

BUSINESS LAWS

B.COM(H) 1<sup>st</sup>

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FREE CONSENT



# Meaning of Free Consent

- Section 13 of Contract Act defines the term 'consent' and lays down that "Two or more persons are said to consent when they agree upon the same thing in the same sense."
- Consent is said to be 'free' when it is not caused by:
  1. Coercion, Section 15
  2. Undue Influence, Section 16
  3. Misrepresentation. Section 18
  4. Fraud, Section 17
  5. Mistake, Sections 20,21& 22

# COERCION

- “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.”

Ranganayakamma vs Alwar Setti

- Threat to file a law suit – Not coercion as it is not forbidden by IPC. But a threat to file suit on false charges constitutes coercion.
- Threat to commit suicide

# Effect of Coercion-

- Voidable contract at the option of the aggrieved party.
- Can rescind a variable contract or agree to it.
- If contract rescind – restore all benefits.
- The burden of proof lies on aggrieved party.

# UNDUE INFLUENCE

- A contract is said to be induced by undue influence where, (i) 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 (ii) he uses the position to obtain **an unfair advantage over the other**.
- A person is deemed to be in a position to dominate the will of another.
  - a) Where he holds a real or apparent authority over the other, e.g., the relationship between master and servant, police officer and accused; or
  - b) Where he stands in a fiduciary relation to the other. Father and son, guardian and ward, solicitor and client, doctor and patient, Guru (spiritual advisor) and disciple, trustee and beneficiary, etc.; 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, eg., old illiterate persons.

# Presumption of Undue Influence

- There is, however, no presumption of undue influence in the following cases:
  1. Husband and wife (in case of persons engaged to marry, presumption of undue influence will arise).
  2. Mother and daughter
  3. Grandson and grandfather
  4. Landlord and Tenant
  5. Creditor and debtor.

# Burden of proof and rebutting the presumption

- The burden of providing that the person who was in a position to dominate the will of another, did not use his position to obtain an unfair advantage, will lie upon the person who was in a position to dominate the will of the other.

# Effect of Undue Influence

- Voidable at the option of the aggrieved policy.
- Restoration of benefits- The court has the discerning onto direct the aggrieved party for refunding the benefits in whole or part or not at all.
- Unconscionable transaction- High rate of interest charged by money lender.



# Contracts with Pardanashin Women

- A women who remains completely secluded from the outsiders (outside her family) because of the custom of her community
- She can rescind the contract on the basis of undue influence.
- For proving the absence of undue influence the other party will have to prove that.
  - a) The terms of the contract were fully explained to her
  - b) She understood their implications
  - c) She freely consented to the contract

# Coercion Vs Undue Influence

<u>Basis</u>	<u>Coercion</u>	<u>Undue Influence</u>
Consent	Given by threatening	Given by dominating the will
Character	Physical Character	Mental pressure or moral pressure
Criminal Act	Involves criminal Act	No criminal act involved
Burden of Proof	Aggrieved party	Dominant Party
Restoration of Benefits	Entire restoration	Court may direct restoration in whole or part

# Misrepresentation

- Statement of fact made by one party to the other either before or at the time of contact, relating to some matter, essential to the contract.
- According to **Section 18** 'Misrepresentation' means and include:
  - a) 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; or
  - b) 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; or
  - c) 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.

- Thus, as per Section 18, there is misrepresentation in the following three cases:
- a) Positive assertion of unwarranted statements of material facts believing them to be true. If a person makes an explicit statement of fact not warranted by his information( i.e., without any reasonable ground), under an honest belief as to its truth though it is not true, there is misrepresentation. *Eg: A says to B who intends to purchase his land, “ My land produces 10 quintals of wheat per acre.” A, believes the statement to be true, although he did not have sufficient grounds for the belief. Later on, it transpires that the land produces only 7 quintals of wheat per acre. This is a misrepresentation.*
- b) Breach of duty which brings an advantage to the person committing it by misleading the other to his prejudice. This clause covers those cases where a statement when made was true but subsequently before it was acted upon, it became false to the knowledge of the person making it. In such a case, the person making the statement comes under an obligation to disclose the change in circumstances to the other party, otherwise he will be guilty of misrepresentation.

# Effects of Misrepresentation

- In case of misrepresentation, the aggrieved party has two alternative courses open to him-
  - i. He can rescind the contract, treating the contract as voidable; or
  - ii. He may affirm the contract and insist that he shall be put in the position in which he would have been if the representation made had been true (Sec 19).


# Fraud

- According to 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 intent to deceive or to induce another party thereto or his agent, to enter into the contract:
  1. The representation that a fact is true when it is not true by one who does not believe it to be true.

2. The active concealment of a fact by a person who has knowledge or belief of the fact- **Mere non-disclosure is not fraud**, where there is no duty to disclose.

**Caveat Emptor** or 'Buyer Beware' is the principle in all contracts of sale of goods. As a rule the seller is not bound to disclose to the buyer the faults in the goods he is selling.

Eg: A, a horse dealer, sells a mare to B. A knows that the mare has a cracked hoof which he fills up in such a way as to defy detection or on enquiry from B, A affirms that the mare is sound. The defect is subsequently discovered by B. There is 'fraud' on the part of A and the agreement can be avoided by B as his consent has been obtained by fraud.

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3. A promise made without any intention of performing it- If a man while entering into a contract has no intention to perform his promise, there is a fraud on his part.
  4. Any other act fitted to deceive-“ The fertility of man’s invention in devising new schemes of fraud is so great that it would be difficult, if not impossible to confine fraud within the limits of any exhaustive definition.



# Can Silence be Fraudulent?

- The explanation declares that “mere silence as to facts likely to affect the willingness of a person to enter into a contract is not fraud, unless:
  - i. The circumstances of the case are such that, regard being had to the, it is the duty of the person keeping silence to speak, or
  - ii. Silence is, in itself, equivalent to speech”

- **Silence is fraudulent, if the circumstances of the case are such that ‘ it is the duty of the person keeping silence to speak’.**
- When the parties stand in a fiduciary relation to each other, the person in whom confidence is reposed is under a duty to act with utmost good faith and to make a full disclosure of all material facts concerning the transaction known to him. Principle and agent, solicitor and client, guardian and ward, and trustee and beneficiary.
- Contracts of insurance
- Contract of marriage engagement
- Contracts of family settlements.
- Share allotment contracts
  
- **Silence is fraudulent where the circumstances are such that “silence is, in itself equivalent to speech.”**

# Effect of Fraud

1. He can rescind the contract i.e., he can avoid the performance of the contract; contract being voidable at his option; or
2. He can ask for restitution and 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.
3. The aggrieved party can also sue for damages, if any. Fraud is a 'civil wrong' hence compensation is payable.

# Special points

- For giving rise to an action for deceit, the following points deserve special attention:
- Fraudulent representation must have been instrumental in inducing the other party to enter into the contract i.e., but for this, this aggrieved party would not have entered into the contract.
- The plaintiff must have been actually deceived by fraudulent statement. A deceit which does not deceive gives no ground for action.
- The plaintiff must be thereby damnified. Unless the plaintiff has sustained a damage or injury, no action will lie.
- In cases of fraudulent silence, the contract is not voidable, if the party whose consent was so caused had the means of discovering the truth with ordinary diligence.

# Loss of Right of Rescission

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1. Affirmation
2. Restitution not possible
3. Lapse of time
4. Rights of third parties

# Mistake

- Mistake may be defined as an erroneous belief concerning something. It may be of two kinds:
  1. Mistake of law
  2. Mistake of fact

# Mistake of Law


- Mistake of law may be of two types:
  - a) Mistake of law of the country or Mistake of law: Every one is deemed to be conversant with the law of his country, and hence the maxim “ignorance of law is no excuse.” Mistake of law, therefore, is no excuse and it does not give right to the parties to avoid the contract.
  - b) Mistake of foreign law: Mistake of foreign law stands on the same footing as the ‘**mistake of fact**’. Here the agreement is void in case of ‘bilateral mistake’ only, as explained under the subsequent heading.

# Mistake of Fact

1. Bilateral mistake- Where parties to an agreement misunderstood each other and are at cross purposes, there is a bilateral mistake. Here there is no real correspondence of offer and acceptance, each party obviously understanding the contract in a different way. In case of bilateral mistake of essential fact, the agreement is *void-ab-initio*.

*Eg- Mistake as to existence of subject matter,  
mistake as to identity of the subject matter,  
mistake as to the title of subject matter,  
mistake as to the quantity or  
quality of subject matter.*





2. Unilateral Mistake- A contract is not voidable merely because it is caused by one of the parties to it being under a mistake as to a matter of fact. Accordingly, in case of unilateral mistake a contract remains valid unless the mistake is caused by misrepresentation or fraud.

However, in the following cases, where the consent is given by a party under a mistake which is so fundamental as goes to the root of the agreement and has the effect of nullifying consent.

# Agreement Void ab-initio

1. Mistake as to the identity of a person contracted with where such identity is important. **Said vs Butt.**

1. Mistake as to the nature and character of the written document

Eg- an old illiterate women executed a deed under the impression that she was executing a power of attorney authorising her nephew to manage her estate, while in fact it was a deed of gift in favour of her nephew. The evidence showed that women never intended to execute such a deed of gift nor was the deed read or explained to her. The document was held void.(Bala devi vs Santi Mazumdar)



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# INDEMNITY AND GUARANTEE

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# INDEMNITY

Definition: **SEC. 124-**

A contract by which one party promises to save or protect the other from loss, injury or financial burden caused to him, it is called a “Contract of Indemnity”.

**E. g.** A lost his share certificate. He applied for a duplicate certificate. The co. asked A to furnish an ‘indemnity bond’ in its favour to protect it against any claim that may be made by any person on original certificate.

# INDEMNITY

- TWO parties- Indemnity holder & Indemnifier

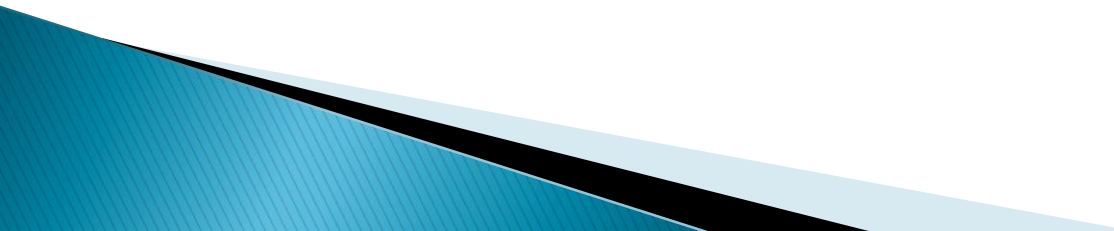
The person who promises to make good the loss is indemnifier (promisor) and the person whose loss is to be made good is called indemnified or indemnity-holder (promisee).

- A contract of indemnity must have all essential elements of a valid contract, it may be express or implied. For eg. When shares are transferred the transferee is impliedly bound to indemnify the transferor against future calls made before the registration of transfer.

- All insurance contracts are contracts of indemnity except life insurance.

# Rights of Indemnity Holder

For instance a vendor contracts to indemnify the vendee against the costs of litigation if title to the property is disturbed, and the vendee is sued by a rival owner, then the vendee, i.e., the indemnity-holder has the following rights:

- To claim damages which he may be compelled to pay in respect of suit
  - To claim costs in bringing or defending such suit
  - Other payments made for compromise authorised by the indemnifier
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# GUARANTEE

Definition: SEC. 126-

A “Contract of Guarantee” is a contract to perform the promise, or discharge the liability, of a third person in case of his default.

E.g. Guarantee for credit sales





# GUARANTEE

## Parties to guarantee

- ❖ **Surety**– Who gives Guarantee
- ❖ **Principal Debtor**– For whom guarantee is given
- ❖ **Creditor**– To whom guarantee is given

## No of Contracts

- ❖ Between principal debtor & creditor
  - ❖ Between creditor & surety
  - ❖ Between surety & principal debtor
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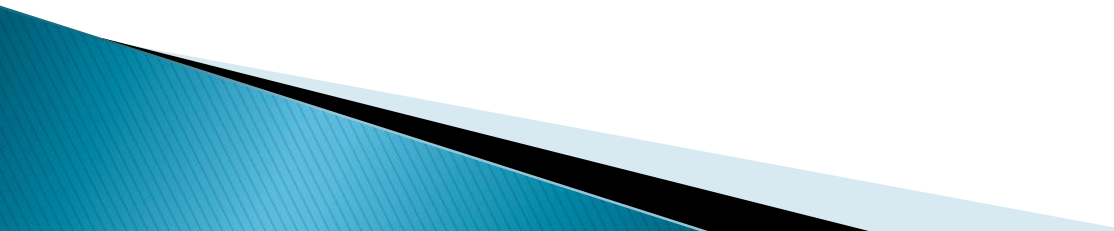
# Difference b/w Indemnity & Guarantee

Basis	Indemnity	Guarantee
Meaning	A contract by which one party promises to save the other from loss caused to him by the conduct of the <b>promisor himself</b> , or by the conduct of <b>any other person</b> , is called a "Contract of Indemnity".	A "Contract of Guarantee" is a contract to perform the promise, or discharge the liability, of a third person in case of his default.
Section	Sec 124	Sec 126
No. of Parties	Two-Indemnifier & indemnity holder	Three-creditor, principal debtor & surety
No. of Contracts	One-b/w Indemnifier & indemnity holder	Three- b/w creditor & principal debtor; creditor & surety; surety & principal debtor

# Difference b/w Indemnity & Guarantee

Basis	Indemnity	Guarantee
Nature of Liability	Primary	Secondary i.e. the surety is liable only on default of principal debtor
Object	Compensation of loss	Surety of Debt
Existence of Debt or duty	In most cases there is no existing debt or duty.	Existence of debt is necessary
Right to Sue	The indemnifier cannot sue the third party for loss caused in his own name.	Surety, after discharging the debt owing to the creditor can proceed against the principal debtor in his own right.

# Nature and Extent of Surety's Liability

- Sec 128 provides “the liability of the surety is co-extensive with that of the principal debtor, unless it is otherwise provided by the contract”. It can neither more nor less, although by a special contract it may be made less than that of principal debtor, but never greater.
1. The liability of the surety is **secondary**, i.e., the surety is liable only on default of principal debtor.
  2. The liability of surety arises immediately on default. If the contract is silent, the creditor may file a suit against the surety directly without suing the principal debtor.
  3. The surety will not be liable where the creditor has obtained guarantee by misrepresenting a material part of the transaction or by keeping silence.
  4. There is no such thing that surety will be liable only if principal debtor is liable. One may be liable while the other may not be.
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# Types of Guarantees


- ▶ **Ordinary or Specific guarantee** is given for a specific debt or transaction, it comes to an end as soon as the liability under that transaction ends.
- ▶ **Continuing guarantee** extends to a series of distinct and separable transactions. It is just like standing offer which is accepted by the creditor every time a subsequent transaction takes place.

**Revocation of continuing guarantee**



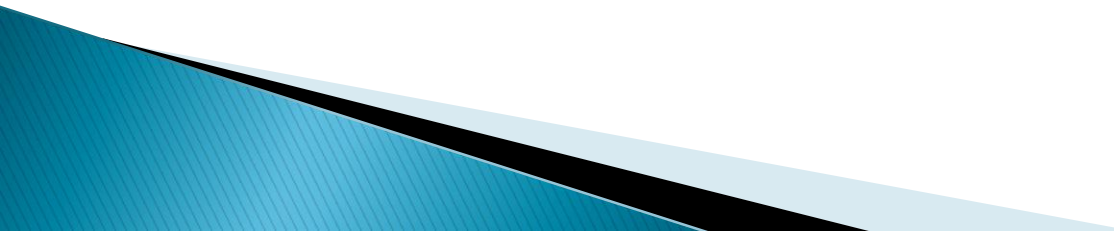
# RIGHTS OF SURETY

## Rights against the **principal debtor**

- Right of SUBROGATION (sec 140): Surety steps into the shoes of creditor after discharge of a liability and is entitled to all the remedies which the creditor could have enforced against the principal debtor.
  - Right to claim INDEMNITY (sec 145): there is an implied promise in every contract of guarantee to indemnify the surety by the principal debtor.
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# RIGHTS OF SURETY

## Rights against the Creditor

- ▶ **Right to benefit of creditor's securities (Sec 141):**  
For instance mortgage of property of principal debtor.
  - ▶ **Right to Claim set-off (if any) :** counter claims that principal debtor might possess against the creditor.
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# RIGHTS OF SURETY

## Right of contribution against **Co- Sureties**

- Where they are sureties for the same debt for **similar amount**. (equality of burden and benefit)
- Where they are sureties for the same debt but for **different sums** : Subject to the limit fixed by his guarantee, each surety is to contribute equally & not proportionately to the liability undertaken
- A:10000 B:20000 C: 40000 as a sureties of D
- Default of 30000: 10000 each
- Default of 40000: A-10000, B-15000, C-15000
- Default of 60000: A-10000, B-20000, C-30000



# DISCHARGE OF SURETY

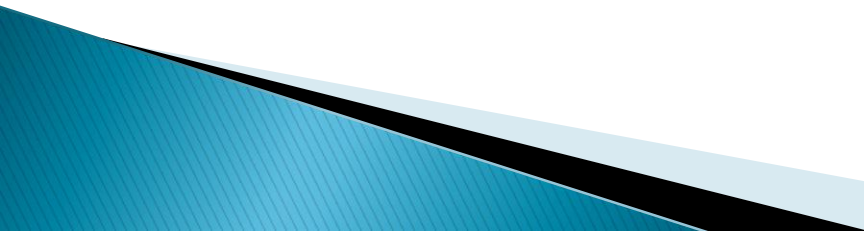
## ❑ **By Revocation**

➤ By notice

➤ By death of surety

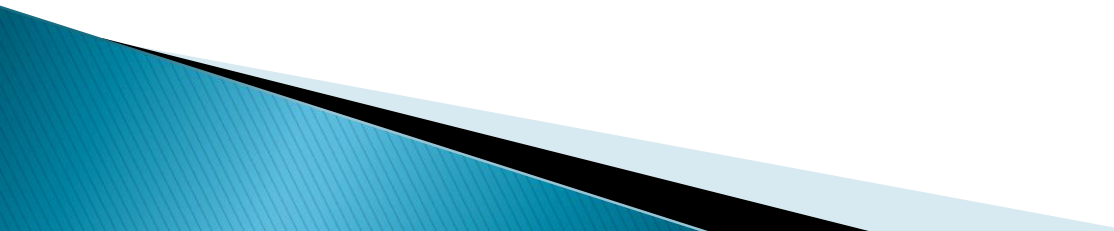
# DISCHARGE OF SURETY

## ❑ **By conduct of creditor-principal debtor**

- By variance in terms of the contract
  - Release or discharge of debtor
  - Arrangement by creditor with principal debtor without surety's consent. (sec 135)
  - By loss of security
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# DISCHARGE OF SURETY

## ❑ **By Invalidation of Contract of Guarantee**

- Guarantee obtained by misrepresentation
  - By concealment
  - Failure of Consideration
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