**CHAPTER 4**

**Consideration (continue)**

**Doctrine of Privity of Contract**

The Indian Contract Act clearly states that there cannot be a stranger to a contract. What does this exactly mean? And are there any [exceptions](https://www.toppr.com/guides/fundamentals-of-economics-and-management/supply/exceptions-of-law-of-supply/)? This is explained through the Doctrine of Privity of a Contract. Let us see.

**Doctrine of Privity of Contract**

The Indian Contract Act. 1872, allows the ‘[Consideration](https://www.toppr.com/guides/business-laws/indian-contract-act-1872-part-i/legal-rules-regarding-consideration/)‘ for an [agreement](https://www.toppr.com/guides/business-laws-cs/indian-contract-act-1872/agreement-with-minor/) to proceed from a third-party. However, a stranger (third-party) to consideration is different from a stranger to a contract. The law does not allow a stranger to file a suit on the contract. This right is available only to a person who is a party to the contract and is called Doctrine of Privity of Contract.

Let’s understand this with the help of an example:

* Peter has borrowed some [money](https://www.toppr.com/guides/economics/money-and-credit/all-about-money-and-credit/) from John.
* Peter owns a property and decides to sell it to Arjun.
* Arjun promises to pay John on behalf of Peter.

However, if Arjun fails to pay, then John cannot sue since Arjun is a stranger to the contract. It is important to note that the Doctrine of Privity has exceptions which allow a stranger to enforce a claim as given below.



**Exceptions to the Doctrine of Privity of Contract**

A stranger or a person who is not a party to a contract can sue on a contract in the following cases:

1. Trust
2. Family Settlement
3. Assignment of a Contract
4. Acknowledgement or Estoppel
5. A covenant running with the [land](https://www.toppr.com/guides/economics/indian-economy-1950-1990/land-reforms/)
6. Contract through an [agent](https://www.toppr.com/guides/business-laws-cs/indian-contract-act-1872/rights-and-duties-of-agents/)

Let’s look at each of them in details:

**Trust**

If a contract is made between the trustee of a trust and another party, then the beneficiary of the trust can sue by enforcing his right under the trust, even if he is a stranger to the contract.

Arjun’s father had an illegitimate son, Ravi. Before he died, he put Arjun in [possession](https://www.toppr.com/guides/legal-aptitude/jurisprudence/kind-of-possessions/) of his estate with a [condition](https://www.toppr.com/guides/business-laws/the-sale-of-goods-act-1930/concept-of-condition-and-warranty/) that Arjun would pay Ravi an amount of Rs 500,000 and transfer half of the estate in Ravi’s name, once he becomes 21 years old.

After attaining that age when Ravi didn’t receive the money and asked Arjun about it, he denied giving him his share. Ravi filed a suit for recovery. The Court held that a trust was formed with Ravi as the beneficiary for a certain amount and share of the estate. Hence, Ravi had the right to sue upon the contract between Arjun and his [father](https://www.toppr.com/guides/essays/essay-on-my-father/), even though he was not a party to it.

**Family Settlement**

If a contract is made under a family arrangement to benefit a stranger (person not a party to the contract), then the stranger can sue in his own right as a beneficiary of the contract.

Peter promised Nancy’s father that he would marry Nancy else would pay Rs 50,000 as damages. Eventually, he married someone else, thereby breaching the contract. Nancy filed a case against Peter which was held by the Court since the contract was a family arrangement with Nancy as the beneficiary.

Ritika was living in a Hindu Undivided Family (HUF). The family had made a provision for her marriage. Eventually, the family went through a partition and Ritika filed a suit to claim her marriage expenses. The Court held the case because Ritika was the beneficiary of the provision despite being a stranger to the contract.

[What is a Contract?](https://www.toppr.com/guides/business-laws/indian-contract-act-1872-part-i/what-is-a-contract/)

**Assignment of a Contract**

If a contract is made for the benefit of a person, then he can sue upon the contract even though he is not a party to the agreement. It is important to note here that nominees of a life [insurance](https://www.toppr.com/guides/general-awareness/capital-markets/insurance-industry-in-india/) policy do not have this right.

**Acknowledgment or Estoppel**

If a contract requires that a party pays a certain amount to a third-party and he/she acknowledges it, then it becomes a binding obligation for the party to pay the third-party. The acknowledgment can also be implied.

Peter gives Rs 1,000 to John to pay Arjun. John acknowledges the receipt of funds to be paid to Arjun. However, he fails to pay him. Arjun can sue John for recovery of the amount.

Rita sold her house to Seema. A real estate broker, Pankaj, facilitated the deal. Out of the sale price, Pankaj was to be paid Rs 25,000 as his professional charges. Seema promised to pay Pankaj the amount before taking possession of the property. She made three payments of Rs 5,000 each and then stopped paying him. Pankaj filed a suit against Seema which was held by the Court because Seema had acknowledged her liability by conduct.

**A Covenant Running with the Land**

When a person purchases a piece of land with the notice that the owner of the land will be bound by all duties and liabilities affecting the land, then he can sue upon a contract between the previous land-owner and a settler even if he was not a party to the contract.

Peter owned a piece of land which he sold to John under a covenant that a certain part of the land will be maintained as a public park. John abided by the covenant and eventually sold the land to Arjun. Though Arjun was aware of the covenant, he built a house in the specific plot. When Peter came to know of it, he filed a suit against Arjun. Although Arjun denied liability since he was not a party to the contract, the Court held him responsible for violating the covenant.

Contract through an Agent

If a person enters into a contract through an agent, where the agent acts within the scope of his authority and in the name of the person (principal).

**Solved Example for You**

Q1. Vidya purchases a property from Krishna. Rajiv is already living in the property on a three-year lease. As a part of the purchase agreement, Vidya takes over the lease. There are some leakages in the house that Krishna promises to fix, as a part of the contract. A few months go by and the leakages are still not fixed. Rajiv calls Vidya, the new owner, and she says that it is Krishna’s responsibility. Can Rajiv file a suit for repairs against Krishna?

Ans.

Since there is no contract between Rajiv and Krishna about repairing the leakage, if he files a suit, it will probably be dismissed by the Court. Krishna had agreed to carry out the repairs in his purchase contract with Vidya. Hence, she can file a suit against Krishna to get the work done.

Rajiv, on the other hand, can sue Vidya for not performing her obligations according to the lease contract.

**Agreements without Consideration**

Consideration is an [integral](https://www.toppr.com/guides/maths/integrals/some-properties-of-definite-integrals/) part of a [contract](https://www.toppr.com/guides/business-laws/indian-contract-act-1872-part-i/what-is-a-contract/). The rules of consideration state that it is essential to have consideration for a contract. But there are some specific exceptions to the “No consideration no contract” rule. Let us take a look.

**Consideration**

Can you make a legal agreement without consideration? No. As per Section 10 and Section 25 of the Indian Contract Act, 1872, [consideration](https://www.toppr.com/guides/business-laws/indian-contract-act-1872-part-i/legal-rules-regarding-consideration/) is essential in a valid contract. In simple [words](https://www.toppr.com/guides/english/vocabulary/words/), no consideration no contract. Hence, you can enforce a contract only if there is a consideration.

While considerations are integral to a contract, the Indian Contract Act, 1872 has listed some [exceptions](https://www.toppr.com/guides/fundamentals-of-economics-and-management/supply/exceptions-of-law-of-supply/) whereby an [agreement](https://www.toppr.com/guides/business-laws-cs/indian-contract-act-1872/agreement-with-minor/) made without consideration will not be void.

**Exceptions to the ‘No Consideration No Contract’ Rule**

Section 25 also lists the exceptions under which the rule of no consideration no contract does not hold, as follows:

**Natural Love and Affection**

If an agreement is in writing and registered between two parties in close [relation](https://www.toppr.com/guides/%2Bmaths/relations-and-functions/relations/) (like blood relatives or spouse), based on natural love and affection, then such an agreement is enforceable even without consideration.

*Example, Peter and John are brothers. In his will, their father nominates Peter as the sole owner of his entire property after his death. John files a case against Peter to claim his right to the property but loses the case. Peter and John come to a mutual decision where Peter agrees to give half of the property to his brother and register a document regarding the same.*

*Eventually, Peter didn’t fulfil his promise and John filed a suit for recovery of his share in the property. The Court held that since the agreement was made based on natural love and affection, the no consideration no contract rule didn’t apply and John had the right to recover his*[*share*](https://www.toppr.com/guides/business-laws/companies-act-2013/types-of-shares/)*.*

**Past Voluntary Services**

If a person has done a voluntary service in the past and the beneficiary promises to pay at a later date, then the contract is binding provided:

* The service was rendered voluntarily in the past
* It was rendered to the promisor
* The promisor was in existence when the voluntary service was done (especially important when the promisor is an [organization](https://www.toppr.com/guides/business-management-entrepreneurship/organizing/structure-of-organization/))
* The promisor showed his willingness to compensate the voluntary [service](https://www.toppr.com/guides/business-studies/business-services/nature-and-types-of-services/)

*Example, Peter finds Johns wallet on the road and returns it to him. John is happy to find his lost wallet and promises to pay Peter Rs 2,000. In this case, too, the no consideration no contract rule does not apply. This contract is a valid contract.*

**Promise to pay a Time-Barred Debt**

If a person makes a promise in writing signed by him or his authorized agent about paying a time-barred debt, then it is valid despite there being no consideration. The promise can be made to pay the debt wholly or in part.

*Example, Peter owes Rs 100,000 to John. He had borrowed the money 5 years ago. However, he never paid a single rupee back. He signs a written promise to pay Rs 50,000 to John as a final settlement of the loan. In this case, ‘the no consideration no contract’ rule does not apply either. This is a valid contract.*

**Creation of an Agency**

According to section 185 of the Indian Contract Act, 1872, no consideration is necessary to create an agency.

**Gifts**

The rule of no consideration no contract does not apply to gifts. Explanation (1) to Section 25 of the Indian Contract Act, 1872 states that the rule of an agreement without consideration being void does not apply to gifts made by a donor and accepted by a donee.

**Bailment**

Section 148 of the Indian Contract Act, 1872, defines bailment as the delivery of goods from one person to another for some purpose. This delivery is made upon a contract that post accomplishment of the purpose, the goods will either be returned or disposed of, according to the directions of the person delivering them. No consideration is required to effect a contract of bailment.

**Charity**

If a person undertakes a liability on the promise of another to contribute to charity, then the contract is valid. In this case, the no consideration no contract rule does not apply.

*Example, Peter is the trustee of his town’s charity organization. He wants to build a small pond in the town to enhance greenery and offer the residents a good place to walk around in the evenings. He raises a charity fund where he appeals to people to come ahead and contribute to the cause. Many people come forward as subscribers the fund and agree to pay Peter their share of the amount once he enters into a contract for constructing the pond.*

*After raising half the amount, Peter hires contractors for building the pond. However, 10 people back out at the last moment. Peter files a suit against them for recovery. The Court ordered the 10 people to pay the amount to Peter since he had undertaken a liability based on their promise to pay. Even though there was no consideration, the contract was valid and enforceable by law.*

**Solved Example on ‘No Consideration No Contract’ rule**

Q: On the eve of his marriage Rahul’s father gifted him a house. They went to register the documents, but such agreement was rejected as there was no consideration. Is this correct? Or can Rahul take legal action?

Ans: The rule of no consideration no contract does not apply to gifts. Also. Rahul’s father was gifting him the house of his natural love and affection. So this is an exception and the agreement can be registered even without consideration.

 **CHAPTER 5**

**Capacity to Contract**

One of the most essential elements of a valid contract is the competence of the parties to make a [contract](https://www.toppr.com/guides/business-laws/indian-contract-act-1872-part-i/what-is-a-contract/). Section 11 of the [Indian Contract Act, 1872](https://www.toppr.com/guides/business-laws/indian-contract-act-1872-part-i/), defines the capacity to contract of a person to be dependent on three aspects; attaining the age of majority, being of sound mind, and not disqualified from entering into a contract by any law that he is subject to. In this [article](https://www.toppr.com/guides/english/articles/introduction-to-articles/), we will look at all [aspects](https://www.toppr.com/guides/accountancy/accounting-for-partnership/special-aspects-partnership-accounts-its-maintenance/) in a detailed manner.

**Capacity to Contract**

According to 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.*”

**So, we have three main aspects:**

1. Attaining the age of majority
2. Being of sound mind
3. Not disqualified from entering into a contract by any [law](https://www.toppr.com/guides/business-law-cs/introduction-to-law/various-definitions-of-law/) that he is subject to

**1] Attaining the Age of Majority**

According to the Indian Majority Act, 1875, the age of majority in [India](https://www.toppr.com/guides/geography/our-country-india/india-our-country/) is defined as 18 years. For the purpose of entering into a contract, even a day less than this age disqualifies the person from being a party to the contract. Any person, domiciled in India, who has not attained the age of 18 years is termed as a minor.

Let’s look at certain laws governing a minor’s agreement:

**A Contract made with a Minor is Void**

Since any person less than 18 years of age does not have the capacity to contract, any agreement made with a minor is void ab-initio (from the beginning).

*Example, Peter is 17 years and 6 months old. He needs some money to go on vacation with his*[*friends*](https://www.toppr.com/guides/essays/essay-on-friendship/)*. He approached a moneylender and borrows Rs 25,000. As security, he signs some papers mortgaging his laptop and motorcycle. Six months later, when he attains the age of majority, he files a suit declaring that the mortgage executed by him when he was a minor is void and should be cancelled. The Court agrees and relieves Peter of all*[*liability*](https://www.toppr.com/guides/accounting-and-auditing/preparation-of-final-accounts-of-sole-proprietor/classification-of-assets-and-liabilities/)*to repay the*[*loan*](https://www.toppr.com/guides/general-awareness/banks/loans/)*.*

Also, if a minor enters into a contract, then he cannot ratify it even after he attains majority since the contract is void ab-initio. And, a void [agreement](https://www.toppr.com/guides/business-laws-cs/indian-contract-act-1872/agreement-with-minor/) cannot be ratified.

**A Minor can be a Beneficiary of a Contract**

While a minor cannot enter a contract, he can be the beneficiary of one. Section 30 of the [Indian Partnership Act, 1932](https://www.toppr.com/guides/business-laws/the-indian-partnership-act/), also specifies that while a minor cannot become a partner in the [partnership firm](https://www.toppr.com/guides/business-studies/forms-of-business-organisations/partnership/), the benefits of the firm can be extended to him.

*Example, Peter lends some money to his neighbour, John and asks him to mortgage his house as security. John agrees and the mortgage deed is made favouring Peter’s 10-year-old son – Oliver. John fails to repay the loan and Peter, as the natural guardian of Oliver, files a suit against John to recover his money. The Court holds the case since a minor can be a beneficiary of a contract.*

A Minor is always given the Benefit of being a Minor

Even if a minor falsely represents himself as a major and takes a loan or enters into a contract, he can plead minority. The rule of estoppel cannot be applied against a minor. He can plea his minority in defence.

**Contract by Guardian**

Under certain circumstances, a guardian of a minor can enter into a valid contract on behalf of the minor. Such a contract, which the guardian enters into, for the benefit of the minor, can also be enforced by the minor.

However, guardians cannot bind a minor by a contract for buying immovable property. But, a contract entered into by a certified guardian of a minor, appointed by the Court, with approval from the Court for the sale of a minor’s property can be enforced.

**Insolvency**

A minor cannot be declared insolvent as he cannot avail [debts](https://www.toppr.com/guides/economics/government-budget-and-the-economy/debt/). Also, if some dues are pending from the properties of the minor and he is not personally liable for the same.

**Joint contract by a Minor and an Adult**

In case of a joint contract between an adult and a minor, executed by the guardian on behalf of the minor, the [liability](https://www.toppr.com/guides/accounting-and-auditing/preparation-of-final-accounts-of-sole-proprietor/classification-of-assets-and-liabilities/) of the contract falls on the adult.

**2] Person of Sound Mind**

According to Section 12 of the Indian Contract Act, 1872, for the purpose of entering into a contract, a person is said to be of sound mind if he is capable of understanding the contract and being able to assess its effects upon his interests.

It is important to note that a person who is usually of an unsound mind, but occasionally of a sound mind, can enter a contract when he is of sound mind. No person can enter a contract when he is of unsound mind, even if he is so temporarily. A contract made by a person of an unsound mind is void.

**3] Disqualified Persons**

Apart from minors and people with unsound minds, there are other people who cannot enter into a contract. i.e. do not have the capacity to contract. The reasons for disqualification can include, political status, legal status, etc. Some such persons are foreign sovereigns and ambassadors, alien enemy, convicts, insolvents, etc.

**Solved Question on Capacity to Contract**

Q1. Rajiv has been in the lunatic asylum for 10 years. The doctors say that he is improving and there are times when he communicates and behaves like a normal person. Also, he is 25 years old. Does Rajiv have the capacity to contract?

Ans: Rajiv has attained the age of majority. Also, the doctors state that he is of a sound mind for intervals of time. Hence, he can enter into a contract during the period when his mind is sound, i.e when he has the capacity to contract.

**CONTRACT OF PERSONS OF UNSOUND MIND**

            According to Section 11 of the Indian Contract Act 1872, Persons of unsound mind are not competent to Contract.

Unsound Mind

     Section 12 of the Indian Contract Act 1872, "a person is said to be of sound mind for the propose of making a contract, if, at the time when he makes it, he is capable of understanding it and of forming a rational judgment as to its effect upon his interest.

**Contracts of persons of unsound Mind**

**1) Lunatics:**

          A lunatic is a person who is mentally deranged due to some mental strain or other personal experience. He suffers from intermittent intervals of sanity and insanity. He can enter into a contract during the period when he is of sound mind. In India a Lunatic's Contract is void.

2) Idiots:

          An idiot is a person who has completely lost his mental power. He does not exhibit an understanding of even ordinary matters. Idiocy is permanent whereas lunacy denotes periodical insanity with lucid intervals. An agreement of an idiot, like that of a minor and it is void.

 **3) Drunken or intoxicated persons:**

          A drunken person who suffer from temporary in capacity to contract. for example: at the time when he is so drunk that he is incapable of forming a rational judgment. The position of a drunken person is similar to that of a lunatic.

         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.

**Persons who are Disqualified by Law from Entering into a Contract in India**

Persons who are disqualified by law from entering into a contract are given below:

**Persons**

**1. Alien enemy:**

All persons other than Indian citizens are aliens. When the sovereign or the state of that alien is at peace with India, he is an alien friend. Contrary to it, he will be an alien enemy.

An alien friend living in India has full contracting competency subject to certain restrictions, which may be imposed by the Government of India, e.g., an alien cannot acquire any ownership interest in Indian shipping.

In case of outbreak of war between India and the alien country, the following rules apply for the performance of agreements:-

No contract can be made with an alien enemy during the subsistence of war, except with the prior approval of the Government of India.

Performance of the contracts made before the outbreak of war will be suspended during the course of war. They can be performed only when the war is over. Even then, the government can put restrictions on the performance of such contracts, if it considers them necessary for national interest.

**2. Foreign sovereigns and ambassadors:**

Foreign sovereigns and accredited representatives of a foreign state or ambassadors enjoy special privilege, by which they cannot be sued in Indian courts. However, they can, if they choose, enter into contracts and can enforce such contracts in Indian courts.

Ex-kings are not entitled to this privilege and therefore, can be sued in Indian courts just as ordinary citizens.

In India, under Sec. 86 of the Civil Procedure Code, previous sanction of the Central Government is to be obtained, for suing the rulers of foreign states, ambassadors and envoys.

**3. Convicts:**

A convict is a person, who is sentenced by a competent court to the death sentence or imprisonment. A convict cannot enter into a valid contract while undergoing sentence, nor can sue. His incompetency is over, when the period of his sentence is over or he is pardoned.

Thus, the competency right to make a contract or sue is only suspended during the course of his sentence and is not lost. Whenever he is freed, he regains such rights.

**4. Professional persons:**

It is only in England, where the barristers cannot sue their clients for their professional fees. In India, no such rule exists.

In India, every barrister, who has got himself enrolled as an advocate of an Indian High Court can sue his clients for his fees. Under Indian Bar Councils Act, 1927, enrolment of an advocate is necessary before he can practice.

**5. Corporations:**

Corporations include registered companies, local bodies and city corporations. Corporations are legal artificial persons. Since they have legal existence, they can acquire property, transact their business and are capable of suing and being sued. But they cannot do so without their seals.

Powers of a corporation are limited by its Memorandum of Association, beyond which it cannot do anything. This is because contracts which are ultra vires of the objects of the company, shall not be binding. Even such contracts cannot be ratified by passing a resolution in the general meeting of the company members.

**6. Married women:**

Law has not made any distinction regarding contractual capacity of males and females. A woman, whether married or unmarried, enjoys the same contractual capacity as a man. Whatever property a woman possesses, she has absolute ownership over it.

She is free to deal with her personal property in the way in which she likes. Her husband is not at all responsible for her contracts.