, the social obligations through set of promises are incapable of giving rise to create legal relations between the parties.<sup>7</sup>
- 2) **The terms of it must be certain or capable of being certain:** The terms of the offer must be certain i.e., without ambiguity or vagueness. In other words, the person to whom it was made must be in a position to understand and respond with his assent.
- 3) **It must be different from the following:**
  - a) **Quotation, catalogue, Auction, Tenders etc.:** These are regarded as invitation to make an offer for a particular thing specified therein by the person who gave the quotation /catalogue. Calling for tenders and auctioning of goods also come under invitation to make offer.
  - b) **Window displays at show rooms:** This is also considered as an invitation to make an offer by the showroom owner from the public.
  - c) **Railway timetables:** Issuing of ticket by the Railway authorities against payment to a commuter is amounting to an offer but the time tables of the railways not regarded as an offer.
- 4) **It must be offered to an individual or to the public at large:** The offer is of two types namely specific offer and General offer. An offer to a specific

person is specific offer and the offer to public at large is general offer. A's offer to sell his watch to B is specific and X offer to pay Rs.1,000/- to anyone who finds his lost dog is the example of general offer.

- 5) **It must be communicated to the offeree:** The offeror is having obligation to communicate to the respective offeree within reasonable time and manner.

In order to convert a proposal into a promise, the acceptance must be absolute and unqualified.<sup>8</sup> It must be expressed in some usual and reasonable manner. If the acceptance is conditional the promisor can withdraw the proposal before the acceptance becomes absolute. Performance of the conditions of the offer or acceptance of any consideration for reciprocal promise which may be offered with a proposal is an acceptance of proposal.<sup>9</sup>

***Essentials of valid acceptance:***

- 1) The acceptance is not valid if it was communicated in the manner otherwise than mentioned in the offer. English law invalidates such acceptance. But Indian law<sup>10</sup> says that after receiving the acceptance in different manner, the receiver must inform the acceptor that your acceptance is not accepted unless and until it is communicated in the specified manner, failing which the proposer accepts the acceptance.
- 2) The offeror may waive the communication of an acceptance.<sup>11</sup>
- 3) Acceptance must be made before the offer lapses or revoked by the proposer.
- 4) It should be absolute in terms with the offer. Variation or addition of terms to the original offer is not valid acceptance. A statement of fact to an offer does not amount to acceptance.<sup>12</sup>

***Lapse or revocation or rejection of offer:*** The proposal of the offeror lapses on the death of the proposer and before the offeree accepts. There will be no contract in English law even the acceptance was made in ignorance of the death of the offeror. But under Indian law, there will be a valid contract except where the acceptance is made with knowledge of the death of the offeror.<sup>13</sup> This rule will be applicable in case of insanity of the offeror also.

If the offeree does not respond to the offer in the manner prescribed or within reasonable time there will be no contract. The term '*reasonable time*' is used in wider sense which varies from the circumstances of each case.

The offeror is at liberty to revoke the offer by communication at any time before the offeree makes the acceptance of it. Even if the offer is valid for a fixed term or period; the offeror can communicate the revocation of the offer before the offeree accepts.

The offeree can communicate his rejection to the offeror or he may make counter offer or he may accept with certain conditions.

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## 5.4 COMPLETION OF CONTRACTS AND JURISDICTION

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Generally, the contract completes when the acceptance of the offeree is posted or put in to transmission. It was made at the place where the acceptance is received

by the offeror. It was easy to determine the completion of contract when the parties negotiate in person. But it will be difficult to determine in case of negotiation by *post, telegram, telephone and mail*, etc. The contract in case of instantaneous contracts completes only when the communication of the acceptance is received by the offeror. In other words, the contract is said to be made at the place where the acceptance received but not at the place where it is transmitted.<sup>14</sup>

The United Nations Commission on International Trade Law (UNCITRAL) adopted the Model Law on Electronic Commerce in 1996. As a result the Information Technology Act, 2000, governs the rules relating to the e-commerce contracts. The offeror and acceptor are substituted by expression *soriginato*<sup>15</sup> and *addressee*. The electronic record sent by the originator may be received intact or it may vary. The addressee has to acknowledge the receipt of electronic record by communication automated or any mode or by conduct.<sup>16</sup> The contract completes where the principal place of business of the originator, in case of more than one place of business of originator or addressee the principal place of business of the originator or addressee and in case of no place of business his usual place of residence will be considered as the completion of the contract for the purpose of jurisdiction.<sup>17</sup>

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## 5.5 ESSENTIALS OF VALID CONTRACT

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Consideration, capacity to contract, free consent, and legality of consideration and object are some of the essentials of a valid contract. These are explained in detail below:

### 1) *Consideration*:

Consideration is one of the essential conditions for the validity of contract.<sup>18</sup> The essential condition for the enforceability of simple contracts is *consideration*, and the rule is expressed by the *Latin maxim*: *ex-nudopacto non oritur actio* which means out of nude pact no cause of action arises. It can be understood in the sense *quid pro quo*.

“A valuable consideration in the sense of the law may consist either some right, interest, profit or benefit accruing to one party, or some forbearance, detriment, loss or responsibility, given suffered undertaken by the other.”<sup>19</sup>

“An act or forbearance of one party or the promise thereof, is the price for which the promise of the other is brought and the promise thus given for value is enforceable.”<sup>20</sup>

“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 promise to do or abstain from doing something, such act or abstinence or promise is called a consideration for the promise.”<sup>21</sup>

The analysis of the above definitions says that the consideration may be executed or executory. In a contract to deliver a watch by A to B for Rs.100, A and B gained money and watch and in another stand point A and B lost watch and Rs.100, respectively. The law insists more upon the presence of the element of detriment to the promisee B and then the presence of benefit to the promisor A.

A promise from one party to the other and a promise from the other to the former support the consideration. In other words, the reciprocity of promises between the parties establishes the consideration.

The absence of consideration makes the contract void.<sup>22</sup> This principle has certain exceptions recognized under the provisions of law. They are:

- i) Where the contract reduced in to writing and registered and made out of natural love and affection between the parties standing in near relationship to each other.
- ii) Where the contract is to compensate the person who voluntarily rendered services in past. In other words, past services rendered at the desire of the promisor constitute a valid consideration in India.<sup>23</sup> But under English law past consideration is not valid.
- iii) Where a promise is made to pay a time-barred debt does not require a fresh consideration.
- iv) Where a gift between the donor and donee is not affected for want of consideration if it is registered and attested by two witnesses.

Though consideration is necessary it need not be adequate. The adequacy and sufficiency of consideration is immaterial. It is said that pepper corn is sufficient for purchase of an elephant.

The consideration is to move from whom is the question to be determined for the enforceability of the contract. It must proceed or move from the promisee. Under English law a stranger to a consideration cannot sue. In other words, the promisee cannot sue the promisor if the consideration doesn't move from him. But under Indian law, a stranger to consideration can sue.

The rule stranger to contract cannot sue is the same both under English law as well as under Indian law. This principle was explained by the doctrine of *Privity of Contract*.<sup>24</sup> Under English law there are certain principles which are fundamental. A person who is a party to the contract can sue on it. This principle has certain exceptions recognized by the provisions of law, as stated hereunder:

- a) Where a trust is created for the benefit of a party, the beneficiary can enforce it though he is a stranger to contract.<sup>25</sup>
- b) Where there is an acknowledgement of liability or estoppel. For example, 'A' receives money from 'B' to pay it to 'C', 'A' admits to 'C' the receipt of this amount and liable to pay it to 'C'.

Apart from the above the Indian law recognizes two more exceptions:

- c) A benamidar in whose name a property was registered is entitled to enforce though he is not a party to the contract.
- d) In family arrangements such as maintenance or expenses for marriages of female members, the beneficiaries can sue though they are not party to the contract.

### ***Consideration and Discharge of Contract:***

The doctrine of consideration is not extended to the discharge of contract. The reciprocal promises between the parties constitute consideration. Subsequently,

if both the parties agree not to enforce the contract also constitute consideration in India. But it is not so in English law. Till 1947 the law of England applied the doctrine of consideration not only to the formation of a contract, but also to its discharge. It was pointed out that a creditor '*might accept anything in satisfaction of his debt except a less amount of money*'<sup>26</sup> A canary or pepper corn may be accepted in full discharge of a debt, but a part payment of the debt cannot be accepted so as to operate as full discharge of the debt. The following are the exceptions to the rule in *Pinnel's* case.<sup>27</sup>

- a) Under the scheme of composition if the debtor agrees to pay a portion of the debt discharges liability without application of the doctrine of consideration under English law.
- b) In case a third party pays a part of the amount less than the amount due from the debtor discharges the debtor without application of the doctrine of consideration under English law.
- c) The doctrine of estoppel or quasi-estoppel neutralized the rule in *Pinnel's* case.<sup>28</sup>

Under Indian law, a contract may be discharged by what is called "*an accord and satisfaction*" i.e., mutually agreed settlement.<sup>29</sup> The English law allows the delivery of horse against the payment of debt but not accept the delivery in future to discharge the debt. The part payment of debt is also not accepted as accord and satisfaction.

## 2) *Capacity to Contract:*

There are certain persons in law who are incapable wholly or in part, of binding themselves by a promise or of enforcing a promise made to them. In mercantile contracts *lex loci contractus* i.e., the law of the place will prevail whereas in case of land *lex situs* i.e., the law of the place where the land situate will be applicable. The incapacity of a party to enter into a contract will arise in two ways namely, on account of status, or on account of mental deficiency. The former would occur on the grounds of political consideration and expediency, the latter is imposed to protect the interest of the disabled person.

The incapacity of a party is broadly divided into two;

**one** which arises out of status of an individual for the following reasons:

- a) Political or Civil status e.g., where the contracting party is a ruler of a foreign state, Ambassador or envoy or alien enemy, or a convict or a bankrupt.
- b) Profession of the contracting person e.g., barrister
- c) Incorporation
- d) Marriage

The **other** which arises from mental deficiency (soundness of mind) of the person contracting in case of:

- a) Minors
- b) Insane persons
- c) Idiots
- d) Drunken persons

The person below the age of 21 is called as an infant as per the Infant Relief Act, 1874 under the Common Law and the person below the age of 18 is a minor as per the Family Reforms Act, 1969, under English law and Indian law respectively. He is a person who is not a major. The Infant Relief Act, 1874 which modified the Common Law of England allows an infant to enter into a contract for the following:

- a) For necessities
- b) Beneficial contracts of service
- c) Contracts involving recurring rights and duties e.g., an interest in property binding on him unless he rescind them either during infancy or within reasonable time of becoming a major
- d) An isolated act or a contract to pay for goods supplied other than necessities, were voidable and not binding on him unless he ratified them within reasonable time after attaining majority.

The law relating to infants/minor contracts is at present provided in Minor's Contract Act, 1987, under English law.

The Indian contract Act, 1872, provides that the contracting party must be a major.<sup>30</sup> A person becomes major on attaining the age of 18 years.<sup>31</sup> The provision of the Contract Act does not specify whether a minor's contract is void or voidable. The analogy of English law made such contracts as voidable and becomes valid by ratification on attaining majority. The *Privy Council* in *Mohori Bibi v. Dharmadas Ghose*<sup>32</sup> pointed out this erroneous view and held that a minor's contract is *void ab initio*. There will be no question of avoiding it or ratifying it. Similar to English law the person supplying necessities to minor is protected under Indian law.<sup>33</sup> The binding nature of a guardian contract on the minor is depending on the legal power of the guardian to enter into a contract or not. There will be no estoppel against a minor as both the parties are aware of the truth. The power to order restitution in India is wider than England. It was clear under Indian law that any benefit, even cash received, may be directed to be restored. But it must be shown that the minor or his estate derived some benefit therefrom.<sup>34</sup>

**Mutuality of mind:** The parties to the contract must have *consensus-ad-idem*<sup>35</sup> which means mutuality of mind as to the subject matter of the contract. The lack of mutuality of mind makes the contract void. 'A' had two houses namely 'X' and 'Y'. 'A' enters into contract with 'B' to sell keeping 'X' house in his mind and 'B' entered into contract with 'A' by keeping 'Y' house in his mind. This results the contract void due to lack of *consensus-ad-idem* on the subject matter of the contract.

### 3) **Free Consent:**

"The consent of the party to the contract is said to be free<sup>36</sup> if it is not caused by; coercion, undue influence, fraud, misrepresentation and mistake. These are explained hereunder:

- i) **Coercion:**<sup>37</sup> "The committing, or threatening to commit, any act forbidden by the Indian Penal code, or the unlawful detaining, or threatening to detain, any property to the prejudice, of any person whatever, with the intention of

causing any person to enter in to an agreement.” The term *duress* in English law defined as causing, threatening to cause, bodily violence or imprisonment, with a view to obtain the consent of the other party to the contract. *Coercion* in Indian law has a much wider connotation than *duress* in English law. The main distinction between *coercion* and *duress* as the first denotes the offense forbidden by Indian Penal Code whereas the latter confined only to bodily violence and imprisonment. The presence of *coercion* or *duress* in both Indian and English law was an invalidating element for the enforceability of contract.

ii) **Undue Influence.**<sup>38</sup> This was also called as constructive fraud. It covers all the contracts where one party will be in a position to dominate the will of the other because of relationship while entering the contract. This influence can be presumed in existence among the following relationships:

- a. Parent and child                      b. Guardian and ward
- c. Trustee and beneficiary              d. Spiritual master and Disciple
- e. Lawyer and client                      f. Doctor and patient

The contract between the parties with above relationship turns it voidable by presuming the existence of undue influence of the former against the other. It is the burden on the former party to prove that he was not in dominating position and that his position was not used to obtain the consent of the other.

iii) **Fraud.**<sup>39</sup> The following acts of a party to a contract establish fraud while entering into a contract with the other:

- a) the suggestion of a fact, of that which is not true by one who does not believe it to be true
- b) the active concealment of a fact by one having knowledge or belief of the fact
- c) a promise made without intention of performing it;
- d) any other act fitted to deceive
- e) any such act or omission as the law specially declares as fraudulent.

The mere silence on the part of party does not amount to fraud. But silence amount to fraud where there is a duty on the party to speak.

iv) **Misrepresentation.**<sup>40</sup> A party may give his consent to enter into a contract because of misrepresentation of the other. These false statements or misrepresentations may be either inducing cause of contract. These statements may be called as innocent misrepresentation and willful or actionable misrepresentation which amounts to fraud.

A misrepresentation consists of the following ingredients:

- a) Failure to disclosure of a fact
- b) Such non-disclosure must relate to a fact not to an opinion
- c) Such representation must be untrue
- d) It must be material to influence the other to enter into a contract

Any representation made by a party with full knowledge of the fact that it is

not true, or without belief in its truth or recklessly, not caring whether it is true or false, it is said to be fraudulent.<sup>41</sup>

Whenever the consent of the party is obtained in the absence of free consent the contract is voidable at the option of the party whose consent is not free because of the presence of coercion, or fraud, or misrepresentation. The aggrieved party of such voidable contract had an option to continue the contract or rescind the contract<sup>42</sup> and entitled for damages. Further, the contract induced by undue influence can be set side or it is voidable at the option of the party whose consent was obtained by dominating the will of the aggrieved party.<sup>43</sup>

- v) **Mistake:**<sup>44</sup> While entering into a contract the parties to the contract may be under a mistake. This mistake may be as to a fact or law. Mistake of fact may be as to subject matter of the contract e.g., regarding the existence, quality or quantity etc.; nature of contract; person entering into contract. Mistake of law may be regarding foreign law, or ordinary law, law of our country, or private rights of the contracting parties. Another classification of these mistakes is bilateral and unilateral.

A mistake of fact in the minds of both the parties negatives the *consensus ad idem* and the contract in such cases is void. Where both parties to an agreement are at mistake as to a matter of fact essential to the agreement, the agreement is void.<sup>45</sup> This will come under the classification of bilateral mistake.

In case of unilateral mistake, i.e., where only one party to a contract is under a mistake, the contract, generally speaking, is not valid. A contract is not merely voidable because it was caused by one of the parties to it being under mistake as to a matter of fact.<sup>46</sup>

A contract is not voidable because it was caused by mistake as to any law in force in India but a mistake as to a law not in force in India has the same effect as a mistake of fact.<sup>47</sup>

#### 4) **Legality of Consideration and Object:**

Apart from the above essentials for the formation of a valid contract **the legality of consideration and object**<sup>48</sup> is must. The unlawful agreements may be classified as follows:

- 1) **Illegal**-where the agreement is contrary to the statute law
- 2) **Immoral**- where it is opposed to public morals e.g., agreement for illicit cohabitation, or separation between husband and wife
- 3) **Opposed to public policy**- where the agreement is forbidden as conflicting with the well-being of the state e.g., agreements tending to the abuse of legal process, agreements in restraint of trade, agreements in restraint of marriage, agreements in restraint of parental rights, etc.

Where a part of consideration or object of an agreement is unlawful the agreement is void. In case of non-separation of the unlawful part from the agreement the total transaction will be void. The rule applicable to separate the unlawful and lawful part is known as *blue pencil rule*. In such cases the lawful part which

separated by drawing blue pencil lining from the unlawful part can be enforceable.<sup>49</sup> A contract without consideration is said to be void with certain exceptions;<sup>50</sup>

- a) Every agreement in restraint of marriage of any person, other than a minor is void.<sup>51</sup>
- b) An agreement in restraint of trade is void with an exception where goodwill is sold or as per the provisions of the Partnership Act, 1932.<sup>52</sup>
- c) Any agreement in restraint of legal proceeding is void with an exception of arbitration agreement.<sup>53</sup>
- d) Where the meaning of an agreement is not certain, or capable of being certain are void.<sup>54</sup>
- e) Agreement by way of wager is void.<sup>55</sup>
- f) The performance of the contract is depending on the happening or non-happening of an event at a future date is called as contingent contract.<sup>56</sup> If the happening of the event is impossible the contract becomes void.<sup>57</sup>
- g) The enforcement of a contingent contract is possible before the impossibility of its occurrence.<sup>58</sup> The promise of A to pay B a sum of money if B marries C. C marries D. Marriage between B and C is impossible during the life time of A makes the agreement void.<sup>59</sup>
- h) The contingent contract to do or not to do within a specified becomes void after the expiry of the time.<sup>60</sup>
- i) Any agreement contingent on impossible events is void.<sup>61</sup>

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## 5.6 PERFORMANCE OF THE CONTRACTS

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Both the parties to the contract either perform, or offer to perform their respective promises until such performance is dispensed with or excused under any provisions of this Act or any other law in force. Even the death of one of the party makes his legal representatives liable unless the intention of the parties to the contract differs.<sup>62</sup> The promisee's non-acceptance of offer of performance of the promisor, the promisor is not responsible for the performance, nor does he lose his rights under the contract subject to the following conditions:<sup>63</sup>

- a) The offer must be unconditional.
- b) It must be made at a proper time and place, and in the circumstances that the person to whom it is made must have a reasonable opportunity to ascertain that the person is able and willing to do i.e., accept
- c) If it is the delivery of anything to the promisee, he must have an opportunity of seeing the delivered thing which the promisor is bound by his promise to deliver.

In case of anticipatory breach of contract by the promisor, the promisee may put an end to the contract, and sue for damages immediately though he had a right to keep open the contract until the performance is actually due.<sup>64</sup> Keeping the promise alive may lead the promisor to take advantage of supervening circumstances.

The performance may be by the person who makes the promise, the promisor or his representatives may employ a competent person to perform depending on the intention of parties to the contract.<sup>6</sup> If the performance from the third person is accepted by the other party, later the promisee can't enforce against the promisor.<sup>7</sup>

When the promise is made jointly, it is to be performed by all such joint promisors during their living and after the death any of them, his representative jointly with surviving promisor. After the death of the last survivor, the representatives must fulfill the promise jointly. This is subject to a contrary condition of the contract.<sup>67</sup> The promisee may compel one of the joint promisor to perform in the absence of express agreement to the contrary. On such performance by one of the promisor he can compel the other promisor to contribute. In an occasion where one of the promisor failed to contribute the remaining promisors has to share the loss of contribution.<sup>68</sup> This is also subject to a contrary appears in the language of the contract. The release of the joint promisor from performance does not discharge the other from liability. There is a point of difference in English law and Indian law. In India, they are presumed to be jointly and severally liable.<sup>69</sup> When a party makes a promise to two or more persons, the right to claim the performance rests between him and them, with them during the life time of the parties and on the event of death of either party, between the representative and survivor/representative as the case may be, with joint promisee or survivor/representative or representatives.<sup>70</sup> This is subject to a contrary condition of the contract.

#### ***Time and Place of Performance:***

When the promisor has to perform without the application of the promisee, and no time is specified in the contract to perform, the performance must be done within reasonable time. What is reasonable time is a question of fact?<sup>71</sup> When the time is specified but no application to be made by the promisee, the promisor may perform it any time during the usual hours of business on such day, and the place at which the promise ought to be performed.<sup>72</sup> It is the duty of the promisee to make the application for performance on certain day to be at proper time and place during the usual hours. What is proper time and place is a question of fact?<sup>73</sup> It is the duty of the promisor to make an application to the promisee as to the time and place to perform when a promise is to be performed without application.<sup>74</sup> The promisee may prescribe or sanction the manner, the time and place of performance.<sup>75</sup>

#### ***Performance of Reciprocal Promises:***

In case of existence of reciprocal promises, the promisor needs to perform only when the promisee is ready or willing to perform his part of promise in the contract.<sup>76</sup> The reciprocal promises are to be performed as per the order specified in the contract, in the absence of such specification of order they must be performed in the order of the transaction requires.<sup>77</sup> The party preventing the other ready to perform his part of the reciprocal promise, the contract becomes voidable at the option of the party so prevented; he is entitled for compensation for loss because of non-performance of the contract.<sup>78</sup> The order of the performance of the reciprocal promises in the sequence as specified. The non-performance does not entitle the performance of the reciprocal promise and must make compensation to the other party for any loss because of his non-performance of the contract.<sup>79</sup> The performance to do a thing at or before specified time has to be performed accordingly. Failing which the contract becomes voidable in case the contract specifies the time is essence of the contract. The intention of the

contract does not specify time as essence of contract, the contract is not voidable and the promisee is entitled for compensation for any loss because of non-performance of the contract.<sup>80</sup> If the promisee agreed the acceptance of performance by the promisor other than at the agreed time, he can't claim damages for the delay in performance. However, he is entitled for compensation if he gives notice to the promisor of his intention to do so at the time of acceptance.<sup>81</sup>

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## 5.7 DOCTRINE OF FRUSTRATION OR AGREEMENT TO DO AN IMPOSSIBLE ACT

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The agreement between two parties to do an impossible act itself is void. A contract may also void because of an event which makes the performance of promise impossible or unlawful after the completion of the contract. Any person who makes promise to perform by knowing it to be impossible or unlawful is liable to pay compensation to the promisee that is not aware of impossibility or unlawful nature of the contract at the time of arriving it.<sup>82</sup> This is known under the doctrine of frustration. This will be applicable in two classes of cases:

- 1) Where a supervening event makes the performance of a contract impossible
- 2) Where a supervening event or events have frustrated the object of both the parties and the changing circumstances the promise fails to be performed.

The dislocation of business in the wake of the first and second World Wars brought before courts a large number of 'frustration cases' and it has now been recognized the term 'frustration' includes the cases of 'impossibility' as well as the 'frustration of adventure.'

### ***Supervening impossibility:***

The very object of the subject-matter relating to the contract disappears; the contract is discharged by frustration on the ground of destruction of subject matter. A contract is also considered as frustrated in case of non-occurrence of expected events. The musician who failed to perform a concert due to illness as agreed in a theatre was held to be frustrated and so discharged by supervening impossibility.<sup>83</sup> The requisitioning of land by government for military purposes from the contract of sale of land by a company which undertook to construct drains and roads on the land to make it suitable for residential purpose is not considered as supervening impossibility as it was a temporary interruption and does not discharge the parties from the performance of the contract.<sup>84</sup>

### ***Supervening Illegality:***

The contracts entered with the enemy nationals prior to the outbreak of war are suspended during the war and revived after restoration of peace only if it is not a continuous mutual duty between the parties. The changes in law also make the contract unlawful and the performance of the contract impossible. The judiciary expressed different theories for the judicial basis on the subject. The *implied theory* propounded by *Viscount Simon* says that no term could be implied to put an end to the contract in those circumstances.<sup>85</sup> According to the *disappearance theory*, if the foundation of the contract disappears either by the destruction of the subject-matter or by reason of interruption of performance, it must be regarded as frustrated. In case of *Just and reasonable solution theory*, even the express term in the contract render the performance impossible, and the contract purporting

to be alive, courts may hold the parties discharged from liability under the doctrine of frustration.

***Doctrine of frustration limitations:***

The party who himself responsible for frustration can't invoke the doctrine. This doctrine is not applicable to leases. In England, this doctrine is not applicable to the contract of sale of land as the buyer becomes the equitable owner of the property. In India, there is no equitable estate as such and so the doctrine is applicable even to contracts for sale of immovable property.<sup>86</sup>

When there are two sets of reciprocal promises between the parties, one is legal and the other is illegal based on the circumstances, the legal one becomes a valid contract and the other is a void agreement.<sup>87</sup> In case of alternative promise, the legal one can be enforced and the other is void.<sup>88</sup>

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## 5.8 APPROPRIATION OF PAYMENTS

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When the payment is made by the debtor, the payment has to be remitted by the creditor towards the amount outstanding as suggested by the debtor.<sup>89</sup> If the debtor not specified to which debt the payment is to be adjusted, the creditor had a right to pay even the time-barred debt also.<sup>90</sup> Neither the debtor or creditor appropriated the payment made by the debtor; the payment must be adjusted towards the first debt which is outstanding between the creditor and the debtor.<sup>91</sup> The above rules for the appropriation of payments are known as *Rule in Clayton's case*.

**Contracts which need not be performed:**

The original contract between the parties need not be performed in case of *novation, rescission and alteration* of such contract. If the parties agree to substitute a new contract instead of the original one, or to rescind or to make an alteration of the contract, the parties to the original contract need not perform the obligations therein.<sup>92</sup> The promisee is at liberty to dispense with performance of the promisor wholly or partly or extend the time of performance or may also accept instead of it any satisfaction which he deems just.<sup>93</sup> When a person having the option of rescinding the voidable contract, exercises his option to rescind the other party need not perform his part of promise in the contract.<sup>94</sup> Further, the party rescinding receives any benefit under voidable contract is liable to restore the benefit to the other. When a contract becomes void afterwards, the party deriving benefit or advantage of such contract is under obligation to restore it.<sup>95</sup> In case of rescission of a voidable contract, the party exercising the option must communicate the rescission of contract in the same manner as followed for communication of the revocation of the proposal.<sup>96</sup> The neglect or refusal of the promisee to afford the reasonable facilities for the performance of the promisor, the promisor is excused for the non-performance caused thereby.<sup>97</sup>

**Of certain relations resembling those created by contract:**

These are also called as *implied contracts or quasi-contracts or Constructive contracts* which are created by lawyers and judges, based on certain equitable considerations. The early common Law of England had only two kinds of remedies: contractual and delictual. The absence of contract, the remedy could only be in tort. *Quasi* is a *Latin* term which means '*as if*.' In quasi contracts, there will be no actual contract between the parties but the law attributes to a

particular situation consequence which is similar to that of a contract. Action of account is the early quasi-contractual liability. This was available against Bailiffs, receivers and guardians who had to account for money kept with them. The 14<sup>th</sup> and 15<sup>th</sup> century extend to every case where money is paid to the defendant by a third party to the use of plaintiff. The underlining principle to determine the liability of the defendant is unjust enrichment at the expense of plaintiff. The equity courts applied the principle of preventing unjust enrichment in evolving the concept of trust.

There is no exact definition of a quasi-contract given anywhere even in the Contract Act. Those given by Dr. Winfield<sup>98</sup> and Dr. Jenks<sup>99</sup> may be accepted in the absence of a better one. 'A' delivers goods to 'B' without any contract either expressly or in writing. 'B' consumed the goods delivered by 'A'. The obligation of 'B' to pay 'A' the price arises from his promise implied by his conduct. This kind of contract is called a tacit contract. Similarly, if 'A' delivers to 'C' assuming him to be 'B', and 'C' consumed them, the obligation of 'C' to pay compensation to A for their value. This is quasi or implied contract.

The following are the examples of quasi-contract:

- 1) **Action for money had and received:**<sup>100</sup> This was based on the equitable principle that no person shall enrich himself at the expense of the other. Even the payments made under mistake of law may be recovered. The payment made under coercion is also recoverable under this principle.
- 2) **Money paid to plaintiff for use of defendant:**<sup>101</sup> Where tenant A pays the taxes due from his landlord B to C in order to protect his possession from being processed against in execution of B's debt. In such cases, there is an obligation on B to repay the amount paid for his benefit. The enforcement of obligation under this head depends on two conditions namely the payment must be bonofide to protect his interest and it should not be a voluntary one.
- 3) **Quantum meruit:**<sup>102</sup> The person derived benefit from an act of another has to compensate the other even there is no contract or invalid contract. This was based on the principle of *quantum meruit* which means 'as much as he deserves.' The compensation is subject to the fact that the delivery of goods is not made gratuitously and the defendant enjoyed the benefit.
- 4) **Obligation of finder of last goods:**<sup>103</sup> Though there is no contract between the finder and loser of the last goods the finder is having an obligation to return the goods find to the owner as a bailee.
- 5) **Necessaries supplied to a person incapable of contracting:**<sup>104</sup> This will discuss the contractual liability of a minor or lunatic to whom the necessaries are supplied which are suited to his condition of life. The person supplied necessaries entitled only to the property of the incapable party but he can't make him personally liable for the dues of the supply.

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## 5.9 CONSEQUENCES OF BREACH OF CONTRACT

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Any party who is responsible for breach of contract is liable to pay damages/compensation to the other party who suffers loss because of non-performance by the other. In other words, the party aggrieved by the default of performance of

the other's obligation leads to breach of contract and entitles him for compensation. There were two remedies available in case of breach of contract by a party.

- 1) **Common Law Remedy, i.e., damages:** The remedy of damages, therefore, only tries to evaluate in terms of money, the loss which a party sustains as a result of breach of contract.
- 2) **Equitable Remedy, i.e., specific performance of contract, injunction, rectification and cancellation, etc.:** Keeping in mind that Specific performance is not available in every case, subject to several limitations; there is no other alternative for courts than to award damages which, of course, is available in every case.

**Measure of damages is the value of performance of the contract to the plaintiff, and not what it costs the defendant to perform it.**

There are four kinds of damages:

- A) **General, or ordinary, or substantial damages:**<sup>105</sup> These are the damages which are to be paid as a consequence of breach of contract. In other words, it means the natural following consequences out of breach.
- B) **Special damages:**<sup>106</sup> These are the damages which are to be paid for the loss of the profit in case of breach of contract of sale by the buyer. In other words, it was a kind of damages which are to be paid on account of usual or extra ordinary circumstances of the case.
- C) **Vindictive, or Punitive or Exemplary damages:** These are awarded with a view to punish the defendant. Generally, vindictive damages are not awarded in case of contracts, but will be awarded in actions in tort. But they may be awarded in contracts like breach of contract to marry and the breach of payment of the customer to honor the cheque.
- D) **Nominal damages:** These are paid in case of technical violation but no substantial loss. Proof of damage necessary even for claiming nominal damages.

The English law on the question of damages is laid down in *Hadely v. Baxendale*.<sup>107</sup> The following are the rules relating the award of damages for breach of contract:

- 1) The injured party is to be placed in the same financial position as if the contract has been performed.
- 2) Damages which are fair and reasonable arising from breach of contract can be recovered.
- 3) Damages which are contemplated in the contract at the time of contract<sup>108</sup> can be recovered though they are not naturally arising. These are called as liquidated damages.
- 4) Damages which will not fall under 2 or 3 above, but arise of special circumstances called special damages are not recoverable, unless they are brought to the notice of the other party before the contract is made.
- 5) It is the duty of the aggrieved party to minimise the damages.

- 6) It should not be more than agreed amount of the damages.
- 7) The injured is not disentitled to damages because of difficulty to assess them.
- 8) Vindictive or exemplary damages can't be awarded, except for the breach of contract of marriage.
- 9) The party rightfully rescinding the contract on the non-performance of the other is entitled to compensation,<sup>109</sup>

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## 5.10 SUMMARY

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The law that is applicable to mercantile transactions is called the mercantile law which includes General Contracts, Special Contracts and the law of Insolvency and Bankruptcy. This law relates to the rights and obligations arising out of mercantile transactions between traders or merchants. Prior to the Indian Contract Act, 1872, the English Common Law with some modifications suited to Indian conditions for some time in the British India Courts.

A contract is an agreement enforceable in a court of law. An agreement is a set of reciprocal promises between the parties to the contract. These set of promises arises from an offer and acceptance from the parties to the contract. The contract may be express or implied i.e., it may be oral words or in writing and even inferred from the conduct of the parties. It may be bilateral or unilateral contract. Generally, the contract completes when the acceptance of the offeree is posted or put in to transmission. It was made at the place where the acceptance is received by the offeror. It was easy to determine the completion of contract when the parties negotiate in person.

Consideration, capacity to contract, free consent, and legality of consideration and object are some of the essentials of a valid contract.

The agreement between two parties to do an impossible act itself is void. A contract may also void because of an event which makes the performance of promise impossible or unlawful after the completion of the contract.

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## 5.11 SELF ASSESSMENT QUESTIONS

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- 1) Discuss the origin and sources of Mercantile Law.
- 2) Explain the formation of contract.
- 3) Describe the completion of contract and jurisdiction.
- 4) What are the essentials of a contract?
- 5) Briefly give a not on the capacity of party to the contract.
- 6) Critically analyze “a contract without consideration is void.”
- 7) When consent is said to be free?
- 8) Differentiate valid, void and voidable contracts.
- 9) Elucidate the performance of the contract and the reciprocal promises.
- 10) ‘Time is not the essence of contract.’ Comment.
- 11) How is the doctrine of frustration applicable in a contract?

- 12) Define the applicability of rule in Clayton's case for the appropriation of payments.
- 13) State the contracts which need not be performed or discharge of contract.
- 14) Enumerate the obligations which resemble the contracts under the head quasi-contracts.
- 15) Mention the consequences of the breach of contract.

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- <sup>2</sup> Section 9 of the Indian Contract Act, 1872.
- <sup>3</sup> Sec.2(a) of the Indian Contract Act, 1872 "when one person signifies to another his willingness to do abstain from doing anything, with a view to obtaining the assent of that other to such abstinence, he is said to make a proposal."
- <sup>4</sup> Sec.2(c) of the Indian Contract Act, 1872
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- <sup>6</sup> Supra note 2
- <sup>7</sup> Lord Atkin Balfour v.Balfour 1919 (2) KB 571

- 8 Section 7 of the Indian Contract Act,1872
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- 48 Section 23 of the Indian Contract Act, 1872
49. Section 24 of the Indian Contract Act, 1872
- 50 See supra note 22
- 51 Section 26 of the Indian Contract Act, 1872
- 52 Section 27 of the Indian Contract Act, 1872
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<sup>88</sup> Section 58 of the Indian Contract Act, 1872

<sup>89</sup> Section 59 of the Indian Contract Act, 1872

<sup>90</sup> Section 60 of the Indian Contract Act, 1872

<sup>91</sup> Section 61 of the Indian Contract Act, 1872

<sup>92</sup> Section 62 of the Indian Contract Act, 1872

<sup>93</sup> Section 63 of the Indian Contract Act, 1872; see also Pinnel's case at Consideration.

<sup>94</sup> Section 64 of the Indian Contract Act, 1872

<sup>95</sup> Section 65 of the Indian Contract Act, 1872

<sup>96</sup> Section 66 of the Indian Contract Act, 1872

<sup>97</sup> Section 67 of the Indian Contract Act, 1872

<sup>98</sup> "as liability not exclusively referable to any other head of law imposed on a particular person to pay money to another , on the ground of unjust benefit."

<sup>99</sup> "a situation in which law imposes upon one person, on grounds of natural justice, an obligation similar to that which arises from true contract, although no contract, express or implied, has in fact been entered into by them."

<sup>100</sup> Section 72 of the Contract Act, 1872

<sup>101</sup> Section 69 of the Contract Act, 1872

<sup>102</sup> Section 70 of the Contract Act, 1872

<sup>103</sup> Section 71 of the Contract Act, 1872

<sup>104</sup> Section 68 of the Contract Act, 1872

<sup>105</sup> Section 73 of the Contract Act, 1872

<sup>106</sup> *ibid*

<sup>107</sup> 1854 9Ex. 341

<sup>108</sup> Section 74 of the Indian Contract Act, 1872

<sup>109</sup> Section 75 of the Indian Contract Act, 1872