



# All contracts are agreements but all agreements are not contracts

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As stated above, an agreement to become a contract must give rise to a legal obligation. If an agreement is incapable of creating a duty enforceable by law, it is not a contract. Thus an agreement is a wider term than a contract. Agreements of moral, religious or social nature e.g., a

promise to lunch together at a friend's house or to take a walk together are not contracts because they are not likely to create a duty enforceable by law for the simple reason that the parties never intended that they should be attended by legal consequences. On the other hand, legal agreements are contracts because they create legal relations between the parties.

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## EXAMPLE:

1. A invites B to dinner. B accepts this invitation but does not attend the dinner. A cannot sue B for damages. It is social agreement because it does not create legal obligation. So it is not a contract.

2. A promises to sell his car to B for one million. It is legal agreement because it creates legal obligations between the parties. So it is a contract. According to Section 10 of the Contract Act 1872, "All agreements are contracts if they are made by the free consent of the parties, competent to contract, for a lawful consideration and with a lawful object and not hereby declared to be void". Thus an agreement becomes a contract when at least the following conditions are satisfied: 1. Free consent 2. Competency of the parties

3. Lawful consideration

4. Lawful object. In a nut shell, an agreement is the basis of a contract and contract is the structure constructed on these basis. Thus we can say that for an agreement to change into a Contract as per the Act, it must give rise to or lead to legal obligations or in other words must be within the scope of the law. Thus we can summarize it as Contract = Accepted Proposal (Agreement) + Enforceable by law (defined within the law) Thus we can say that all contracts are agreements but all agreements are not contracts.

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The Indian Contract Act, 1872 also determines which promises and agreements are binding on the parties. And the contract will lead to the birth of some rights and duties for the parties to the transaction. Let us take a closer look at the rights available to parties under the contract act.

1. 'Right in Rem' or 'Jus in Rem' As per the law of India, every person entering into a contract has rights in rem. This is right available to him or her against the entire world. It protects a person's property from the entire world. This means that no other person can interfere with his right. This right in rem is available to every person i.e. available to all.

**For example:**

- Mr. X owns a house. This house exclusively belongs to him. He has right in rem with respect to the house. So nobody can interfere with his ownership of the house. No one can disturb his right in rem.
- Mr. Y has a suitcase full of cash. This money belongs to Mr. Y exclusively. The world or anyone in it cannot take away the money from him, .i.e. they cannot disturb his possession or interfere with his ownership of the money.

2. 'Right in Personam' or 'Jus in Personam' This is the opposite of right in rem. Right in personam gives the person right against one person or party to the contract. It generally will correspond with a duty imposed on the said person or party. The Indian Contract Act grants rights in personam to the parties of a

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contract. So the parties of a contract have these contractual rights only against each other, i.e. jus in personam.

**For example:**

- A sold his car to B. A has the right to receive the sale proceeds. This right to receive the money only belongs to A, so it is a right in personam. No other party is involved.
- B loaned money to C. The right to recover the money belongs only to B, not the world in general. Law of contract creates 'Jus In Personam' and not in 'Jus In Rem'.

**ESSENTIALS OF A VALID CONTRACT**

A contract that is not a valid contract will have many problems for the parties involved. It may lead to obstruction of businesses and unlawful and insincere dealings. For this reason, we must be fully aware of the various essentials so as to make a contract valid. The Indian Contract Act, 1872 itself defines and lists the Essentials of a Contract either directly or through interpretation through various judgments of the Indian judiciary. Section 10 of the Indian Contract Act, 1872 enumerates 5 points that are essential for valid contracts. "All agreements are contracts, if they are made –

- by free consent of the parties,
- competent to contract,
- for a lawful consideration and
- with a lawful object, and
- not hereby expressly declared to be void.” Other than these there are some other essentials for a valid contract.

**These can be explained as under:**

**1. Lawful Offer and Acceptance:** There must be at least two parties, one of them making the offer and the other accepting it. Such offer and acceptance must be valid. Valid means, it must conform to the rules laid down in the Indian Contract Act, 1872. For an agreement, there must be a lawful offer by one and lawful acceptance of that offer from the other party. The term lawful means that the offer and acceptance must satisfy the requirements of Contract Act. The

offer must be made with the intention of creating legal relations otherwise, there will be no agreement.

**Example:**

- A says to B that he will sell his cycle to him for Rs.2000. This is an offer. If B accepts this offer, there is an acceptance.
- A and B agree to go to a movie on coming Sunday. A does not turn in resulting in loss of B's time B cannot claim any damages from B since the agreement to watch a movie is a domestic agreement which does not result in a contract.

**2. Intention to Create Legal Relationship:** The parties to contract must intend to create legal relationship. In commercial or business agreements, it is assumed that the parties intend to create legal relationship unless otherwise agreed upon. An agreement which gives rise to a moral or social obligation is not a contract. The leading case on this point is *Balfour v/s. Balfour* (1919) A husband and wife were residents of Ceylon. They went to England on leave. At the end of time, the husband had to return alone as his wife could not accompany him due to illness. Mr. Balfour promised to send his wife an allowance of £ 30 per month, until she returned to Ceylon. He failed to pay the said amount.

The wife sued for the allowance. The court held that it was mere domestic agreement and parties did not intend to create any legal relations. In case of social agreement there is no intention to create legal relationship and there is no contract (Balfour v. Balfour) In case of commercial agreements, the law presumes that the parties had the intention to create legal relations. [An agreement of a purely domestic or social nature is not a contract] The parties that are subject to a contract must have clear intentions of creating a legal relationship between them.

What this means is, those agreements that are not enforceable by the law e.g. social or domestic agreements between relatives or neighbours are not enforceable in a court of law and thus any such agreement can't become a valid contract. It is presumed in commercial agreements that parties intend to create legal relations.

**Example:**

- A father promises to pay his son Rs.500 every month as pocket money. Later, he refuses to pay. The son cannot recover as it is a social agreement and does not create legal relations.
- A offers to sell his watch to B for Rs.200 and B agrees to buy it at the same price, there is a contract as it creates legal-relationship between them.

**3. Lawful Consideration:** The third essential of a valid contract is the presence of consideration. Consideration is quid pro-quo i.e., “something in return”. It may be some benefit to the party. Consideration has been defined as the price paid by one party for the promise of the other. An agreement is enforceable only when both the parties get something and give something. The something given or obtained is the price of the promise and is called consideration. An agreement must be supported by lawful consideration.

According to Pollock, “A consideration is the price paid for which promise of another is bought.” In Section 23 of the Act, the unlawful considerations are defined as all those which:

- it is forbidden by law.
- is of such a nature that, if permitted, it would defeat the provisions of any law; or is fraudulent.
- involves or implies, injury to the person or property of another
- the Court regards it as immoral or opposed to public policy These conditions will render the agreement illegal.

“An agreement without consideration is a void agreement under section 25 of ICA, 1872”

**Example:**

- A agrees to sell his house to B for Rs.10 Lac is the consideration for A's promise to sell the house, and A's promise to sell the house is the consideration for B's promise to pay Rs.10 lac. These are lawful considerations.

- A promise to obtain for B employment in the public service, and B promise to pay 10,000 rupees to A. the agreement is void, as the consideration for it is unlawful.

- Gratuitous promises are not enforceable a law.

**4. Capacity to Contract:** The parties of an agreement must be competent to contract, otherwise it cannot be enforced. No valid contract will come into existence. Section 11 of the Indian contract Act specifies that every person is competent to contract provided:

- is of the age of majority according to the law which he is subject,

- who is of sound mind and

- is not disqualified from contracting by any law to which he is subject. Lunatics, Idiots, Alien enemy, Convicts, Minors etc. are incompetent to contract. If one of the parties to the agreement suffers from minority, madness, drunkenness etc., the agreement is not enforceable at law, except in some cases. A contract with a person of unsound mind and with a minor is void-ab-initio (from the beginning).

### **Example:**

- A minor borrowed money from money lender and agreed to repay it within 90 days. This is not a valid contract as minor is not competent to contract.
- M, a person of unsound mind, enters into an agreement with S to sell his house for Rs.2 lac. It is not a valid contract because M is not competent to contract.
- A, aged 20 promises to sell his car to B for Rs.3 Lac. It is a valid contract because A is competent to contract.

**5. Free Consent Consent:** is crucial for an agreement and thus for a valid contract. If two people reach a similar agreement in the same sense, they are said to consent to the promise. Consent of the parties must be genuine. However, for a valid contract, we must have free consent which means that the two parties must have reached consent without either of them being influenced, coerced, misrepresented or tricked into it. In other words, we say that if the consent of either of the parties is vitiated knowingly or by mistake, the contract between the parties is no longer valid. It is another essential of a valid contract. Consent means that the parties must have agreed upon the same thing in the same sense. There should be consensus – ad – idem. For a valid contract it is necessary that the consent of parties to the contract must be free. An agreement should be made by the free consent of the parties.

According to section 14,

“Consent is said to be free when it is not caused by:

(i) Coercion- consent obtained by physical threat If the consent is obtained by any of these four factors, the contract will be voidable contract, at the option of the aggrieved party.

(ii) Undue influence – consent obtained by mental threat or psychological pressure

(iii) Fraud- consent obtained by intentionally deceiving the other

(iv) Misrepresentation- consent obtained by unintentionally deceiving the other. Innocent untrue statement, i.e. giving wrong statement without knowing that it is wrong. (v) Mistake- consent obtained by committing a mistake/error. If the agreement is induced by mutual mistake (if material), it would be void agreement

**Example:**

- A threatens to kill B if he does not sell his house to him. B agrees to sell. B's consent cannot be regarded as free.

- A compels B to enter into a contract on the point of pistol. It is not a valid contract as the consent of B is not free.

**6. Lawful object:** ‘Object’ means the basic purpose of entering into contract. The object or the purpose of the agreement must be lawful. According to section 23 of the Indian Contract Act, 1872, “The object is considered not lawful if:

- It is forbidden by law; or
  - It is of such nature that, if permitted, it would defeat the provisions of the law;
- or
- Is fraudulent; or
  - Involves or implies injury to the person or property of another; or
  - Is immoral or is opposed to public policy.” It is, therefore, necessary that agreement should be made for a lawful and legal object.

The object for which the agreement has been entered into must not be fraudulent, illegal, immoral, or opposed to public policy or must not imply injury to the person or property of another. Two persons cannot enter into an agreement to do a criminal act. Every agreement of which the object or consideration is unlawful is illegal and the therefore void.

**Example:**

- A promise to pay B Rs.5 thousand if B beats C. The agreement is illegal as its object is unlawful.
- A lets a flat to B (a smuggler), knowing that it would be used for immoral purposes. The agreement is void.

7. Agreement not Declared to be void An agreement must not be one of those, which have been expressly declared to be void by the Act. Certain agreements have been expressly declared illegal or void by the law.

Section 23 -30 explains certain types of agreement, which have been expressly declared to be void. Such expressly declared void agreements are stated as under:

- Unlawful agreement ( Section 23 and Section 24)
- Agreements without consideration (Section 25)
- Agreement in restraint to marriage (Section 26)
- Agreement in restraint of Trade (Section 27)
- Agreement in restraint of proceedings (Section 28)
- An uncertain agreement (Section 29)
- Wagering agreements (Section 30)
- Agreements to do impossible acts (Section 56) Example:
  - A promise to close his business against the promise of B to pay him Rs.2 lac is a void agreement because it is restraint of trade.

- A agreed to pay Rs. 50 lac to Y if Y does not marry throughout his life. Y accepted the offer. The agreement is void.

**8. Certainty of Meaning:** To be a contract, the agreement must not be vague or uncertain. It must have certain meaning. Otherwise it cannot be enforced. For a valid contract, the terms and conditions of an agreement must be clear and certain. According to Section 29 of the Contract Act, “Agreements the meaning of which are not certain or capable of being made certain are void.”

**Example:**

- A promised to sell 20 books to B. It is not clear which books A has promised to sell. The agreement is void because the terms are not clear.
- O agreed to purchase a van from S on hire-purchase terms. The price was to be paid over two years. Held there was no contract as the terms were not certain about rate of interest and mode of payment.
- A agrees to sell B a hundred tons of oil. It is not clear what the kind of oil is. The agreement is void because of its uncertainty.
- A agreed to sell cloth to B but it is not clear what kind of cloth and how much cloth is intended to be sold. The agreement is not valid.

- A agreed to pay Rs.5 lac to B for ultra-modern decoration of his drawing room. The agreement is void because the meaning of the term “ultra – modern” is not certain.

- I agree to pay Mr. X a desirable amount for his house at so and so location”. This is not a valid contract even if all the parties agree to this term as “desirable amount” is not well defined and has no certainty of meaning. Thus we say that a valid contract must have a certainty of meaning.

**9. Possibility of Performance:** According to section 56, “An agreement to do an impossible act is void.” The performance of an agreement or the terms of the agreement must be possible. If the act is legally or physically impossible to perform, the agreement cannot be enforced at law.

For example, X agrees with Y, to print currency notes by magic. The agreement is not enforceable. Example:

- A agrees with B to put life into B’s dead brother. The agreement is void as it is impossible of performance. The agreement is not valid.

- A agrees to B to discover treasure by magic. The agreement is void and hence not enforceable because the act in itself is impossible to be performed from the very beginning.

**10. Legal Formalities:** According to Contract Act, a contract may be oral or in writing. Although in practice, it is always in the interest of the parties that the contract should be made in writing so that it may be convenient to prove in the court. However, a verbal contract if proved in the court, will not be considered invalid, merely on the ground that it not in writing. Some of the common legal formalities are as follows:

- To be a contract, the agreement may be oral or in writing.
- If any legal formality is required, then it must comply with the necessary formalities as to writing, registration, stamping etc.
- Where a particular type of contract is required by law to be in writing and registered, it must comply with necessary formalities as to writing, registration and attestation. For example, An oral agreement for sale for immovable property is unenforceable because the law requires that such sale deeds must be in writing and registered
- If legal formalities are not carried out then the contract is not enforceable by law. Example: A promise to pay a time. Barred debt must be in writing
- It is essential for the validity of a contact that it must be in writing signed and attested by witness and registered if so required by the law.

**Example:**

1. A verbally promises to sell his book to Y for Rs.200. It is a valid contract because the law does not requires it to be in writing.

2. A verbally promises to sell his house to B. It is not a valid contract because the law requires that the contract of immovable property must be in writing.

**Disclaimer:** The article is based on the relevant provisions and as per the information existing at the time of the preparation. In no event, I shall be liable for any direct and indirect result from this article. this is only a knowledge sharing initiative.

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