

CAPACITY TO CONTRACT

Meaning: Capacity refers to the competence of the parties to make a contract. It is one of the essential element to form a valid contract.

Who is competent to contract (Section 11)

“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 he is subject”.

Analysis of Section 11

This section deals with personal capacity of three types of individuals only. Every person is competent to contract who-

- (A) has attained the age of majority,
- (B) is of sound mind and
- (C) is not disqualified from contracting by any law to which he is subject.

(A) Age of Majority: In India, the age of majority is regulated by the Indian Majority Act, 1875.

Every person domiciled in India shall attain the age of majority on the completion of 18 years of age and not before. The age of majority being 18 years, a person less than that age even by a day would be minor for the purpose of contracting.

Law relating to Minor's agreement/Position of Minor

- 1) **A contract made with or by a minor is void ab-initio:** A minor is not competent to contract and any

agreement with or by a minor is void from the very beginning.

In the leading case of *Mohori Bibi vs. Dharmo Das Ghose (1903)*, “A, a minor borrowed ` 20,000 from B and as a security for the same executed a mortgage in his favour. He became a major a few months later and filed a suit for the declaration that the mortgage executed by him during his minority was void and should be cancelled. It was held that a mortgage by a minor was void and B was not entitled to repayment of money.

It is especially provided in Section 10 that a person who is incompetent to contract cannot make a contract within the meaning of the Act.

- 2) **No ratification after attaining majority:** A minor cannot ratify the agreement on attaining majority as the original agreement is void ab initio and a void agreement can never be ratified.

Example: X, a minor makes a promissory note in the name of Y. On attaining majority, he cannot ratify it and if he makes a new promissory note in place of old one, here the new promissory note which he executed after attaining majority is also void being without consideration.

- 3) **Minor can be a beneficiary or can take benefit out of a contract:** Though a minor is not competent to contract, nothing in the Contract Act prevents him from making the other party bound to the minor. Thus, a promissory note duly executed in favour of a minor is not void and can be sued upon by him, because he though incompetent to contract, may yet accept a benefit.

A minor cannot become partner in a partnership firm. However, he may with the consent of all the partners, be admitted to the benefits of partnership (Section 30 of the Indian Partnership Act, 1932).

Example: A mortgage was executed in favour of a minor. Held, he can get a decree for the enforcement of the mortgage.

- 4) **A minor can always plead minority:** A minor can always plead minority and is not stopped to do so even where he has taken any loan or entered into any contract by falsely representing that he was major. Rule of estoppel cannot be applied against a minor. It means he can be allowed to plea his minority in defence.
- 5) **Liability for necessities:** The case of necessities supplied to a minor or to any other person whom such minor is legally bound to support is governed by section 68 of the Indian Contract Act. A claim for necessities supplied to a minor is enforceable by law. But a minor is not liable for any price that he may promise and never for more than the value of the necessities. There is no personal liability of the minor, but only his property is liable.

To render minor's estate liable for necessities two conditions must be satisfied.

(i) The contract must be for the goods reasonably necessary for his support in the station in life.

(ii) The minor must not have already a sufficient supply of these necessities.

Necessaries mean those things that are essentially needed by a minor. They cannot include luxuries or costly or unnecessary articles. Necessaries extend to all such things as reasonable persons would supply to an infant in that class of society to which the infant belongs. Expenses on minor's education, on funeral ceremonies come within the scope of the word 'necessaries'.

The whole question turns upon the minor's status in life. Utility rather than ornament is the criterion.

- 6) **Contract by guardian - how far enforceable:** Though a minor's agreement is void, his guardian can, under certain circumstances enter into a valid contract on minor's behalf. Where the guardian makes a contract for the minor, which is within his competence and which is for the benefit of the minor, there will be valid contract which the minor can enforce.

But all contracts made by guardian on behalf of a minor are not valid. For instance, the guardian of a minor has no power to bind the minor by a contract for the purchase of immovable Property. But a contract entered into by a certified guardian (appointed by the Court) of a minor, with the sanction of the court for the sale of the minor's property, may be enforced by either party to the contract.

- 7) **No specific performance:** A minor's agreement being absolutely void, there can be no question of the specific performance of such an agreement.
- 8) **No insolvency:** A minor cannot be declared insolvent as he is incapable of contracting debts and dues are payable from the personal properties of minor and he is not personally liable.
- 9) **Partnership:** A minor being incompetent to contract cannot be a partner in a partnership firm, but under Section 30 of the Indian Partnership Act, he can be admitted to the benefits of partnership.
- 10) **Minor can be an agent:** A minor can act as an agent. But he will not be liable to his principal for his acts. A minor can draw, deliver and endorse negotiable instruments without himself being liable.
- 11) **Minor cannot bind parent or guardian:** In the absence of authority, express or implied, an infant is not capable of binding his parent or guardian, even for necessities. The parents will be held liable only when the child is acting as an agent for parents.
- 12) **Joint contract by minor and adult:** In such a case, the adult will be liable on the contract and not the minor. *In Sain Das vs. Ram Chand*, where there was a joint purchase by two purchasers, one of them was a minor, it was held that the vendor could enforce the contract against the major purchaser and not the minor.
- 13) **Surety for a minor:** In a contract of guarantee when an adult stands surety for a minor then he (adult) is liable to third party as there is direct contract between the surety and the third party.
- 14) **Minor as Shareholder:** A minor, being incompetent to contract cannot be a shareholder of the company. If by mistake he becomes a member, the company can rescind the transaction and remove his name from register. But, a minor may, acting through his lawful guardian become a shareholder by transfer or transmission of fully paid shares to him.
- 15) **Liability for torts:** A tort is a civil wrong. A minor is liable in tort unless the tort in reality is a breach of contract. Thus, where a minor borrowed a horse for riding only he was held liable when he lent the horse to one of his friends who jumped and killed the horse. Similarly, a minor was held liable for his failure to return certain instruments which he had hired and then passed on to a friend.

(B) Person of sound mind: According to section 12 of Indian Contract Act, "a person is said to be of sound mind for the purposes of making a contract if, at the time when he makes it is capable of understanding it and of forming a rational judgement as to its effect upon his interests."

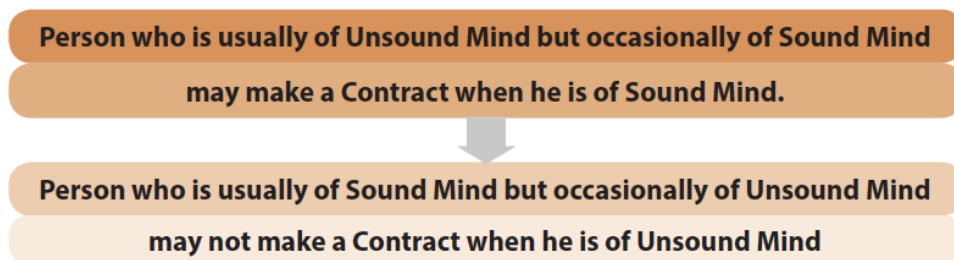
A person who is usually of unsound mind, but occasionally of sound mind, may make a contract when he is of sound mind.

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

Example 1: A patient in a lunatic asylum, who is at intervals, of sound mind, may contract during those intervals.

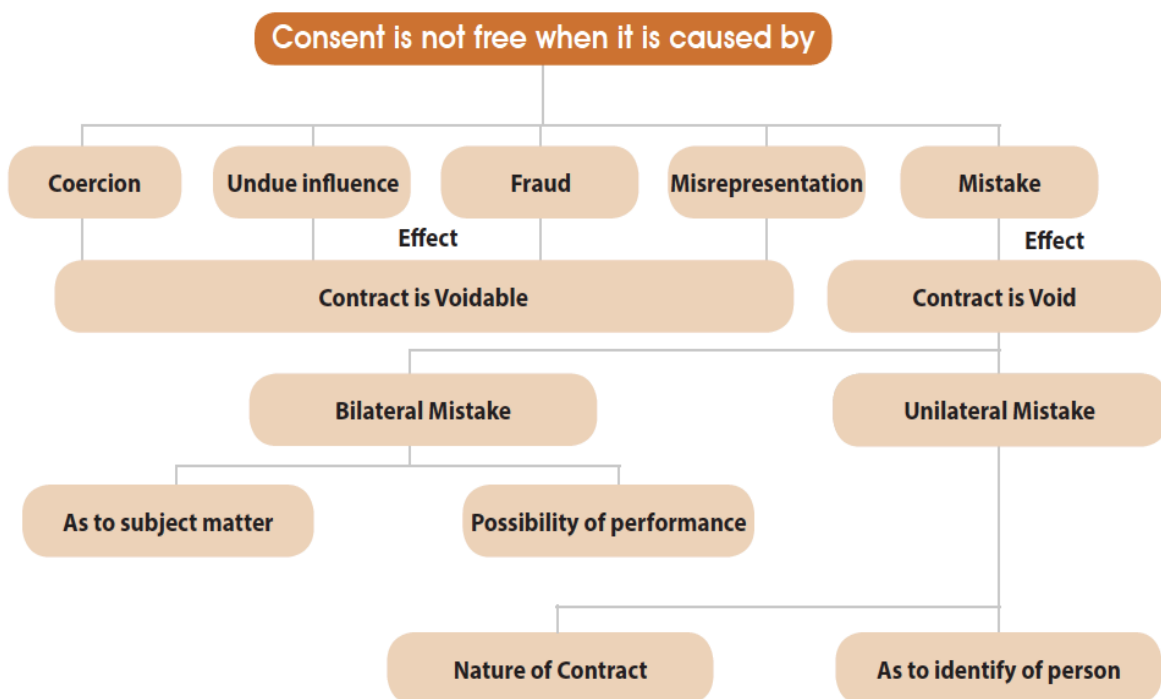
Example 2: A sane man, who is delirious from fever, or who is so drunk that he cannot understand the terms of a contract, or form a rational judgement as to its effect on his interests, cannot contract whilst such delirium or drunkenness lasts.

Position of unsound mind person making a contract: A contract by a person who is not of sound mind is void.



(B) Contract by disqualified persons: Besides minors and persons of unsound mind, there are also other persons who are disqualified from contracting, partially or wholly, so that the contracts by such person are void. Incompetency to contract may arise from political status, corporate status, legal status, etc. The following persons fall in this category: Foreign Sovereigns and Ambassadors, Alien enemy, Corporations, Convicts, Insolvent etc.

FREE CONSENT



“two or more persons are said to consent when they agree upon the same thing in the same sense.”

Parties are said to have consented when they not only agreed upon the same thing but also agreed upon that thing in the same sense. ‘Same thing’ must be understood as the whole content of the agreement. Consequently, when parties to a contract make some fundamental error as to the nature of the transaction, or as to the person dealt with or as to the subject-matter of the agreement, it cannot be said that they have agreed upon the same thing in the same sense. And if they do not agree in the same sense, there cannot be consent. A contract cannot arise in the absence of consent.

If two persons enter into an apparent contract concerning a particular person or ship, and it turns out that each of them, misled by similarity of name, had a different person or ship in his mind, no contract would exist between them as they were not *ad idem*, i.e., of the same mind. Again, ambiguity in the terms of an agreement, or an error as to the nature of any transaction or as to the subject-matter of any agreement may prevent the formation of any contract on the ground of absence of consent. In the case of fundamental error, there is really no consent whereas, in the case of mistake, there is no real consent.

As has been said already, one of the essential elements of a contract is consent and there cannot be a contract without consent. Consent may be free or not free. Only free consent is necessary for the validity of a contract.

Definition of ‘Free Consent’ (Section 14)

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

1. Coercion, as defined in Section 15; or
2. Undue Influence, as defined in Section 16; or
3. Fraud, as defined in Section 17; or
4. Misrepresentation, as defined in Section 18 or
5. Mistake, subject to the provisions of Sections 20, 21, and 22.

When consent to an agreement is caused by coercion, fraud, misrepresentation, or undue influence, the agreement is a contract voidable at the option of the party whose consent was so caused. When the consent is vitiated by mistake, the contract becomes void.

ELEMENTS VITIATING FREE CONSENT

We shall now explain these elements one by one.

(I) Coercion (Section 15)

“Coercion’ is 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 into an agreement.”

Analysis of Section 15

The section does not require that coercion must proceed from a party to the contract; nor is it necessary that subject of the coercion must be the other contracting party, it may be directed against any third person whatever. Following are the essential ingredients of coercion:

- (i) Committing or threatening to commit any act forbidden by the India Penal Code; or
- (ii) the unlawful detaining or threatening to detain any property to the prejudice of any person whatever,
- (iii) With the intention of causing any person to enter into an agreement.
- (iv) It is to be noted that is immaterial whether the India Penal Code is or is not in force at the place where the coercion is employed.

Effects of coercion under section 19 of Indian Contract Act, 1872

- (i) Contract induced by coercion is voidable at the option of the party whose consent was so obtained.
- (ii) As to the consequences of the rescission of voidable contract, the party rescinding a void contract should, if he has received any benefit, thereunder from the other party to the contract, restore such benefit so far as may be applicable, to the person from whom it was received.
- (iii) A person to whom money has been paid or anything delivered under coercion must repay or return it. (Section 71)

Example: Where husband obtained a release deed from his wife and son under a threat of committing suicide, the transaction was set aside on the ground of coercion, suicide being forbidden by the Indian Penal Code. The threat of suicide amounts to coercion within Section 15.

II Undue influence (Section 16)

According to section 16 of the Indian Contract Act, 1872, “A contract is said to be induced by ‘undue influence’ where the relations subsisting between the parties are such that one of the parties is in a position to dominate the will of the other and he uses that position to obtain an unfair advantage over the other”.

A person is deemed to be in position to dominate the will of another:

- (a) Where he holds a real or apparent authority over the other; or
- (b) Where he stands in a fiduciary relationship to the other; or
- (c) Where he makes a contract with a person whose mental capacity is temporarily or permanently affected by reason of age, illness or mental or bodily distress for example, an old illiterate person.

Example 1:

A having advanced money to his son, B, during his minority, upon B's coming of age obtains, by misuse of parental influence, a bond from B for a greater amount than the sum due in respect of the advance. A employs undue influence.

Example 2:

A, a man enfeebled by disease or age, is induced by B's influence over him as his medical attendant, to agree to pay B an unreasonable sum for his professional services. B employs undue influence.

Example 3:

A, being in debt to B, the money-lender of his village, contracts a fresh loan on terms which appear to be unconscionable. It lies on B to prove that the contract was not induced by undue influence.

Example 4:

A applies to a banker for a loan at a time when there is a stringency in money market. The banker declines to make the loan except at an unusually high rate of interest. A accepts the loan on these terms. This is a transaction in the ordinary course of business, and the contract is not induced by undue influence.

Analysis of Section 16

The essential ingredients under this provision are:

(1) *Relation between the parties:* A person can be influenced by the other when a near relation between the two exists.

(2) *Position to dominate the will:* Relation between the parties exist in such a manner that one of them is in a position to dominate the will of the other. A person is deemed to be in such position in the following circumstances:

(a) *Real and apparent authority:* Where a person holds a real authority over the other as in the case of master and servant, doctor and patient and etc.

Example: A father, by reason of his authority over the son can dominate the will of the son.

(b) *Fiduciary relationship:* Where relation of trust and confidence exists between the parties to a contract. Such type of relationship exists between father and son, solicitor and client, husband and wife, creditor and debtor, etc.

Example: By reason of fiduciary relationship, a solicitor can dominate the will of his client and a trustee can dominate the will of the beneficiary.

(c) Mental distress: An undue influence can be used against a person to get his consent on a contract where the mental capacity of the person is temporarily or permanently affected by the reason of mental or bodily distress, illness or of old age.

Example: A doctor is deemed to be in a position to dominate the will of his patient enfeebled by protracted illness.

(d) Unconscionable bargains: Where one of the parties to a contract is in a position to dominate the will of the other and the contract is apparently unconscionable i.e., unfair, it is presumed by law that consent must have been obtained by undue influence. Unconscionable bargains are witnessed mostly in money-lending transactions and in gifts.

Example: A youth of 18 years of age, spend thrift and a drunkard, borrowed Rs. 90,000 on a bond bearing compound interest at 2% per mensem (p.m.). It was held by the court that the transaction is unconscionable, the rate of interest charged being so exorbitant [*Kirpa Ram vs. Sami-Ud-din Ad. Khan (1903)*]

(3) The object must be to take undue advantage: Where the person is in a position to influence the will of the other in getting consent, must have the object to take advantage of the other.

(4) Burden of proof: The burden of proving the absence of the use of the dominant position to obtain the unfair advantage will lie on the party who is in a position to dominate the will of the other.

Power to set aside contract induced by undue influence- (Section 19A)

When consent to an agreement is caused by undue influence, the agreement is a contract voidable at the option of the party whose consent was so caused.

Any such contract may be set aside either absolutely or, if the party who was entitled to avoid it has received any benefit thereunder, upon such terms and conditions as to the Court may seem just.

Example 1:

A, a money lender advances Rs. 1,00,000 to B, an agriculturist, and by undue influence induces B to execute a bond for Rs. 2,00,000 with interest at 6 percent per month. The court may set aside the bond, ordering B to repay Rs. 1,00,000 with such interest as may seem just.

Case study: A student was induced by his teacher to sell his brand new car to the latter at less than the purchase price to secure more marks in the examination. Accordingly the car was sold. However, the father of the student persuaded him to sue his teacher. State on what ground the student can sue the teacher?

Yes, the student can sue his teacher on the ground of undue influence under the provisions of Indian Contract Act, 1872. A contract brought as a result of coercion, undue influence, fraud or misrepresentation would be voidable at the option of the person whose consent was caused.

(III) Fraud (Section 17)

Definition of Fraud under Section 17: 'Fraud' means and includes any of the following acts committed by a party to a contract, or with his connivance, or by his agent, with an intent to deceive another party thereto or his agent, or to induce him to enter into the contract:

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

Explanation to Section 17

Mere silence as to facts likely to affect the willingness of a person to enter into a contract is not fraud, unless the circumstances of the case are such that, regard being had to them, it is the duty of the person keeping silence to speak, or unless his silence is, in itself, equivalent to speech.

Example 1:

A sells, by auction, to B, a horse which A knows to be unsound, A says nothing to B about the unsoundness of the horse. This is not fraud by A.

Example 2:

B is A's daughter and has just come of age. Here, the relation between the parties would make it A's duty to tell B if the horse is unsound.

Example 3:

B says to A – "If you do not deny it, I shall assume that the horse is sound". A says nothing. Here A's silence is equivalent to speech.

Example 4:

A and B being traders, enter into a contract. A has private information of a change in prices which would affect B's willingness to proceed with the contract. A is not bound to inform B.

Analysis of Section 17

The following are the essential elements of the fraud:

- (1) There must be a representation or assertion and it must be false. However, silence may amount to fraud or an active concealment may amount to fraud.
- (2) The representation must be related to a fact.

(3) The representation should be made before the conclusion of the contract with the intention to induce the other party to act upon it.

(4) The representation or statement should be made with a knowledge of its falsity or without belief in its truth or recklessly not caring whether it is true or false.

(5) The other party must have been induced to act upon the representation or assertion.

(6) The other party must have relied upon the representation and must have been deceived.

(7) The other party acting on the representation must have consequently suffered a loss.

Effect of Fraud upon validity of a contract: When the consent to an agreement is caused by the fraud, the contract is voidable at option of the party defrauded and he has the following remedies:

(1) He can rescind the contract within a reasonable time.

(2) He can sue for damages.

(3) He can insist on the performance of the contract on the condition that he shall be put in the position in which he would have been had the representation made been true.

Mere silence is not fraud

A party to the contract is under no obligation to disclose the whole truth to the other party. 'Caveat Emptor' i.e. let the purchaser beware is the rule applicable to contracts. There is no duty to speak in such cases and silence does not amount to fraud. Similarly there is no duty to disclose facts which are within the knowledge of both the parties.

Example: H sold to W some pigs which were to his knowledge suffering from fever. The pigs were sold 'with all faults' and H did not disclose the fact of fever to W. Held there was no fraud. [*Word vs. Hobbs. (1878)*].

Silence is fraud:

1. **Duty of person to speak:** Where the circumstances of the case are such that it is the duty of the person

observing silence to speak. For example, in contracts of *uberrimae fidei* (contracts of utmost good faith).

Following contracts come within this category:

(a) Fiduciary Relationship: Here, the person in whom confidence is reposed is under a duty to act with utmost good faith and make full disclosure of all material facts concerning the agreement, known to him.

Example: A broker was asked to buy shares for client. He sold his own shares without disclosing this fact. The client was entitled to avoid the contract or affirm it with a right to claim secret profit made by broker on the transaction since the relationship between the broker and the client was relationship of utmost good faith. (*Regier V. Campbell Stuart*)

(b) Contracts of Insurance: In contracts of marine, fire and life insurance, there is an implied condition that full disclosure of material facts shall be made, otherwise the insurer is entitled to avoid the contract.

(c) Contracts of marriage: Every material fact must be disclosed by the parties to a contract of marriage (*Hazi Ahmed v. Abdul Gassi*).

(d) Contracts of family settlement: These contracts also require full disclosure of material facts within the knowledge of the parties.

(e) Share Allotment contracts: Persons issuing 'Prospectus' at the time of public issue of shares/ debentures by a joint stock company have to disclose all material facts within their knowledge.

2. Where the silence itself is equivalent to speech: For example, A says to B "If you do not deny it, I shall assume that the horse is sound." A says nothing. His silence amounts to speech.

In case of fraudulent silence, contracts is not voidable if the party whose consent was so obtained had the means of discovering the truth with ordinary diligence (Exception to section 19)

(IV) Misrepresentation (Section 18)

Misrepresentation means and includes -

- (1) the positive assertion, in a manner not warranted by the information of the person making it, of that which is not true, though he believes it to be true;
- (2) any breach of duty which, without an intent to deceive, gains an advantage to the person committing it, or any one claiming under him; by misleading another to his prejudice or to the prejudice of any one claiming under him;
- (3) causing, however, innocently, a party to an agreement to make a mistake as to the substance of the thing which is the subject of the agreement.

Analysis of Section 18

According to Section 18, there is misrepresentation:

- (1) statement of fact, which of false, would constitute misrepresentation if the maker believes it to be true but which is not justified by the information he possesses;
- (2) When there is a breach of duty by a person without any intention to deceive which brings an advantage to him;
- (3) When a party causes, even though done innocently, the other party to the agreement to make a mistake as to the subject matter.

Example 1:

A makes a positive statement to B that C will be made the director of a company. A makes the statement on information derived, not directly from C but from M. B applies for shares on the faith of the statement which turns out to be false. The statement amounts to

misrepresentation, because the information received second-hand did not warrant A to make the positive statement to B.

Example 2:

'A' believed the engine of his motor cycle to be in an excellent condition. 'A' without getting it checked in a workshop, told to 'B' that the motor cycle was in excellent condition. On this statement, 'B' bought the motor cycle, whose engine proved to be defective. Here, 'A's statement is misrepresentation as the statement turns out to be false.

Difference between Coercion and Undue influence:

Basis of difference	Coercion	Undue Influence
Nature of action	It involves the physical force or threat. The aggrieved party is compelled to make the contract against its will.	It involves moral or mental pressure.
Involvement of criminal action	It involves committing or threatening to commit an act forbidden by Indian Penal Code or detaining or threatening to detain property unlawfully.	No such illegal act is committed or a threat is given.
Relationship between parties	It is not necessary that there must be some sort of relationship between the parties.	Some sort of relationship between the parties is absolutely necessary.
Exercised by whom	Coercion need not proceed from the promisor nor need it be directed against the promisor. It can be used even by a stranger to the contract.	Undue influence is always exercised between parties to the contract.
Enforceability	The contract is voidable at the option of the party whose consent has been obtained by the coercion.	Where the consent is induced by undue influence, the contract is either voidable or the court may set it aside or enforce it in a modified form.
Position of benefits received	In case of coercion where the contract is rescinded by the aggrieved party, as per Section 64, any benefit received has to be restored back to the other party.	The court has the discretion to direct the aggrieved party to return the benefit in whole or in part or not to give any such directions.

Distinction between fraud and misrepresentation:

Basis of difference	Fraud	Misrepresentation
Intention	To deceive the other party by hiding the truth.	There is no such intention to deceive the other party.
Knowledge of truth	The person making the suggestion believes that the statement is untrue.	The person making the statement believes it to be true, although it is not true.
Rescission of the contract and claim for damages	The injured party can repudiate the contract and claim damages.	The injured party is entitled to repudiate the contract or sue for restitution but cannot claim the damages.
Means to discover the truth	The party using the fraudulent act cannot secure or protect himself by saying that the injured party had means to discover the truth.	Party can always plead that the injured party had the means to discover the truth.

Legal effects of agreements without free consent - (Section 19)

When consent to an agreement is caused by coercion, fraud or misrepresentation, the agreement is a contract voidable at the option of the party whose consent was so caused.

A party to contract, whose consent was so caused by fraud or misrepresentation may, if he thinks fit, insist that the contract shall be performed, and that he shall be put in the position in which he would have been if the representation made had been true.

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

Explanation to Section 19 - A fraud or misrepresentation which did not cause the consent to a contract of the party on whom such fraud was practiced, or to whom such misrepresentation was made, does not render a contract voidable.

Example: A, intending to deceive B, falsely represents that 500 maunds of indigo are made annually at A's factory, and thereby induces B to buy the factory. The contract is voidable at the option of B. This is because when consent to an agreement is caused by coercion, fraud or misrepresentation, the agreement is a contract voidable at the option of the party whose consent was so caused.

Analysis of Section 19

It has already been considered that when consent to an agreement is caused by coercion, undue influence, fraud or misrepresentation, though the agreement amounts to a contract, such a contract is voidable at the option of the party whose consent was so obtained. The party, however, may insist that the contract should be performed and that he should be put in the same position in which he would have been, if the representation made had been true.

But a person who had the means of discovering the truth with ordinary diligence cannot avoid a contract on the ground that his consent was caused by misrepresentation or silence amounting to fraud.

Example: A by a misrepresentation leads B to believe erroneously that 750 tons of sugar is produced per annum at the factory of A. B examines the accounts of the factory, which should have disclosed, if ordinary diligence had been exercised by B, that only 500 tons had been produced. Thereafter B purchases the factory. In the circumstance, B cannot repudiate the contract on the ground of A's misrepresentation.

Where a party to a contract commits fraud or misrepresentation, but the other party is not, in fact, misled by such fraud or misrepresentation, the contract cannot be avoided by the later. **(Explanation to Section 19).** Thus, when a seller of specific goods deliberately conceals a fault in order that the buyer may not discover it even if he inspects the goods but the buyer does not in fact, make any inspection, the buyer cannot avoid the contract, as he is not in fact deceived by the conduct of the seller.