

# Business Law

By: Harish Arora

This reference book can be useful for  
BBA, MBA, B.Com, BMS, M.Com, BCA, MCA  
and many more courses for Various Universities



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# Sample Preview of The Chapter

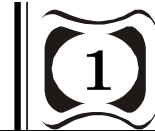
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# BUSINESS LAW



## Essentials of A Contract

### INTRODUCTION

The law of contract is very important for smooth functioning of business transactions and the law is also applicable to our everyday dealings with others. A contract is an agreement which is legally binding and it recognizes and governs the rights and duties of the parties. Law contains rules with regard to human conduct and actions which are enforceable in a court of law. The different branches of law include international law, constitutional law, criminal law, civil law, etc. Business law is an important branch of civil law and it deals with laws relating to business transactions. The chief sources of Indian business laws are English laws, Indian statute laws, past judicial decisions, local customs and usages. Law of contracts is the most important business law dealing with general rules relating to all types of contracts and covers special provisions about some specific contracts. Contract is an agreement which is enforceable by law and its two main elements are an agreement and its legal enforceability. Contracts can be classified according to its creation, execution and enforceability. An agreement not enforceable by law is void agreement. Void contract means an agreement which was valid when it was entered into but become void later on because of some reason. Voidable contract is a contract which can be avoided at the option of an aggrieved party and not the other. In an illegal agreement, the object or the consideration is unlawful; it is also void and not enforceable by law

### CHAPTER AT A GLANCE

#### WHAT IS LAW?

Laws ensure that our rights are not abused by others; it helps in regulating the conduct of people and

in safeguarding rights. Law is a rule of conduct developed by a government or society, applicable within certain geographical boundaries. Law regulates human actions in respect of one another and with society. Laws such as international law, constitutional law, criminal law, civil law, etc. are enacted for controlling and regulating the specific field of activity. Business law deals with customs and practices of local and international business.

#### MEANING AND SOURCES OF BUSINESS LAW

The business laws contain those laws which help in smooth conduct of business, including those concerning contracts, partnerships, companies, negotiable instruments, insurance, carriage of goods, arbitration, etc. Indian business law is based on the English law. The sources of Indian business laws are as under:

- *English Mercantile Laws* were developed by customs and usages of merchants in business dealings with others in England and Indian business laws are based on these laws.
- *Indian Statute Laws* include acts enacted by Indian Legislature and are the main source of Indian business law.
- *Judicial Decisions* are past decisions of courts which have guiding values. These are important source of law which is followed by courts at the time of deciding similar cases.
- *Customs and Usages* in trades also help in regulating dealings between the merchants of the trade. Indian Contract Act also recognizes that nothing contained therein shall affect any usage or custom of trade.

#### THE LAW OF CONTRACT

This law of contract is concerned with making of and enforcing agreements. It determines the circum-

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stances when a promise made by the parties to a contract shall be binding on them and also mentions the remedies available against parties which do not perform his promise. Indian Contract Act, 1872 deals with general principles of law governing contracts and the special provisions relating to bailment, pledge, indemnity, guarantee and agency.

**WHAT IS A CONTRACT?**

A contract is an agreement made between two or more persons to do or to abstain from doing a particular act. It creates a legal obligation giving legal rights to a certain person and the duty for the same is imposed on the other party. So, the elements of a contract are an agreement and its enforceability.

**Difference between an Agreement and a Contract**

Agreement	Contract
Offer and its acceptance	Agreement and its enforceability.
May/may not create a legal obligation	Necessary to create a legal obligation
Not a binding contract	Binds all the parties
Every agreement is not a contract	Every contract is an agreement

**CLASSIFICATION OF CONTRACTS**

Contracts can be classified:

**On the Basis of Creation:**

- *Express Contract* is one in which the terms are clearly stated in words or in writing.
- *Implied Contract* is not written/spoken. It arises from acts/conduct of parties. For example, while boarding a train, there is an implied contract that we agree to pay the fare.

**On the Basis of Execution:** On the basis of the extent to which these have been performed, contracts can be classified as:

- *Executed Contracts* is a contract in which both parties have fulfilled their respective obligations under the contract.
- *Executory Contracts* is a contract in which both the parties have still to perform their obligations. Contract may also be partly executed and partly executory, when only one of the parties has performed his obligation.

**On the Basis of Enforceability:** *Valid Contract* is one which satisfies all the conditions prescribed by law. When one or more such elements are missing, the contract is not a valid contract.

**Agreement:** According to Section 2(e) of the Contract Act an agreement is every promise and every set of promises forming the consideration for each other. A promise is an offer by one party which is accepted by another party.

**Legal Obligation:** It is important that the contract gives rise to a legal obligation. There is no legal obligation in social, moral or religious agreements, these not create a duty enforceable by law and hence, are not contracts. The law of contract is concerned with only those obligations which arise out of agreement. Obligations arising from wrongful acts, judicial decisions or decree of a court, husband and wife relationship do not come under the category of contracts.

*Void Contract* is a contract becomes void at the time when it ceases to be enforceable by law. It subsequently becomes unenforceable due to some reasons and treated void. It can be due to reasons such as impossibility of performance of the contract, change of law or some other reasons. Section 2(g) says that an agreement not enforceable by law is void and in case of void agreement, no contract comes into existence and it does not create any rights/obligation on any person. A void agreement is *void ab initio* (from the very beginning).

*Voidable Contract* is the agreement which is enforceable by law at the option of one or more parties, not at the option of the other and such a contract can be set aside at the option of the aggrieved party. Until the contract is set aside by a party who is entitled to do so, it remains a valid contract. When consent of a party was not free but it was obtained either by coercion, undue influence, misrepresentation or fraud. Such contract is voidable at the option of the party and when he sets the contract aside, other party is also freed from his obligation.

**Difference between Void and Voidable Contract:**

Void Contract	Voidable Contract
In a void contract no obligation or right arises or accrues to parties to the contract from a void contract. Such contracts are not covered by law.	A voidable contract continues at the option of one party; it is the desire of one party either to rescind it or continue; it is enforceable at the option of one party and is covered by law.
A void contract can give rise to no legal liability since transaction is nullity.	A voidable contract remains valid until rescinded.
A void contract cannot confer any right.	A voidable contract confers enforceable right till is not essential.
The contract becomes void when it ceases to be enforceable.	A contract becomes voidable only when consent to agreement is obtained by coercion, undue influence fraud or misrepresentation.

**Illegal or Unlawful Contract:** A contract cannot be illegal but agreement can be illegal or contrary to law. For example, an agreement to marry a minor is void but not illegal because the object is not unlawful.

An illegal agreement is such an agreement which is specifically declared to be unlawful under the Contract Act or is against the provisions of any other law. All illegal agreements are void but all void agreements are not necessarily illegal.

**Difference between Void Agreement and Illegal Agreement:**

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

**Unenforceable Contract** is one which is valid but cannot be enforced because of technical defect such as non-registration of agreement, non-payment of stamp fee, etc. Also, an agreement which the law requires to be in writing (e.g. agreement for arbitration) is unenforceable if it is oral. But if such defect is removed, the contract becomes enforceable.

**ESSENTIALS OF A VALID CONTRACT**

**According to Section 10:** All agreements are contracts if they are made by the free consent of the parties competent to contract, for a lawful consideration and with a lawful object, and are not hereby expressly declared to be void. So, following are elements of a valid contract:

**1. Proper Offer and Proper Acceptance:** There must be a maker of offer and its acceptor and other prescribed rules for making/accepting the offer must be satisfied while entering into an agreement. The offer must be unconditional, definite and duly communicated to the other party.

**2. Intention to Create Legal Relationship** has to be there among parties. In social/domestic agreements, such intention is not there. Business transactions presume intention of the parties to create legal relations which may be taken away by any express terms to the contrary.

**3. Free Consent** means that the parties have made the contract by their own free will, without any fear or pressure. Section 14 of the Act states that consent is said to be free when it is not caused by: (i) coercion (ii) undue influence (iii) fraud (iv) misrepresentation or (v) mistake. When the consent is obtained by (i) to (iv) above, the contract would be voidable at the option of aggrieved party. In case there is a material mutual mistake, the agreement becomes void.

**4. Capacity of Parties:** When any party is not competent to contract, the contract is not valid. Section 11 states that every person is competent to contract who is of the age of majority according to the law to which he is subject and who is of sound mind, and is not disqualified from contracting by any law to which

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he is subject. The parties must be major, of sound mind and not disqualified from entering into a contract by any.

**5. Lawful Consideration:** Consideration means a return that may or may not be monetary. For an agreement, there has to be a lawful consideration in an agreement, i.e. the price paid by one party to buy the promise of the other. Consideration may be an act or promise of doing something or for not doing. It may be past, present or future but it must be real and must have some value in the eyes of law, it need not be adequate.

**6. Lawful Object** means that the object of the agreement must be lawful and the act should not be prohibited by law. Both the consideration and the object of the agreement should be lawful.

**7. Agreement not Expressly Declared Void:** It is also required that the agreement must not have been expressly declared void under Sections 24 to 30 of the Contract Act.

**8. Certainty of Meaning:** As per Section 29 of the Contract Act, the agreements, the meaning of which is not certain or capable of being made certain, are void. So, it is important that the terms of a valid agreement must be clear and not vague/uncertain. It may still be valid if meaning of the agreement can be made certain from the prevailing circumstances.

**9. Possibility of Performance:** The act covered in the agreement should not be impossible. An agreement to do an act impossible in itself is void (Section 56).

**10. Legal Formalities:** The Contract Act specifies that certain agreements must be made in writing and some agreements must be registered. A promise to pay a time barred debt must be in writing. If it is not done, the contract is not legally enforceable.

All the above elements must be present in a valid contract. In case, any one is missing or absent, the agreement will not be enforceable by law.

**CHECK YOUR PROGRESS**

**Q. 1. What is Law?**

**Ans.** Law is a rule of conduct developed by a Government or society, applicable within certain geographical boundaries. Law regulates human actions in respect of one another and with society. With the changes in requirements, the laws are also changed. Laws keep us safe and ensure that our rights are not abused by other people. Law helps in the regulating the conduct of people and in safeguarding their property and rights. Therefore, every country has enacted laws

in this regard. Ignorance of law is not any excuse, so it is very important that we know proper laws, which we are subject to. When somebody eats in restaurant and does not pay, he cannot say that he was unaware of the laws pertaining to non-payment. There are different types of laws (international law, constitutional law, criminal law, civil law, etc.) for controlling and regulating one specific field of activity. Business law (or Mercantile or Commercial Law) is a part of civil law, which deals with customs and practices of local and international commerce.

**Q. 2. Define Contract.**

**Ans.** A contract is an agreement made between two or more persons to do or to abstain from doing a particular act. It creates a legal obligation giving legal rights to a certain person and the duty for the same is imposed on the other party. Sir Fredrick Pollock has defined a contract as 'Every agreement and promise enforceable at law is a contract'. The law of contract is contained in the Indian Contract Act which states that an agreement enforceable by law is a contract. So, the elements of a contract are an agreement which is enforceable by law.

**Q. 3. Define an agreement.**

**Ans.** According to Section 2(e) of the Contract Act an agreement is every promise and every set of promises forming the consideration for each other. A promise is an offer by one party which is accepted by another party. An agreement = Offer + Acceptance.

So, there must be at least two parties in a contract, the offerer and the acceptor. Further, it is also important that both the parties must agree on the same thing in the same sense (*Consensus-ad-idem*).

**Q. 4. What do you mean by legal obligation?**

**Ans.** The contract must give rise to a legal obligation. There is no legal obligation in social, moral or religious agreements, these not create a duty enforceable by law and hence, are not contracts. In business agreements, there is a presumption to create a legal relationship. An agreement to buy a particular house for Rs. one lac is a contract which gives rise to a legal obligation enforceable by law. When all the essentials of a valid contract are present in an agreement and if there is default by either party, then an action for breach of contract can be enforced through a court of law. The law of contract is concerned with only those obligations which arise out of agreement and those obligations which arise from sources such as wrongful acts, judicial decisions or decree of a court, husband and wife relationship are not contracts.