

MBA –III Semester,
MB 302, LEGAL ASPECTS OF BUSINESS

Unit: 1

Topic: Introduction to Indian Contract Act, 1872.

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THE INDIAN CONTRACT ACT, 1872

Nature and Application of the Act

The Law of Contract deals with agreements which can be enforced through courts of law and is the most important part of commercial law because every commercial transaction starts from an agreement between two or more parties. The main objective of the law of contract is to introduce definiteness in commercial and other transactions. This can be illustrated by the following example.

Example

X entered into a contract to deliver 10 tonnes of mustard oil to Y on a certain date. Since such a contract is enforceable by the courts, Y can plan his activities on the basis of getting the mustard oil on the fixed date. If X breaches the contract, Y will get damages from X and will not suffer any loss.

The Indian Contract Act, 1872 came into force on September 1, 1872 and is extended to the whole of India except to the State of Jammu and Kashmir. As discussed above, unlike other laws enforceable in the country, the law of contract does not lay down any rights and duties that it will enforce. It contains the limiting principles guiding the parties to create their own rights and duties which the law will uphold. The Act provides certain general rules regarding contracts and is not exhaustive. There are other Acts relating to particular types of contracts, e.g. the

Negotiable Instruments Act, Transfer of Property Act, etc. The Act does not affect any usage or custom of trade, or any incident of any contract not inconsistent with the provisions of the Act.

'Jus in Personam' Distinguished from Jus in Rem' under the Act

Jus in Personam is a Latin term which means right against a person that is the right to enforce a particular person's obligation by instituting an action against such person only. On the other hand *Jus in Rem* means the right against a thing at large. The law of contract creates *Jus in Personam* and not *Jus in Rem* which means that the rights protected by a valid contract are enforceable only against a person who is a party to the contract, not against the whole world. These two rights can be further distinguished with the help of the following illustrations.

Examples

- (a) Mr A owes an amount of Rs. 50,000 to Mr B. In this case Mr B has the right to recover this amount from Mr A only, and not from anybody else. This right is known as *Jus in Personam*.
- (b) Mr. A owns 30 acres of land. In this case Mr A has full liberty to enjoy the land against every member of the public. Likewise, every member of the public has an obligation that they should not disturb the right of Mr A over the stated land. This right of Mr A is known as *Jus in Rem*.

MEANING OF VALID CONTRACT UNDER THE ACT

Usually, a contract is an agreement between two or more persons to do a particular act or abstain from doing a particular act. When parties enter into a contract they

create legal obligation between themselves. It also provides certain rights to the parties to do a particular task. Different authors have defined “Contract” in various ways. Some important ones are discussed below:

1. Every agreement and promise enforceable at law is a contract. – SIR FREDERICK POLLOCK
2. A contract is an agreement, creating and defining the obligation between parties. - SALMOND
3. A contract is an agreement enforceable at law made between two or more persons by which rights are acquired by one or more to acts or forbearances on the part of others. - SIR WILLIAM ANSON

An analysis of these definitions reveals that an agreement is an offer and its acceptance. However, an agreement which can be enforced by law must have some essential elements. The definition of contract provided under the Act is closely linked to Pollock's definition explained above. Section 2(h) of the Act defines a contract thus:

"An agreement, enforceable by law is a contract."

From the above definitions we can understand that a contract essentially has two following elements:

1. An Agreement
2. Enforceability, or legal obligation

1. Agreement

Section 2(e) of the Act defines agreement as:

"Every promise and every set of promises forming the consideration for each other is an agreement."

From this definition it is clear that the promise means a proposal or offer which has been accepted. It can be further explained with the following example.

Example

Ram offers to sell his car to Shyam for 2,75,000. Shyam accepts this offer. Now this offer to sell and acceptance to purchase can be treated as an agreement between Ram and Shyam.

Number of parties: It is worth noticing here that for making a valid agreement, there has to be two parties- one party who makes an offer and the other party who accepts the offer made by the first party. That means that an agreement consists of an offer and acceptance, involving two separate parties. Thus.

Offer + Acceptance = Agreement

Consensus ad idem: Another important aspect of a valid agreement is consensus ad idem that is the identity of minds. Difference in opinion of two parties involved in forming an agreement will render the agreement void. Therefore, both parties must agree for the deal and there must be identity of minds in respect of the subject matter of the contract.

2. Enforceability, or Legal Obligation

To treat an agreement as a contract, the contract must give rise to legal obligation. If an agreement is not enforceable by law then it cannot be called a contract. There is no legal obligation for moral, religious or social agreements. That is why an agreement to go to watch a cricket match or eat dinner together will not lead to a

valid contract because such agreements do not create a duty enforceable by law. In such cases, the involved parties do not intend to create legal relation and this kind of agreement is just of social nature having no enforceability in the eyes of law.

On the other hand, all business agreements are created with an intention to create legal obligation with the parties who enter into that agreement. Agreement for buying a car for Rs. 2,75,000 is an agreement with legal obligation and can be enforced by law by meeting the essential conditions of the contract. So this kind of agreement will lead to a valid contract.

Thus it can be said that all obligations which are enforceable by law are not automatically regarded as contract. Therefore, only those obligations which arise out of an agreement are of concern to the law of contract.