

PAPER

F4

**CORPORATE AND
BUSINESS LAW (ENG)**

STUDY TEXT

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SECTION B - THE LAW OF OBLIGATIONS**FORMATION OF CONTRACT****Get through intro**

We frequently enter into contracts in our daily life. Even ordinary transactions such as buying a newspaper or purchasing goods for a certain price from a shop are **examples of contracts.**

A contract is simply an **exchange of commodities / services between two parties for a price.** Individual owners of commodities meet at a common place, known as a market, and freely enter into negotiations to decide the terms on which they are willing to exchange those commodities.

The **law of contract** is based on an idealised model of how the market operates and has been formulated to **facilitate the smooth functioning of the market.**

This Study Guide deals with the study and analysis of the nature of a contract, when a simple agreement becomes a contract, which contract is a void contract and which is a valid one, the meaning of offer and acceptance etc.

You need to devote considerable time to the study of this topic as you will always have a question on this topic in your examination. In your professional life, knowledge of the law of contracts will always be useful as **contracts are the basis of all commercial transactions.**

LEARNING OUTCOMES

- a) Analyse the nature of a simple contract
- b) Explain the meaning of offer and distinguish it from invitations to treat
- c) Explain the meaning and consequence of acceptance
- d) Explain the need for consideration
- e) Analyse the doctrine of privity
- f) Distinguish the presumptions relating to intention to create legal relations

Introduction

Case Study

On March 4, Hardy, a football player, signed a contract with a football club, 'the Wessex Wanderers'.

A clause stating, 'This agreement shall become valid and binding upon each party only when and if it shall be approved by the League Commissioner' was included in the contract.

In late March, Hardy told the Wessex Wanderers that he could not play for them because he had joined another football club, 'Wessex United'.

The commissioner approved the contract on April 14.

Wanderers then sued Hardy for breach of contract.

As students of a professional course you would want to know the meaning of a proper contract system. Was there ever a contract between Hardy and the Wessex Wanderers?

This Study Guide which deals with formation of contract will give you your answers.

1. Analyse the nature of a simple contract

[Learning outcome a]

We need to know the following terms in order to understand the meaning of a contract.

Void: Not valid legally. It is something which has no legal force.

Example

A contract to kill a person is a void contract, as killing is not allowed legally.

Voidable: Something which can be legally rescinded i.e. set aside at the option of the innocent party

Example

A contract entered into by a minor is voidable by the minor. Within a reasonable time after attaining majority, he can claim that he was a minor when he entered into the contract. Hence, he was not competent to foresee that the contract was not beneficial for him. After becoming a major, he may cancel the contract or affirm it.

Ultra vires: Beyond the legal capacity of a person, company or other legal entity.

Example

Under traditional ultra vires doctrine, a corporation that has as its purpose the manufacturing of shoes cannot, under its charter, manufacture motorcycles.

Void ab initio: Invalid, at the very beginning.

Example

In many jurisdictions where a person signs a contract under duress, that contract is void ab initio. Duress means force, threat, coercion or compulsion.

An offer: When one person expresses his willingness to do or to abstain from doing something, to another person, with a view to obtaining the assent of that other person, he is said to be making an offer.

Example

Merry needs to rent a shop. Cherry, her friend, has a shop which is vacant. Merry offers to rent Cherry's shop for £10,000 per year. In this case, Merry has made Cherry an offer. Merry is the 'offeror' and Cherry is the 'offeree'.

Acceptance: When the person to whom the offer is made agrees to it, it is said that the offer is accepted.

Example

In the above example, if Cherry agrees to give her shop on rent to Merry, the offer is accepted.

Consideration: Consideration is required for a contract to be enforceable. Consideration is something that is done or promised in return for a contractual promise.

Example

In a contract between Amy and Bob for the sale of Amy's car to Bob, Bob's payment of the price of the car (or promise to do so) is the consideration for the contract.

Agreement: When an offer made by the offeror is accepted by the offeree, it becomes an agreement.

Example

Merry promises to pay Cherry an annual rent of £10,000 and Cherry promises to give the keys to the office to Merry. This is an agreement. The availability of the shop is consideration for Merry and £10,000 is consideration for Cherry.

It is important to note that, although, all contracts are agreements, **not all agreements are contracts**. This is because **all agreements are not legally enforceable**.



Tips

Contract = Enforceable agreement + Consideration



Tips

Agreement = Offer + Acceptance

1.1 Meaning of contract

1. A contract consists of an actionable promise or promises
2. Every such promise involves two parties, a promisor and a promisee
3. It involves a common intention of acceptance
4. There must be a consideration as to the act (i.e. agreeing to) or forbearance promised (i.e. not doing something)



Example

Ajay and Ben enter into an agreement. Ajay promises Ben to sell his house for £15,000 and Ben accepts to purchase it for the said amount.

This is a contract between Ajay and Ben where Ajay is the offeror and Ben is the offeree. The promise to pay £15,000 is the consideration by Ben. The promise to sell the house is the consideration by Ajay.

**Definition**

The simplest possible description of a contract is "**an agreement enforceable by law for a consideration**"

**Tips**

Contract = Agreement + Enforceability + Consideration

**Tips**

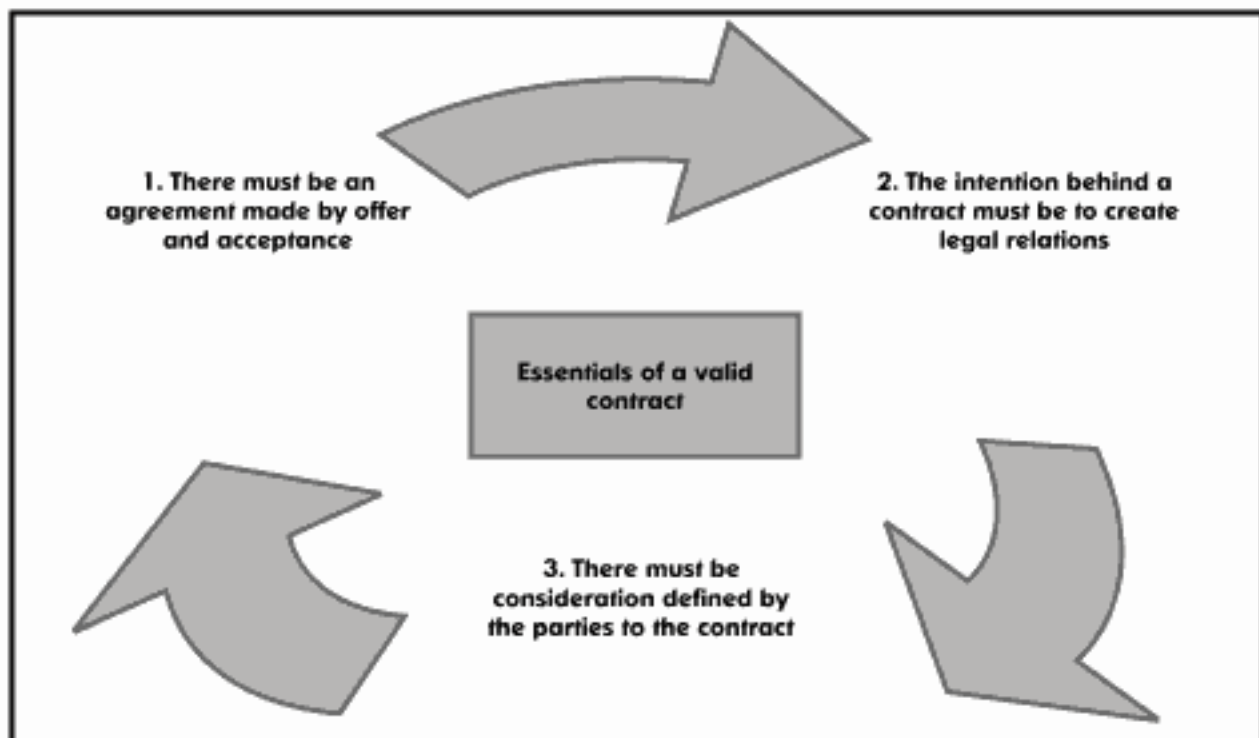
Consideration is the element that makes the agreement a contract

1.2 Legal requirements for the creation of a contract (Essentials of a valid contract)

There are **three essential elements**, which would be examined by a court as the evidence of any contract. These are:

1. Agreement made by offer and acceptance
2. Intention to create legal relations
3. Consideration

Diagram 1: Essentials of a valid contract



1. The agreement must have an offer and an acceptance: a contract is a **bilateral agreement** between two or more parties. Every contract has to go through the **stages** of:

- a) an **offer being made**
- b) **negotiations** among the parties which lead to a settlement
- c) **acceptance** of the offer **for a consideration**

Therefore the presence of an offer and its acceptance are of utmost importance for any contract to take place.



Example

Lee and Chee enter into an agreement. Lee promises Chee to sell his house for £15,000 and Chee accepts to purchase it for that amount. Lee is said to be the offeror and Chee the acceptor. An offer becomes a promise when it is accepted.

2. The intention behind a contract must be to create legal relations: A contract, which is governed by the law of contract, must be made with a view to creating legal relations.

Example

David is leaving on a business trip. He promises his daughter that he will bring her back a camera. This cannot be considered a contract as he does not intend to bind himself legally.

However, if David while leaving the office makes a written agreement with James that he will bring goods according to his description for a given price then this can be considered a contract. This is because both mutually intend to bind themselves legally.

Case Study

Intension to create legal relation is essential to create a contract

Balfour v Balfour (1919)

In this case the defendant, who was working in Ceylon, went on holiday to England with his wife. At the end of the holiday, his wife fell ill and was advised to remain in England for medical treatment. Before returning to Ceylon, the husband promised to pay £30 a month to his wife for her maintenance. Initially, he sent the amount regularly. However, he stopped paying as certain differences between them led to their separation. By the time of the separation, the allowance had fallen into arrears, so the wife brought an action to recover the arrears.

Court's decision: Her action was dismissed. It was held there was no indication that the arrangement was intended to be a contract.

While rejecting her claim, Lord Atkins observed: "there are agreements between parties which do result in contracts within the meaning of that term in our law. The ordinary example is where two parties agree to take a walk together, or where there is an offer and acceptance of hospitality. However, they are not a contract because the parties did not intend that they shall be attended by legal consequences."

3. There must be consideration defined by the parties to contract: consideration is necessary for the formation of every simple contract. **Consideration is the incentive, price or motive that causes a party to enter into an agreement or contract.**

It is something of value that is given in exchange for receiving something from another person.



An informal promise without consideration is not actionable in law even though the promisor may have acted upon it to his detriment.

Example

John wanted to go for an important meeting. David promised John to drive him to the station at the right time. However David failed to keep his promise, as a result of which John missed the train and ultimately missed the meeting.

In this situation, John cannot take any action against David for the loss of potential benefits from the meeting as the promise made by David was an informal promise without consideration.

Tips

It is important to understand that every contract is a bilateral agreement (i.e. an agreement between two or more parties) and hence all the parties to the contract must have some agreed consideration.

Example

Alden enters into a contract with Bayol whereby he agrees to pay £500 to Bayol if Bayol's horse wins the race. Bayol's horse wins the race and he claims £500 from Alden.

Bayol is not entitled to get £500 from Alden because there is no consideration from his side. The contract contains no condition because of which Bayol will have to pay Alden some consideration.

Hence this is not a valid contract.

Besides the three essential conditions explained earlier, there are **some additional elements** which decide the validity of a contract. These are:

- a) Capacity to contract
- b) Legality of object.
- c) Certainty of terms of contract

a) Capacity to contract: One of the essential requirements of a **valid contract** is that the parties must be competent to contract. Capacity refers to a person's ability to enter into a contract. In general, all adults of sound mind have full capacity to contract. However the capacity of certain individuals is limited. Normally, the following persons are considered to be incompetent to contract:

- i. Minor
- ii. Incorporated body: If the contract is against the clauses of or outside the scope of its Memorandum of association.
- iii. Mental incapacity and intoxication
- iv. Disqualification by law
- v. Free consent

i. **Minor:** A minor is a person below the age of 18 years. Their contractual capacity is restricted by the law to prevent them from entering into disadvantageous agreements. However, not all contracts entered into by a minor are void.

Agreements entered into by minors may be classified within three possible categories:

- Valid contracts
- Voidable contracts
- Void contracts

**Definition**

Valid contracts: a valid contract is one which has all the essential elements of contract i.e. agreement, intention to create legal relations and consideration, and which is legally enforceable.

There are again two types of valid contracts which can be enforced against a minor:

- ✓ Contracts for necessities
- ✓ Beneficial contracts of service

Contracts for necessities: When a contract is relating to a payment for a supply of necessities to a minor, then such a contract is binding on the minor.



Necessaries refer to things that are necessary to maintain a minor. However, whether any particular goods supplied are necessary or not will depend upon the facts and circumstances of each case.

As pointed out by **Cheshire and Fifoot**, the word necessities is not confined to articles necessary for the support of life, but include articles and services fit to maintain the particular person in the station of life in which he moves.

Therefore, there is no definition of the term necessities. Generally it means **goods and services which are most essential for the survival** of human life. It includes:

- food
- clothing
- shelter
- education

➤ medical and legal aid etc.

It also varies from person to person subject to his social status and family background. What is a luxury to one person may be a necessary to another.

Example

A car is a luxury for a poor boy whereas it may be a necessary for a prince who hails from a royal family.

The **necessaries must be things which the minor actually needs**. It is not enough that they be of a kind which a person of his condition may reasonably want for ordinary use. Items, which are generally necessities, will prove to be **unnecessary** if the minor is **already supplied with items of that kind**. Whether the other party knows this fact or not will be held immaterial.

Case Study

Contract for necessities is binding on a minor

Nash v Inam (1908)

In this case, a tailor supplied an undergraduate minor with some clothing. The minor was studying at Cambridge University. The clothing consisted of 11 fancy waistcoats at the price of two guineas each. It was proved that the Cambridge undergraduate already had a sufficient supply of clothing for his position in life.

Court's decision: It was held by the Appellate Court that the tailor was not entitled to be reimbursed for the supply of clothing as he failed to prove that the clothing was suitable to the minor's actual requirements at the time of sale and delivery.

The crux of the case is that, although the clothes were suitable according to the minor's station in life, they were not **necessary**, as he already had sufficient clothing.

This shows that the supply of more than adequate clothing can be considered **not** to be supply of necessities.

Beneficial contracts of service: a minor is bound by a contract of apprenticeship or employment, as long as it is, **on the whole, for his / her benefit**.

Case Study

Minor is bound only by beneficial Contracts of service

Doyle v White City Stadium (1935)

Doyle, a minor, was granted a professional boxer's licence, which was treated as a contract of apprenticeship. The licence provided that he would be bound by the rules of the Boxing Board of control. According to one of the rules, the Board had the power to retain any prize money if he was ever disqualified in a fight. Doyle claimed that the licence was void, as it was not for his benefit.

Courts decision: It was held that, in spite of the penal clause, the licence, taken as whole, was beneficial to him. Hence the conditions of the licence were held enforceable.



Definition

Voidable contracts: Voidable contracts are those contracts which may be avoided, that is, set aside, by one of the parties. If, however, no steps are taken to avoid the contract, then the contract is considered to be a valid contract.

There are some contracts which may bind the minor. They remain valid until cancelled by the minor.

These contracts are binding on the minor, unless they are expressly disclaimed by the minor during the period of minority or within a reasonable time after attaining the age of majority.

Example

Fancy, a minor and a very famous child artist enters into a contract with a film producer to do a lead role in his film immediately after she becomes a major. However, this contract is voidable at the option of Fancy on becoming a major.

If she does not expressly disclaim fulfilling the contract within a reasonable time after attaining majority, then the contract will be binding on her.

**Definition**

Void contracts: A void contract is one which is not legally enforceable and the parties thereto are not legally obligated to each other.

Generally, contracts are void because the subject matter is not legal or one of the contracting parties does not have the competency to contract.

The following contracts entered into by a minor are always void:

- ✓ Contracts entered into by a minor for repayment of money lent or to be lent.

Example

John had lent Ted £10,000. Ted's minor son, Jimmy, entered into a contract with John for repayment of the loan his father had taken.

This is a void contract.

- ✓ Contracts for goods supplied or to be supplied (other than necessities)

Example

Lilly, a minor, enters into a contract with Peter to buy his car.
This is a void contract.

Case Study**Contracts with minor are void****Mercantile Union Guarantee Corp v Ball (1937)**

A minor was engaged in the haulage business. He had entered into a hire purchase contract which was related to the business.

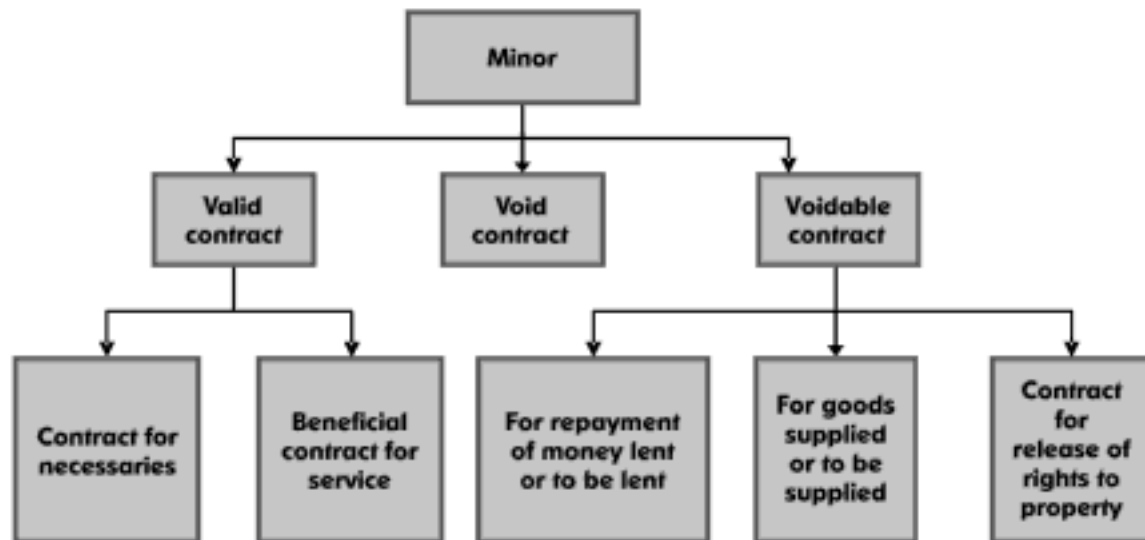
Courts decision: It was decided by the court that a minor was not liable for the hire purchase entered into by him with regards to the haulage business. Contracts with minor for goods supplied are void.

- ✓ Contracts for release of rights in property.

Example

Jack, a minor, enters into a contract with his Uncle John whereby Jack agrees to release his right to their ancestral property.
This is a void contract.

Diagram 2: Minor



ii. **Incorporated body:** Every incorporated body is a legal body created by the law. It can contract only through its agents such as a board of directors or chief officers in accordance with its internal management.

A company cannot make any contract, which is inconsistent with the objective set out in the Memorandum of Association. If the company enters into such a contract, it is ultra vires i.e. beyond its powers and therefore void at common law but under S35 Companies Act 1985 (as amended by the Companies Act 1989) a third party acting in good faith will be able to enforce the transaction against the company.

iii. **Mental incapacity and intoxication:** A contract entered into by a person who is of unsound mind or under the influence of drugs, or drunk is prima facie valid. Such contract can be held void if the person in contract proves:

- That at the time their mind was so affected that they were incapable of understanding the nature of their actions
- That the other party either knew or ought to have known of their disability. In any case, however, the person claiming such incapacity must pay a reasonable price for the goods supplied to them

Tips



Prima facie: a Latin term meaning "on the face of it." It is a fact which, unless disproved, is presumed to be true. In day-to-day speech, the term prima facie is used to describe the apparent nature of something at first glance.

Test Yourself 1

Sunny went to a bar. There he met Bobby, who was a painter. Sunny made an offer to Bobby that he paint his farm house for £500. Bobby accepted the offer. Sunny gave him the address of the farm house, the keys and £100 as an advance.

The next day Bobby went to Sunny's farm house and painted the farm house. However Sunny refused to pay the balance amount. He claimed that he was under the influence of alcohol and hence was unable to make a rational decision. In your opinion, is the contract valid?

iv. **Disqualifications by law:** A person may also be disqualified from entering into a contract by any law to which he is a subject.

Example

A contract entered into with an alien enemy will be void.

An alien is a person who resides in a foreign country. An alien becomes an enemy when the country of which he is a citizen is at war with a country of which the other party to contract is a citizen.

Hence, at the time of a war between these two countries, an agreement with an alien enemy is illegal and therefore void.

In Potts v Bell (1918), it was held that all rights and obligations arising out of a contract with an alien enemy are suspended during war and that the contract may be void on the grounds of public policy. This is because it may promote the economic interests of the enemy state (i.e. make money for the enemy country) or it may prejudice the economic interests of the state at war with enemy state.

v. Free consent: Two or more persons are said to consent when they agree upon the same thing in the same sense. A consent is said to be free when it is **not caused** by:

a) **Duress (Coercion):** This means committing, or threatening to commit any act against a person's will. Duress is some element of force, either physical or economic, which is used to override one party's freedom to choose whether to enter into a particular contract or not. Such contracts are voidable at the insistence of the innocent party.

In order to benefit from the doctrine of duress, claimants must prove two points:

- That the pressure, which has resulted in an absence of choice on their part, was brought on them against their will.
- That the pressure was of a nature considered to be illegal by the court.

Example

Armstrong threatened to kill Barton if he did not sign a contract. The contract was set aside due to duress to Barton.

b) **Undue influence:** A contract is said to be influenced by 'undue influence' when all the essential elements of undue influence are satisfied i.e.:

- The relationship between the parties is such that one of the parties is in a **position to dominate the will of the other**
- He **uses that influence to obtain an unfair advantage** over the other and
- Unfair **advantage is in fact obtained.**

**Example**

Alan advances some money to his son Bobby because he has financial problems in his business. When Bobby's financial problems end, Alan obtains a contract from Bobby for a greater amount than the sum due in respect of the advance.

The facts of the case needs to be compared with the essential elements of undue influence that:

1. The relationship between the parties is that of father and son. The father is in a position to dominate the will of his son.
2. The father uses his influence to obtain a greater amount than the sum which is due.
3. Unfair advantage, in fact has been obtained as there is already a contract between Alan and Bobby.

As all the essential elements of undue influence are satisfied, therefore this is a case of undue influence.

Tips



While considering this example, the important points that are essential for undue influence is briefly summarised in the answer. It is recommended to follow this technique in the exam. This gives the examiner an idea of your understanding of the topic and will earn you more marks.

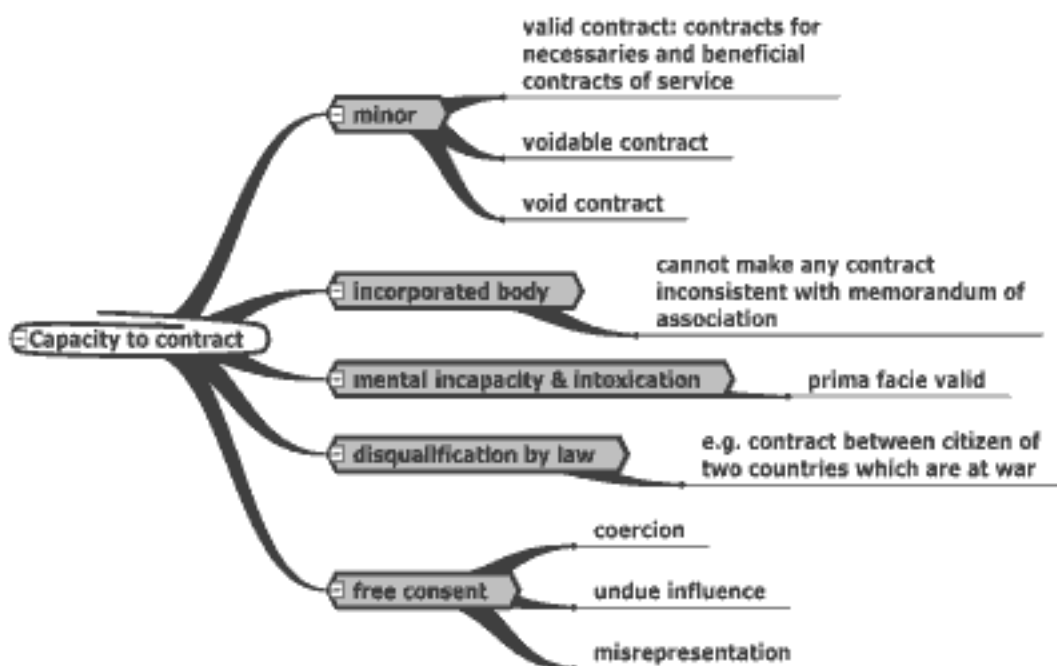
Test yourself 2

Brown approaches a bank for a loan at a time when banks generally are not giving loans. The bank declines to make the loan except at an unusually high rate of interest. Brown accepts the loan on these terms.

Do you consider this to be a case of undue influence?

Misrepresentation is not covered in syllabus.

SYNOPSIS



b) Legality of object: The legality of object is yet another essential element of a valid contract. A contract that breaks the law is illegal. The courts have recognised that any contract that tends to prejudice any social or economic interest of the country must be forbidden.

However, contracts that would be contrary to public policy depend on the facts and circumstances of the case under consideration.

Some examples of illegal contracts are:

i. Contracts prohibited by statute.

Example

A contract to employ a child in a factory. Child labour is illegal and therefore this contract is illegal.

ii. Contracts to defraud the Inland Revenue.

Example

A contract showing a sale price which is less than the actual price and accepting the difference in cash without disclosing it to the Inland Revenue.

iii. Contracts involving commission of crime.

Example

A contract to kill a person

iv. Contracts against the interest of the UK or friendly states.

Example

A contract to sell weapons to an enemy state

v. Contracts leading to corruption in public life.

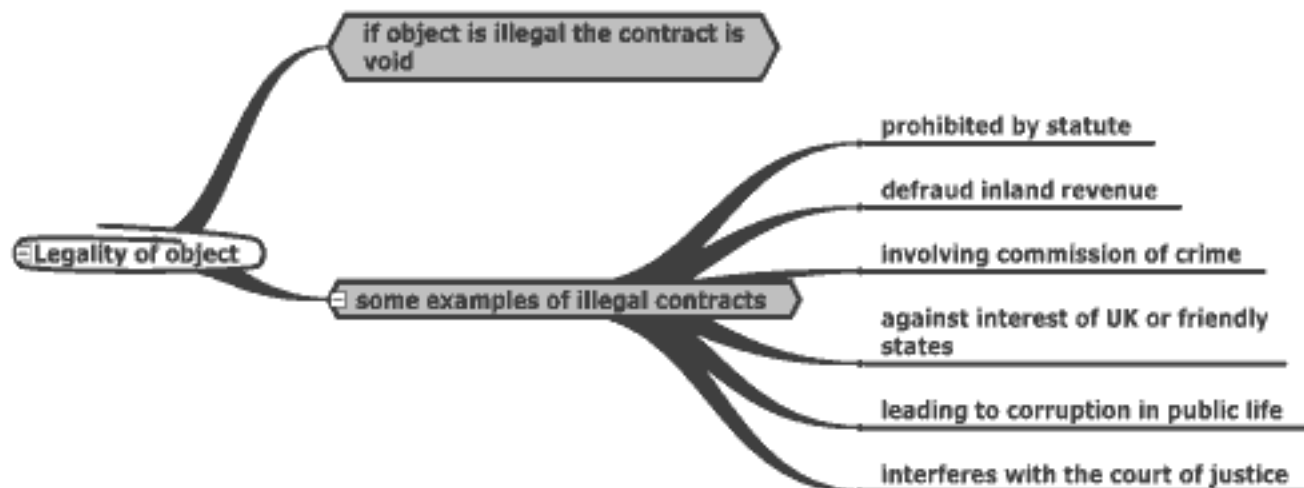
Example

An amount paid to secure a high-profile job in government

vi. Contracts which interfere with the court of justice.

Example

A promise to indemnify a person who will do an illegal act

SYNOPSIS

c) **Certainty of terms of contract:** The contract terms should not be vague. They must be certain and definite. The intentions of the parties to contract must be clearly indicated by the terms of contract.

Example

Annie makes an offer to Bob to supply her with 100 metres of cloth. Here, the terms of offer are not clear since the type of cloth, colour, and price is not mentioned.

Hence this is not a contract.

Case Study

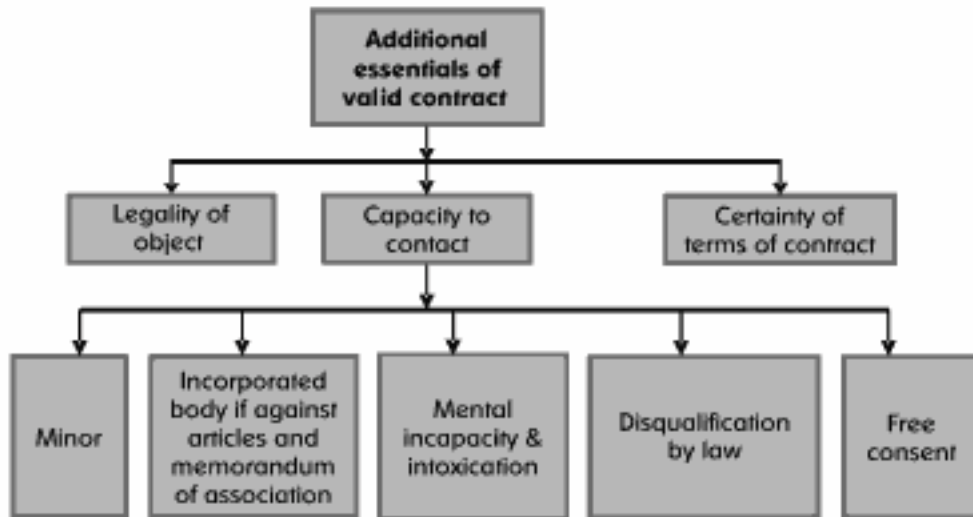
The contract is not enforceable if the terms are vague and uncertain.

Taylor v Portington (1885)

The claimant in this case, promised to take the defendant's house on lease for a period of three years provided, "it is thoroughly repaired and the drawing rooms are decorated according to the latest style.

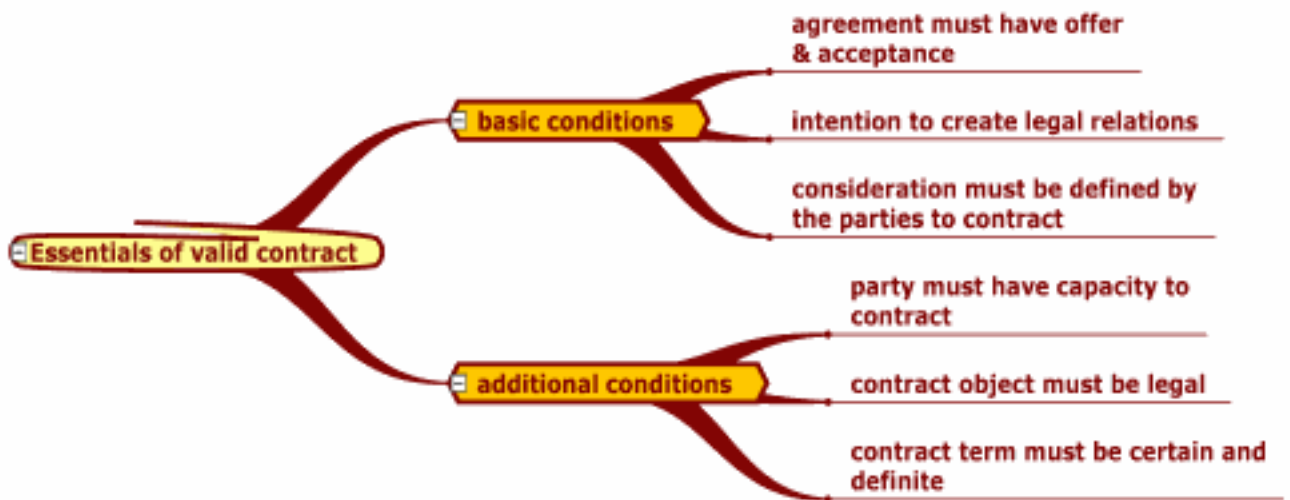
Courts decision: It was held that the contract is not enforceable, since the terms were vague and uncertain.

Diagram 3: Additional essentials of a valid contract



SYNOPSIS

Essentials of valid contract



1.3 Form of contract – written or oral or inferred from the conduct of parties: As a general rule, a contract may be made in any form. There is no requirement that a contract has to be in writing. They can be created by **word of mouth or by an action**, as well as in writing.

However, the following types of contracts must be in writing

1. Contracts that must be made by a deed: A deed is a legal instrument used to grant a right. A contract by deed must be in writing. The deed must be signed by parties to the deed.



The contracts that must be in the form of a deed are:

- a) **Leases of property** for a period of more than 3 years.

Example
Jennifer entered into a contract with Maria to lease her flat to Maria for 10 years. As the lease period is more than 3 years, the contract must be made by a deed.

b) Conveyance or **transfer of land****Example**

Marion owns a plot of land. She entered into a contract with Leonardo to sell him that plot for £25,000. This contract must be made by a deed.

c) An **agreement not supported by consideration****Example**

Vandana pledges to donate an agreed amount of money monthly for 5 years to an orphanage near her house. The orphanage is not giving anything in return. As the agreement is not supported by consideration from the orphanage, Vandana must sign a Deed. This becomes a contract for Vandana to give the money.

2. Contracts that must be in writing (but not necessarily by deed): Some types of contracts are required to be in the form of a written document, usually signed by both the parties. Some of these contracts are:

- Bills of exchange, cheques and promissory notes.
- Consumer credit instruments, e.g. a hire purchase agreement
- Transfer of shares in a company
- Sale or disposition of interest in land

3. Contracts that must be evidenced in writing: Certain contracts even though made orally, are enforceable in a court of law only if they are evidenced in writing. The most important contract of this type is a contract of guarantee.

A 'contract of guarantee' is a contract to perform the promise, or discharge the liability, of a third person in case of his default. The person who gives the guarantee is called the 'surety', the person in respect of whose default the guarantee is given is called the 'principal debtor', and the person to whom the guarantee is given is called the 'creditor'. A guarantee may be either oral or written.

Example

Ziya took a loan of £10,000 from Mira. Tina agreed that if Ziya failed to repay the loan, she would repay the loan to Mira.

Here,

- Tina is the surety
- Ziya is the principal debtor
- Mira is the creditor

Test Yourself 3

Is an agreement for service with relatives or friends legally enforceable?

Test Yourself 4

David, a man enfeebled by disease and age, is induced by Baul's influence over him as his medical attendant, to agree to pay Baul an unreasonable sum for his professional services. Is the contract affected by undue influence?

Test Yourself 5

Andrew threatened to have Brian killed if he did not buy Alan's shares in a company of which Brian was the managing director. Is the contract to buy shares by Brian valid?

Test Yourself 6

Fenny promises to pay Campbell £5,000 if he murders her husband. Is the contract valid?

Test yourself 7

Which of the following relationships do not raise the presumption of undue influence?

- Doctor and Patient
- Trustee and Beneficiary
- Landlord and Tenant
- None of the above

SYNOPSIS**2. Explain the meaning of offer and distinguish it from invitations to treat****[Learning outcome b]****2.1 What is an offer?****Definition**

An offer is a definite promise to be bound by particular terms and it must be capable of acceptance.

When one person signifies to another his willingness to do or to abstain from doing anything, with a view to obtain the assent of the other person to such act or abstinence, he is said to make an offer.

The person who makes the offer is the offeror and the person to whom the offer is made is the offeree.

The offer sets out the terms upon which the offeror is willing to enter into contractual relations with the offeree.

2.2 Elements of offer: The following are important elements of an offer:

- There shall be at least two persons: the offeror and the offeree, who are competent to contract.
- One person (the offeror) expresses his willingness to another (the offeree) to do, or abstain from doing something.
- The offeror has the intention of getting the consent of the offeree to do such an act or abstain.

2.3 The offer can be made to whom?

The offer may be made to:

1. One person
2. A class of persons
3. The world at large

An offer need not always be made to a certain person (an ascertained person), but it is necessary that someone should accept it.

Example

If a person offers a reward to anyone who finds his lost diamond ring, the finder can successfully claim the reward.

Where an offer is made to the world at large, acceptance of the offer and performance by the party replying to it will be sufficient to make it an enforceable contract.

THE ILLUSTRATED LONDON NEWS

£100 REWARD
 FOR THE RECOVERY OF A LOST DIAMOND RING

CARBOLINC SMOKE BALL CO. LTD.

TO ANY PERSON WHO FINDS A LOST DIAMOND RING

£200 REWARD
 FOR THE CURE OF THE FOLLOWING AILMENTS:

INFLUENZA	CATARH	THROAT DRAINNESS	DIPHTHERIA
COUGHS	ASTHMA	LOSS OF VOICE	CHOLERA
COLD IN THE HEAD	BRONCHITIS	LARYNGITIS	WHOPPING COUGH
COLD IN THE CHEST.	SORE THROAT	SNORING	NEURALGIA
	HOARSENESS	SORE EYES	MIGRAINE

CARBOLINC SMOKE BALL CO., LTD.,
 27, PRINCES STREET, MANCHESTER SQUARE, LONDON, W.

THE ILLUSTRATED LONDON NEWS

CARBOLINC SMOKE BALL
 WILL POSITIVELY CURE

£100 REWARD
 FOR THE RECOVERY OF A LOST DIAMOND RING

CARBOLINC SMOKE BALL CO. LTD.

TO ANY PERSON WHO FINDS A LOST DIAMOND RING

£200 IS DEPOSITED
 FOR THE CURE OF THE FOLLOWING AILMENTS:

INFLUENZA	CATARH	THROAT DRAINNESS	DIPHTHERIA
COUGHS	ASTHMA	LOSS OF VOICE	CHOLERA
COLD IN THE HEAD	BRONCHITIS	LARYNGITIS	WHOPPING COUGH
COLD IN THE CHEST.	SORE THROAT	SNORING	NEURALGIA
	HOARSENESS	SORE EYES	MIGRAINE

CARBOLINC SMOKE BALL CO., LTD.,
 27, PRINCES STREET, MANCHESTER SQUARE, LONDON, W.

Very important case in the law of contract!!

Case Study

Acceptance of the offer

Carlill v Carbolic Smoke Ball Co (1893)

The defendants were proprietors and vendors of 'Carbolic Smoke Ball Co'.

They advertised a reward of £100 to any person who contracted influenza after using the Smoke Ball for a certain period, according to the printed directions. In order to show their sincerity, they also deposited £1,000 in a bank. The claimant used the Smoke Ball according to the printed directions yet she contracted influenza. She brought an action to claim the reward.

Arguments by the defendant company

1. The offer was so vague that it could not form the basis of a contract, as no time limit was specified in the offer.
2. There was no contract between the parties because a notification of acceptance had not been communicated to the company by the offeree.
3. Cannot contract with the whole world
4. Mrs Carlill had not provided any consideration for their promise
5. The advertisement did not constitute an offer but was simply sales talk.
6. There was no intention to create legal relations

Courts decision

The Court disagreed with the company's arguments, and awarded the claimant damages. It was pointed out by the court that:

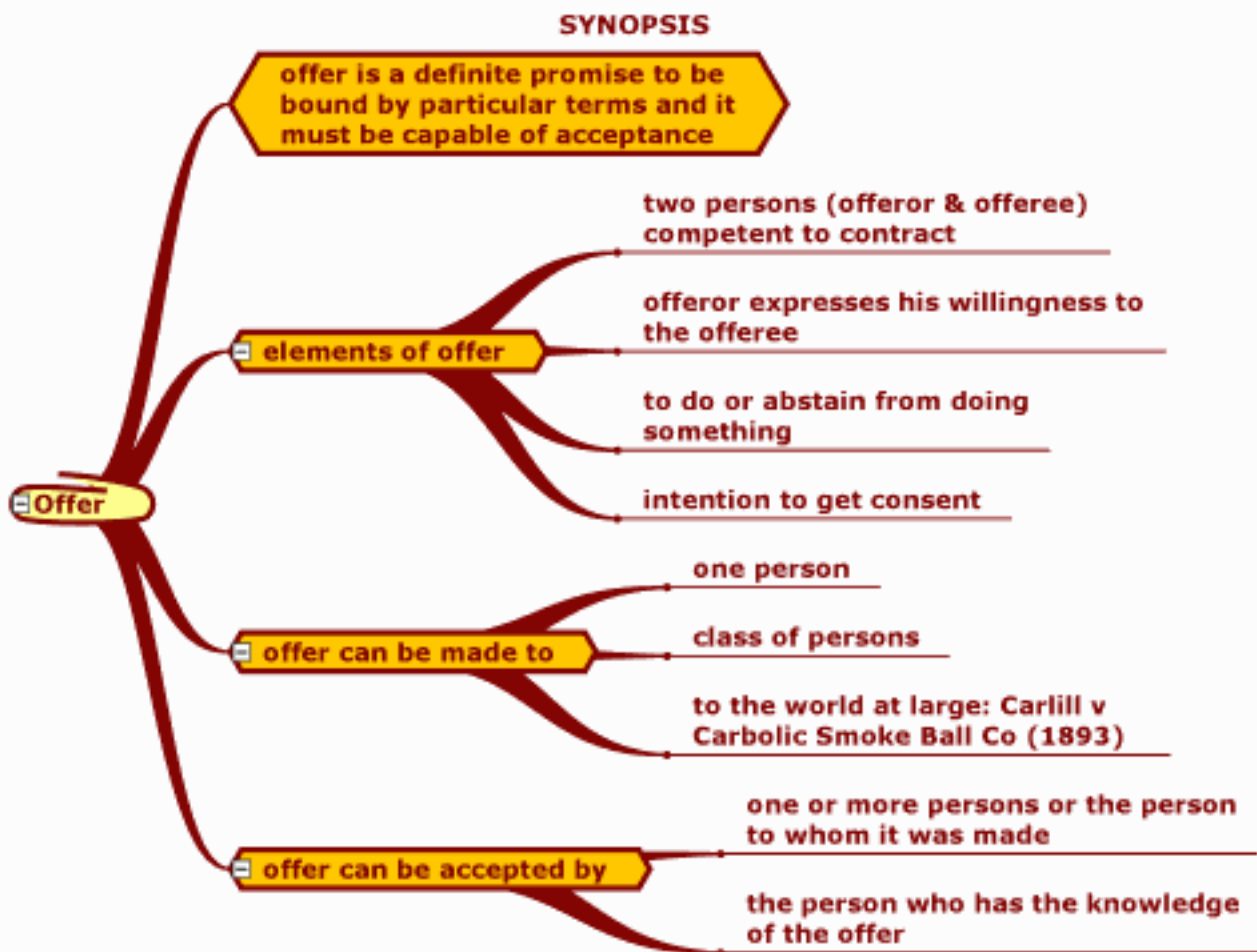
1. In advertisement cases, an offer may be made to the world at large but it becomes a promise only when it is accepted by an ascertained person
2. The company must protect the user during the period of use- the offer was not vague.

2.4 Who can accept the offer?

1. Only the person or one of the persons **to whom the offer is made** can accept the offer.
2. Only a person who has knowledge of an offer can accept the same.

Example

Rocky loses his wallet and he offers a reward for it without advertising the fact that there would be a reward for it. Jacky finds the wallet and does not know about the reward offered by Rocky. He therefore cannot claim the reward.



2.5 Essentials of a valid offer

A valid offer must fulfil the following two conditions:

1. **An offer cannot be vague:** offers with uncertain meaning are void.

Case Study

An offer cannot be vague

Gunthing v Lynn (1831)

The offeror offered to pay a further sum for a horse if it was "lucky".

Court's decision: The offer was too vague and hence the contract is void.

2. **An offer must be distinguished from supply of information, statement of intention and an invitation to treat.**

a) Supply of information

Information may be necessary for the parties who are negotiating the terms of a contract before a definite offer is made. However, the mere supply of information cannot be a valid offer.



Case Study

Mere supply of information is not an offer.

Harvey v Facey (1893)

The claimant offered to purchase a plot of land, Bumper Hall Pen, belonging to the defendant. He telegraphed the defendant: 'Will you sell us the land known as Bumper Hall Pen? Telegraph lowest cost price'.

The defendant sent the reply through the telegraph quoting, 'lowest price for Bumper Hall Pen £900'.

The claimant was ready to purchase the land at the quoted price. He telegraphed, 'We agree to buy Bumper Hall Pen for £900'.

But the defendant refused to sell the land for £900. On the denial of the defendant to sell the land, the claimant brought this suit.

Court's decision: It was held that no contract was made. The **defendant had not made an offer** by stating the lowest price of the land known as Bumper Hall Pen. He had **merely supplied information**. In other words, no offer had been made by the defendant and no acceptance of the offer was made by the claimant.

b) Statement of intention

A statement showing a present intention, which can be altered in the future as one wishes, is not an offer. Such a statement cannot be the basis of a contract, even though the party to whom it was made acts on it.



Case Study

Statement of intention is not an offer

Harris v Nickerson (1873)

The auctioneer had advertised that an auction sale would be held on a particular day. The claimant saw the advertisement and reached the place of the auction on the specified day. However, due to the auctioneer's illness the proposed sale was postponed.

Court's decision: It was held that the **auctioneer was not liable for damages**. An advertisement that an auction would be held at a particular time and place is not an offer to hold an auction. Any person who on the faith of the advertisement had incurred expenses to attend the proposed sale has no right of action if it is cancelled. This advertisement was a **statement of intention**.

c) Invitation to treat

This is an invitation to others to make offers. An offer comes into existence only when a person shows his readiness and willingness to enter into a contract. Where a person invites others to make an offer to him, the invitation made by him is not an offer, but only "an invitation to treat".

The purpose of making an invitation to treat is to receive the offer.

Example

A menu of a restaurant showing the various food items available at that restaurant and their prices. When the restaurant owner gives you the menu card, he is inviting an offer from you.

The contract of the owner of the restaurant serving food and you paying money does not exist.

It is only when you order something from the menu card and the restaurant owner agrees to serve you that the contract begins.

The person extending the invitation is not bound by the offers made to him. If you order some food item which is not on the menu, the hotel owner will reject your offer.

An invitation to treat is different from an offer primarily on the grounds that it is not made with the intention that it become binding as soon as the addressee communicates his assent to its terms. The contract comes into existence only when the offer made by others is accepted by the person who had made the "invitation to treat".

Some of the common situations involving an invitation to treat are:

- i. An advertisement in the newspaper inviting applications for jobs is generally not deemed to be an offer.

However, a situation where an advertisement specifies the performance of a task or terms that are clear and leave no room for negotiation are exceptions to this. The **Carlill v Carbolic Smoke Ball Co case** shown earlier is a good example of this exception.

- ii. Goods exhibited with a price-label in a display case.

Case Study

Goods exhibited with a price label are merely an invitation to treat.

Fisher v Bell (1961)

In this case, a shopkeeper was prosecuted for offering offensive weapons for sale, by having flick-knives on display in his window.

Court's decision: It was held that the shopkeeper was not guilty as the display in the shop window was not an offer for sale but only an invitation to treat.

Unless somebody offers the shopkeeper to purchase those weapons, and he accepts to sell them, he cannot be held guilty.

- iii. Circulation of catalogue or price list by a seller
- iv. A personal quotation of the price of goods
- v. Prospectus of a company inviting public to subscribe to their shares and debentures
- vi. Auction sale
- vii. Invitation for tenders is not an offer. A tender which is received in response to such an invitation is an offer.

Case Study

Auction is invitation to treat and not an offer itself.

Harris v Nickerson

An auctioneer made an advertisement in the newspaper that an auction of office furniture would be held on a particular day. The claimant came from a distant place to buy the furniture, but the auction was cancelled.

Court's decision: It was held by the court that the advertisement of the auction was only an "invitation to treat" and not an offer itself.

Since there was no offer, there could not be any acceptance. Hence there was no contract between the auctioneer and the claimant.

Case Study

Goods displayed in shops are invitations to the customer to offer to buy.

Pharmaceuticals Society of Great Britain v Boots Cash Chemicals Ltd (1953)

In this case, the defendant was charged with breaking the law, which stated that certain drugs could only be sold under the supervision of a qualified pharmacist. They had placed the drugs in an open display in their self service store, although a qualified person was stationed at the cash desk.

It was claimed by the claimant that once the customer picked up an article and put it into the basket (supplied by the shopkeeper for the purpose), the contract of sale was complete: the shopkeeper could not then refuse to sell it.

Court's decision: The defendant was found not guilty. It was held that the mere fact that a customer picks up a bottle of medicine from the shelves does not amount to an acceptance of an offer to sell. It is an offer by the customer to buy, and there is no sale confirmed until the buyer's offer to buy is accepted by the acceptance of the price.

SYNOPSIS

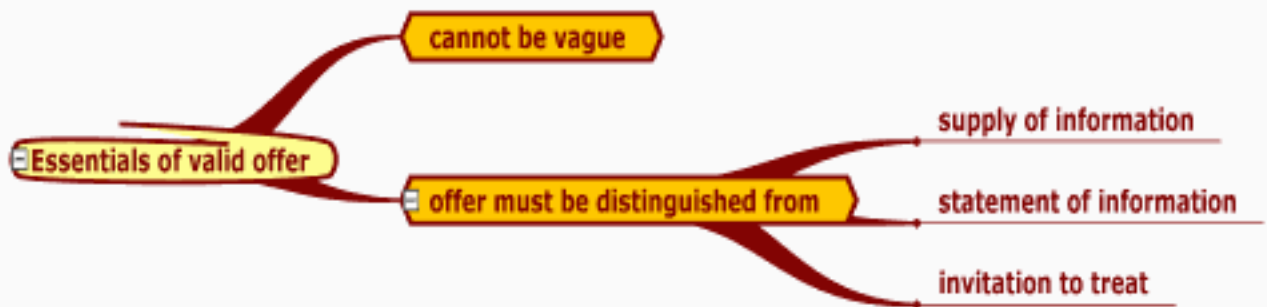
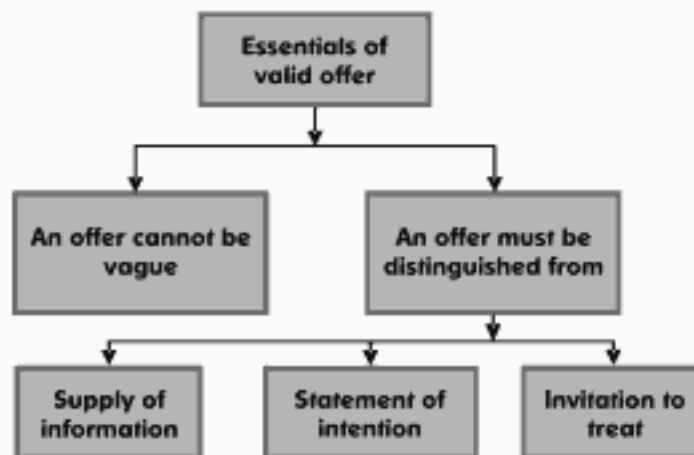


Diagram 4: Essentials of valid offer



Test yourself 8

Distinguish between an "offer" and an "invitation to treat".

2.6 How can an offer be terminated?

Termination means putting an end to an offer. An offer can be terminated in any one of the following ways:

1. **By rejection of offer:** Expressed rejection of an offer terminates the offer. A **counter-offer** also terminates the original offer.

Case Study**A counter-offers terminates the original offer****Hyde v Wrench (1840)**

Wrench offered to sell his farm for £1,000. Hyde offered £950, which Wrench rejected. Hyde then informed Wrench that he accepted the original offer of £1,000. But Wrench refused to sell the farm to Hyde.

Court's decision: It was held that there was no contract.

Hyde's **counter-offer** had terminated the original offer and therefore the original offer was no longer open for acceptance. Hyde was now making an altogether new offer to buy Wrench's land for £1,000, and it was for Wrench to decide whether to accept the offer or reject it.

The offeror and offeree have replaced each other.

2. **By lapse of time:** An offer is terminated by the lapse of time prescribed in the offer for its acceptance. If no time for acceptance is mentioned in the offer, then the offer is terminated by the lapse of reasonable time.

**Example**

Daisy purchased a new laptop. She made an offer to Alvin to purchase her old desktop computer for £250. Alvin decided to purchase the computer within a fortnight. However, he did not communicate his decision to Daisy during or after the expiry of the fortnight.

In this case, the offer is terminated at the expiry of the fortnight and Daisy is free to sell the desktop computer to another person. If Alvin approaches her to purchase the desktop computer after the expiry of the fortnight, she may refuse to sell it to him.

3. **By the failure of the acceptor to fulfil the condition precedent to acceptance:** This is called a conditional offer. Where an offer is subject to any condition for its acceptance, then the offer terminates on non-fulfilment of the condition.

Example

Jaya offers to sell a painting to Maya for £100, provided that Maya gives her an advance of £20 within two days. Maya came on the third day with £100 to buy the painting. However, as the condition of giving an advance of £20 within two days was not fulfilled, the offer was terminated.

4. **By revocation of offer:** An offeror may revoke an offer at any time before its acceptance. Once revoked, it is no longer open to the offeree to accept the offer.

Case Study**On revocation of offer, offer is no longer open to the offeree.****Routledge v Grant (1828)**

Grant offered to buy Routledge's house and gave him six weeks to accept the offer. However, he withdrew the offer before the end of the 6 weeks. Routledge claimed that Grant was bound to buy his house.

Court's decision: It was held that Grant was entitled to withdraw the offer at anytime before the acceptance. As the offer was already withdrawn, Routledge could no longer create a contract by accepting the offer.

Important points to note

- i. Revocation is not effective until it is actually received by the offeree.

Case Study

Revocation of offer has no effect until it is communicated to the person to whom the offer has been made.

Byrne v Van Tinehoven (1880)

In this case, on October 1, an offer to sell was mailed by the offeror.

It was received by the offeree on October 11. The offeree accepted the offer by sending a telegram on October 11. On October 15, the offeree again mailed a letter to the offeror to confirm the acceptance.

However, on October 8, a letter was sent by the offeror revoking the offer. On October 20, the offeror received the letter of acceptance sent by the offeree.

Court's decision: It was held that the revocation was inoperative.

The court said that 'an offer can be withdrawn before it is accepted and it is immaterial whether the offer is expressed to be open for acceptance for a given time or not.'

However, withdrawal of offer has no effect until it is communicated to the person to whom the offer has been sent. An uncommunicated revocation is no revocation at all under the law.

Case Study

Implied revocation of offer

Dickinson v Doodds (1876)

Once a person is informed that the item that was offered to him was sold to another person, there is an implied communication of the revocation of the offer and it is too late for acceptance (full case below)

- ii. Communication of revocation may be made through a reliable third party.

Example

Charley offered to sell his car to Eddy. However the next day, he sold the car to another person. Charley informed Eddy's wife, that the offer to Eddy is now revoked as he had already sold the car to somebody else. In this case, the revocation is effective as the communication of revocation of the said offer was made through a reliable third party.

Case Study

Communication of revocation of offer may be made by a reliable third party.

Dickinson v Doodds (1876)

Dodds offered to sell a property to Dickinson. He also told Dickinson that the offer would be left open until Friday. On Thursday, Dodds informed Dickson through a person who was acting as an intermediary that he intended to sell the property to someone else. Dickson still attempted to accept the offer on Friday. But the property was already sold before Friday.

Courts decision: It was held that the sale of the property amounted to revocation. The revocation communicated by a reliable third party amounts to effective communication of revocation.

5. By death of one of the parties

- a) In the case of personal contract, where the offeree dies, the offer automatically ends.

Example

Rani, a finance consultant offers to handle Mani's financial matters from the month of April. However Rani dies in March. The offer to Mani automatically ends.

b) In the case of non personal contracts e.g. sale of a vehicle, the contract can be enforced by a representative of the deceased.

Example

John offered to buy flowers from Kim's farm in the month of March for £5,000. Kim accepted the offer. However John died in February and his son Jacky took over the charge of his business. In this case, Jacky can enforce the contract against Kim. Kim will have to supply the flowers to Jacky.

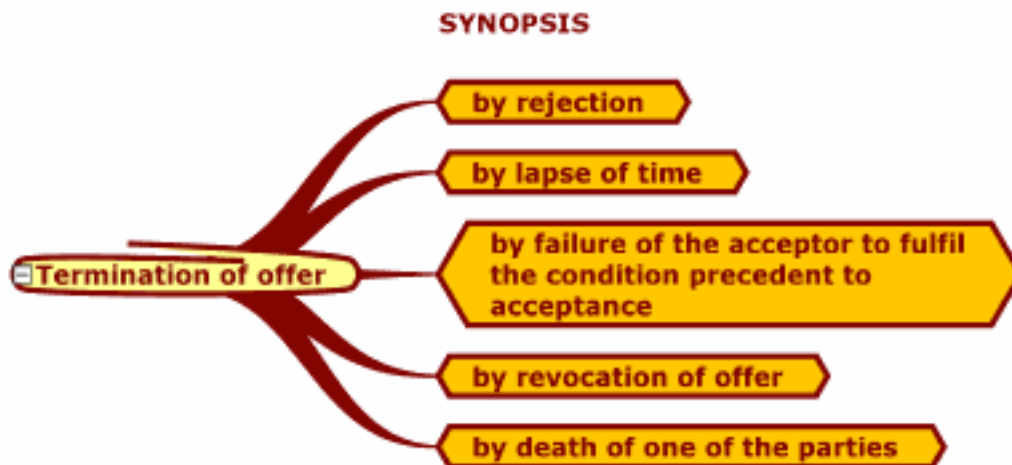


Diagram 5: Termination of an offer



Test yourself 9

Which of the following offers constitute a valid offer?

- An auctioneer displays a T.V. set before a gathering in an auction sale.
- John advertises in a newspaper that he would pay £500 to anyone, who finds and returns his lost briefcase containing valuables.
- Ron who is in possession of three cars purchased in different years says 'I will sell you a car'
- A clothing store owner announces that prices of formal shirts are reduced by 60%
- Julie communicates to Lilly that she will sell her car for £4000.

Test Yourself 10

Explain the rules relating to revocation of an offer in relation to the law of contract.

3. Explain the meaning and consequence of an acceptance**[Learning outcome c]****3.1 What is an acceptance?****Definition**

"When a person to whom an offer is made signifies his assent to the same, the offer is said to be accepted. Acceptance of an offer is a necessary and vital ingredient towards the creation of a contract".

After an offer has been made, the next important step for the formation of a contract is acceptance. An offer creates no legal rights or duties unless it has been accepted. **Acceptance converts an offer into a contract.**

3.2 Conditions for valid acceptance

For an acceptance to be binding, it must fulfil the following conditions:

- Acceptance must be communicated:** Even if the offeree has made up his mind to accept the offer, the agreement is not yet complete. There must be an external expression of assent. The acceptance of an offer must be communicated to the offeror. The communication of acceptance should be clear and unambiguous.
- Mode of communication:** Acceptance can be communicated in any of the following three ways:
 - Acceptance by express words
 - Acceptance by action
 - Acceptance inferred from conduct



Case Study

Mode of communication

Felthouse v Bindley (1862)

The claimant wrote a letter to his nephew offering to buy his nephew's horse for £30.15s. He also wrote in his letter, "If I hear no more about him I shall consider the horse to be mine at £30.15s." The nephew did not reply to this letter. However, he told the defendant, an auctioneer, not to sell the horse. Hence, **he intended to reserve the horse for his uncle**. But the auctioneer sold the horse to someone else. The claimant thereupon sued the defendant, the auctioneer.

Court's decision: Dismissing the action, the court held that since the nephew **did not communicate his acceptance**, no contract took place between the claimant and his nephew. Hence, he had no right to make a complaint regarding the sale.

The court also held that the communication of acceptance must be made to the offerer himself or to his agent. Here the communication of acceptance was made to the auctioneer who was a stranger to the claimant.

3. **The offeror cannot impose upon the offeree an obligation to refuse:** In *Felthouse v Bindley* discussed above, it was also held that the offeror cannot impose upon the offeree the obligation of refusal. The uncle wrote to his nephew, "If I hear no more about him I shall consider the horse to be mine at £30.15s." In this case, **mere silence from the nephew would not constitute acceptance**.
4. **Communication of acceptance must be by a person who has authority to accept:** A communication of acceptance to be valid must be made either by the offeree himself or by his authorised agent. A communication of acceptance by any other person will not be valid.

Case Study

Communication of acceptance must be by a person who has authority to accept

Powell v Lee (1908)

The board of managers of a school passed a resolution selecting the claimant (a candidate) for the post of headmastership but the decision about his selection was not communicated to him. One of the managers, in his individual capacity, informed him about the resolution. Subsequently, the board of managers rescinded their decision and so the claimant was not appointed as the headmaster. The claimant, thereupon, brought an action for breach of contract.

Court's decision: The court held that no contract was concluded because for a communication of acceptance to be valid it must be made by the offeree himself or his authorised agent.

A communication of acceptance from an unauthorised person is not valid.

There are, however, **exceptions to the general rule that acceptance must be communicated**. Communication of acceptance is not required in the following cases:

- a) **Communication may be waived by the offeror:** Since the notification of the communication is for the benefit of the offeror, he may waive it if he deems it fit.

In *Carlill v Carbolic Smoke Ball Co*, the facts of which were discussed earlier, the court observed that it was sufficient for the claimant to act on the offer without notifying her acceptance of it. The contract was a unilateral contract, where the offer takes the form of a promise to pay money in return for an act.



Acceptance through postal services complete when letter of acceptance is posted by the offeree

Case Study

Adams v Lindsell (1818)

The defendants made an offer to sell wool to the claimant in a letter dated September 2, 1817. This letter arrived on September 5, 1817. The claimant posted his letter of acceptance on the same day, i.e. on the 5th September 1817. The defendants received the letter on September, 9, 1817. But the defendants had already sold the wool to some other party after waiting until 8th September 1817. An action was brought against them by the claimant for the breach of contract.

Court's decision: The court held the defendants liable to pay.

The court observed: "...if the defendants were not bound by their offer when accepted by the claimant until the answer was received, then the claimant ought not to be bound until after they had received the notification that the defendants had received the answer and assented to it. And, so there will be no end to this".

It was therefore decided that the contract was made when the acceptance was posted, regardless of the fact that the letter of acceptance was lost or not received.

b) **Where acceptance is through postal services:** The general rule is that acceptance is complete as soon as the letter is posted, provided post is a reasonable method of communication. An acceptance by post is a well-established exception to the general rule that acceptance must be communicated.

SYNOPSIS

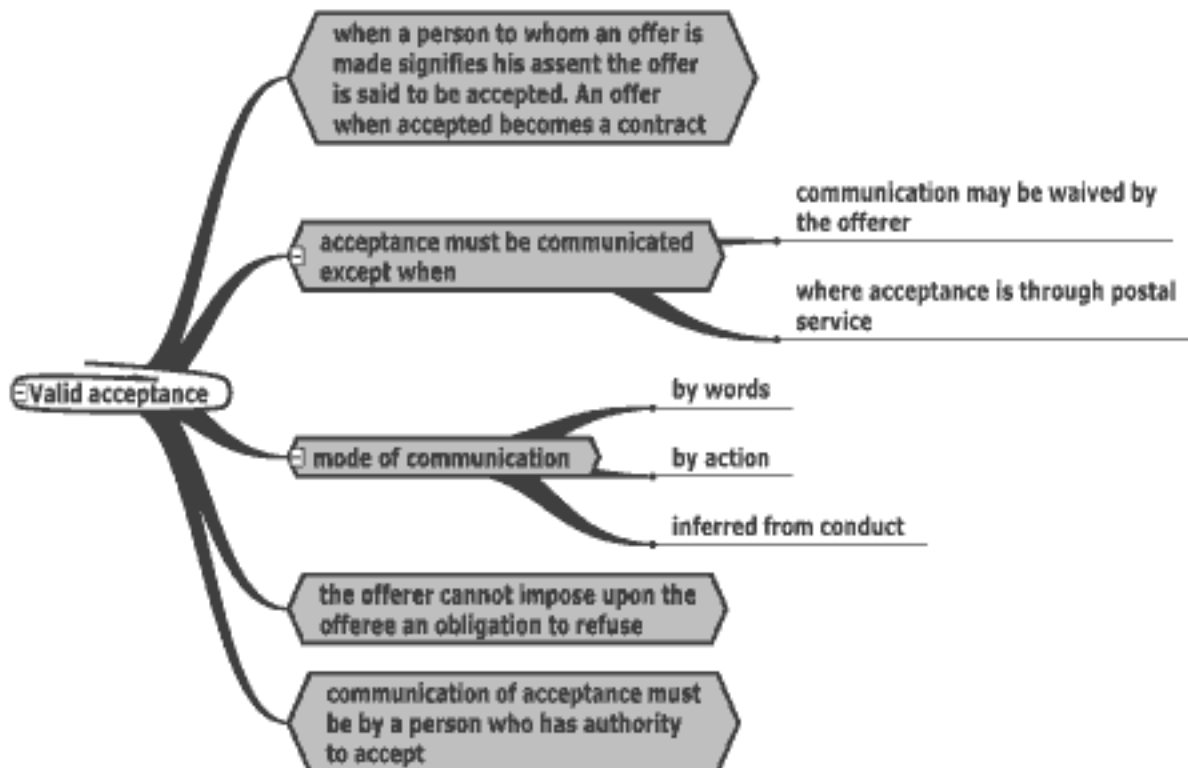
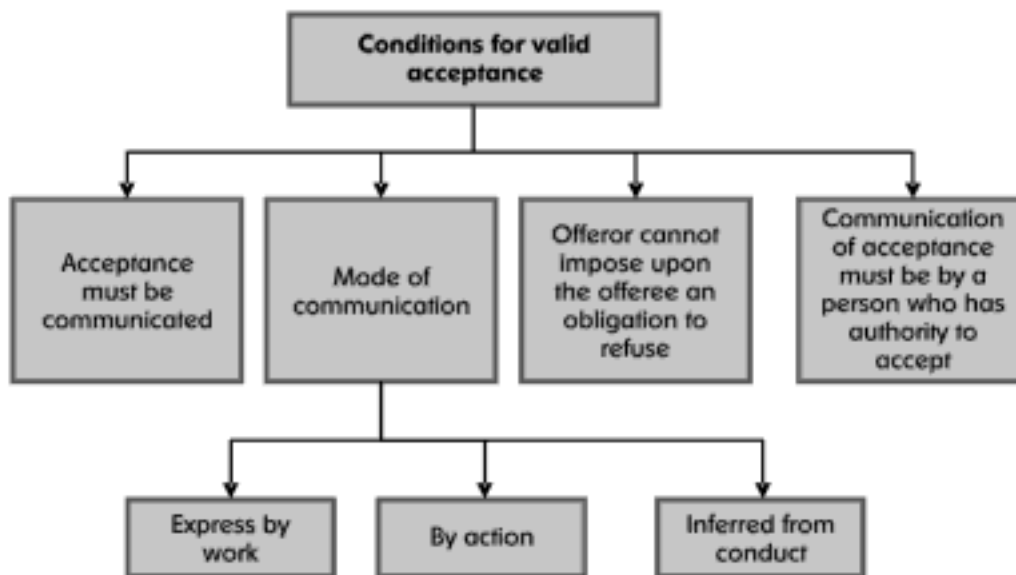
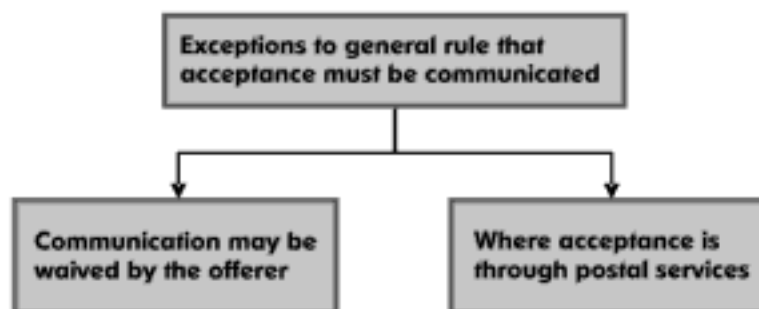


Diagram 6: Conditions for valid acceptance**Diagram 7: Exceptions to general rule that acceptance must be communicated****3.3. Some other important points**

1. **Conditional contracts:** A conditional contract is a contract to do or not to do something, if any stipulated condition stated in the contract, does or does not happen.

Important elements of conditional contract

a) A valid contract that is currently being contemplated is a conditional contract.

Example

A buyer places a condition that the car (he wishes to buy) must pass a mechanical check before he will purchase it.

Therefore the passing of the mechanical check is the condition without which this contract cannot take place. If the car fails to pass the mechanical check the buyer can choose to cancel the contract. Any deposit that has been paid will have to be refunded.

- b) Such a contract becomes due for performance either on
- i. The occurrence of a future event or

Example

Roger offers to sell his sports car to Bali if Bali wins a car race. Here, the performance by Roger (selling his car) will become due when Bali wins the car race.

- ii. The non-occurrence of a future event.

Examples of conditional contracts

- **Contract of insurance:** The insurer is liable to pay the damages to the insured only when the insured suffers damages to the insured property. The causing of damages is the condition attached for the payment of sum assured by the insured.
 - **Contract of life insurance:** The sum assured under a life insurance contract is payable to the nominee of the insured only on the death of the person insured. The death of the person insured is the condition stipulated for the payment of the sum insured.
2. **Collateral contracts:** A collateral contract is a contract which requires some other contract for its fulfilment. A collateral contract may be between one of the parties and a third party.

Example

There are two separate contracts: one between A and B and the other between A and C. The terms of both the contracts require some action between B and C and hence there may be a contract between B and C.

The case study given below will help you to understand this.

Case Study**Collateral contracts****Shanklin Pier Ltd v Detel Products Ltd (1951)**

In this case, the defendant gave assurances to the claimant that their paints would be satisfactory and durable for repainting the claimant's pier. The pier company, relying upon representations made by the defendant, the paint manufacturer, specified a particular type of paint for the redecoration and protection of their pier. The redecoration work was carried out by a painting contractor who purchased paint from Detel Products. When the product later proved to be defective and failed, the contractor pointed out that the particular type of paint was specified by the pier company itself and he only complied with the pier company's specification.

The defendant (Detel Products Ltd) argued that they had not supplied paint to the claimants (Shanklin Pier Ltd) under a purchase agreement. As there was no contract with Shanklin Pier, they could not therefore recover damages.

Court's decision: However, the court decided that collateral to the redecoration contract, there was an implied agreement between the claimant and the defendant. Owing to this implied agreement, the choice of the defendant's product was made in response to their (false) representations as to its suitability.

Shanklin Pier Ltd therefore recovered damages for breach of this collateral undertaking on the part of the paint supplier.

3. **Unilateral contract:** A contract where one party promises a reward or action in return for some desired action on the part of the second party is called a unilateral contract. In this case the offeror cannot revoke the contract once the offeree has started executing the action. *Errington v Errington (1952)*

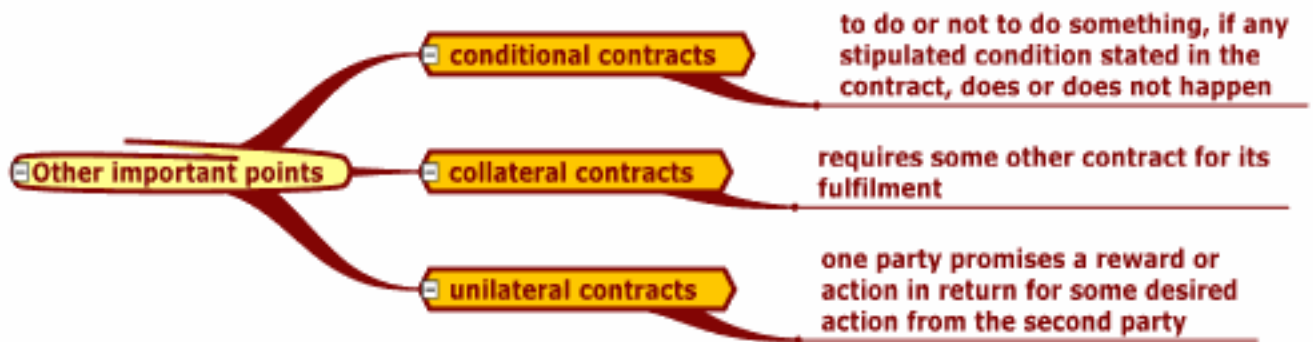
Example

In *Carlill v Carbolic Smoke Ball Co* (1893), the company promised to pay £100 to anyone who caught influenza after using their product. There was no force to buy the product. However, once any person bought it and started using it the company was bound by its promise.

Test Yourself 11

Explain the following terms:

- A unilateral contract
- The rules relating to acceptance of an offer

SYNOPSIS**4. Explain the need for consideration****[Learning outcome d]****4.1 What is consideration?**

Another essential element of a contract is the consideration. Consideration, in simple terms is a reasonable equivalent or other valuable benefit passed on by the contractor to the contractee. We will discuss the need for consideration, the adequacy and sufficiency of consideration in this section.

1. Need for consideration

Consideration is necessary for the formation of every contract. An agreement can take the form of a contract only when it is made by the free consent of parties competent to contract, for a lawful consideration and with a lawful object. Therefore consideration is one of the essential ingredients of a contract.

Example

Alan promises to give Baron £100. Baron has to give nothing in return. As there is no consideration, this is a gratuitous promise and not legally enforceable.

2. Meaning of consideration**Definition**

The term 'consideration' has been defined as:

"A valuable consideration in the eye of law may consist either in some right, interest, profit, or benefit accruing, to one party, or some forbearance and detriment, loss or responsibility given, suffered or undertaken by the other".

From *Currie v Misa* (1875)

"An act or forbearance of one party, or the promise thereof, is the price for which the promise of the other is bought, and the promise thus given for value is enforceable".

From *Dunlop v Selfridge* (1915)

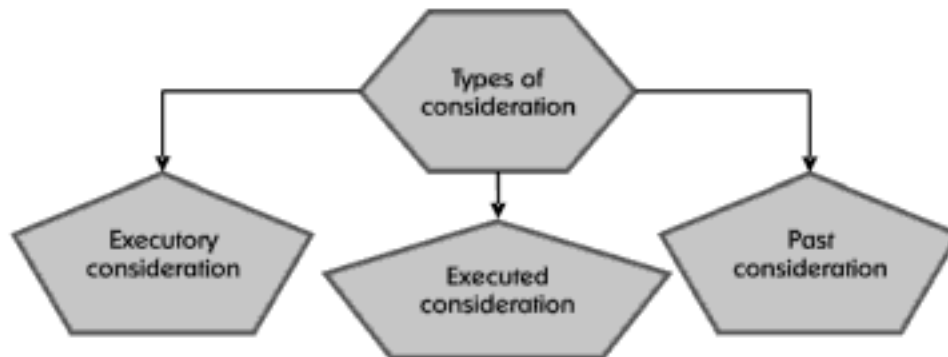
Consideration simply, is the price paid for the promise. **Consideration need not be in the form of money only.** It can be in any form such as rights, interest, profits or benefits. Some of the examples of consideration are:

- The giving of employment
- Permitting goods to remain in the promisor's possession.
- The assignment of contract
- The guarantee of an overdraft

Consideration may also be forbearance, detriment, loss or responsibility suffered, or undertaken by the promisee.

3. Types of consideration

Diagram 8: Types of consideration



Consideration can be divided into the following three categories:

- Executory consideration:** This is a **promise** to perform an action in return **of a promise**, at some future time.

Example

- Omar promises to do some work in return for a promise of payment.
- Shopkeeper's promise to supply the goods and customer's promise to accept the goods and pay.

In the above examples, neither party has yet done any act but each party has given a promise in order to obtain the promise of the other person. It would be a breach of contract if either party withdrew from his / her promise without the consent of the other.

- Executed consideration:** This is an **act in return for a promise**. The promise only becomes enforceable when the offeree has actually performed the required act.

Example

- Richard loses his wallet and offers Bogdan a reward if he finds and returns the lost wallet. It is only when Bogdan finds the wallet and duly returns it to Richard that the reward becomes enforceable and the consideration becomes valid.
- **In Carill v Carbolic Smoke Ball Co's case**, Mrs. Carill's act of using the smoke ball for the prescribed period in response to the company's promise of reward **was therefore executed consideration**.

- Past consideration:** Such consideration, actually, is **not regarded as a valid consideration**. Usually, consideration is provided either at the time of the creation of a contract or at a later date.

Case Study**Past consideration is no consideration at all.****Re McArdle (1951)**

In this case, according to the will of the father a certain number of children were entitled to a house after the death of their mother. In the mother's lifetime one of the children and his wife lived in the house with the mother. The wife made some improvements in the house during this period. All the children subsequently undertook in writing to pay a sum of £488 to the said wife in consideration of her carrying out the improvements. But at the mother's death they refused to pay her any thing.

Court's decision: It was held that the said promise was without consideration for the obvious reason that improvements to the house had been completed before the document containing the promise were signed. Thus, it was a past consideration which is no consideration at all.

In the case of a past consideration, however, the **action is performed before the promise**. So it cannot become the consideration for the promise. Since past consideration arises out of a promise "**subsequent to and independent of the transaction**", it is considered to be no consideration at all.

Exceptions to the rule that past consideration will not support a valid contract are as follows:

- i. Under s.27 of the Bills of Exchange Act 1882, "past consideration can create liability on a bill of exchange (such as cheque)".

Example

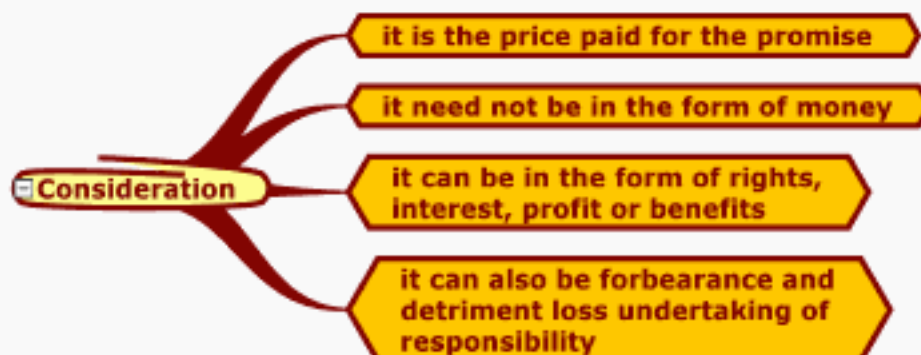
Robert mows Mike's lawn and a week later Mike gives Robert a cheque for £10. Robert's work is valid consideration in exchange for the cheque.

- ii. Under s.29 of the Limitation Act 1980, "a time barred debt becomes enforceable again if it is acknowledged in writing".
- iii. Where the claimant performed the action at the request of the defendant and payment was expected, then any subsequent promise to pay will be enforceable. An illustrative case on this point is:

Case Study**Past consideration .****Lampleigh v Braithwaite (1615)**

In this case, the defendant had killed a man and had asked the claimant to obtain royal pardon for him. The claimant did so at his own expense. The defendant then promised to pay him £100. He failed to pay and was sued.

Courts decision: It was held that there was an implied promise to pay and the subsequent promise merely fixed the amount. Hence the consideration (to obtain royal pardon) was valid.

SYNOPSIS



4. Rules relating to consideration

Along with the past consideration rule, some other rules that govern the legal definition and operation of consideration are:

1. **An act, abstinence or promise to be a good consideration, must be something more than what the promisor is already bound to do:** to do something which a person is already bound to do, is not a good consideration. A person may be bound to something in the following two ways:

a) By law

For example, performance of a legal duty is no consideration for a promise.

Case Study

Act, abstinence or promise to be a good consideration, by law

Collins v Godfrey (1831)

In this case, the claimant had been summonsed to give evidence on behalf of the defendant in a case. He argued that the defendant had promised to pay him six guineas for appearing before the court.

Courts decision: There was no consideration for this promise as appearing before the court to give evidence is the duty imposed by statute.

However, when a person has done something more than what he was bound to do by law, then that would be a good consideration.

Case Study

If an act is performed over and above that required by law or public duty, that act is sufficient consideration for a promise.

Glassbroke Brothers Ltd v Glamorgan County Council (1925)

In this case, due to a strike in the colliery, a colliery manager requested police protection for his colliery. Rejecting the view of the police that a mobile force was enough, the manager agreed to pay for a special guard at the mine. Later, he refused to pay arguing that the police were already bound to protect the life and property of persons and had done no more than perform their public duty of maintaining order.

Courts decision: The court pointed out that the police were bound to protect the life and property of the public. However, if any person wanted any special kind of protection (which was usually not provided for by the police) then the person concerned must pay for it.

b) By contract

A person may also be already bound to do something under a pre-existing contract. This pre-existing contract may be:

- i. With the third party or
- ii. With the promisor himself.

i. Pre-existing contract with the third party

If Julie promises Millie a reward if Millie performs her existing contract with Lilly, then Julie is entitled to some right for which she was previously not entitled and Millie is under a new obligation. **Here the question arises of whether a promise for the performance of an existing duty constitutes a good contract?**

The case study given below is a good example to understand this concept.

Case Study

Pre-existing contract with the third party

Shadwell v Shadwell (1860)

In this case, the claimant had promised to marry a girl. The claimant's uncle (the defendant), in consideration of his intended marriage with the said girl, promised, in a letter, to pay him (the claimant) £150 yearly during his (i.e. the uncle's) life or until the claimant's income as a practising lawyer increased to 600 guineas. The claimant married the girl. His annual income never increased to 600 guineas. The annuity fell into arrears as the uncle died. The claimant filed a suit to enforce the said promise.

Courts decision: It was held that entering into the marriage was **sufficient consideration** for the uncle's promise, even though the claimant was already contractually bound to his fiancée. The uncle received benefit from the marriage taking place (in his capacity as a close relative), and the nephew was therefore entitled to the arrears of the promised annuity.

ii. Pre-existing contract with the promisor himself

A promise to do a particular thing which the promisee is already bound to do under a pre-existing contract with the promisor will not constitute a good consideration.

Example

In **Pinnel's case (1602)**, it was held that if a debtor pays a smaller sum in satisfaction of a large sum, it will not be regarded as a good discharge of the debt because the debtor was already bound to pay the whole amount. The payment of a lower debt for a larger sum is not a good discharge of debt; it is against ethical commercial practices. Hence it is considered a part payment, not a full payment.

2. **Consideration must be sufficient but need not be adequate:** the court will **not inquire into the 'inadequacy of consideration'**. This means:

- i. They will not seek to measure the comparative value between the defendant's promise and of the act or promise given by the claimant in exchange for it
- ii. They will not denounce the agreement merely because it seems to be unfair

It is presumed that each party is capable of serving his / her own interests. The courts will not seek to weigh the comparative value of the promises or acts exchanged.

The court will not intervene and require equality in the value exchanged as long as the agreement has been freely entered into.

Case Study

Consideration need not be adequate.

Thomas v Thomas (1842)

In this case, by his will, the claimant's husband expressed his wish that his widow should be allowed to use his house during her lifetime. The executors of the husband's will promised to let his widow live in his house, in return for rent of £1 per year. However, they later said that their promise to let her occupy the house was not supported by consideration.

Courts decision: It was decided that £1 was **sufficient consideration to validate the contract**, although it did not represent an adequate rent in economic terms.

3. **Sufficiency of consideration:** Consideration is sufficient if it has some identifiable value. The law only requires an element of bargain, not necessarily that it should be a good bargain.

Example

In **Chappell & Co v Nestle Co (1959)** Nestle offered a record to customers who sent a certain number of chocolate bar wrappers. It was held that a used chocolate wrapper was consideration sufficient to form a contract, although it had no economic value whatsoever to Nestle and was in fact thrown away after it was returned to them.

4. **Performance must be possible:** A binding valid contract cannot be framed if the consideration is the promise to perform an act that is clearly impossible.

Promise to perform an impossible act cannot form the basis of a binding contractual agreement.

Example

- Aurelia agrees to pay Benedict £1,000 if Benedict will marry Aurelia's daughter Claudia. Claudia was dead at the time of the agreement. The agreement is void.
- Ahmed agrees to pay Burquah £1,000 if two straight lines enclose a space. The agreement is void.
- Harry promises to bring a dead body back to life for £100,000. This is impossible hence void

5. **Promissory Estoppel:** The doctrine of promissory estoppel prevents one party from withdrawing a promise made to the second party **if the latter has relied on that promise and acted upon it.**

In law, a promise made without consideration is generally not enforceable. It is known as a bare or gratuitous promise.

Example

If a car salesman promises not to sell a car until the weekend, but does so, the promise cannot be enforced against him. But should the car salesman accept even one penny in consideration for the promise, the promise will be binding and enforceable in court.

Case Study**Promissory Estoppel****Central London Property Trust Ltd v High Trees House Ltd (1947)**

In this case, the claimants leased a block of flats to the defendants in 1937 at an annual rent of £2,500. However, the defendants were unable to find enough tenants during WWII. Therefore they agreed to accept a reduction in rent to £1,250.

There was no consideration for this promise to accept a lower rent.

At the end of the war the flats were again fully let. The claimants wanted to return to the terms of the original agreement. They claimed the full rent (£2,500) for the future period. They also wanted to recover the rent lost during the war time period when they received only half rent.

Courts decision: It was held that the claimants were entitled to the full rent from the end of the war. However, they were stopped from claiming the rent lost during the wartime period

Estoppel is an exception to this rule.

Estoppel is "a shield not a sword" – it cannot be used as the basis of an action on its own. It can be used in defence by a party sued and cannot be used as a cause of action. It also does not extinguish rights.

Example

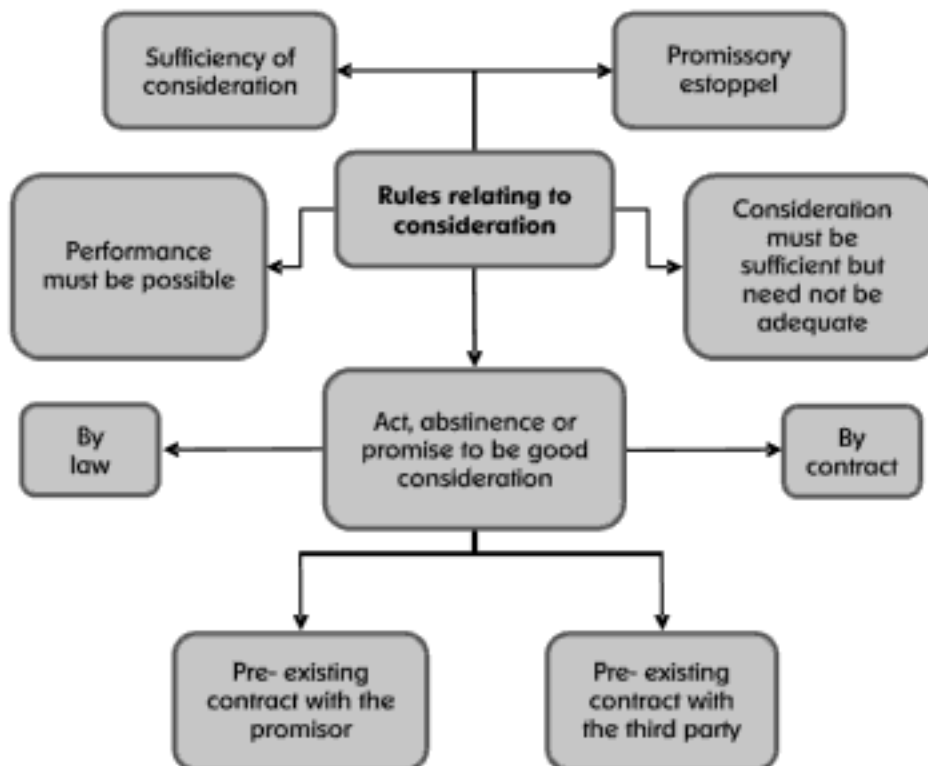
In **Combe v Combe**, the court refused to allow using estoppel as a "sword" by an ex-wife to extract funds from the destitute husband.

If a payment is made early then there is consideration for the promise and it is binding. Estoppel can be raised if a party agrees to accept a smaller amount and then changes his mind.

Test yourself 12

Which of the following is false?

- a) Consideration must be real
- b) Consideration must have some identifiable value
- c) Consideration can be inadequate
- d) A promise to do something which one is already bound to do by law, will be treated as good consideration

Diagram 9: Rules relating to consideration**Test Yourself 13**

Define consideration.

Test Yourself 14

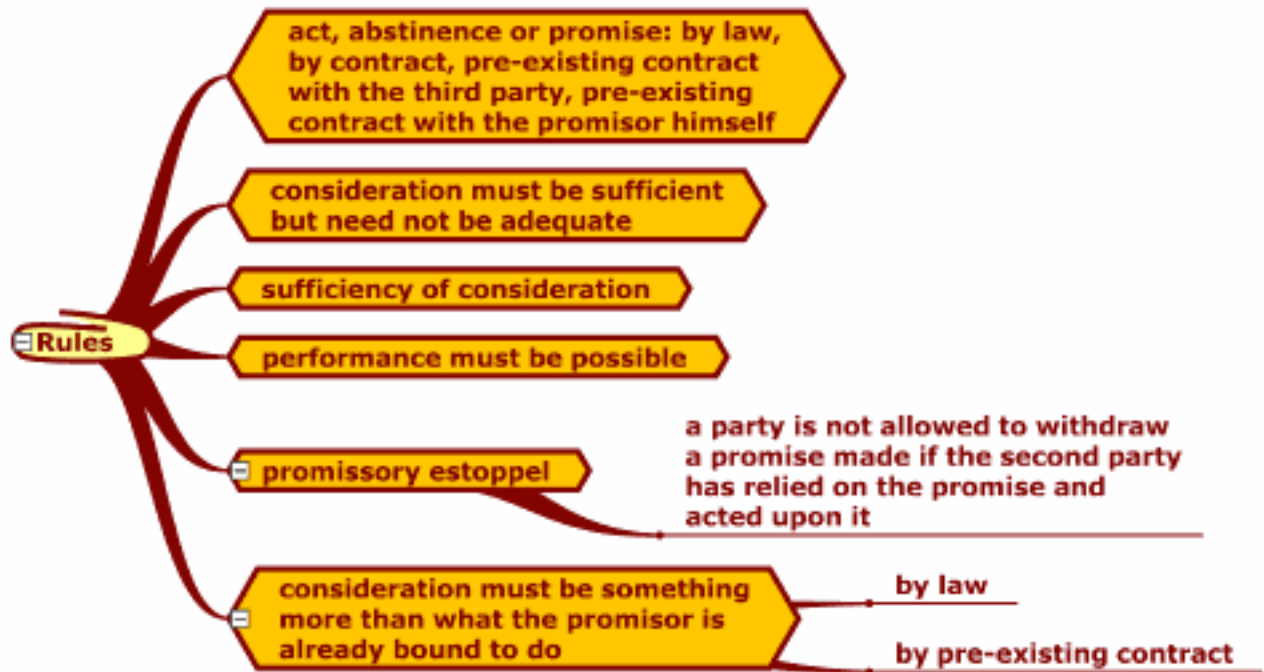
Explain and distinguish between the following terms:

- i. Executory consideration
- ii. Executed consideration
- iii. Past consideration

Test Yourself 15

Alan offered to pay Tom a sum of £50 if Tom dry-cleaned Alan's suit. Alan subsequently lost his baggage, including his suit, at the hotel. Alan then offered a reward of £100 to Greg to find the suit. Greg found the suit and returned it to Alan who later gave it to Tom to dry-clean. Tom dry-cleaned the suit and handed it back to Alan.

State with explanation which of the above considerations is executory consideration and which is executed consideration.

SYNOPSIS**5. Analyse the doctrine of Privity****[Learning outcome e]**

The general rule is that, parties to a contract alone can sue and be sued on the contract. Any person other than the parties to contract is a "stranger to the contract". A contract neither confers any rights nor imposes any duties / obligations on such a person.

The principle of privity states that a **person with whom a contract is made is only able to enforce it because he had given the consideration to the promisor. A third party has no right of action except in certain exceptional instances.**

Example

Yen Yen promises to pay Chang £1,000 if Chang gives his car to Lee. In this case, Lee cannot enforce Chang's promise, because he has not provided the consideration for the promise.

Lee is a stranger to the contract between Yen Yen and Chang.

Case Study

Privity of contract

Tweedle v Atkinson (1861)

In this case, on the occasion of marriage of A (claimant) and B, their respective fathers entered into a contract to pay money to A. When one of the parents died without having made the payment, A (claimant) tried to enforce a contract against his estate.

Courts decision: It was held by the court that a stranger to the consideration cannot take advantage of a contract although made for his benefit. It was held that A (claimant) could not enforce the contract, as he personally provided no consideration for the promise.

Another important case study on privity of contract:

Case Study

Privity of contract

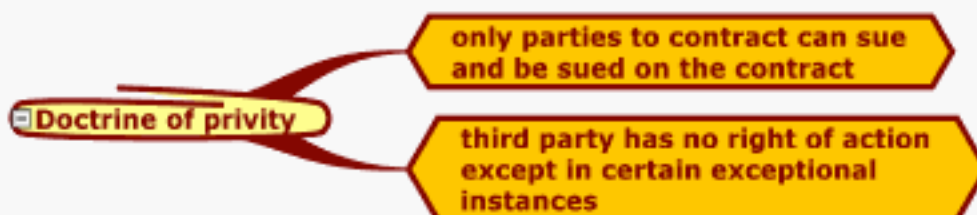
Dunlop Pneumatic Tyre Co Ltd v Selfridge and Co Ltd (1951)

In this case, Dunlop sold tyres to a distributor: Dew and Co. Dunlop instructed the distributor not to sell the tyres and the tubes below the listed price. They were also told to take a similar undertaking from anyone to whom they supplied the tyres.

Dew and Co sold the tyres to Selfridge, who agreed to abide by the restrictions and pay Dunlop £5 for each tyre they sold below the listed price. When Selfridge sold tyres below Dunlop's listed price, Dunlop sought to recover the promised £5 per tyre.

Courts decision: It was held by the court that Dunlop could not recover damages on the basis of the contract between Dew and Co and Selfridge.

Dunlop was a third party hence not entitled to enforce the contract.

SYNOPSIS**5.1 Exceptions to the rule of privity of contract****1. Common law exceptions**

There are exceptions to the general rule that a third party cannot enforce a contract. These exceptions allow the rights to the third parties to enforce the contract. These are:

- a) **Beneficiary sues in some other capacity:** Although a beneficiary cannot sue in his personal capacity because he was not a party to the contract, he can sue in some other capacity e.g. as an executor of a deceased person.

Case Study

Exceptions to the rule of privity of contract

Beswick b Beswick (1966)

In this case, a nephew bought his uncle's coal business. One of the terms was that the nephew would pay support to the uncle's wife upon the uncle's death. When the uncle died, the nephew stopped paying the widow. The widow sued.

Courts decision: The widow was able to sue, not personally, but as an executor of the uncle's estate and on his behalf (the uncle, of course, having been a party to the contract). 'Where a contract is made with A for the benefit of B, A can sue on the contract for the benefit of B and recover all that B could have recovered if the contract had been made with B himself.'

- b) **Collateral Contracts:** This is a contract between the third party and one of the contracting parties. This has been explained at section 3.3 (b) above.
- c) **Beneficiary under the trust:** There are usually three parties to the trust.
- i. **Author of the trust:** The person creating the trust is the author of the trust.
 - ii. **Beneficiary of the trust:** The person for whose benefit the trust is created is the beneficiary.
 - iii. **Trustee:** The person who is entrusted with the trust property and to execute the trust is called the trustee.

The beneficiary is not a party to the agreement creating a trust. However, he is the person for whose benefit the trust is created. Therefore, the beneficiary of a trust may sue the trustee to carry out the contract.

Example

Jackson formed a trust of his property for the benefits of his daughter Angelina. He appointed Thomas as the trustee of the trust.

Peter, the manager of the trust, misappropriated some of the property of the trust. Thomas refused to file a suit against the manager for misappropriation of trust property.

Here,
Jackson is the author of the trust.
Angelina is the beneficiary.
Thomas is the trustee.

The trust agreement was created between Jackson and Thomas. However, Angelina is the beneficiary of the trust. If Thomas refuses to sue, she can sue the manager for misappropriation of trust property.

- d) **Contract entered into through agent:** The principal can enforce the contracts entered into by his agent provided the agent has acted in the name of the principal and within the scope of the principal's authority.

Example

Vivian appointed John as her agent. John entered into a contract with Toby to sell goods from Vivian's factory for £50,000. Toby paid an advance of £30,000.

Meanwhile, Vivian terminated her agency with John. Toby refused to pay the balance amount.

Here, Vivian (the principal) can enforce the contracts against Toby entered into by her agent (John).

- e) **The assignment of rights:** Assignment is a process by which the rights of one person are transferred to another person. The person **assigning the rights is called the assignor** and the person **to whom the rights are assigned** is called the **assignee**.

After assignment, the assignee is entitled to exercise all the rights which could have been exercised by the assignor previously, even though the assignee was not a party to the contract as originally made.

Example

Ram and Vijay were partners. Vijay assigned his partnership rights to his brother Ajay. Ram uses the partnership's money for his personal use. Here, **Ajay is entitled to recover** the partnership money **from Ram**.

Although, Ajay was not a party to the partnership agreement, Vijay has assigned him Vijay's rights in partnership. Therefore, **Ajay (the assignee)** is entitled to exercise all the rights which could have been exercised by the assignor (Vijay) previously.

2. Statutory exception

In some cases the doctrine of privity is justified by statute.

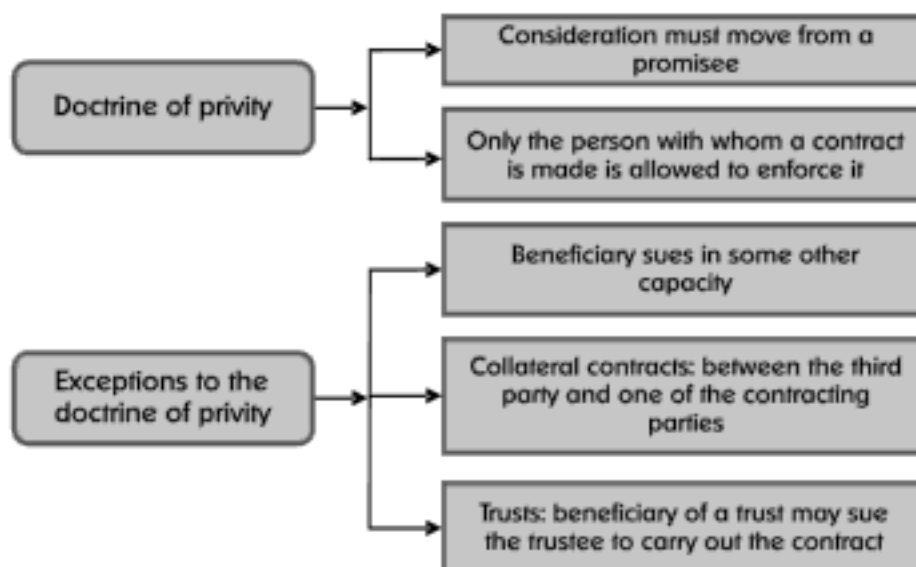
Example

In relation to car insurance a third party can claim directly against the insurers of the party against whom they have a claim in respect of damages.

The provisions of the Contracts (Rights of third parties) Act 1999 set out various **circumstances in which a third party can enforce the terms** of a contract:

- i. For the enforcement of a third party right, the contract in question must confer such right on them or it must have been made for their benefit.
- ii. The contract must specify the identity of the third party either by name or by a specific description or as a member of particular class of persons.
- iii. It is not necessary that the third person must be in existence, when the contract was made. Therefore it is possible to make the contracts for the benefit of unborn children.

The act also provides that where the third party has rights by virtue of this Act, unless the original contract contains an express term to that effect, the original parties to the contract cannot in any way rescind or vary the terms without the consent of third party.

Diagram 10: Doctrine of privity**Test Yourself 16**

Explain the principle of doctrine of privity and state the exceptions to this rule.

SYNOPSIS



6. Distinguish the presumptions relating to intention to create legal relations

[Learning outcome f]

6.1 In ordinary **commercial contracts**, there is a strong presumption that the parties to the contract have an intention to enter into a legally binding relationship. However, this presumption is rebuttable if:

1. Legal binding is expressly disclaimed in the contract or
2. The circumstances indicate that there is no intention to be bound legally by the contract.



Case Study

Presumption relating to intention to create legal relations

Rose and Frank Co v Crompton Brothers (1923)

In this case, the defendant (a British company) agreed to make the claimant (an American company) its sole vendor in America. The agreement included a clause stating that the document was not a formal one and was not subject to legal jurisdiction in either country.

Subsequently, when the defendant terminated the agreement after notice, the claimant brought an action for damages for the breach of contract and for delivery of goods.

Courts decision: It was held that the documents were not legally binding and consequently the breach of its terms did not give rise to any cause for action.

The court, however, held that where the orders had already been placed, there was a binding contract and the claimant would be entitled to the delivery of goods. The claim for damages for breach of agreement failed, but the claim for damages for non-delivery of goods ordered was upheld.

6.2 In **domestic and family arrangements** there is a presumption that there is no intention to create legal relations. (**Balfour v Balfour (1919)**)

However, the intention not to create legal relations in such relationships is only a presumption. It may be rebutted by the actual facts and circumstances of a particular case.

Case Study

Presumption relating to intention to create legal relations

Merritt v Merritt (1970)

In this case, the husband left the matrimonial home, which was jointly owned by the husband and the wife. The husband met the wife after that and promised to pay her £40 per month, from which she undertook to pay the outstanding mortgage on their house. The wife made the husband sign a note stating these terms and an undertaking to transfer the house into her name when the mortgage had been paid off. The wife paid off the mortgage but the husband refused to transfer the house in her name.

Courts decision: It was held that an agreement was enforceable because the circumstances of the case clearly indicate that the parties had an intention to enter into a legally binding contract.

SYNOPSIS



Test yourself 17

Distinguish the presumptions relating to intention to create legal relations.

Answers to Test Yourself

Answer 1

The contract, prima facie, appears to be a valid contract. However, the contract can be held void if Sunny proves that:

1. At the time of making the contract, his mind was so affected that he was incapable of understanding the nature of his actions.
2. The other party i.e. Bobby either knew or ought to have known of his disability.

In any case, however, Sunny must pay a reasonable price for the work done by Bobby.

Answer 2

Perhaps not, because this is a transaction in the ordinary course of business, because:

1. The relationship between Brown and the banker is not of such a nature that the banker can dominate the will of Brown.
2. The banker has not used any influence.
3. Signing loan documents on agreed terms is a usual business practice.

Answer 3

This depends on whether the two parties in question had the intention to enter into a legal relationship when they made their promises. If the promises were made casually on a social occasion, the law would presume that the parties had no such intention. If this presumption can be rebutted and the intention to enter into a legal relationship can be proved, then the agreement would be legally enforceable.

Answer 4

Yes, as the relationship between the attendant and patient is such that the patient may be affected by undue influence. This is because a patient is physically and psychologically dependent on his attendant to look after him and finds himself handicapped without him. He fears that if the amount demanded by him is not paid, the attendant may not work for him or will become less concerned.

Answer 5

This is not valid as the agreement was vitiated under duress.

Answer 6

No, because the object of the contract is unlawful. Hence this contract is illegal.

Answer 7

Correct answer is (c). 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. The relationship of landlord and tenant does not raise the presumption of undue influence.

Answer 8

Basis of distinction	Offer	Invitation to treat
Meaning	It signifies the intention or willingness of a person to enter into a contract	Where a person invites others to make an offer to him, such invitation is not an offer but only an "invitation to treat"
Purpose	An offer is made to obtain acceptance of another person	An invitation to treat is made to obtain an offer from another person.
Legal effect	An offer, if accepted by the other person, results in a "contract"	An invitation to treat if accepted by the other person, results in an "offer"
Status	It is a proposal prior to acceptance	It precedes an offer

Answer 9

The valid offer is the offer in option (e) as there is an offeror (Julie) and an offeree (Lilly). Julie is offering the car as consideration and Lilly will pay £4,000 as consideration. Hence the elements of an offer are complete.

Options (a), (b), (c) and (d) are examples of invitation to offer, as they have not been made to ascertained people and most of the options are vague.

Answer 10

Revocation: Revocation refers to the cancellation of an offer and occurs when the offeror withdraws the offer. The rules relating to revocation are as follows:

- i. An offer may be revoked at any time before acceptance. However, once revocation has occurred, it is no longer open to the offeree to accept the original offer.
- ii. Revocation is not effective until it is actually received by the offeree. This means that the offeror must make sure that the offeree is made aware of the withdrawal of the offer, otherwise it might still be open for the offeree to accept the offer.
- iii. Communication of revocation may be made through a reliable third party. Where the offeree finds out about the withdrawal of the offer from a reliable third party, the revocation is effective and the offeree can no longer seek to accept the original offer.

Answer 11

- a) A contract where one party promises a reward or action in return for some desired action on the part of the second party is called a unilateral contract. In the case of such contracts, the offeree cannot revoke the contract once he has started executing the action.

For e.g., in **Errington v Errington (1952)** a father promised his son and daughter in law that he would give the ownership of the house to them if they paid off the outstanding mortgage. After the father's death, his widow sought to revoke the promise. It was held by the court that the promise cannot be withdrawn as the payments were made regularly.

- b) **Acceptance:** Acceptance is necessary for the formation of a contract. Once the offeree has accepted the terms offered, a contract comes into effect and both the parties to the contract are bound by the contract. Thereafter the offeror cannot withdraw his offer, nor can the offeree withdraw his acceptance.

Rules relating to acceptance:

- i. Acceptance must correspond with the terms of the offer. Therefore, the offeree must not seek to introduce new contractual terms into their acceptance.
- ii. A counter-offer does not constitute acceptance (*Hyde v Wrench*). Also, a conditional acceptance cannot create a contract relationship.
- iii. Acceptance may be in the form of express words, either oral or written or may be implied from conduct.
- iv. Generally, acceptance must be communicated to the offeror. Consequently, silence cannot amount to acceptance.

Where acceptance is communicated through the postal service then it is complete as soon as the letter, properly addressed and stamped, is posted. The contract is concluded even if the letter subsequently fails to reach the offeror.

However the postal rule will only apply where it is in the contemplation of the parties that the post will be used as the means of acceptance.

If the parties have negotiated either, face to face, in a shop, for example or over the telephone, then it might not be reasonable for the offeree to use the post as a means of communicating their acceptance and they would not gain the benefit of the postal rule.

Answer 12

(d) is false whilst the others are all true.

Answer 13

Consideration is one of the basic elements for the formation of the contract. Without consideration an agreement cannot be enforced and be a binding contract.

The term 'consideration' has been defined as:

"A valuable consideration in the eyes of law may consist either some right, interest, profit, or benefit accruing, to one party, or some forbearance and detriment, loss or responsibility given, suffered or undertaken by the other". **From Currie v Misa (1875)**

"An act or forbearance of one party, or the promise thereof, is the price for which the promise of the other is bought, and the promise thus given for value is enforceable". **From Dunlop v Selfridge (1915).**

Answer 14

Consideration can be divided into the following categories:

- i. **Executory consideration:** it is the promise to perform an action at some future time. One party to a contractual agreement may pay money to another on the understanding that the latter will perform some act for them in the future.
- ii. **Executed Consideration:** this is an **act in return for a promise**. The promise only becomes enforceable when the offeree has actually performed the required act.
- iii. **Past Consideration:** normally consideration is provided either at the time of the creation of a contract or at a later date. In the case of past consideration, however the action done is performed before the promise. Such prior action is not deemed sufficient to support the later promise.

In **Re McArdle (1951)**, according to the will of the father a certain number of children were entitled to a house after the death of their mother. In the mother's lifetime one of the children and his wife lived in the house with the mother. The daughter-in-law made some improvements in the house during this period. All the children subsequently undertook in writing to pay a sum of £488 to the said wife in consideration of her carrying out the improvements. But at the mother's death they refused to pay her any thing.

It was held that the said promise was without consideration for the obvious reason that improvements to the house had been completed before the document containing the promise was signed. Therefore, it was a past consideration which is no consideration at all.

Answer 15

1. Executory consideration is the promise to perform an action at some future time. One party to a contractual agreement may pay money to another on the understanding that the latter will perform some act for them in the future.

In the given case, consideration of £50 by Alan to Tom is executory consideration as it is payable when Tom dry-cleans Alan's suit and returns it to Alan.

2. Executed Consideration is an **act in return for a promise**. The promise only becomes enforceable when the offeree has actually performed the required act.

In the given case, the consideration of £100 promised by Alan to Greg is the executed consideration. Because it is payable only when Greg finds Alan's suit and duly returns it to Alan.

Answer 16

According to this principle, consideration must move from a promisee. A person with whom a contract is made is only able to enforce it as consideration must have been given by him to the promisor. A third party has no right of action except in certain exceptional instances.

Exceptions to the rule of privity of contract:

There are exceptions to the general rule, allowing the rights to third parties and some impositions of obligations. These are:

- a) **Beneficiary sues in some other capacity**
Although, a beneficiary cannot sue in his personal capacity because he was not a party to contract, he can sue in some other capacity e.g. an executor of a deceased person.
- b) **Collateral Contracts**
Between the third party and one of the contracting parties
- c) **Trusts**
The beneficiary of a trust may sue the trustee to carry out the contract.
- d) **Statute**
In some cases the doctrine of privity is justified by statute. For e.g., in relation to car insurance, a third party can claim directly against the insurers of the party against who they have a claim in respect of damages.

Answer 17

In ordinary **commercial contracts**, there is a strong presumption that parties to contract **have intention to enter into a legally binding relationship**.

However, this presumption is rebuttable if

- a) Binding by legal relations is expressly disclaimed in the contract or
- b) The circumstances indicate that there is no intention to be bound legally by the contract.

In **domestic and family arrangements** there is a presumption that there is no intention to create legal relations

However, this presumption may be rebutted by the actual facts and circumstances of a particular case.

Quick Quiz**1. State true or false**

- a) All contracts are agreements but all agreements are not contracts.
- b) Every contract must be in writing.
- c) Acceptance may also be communicated by an unauthorised person
- d) Acceptance must be communicated in writing only.
- e) Contract without consideration is not enforceable.

2. Choose the correct option

- i. Communication of acceptance made by post is complete as against the offeror when the letter of acceptance
 - a) Reaches the offeror
 - b) Is posted to him
 - c) Is in transit
 - d) Is signed by the offeree
- ii. Under which of the following instances, does the offer automatically lapse?
 - a) If it is revoked by the offeror at any time before its acceptance
 - b) If the offeror or offeree dies
 - c) Upon failure to fulfill a condition precedent to acceptance
 - d) All of the above
- iii. Rani accepts Sunny's invitation to dinner by phone. This is not a contract because
 - a) Acceptance is given orally
 - b) There is no intention to create legal relations
 - c) There is no consensus between the two parties
 - d) None of the above
- iv. Alan took up the responsibility of providing education to Jessica who is a minor. Which of the following is true?
 - a) The contract is void
 - b) Alan can rescind the contract
 - c) Jessica is liable to reimburse Alan out of her property
 - d) Jessica is not liable to reimburse Alan and can claim exemption as she is minor

Answers to Quick Quiz

- 1.
 - a) **True**, because all agreements are not legally enforceable.
 - b) **False**, a contract can be written or oral or inferred from conduct of parties.
 - c) **False**, acceptance must be communicated by acceptor or his authorised agent or by a reliable third party.

- d) **False**, as acceptance can be in either of three ways:
- i. Acceptance by express words
 - ii. Acceptance by action
 - iii. Acceptance inferred from conduct

e) **True**.

2.

- a. Correct answer is (b)
- b. Correct answer is (d)
- c. Correct answer is (b)
- d. Correct answer is (c). A minor's estate is liable to a person who supplies necessities (both goods and services) to a minor. The provision of education falls under the category of necessary services.

Self Examination Questions

Question 1

An invitation to treat is not an offer: explain.

Question 2

All illegal agreements are void but all void agreements are not illegal: explain.

Question 3

Define consent. When can consent be said to be free consent?

Question 4

Alvin agrees to sell his car to Charley for £1,500. Is the contract valid?

Question 5

Distinguish between an agreement and a contract.

Question 6

Merry deals with antique sculptures. One morning, John approached Merry to sell her an antique piece in his possession for £20,000. Merry was willing to pay £12,000 only. John replied that he would sell it for £15,000. Merry then said that she needed some time to buy it for that price. John agreed not to sell the piece to any other person until Merry phoned him back in five days time with her final decision.

After sometime, John phoned Merry but as she was out he placed a message with her assistant that he was not willing to sell her the antique piece.

On the same evening, Merry met Lilly at a party and while talking to her Merry came to know that Lilly was looking for the same antique that John wanted to sell and she was willing to pay even £30,000 for that antique.

The next day, Merry called John to tell him that she was ready to buy the antique piece for £12,000. However, John informed her that he had already sold it to Sunny for £22,000.

Analyse the situation in relation to the provisions of law of contract.

Question 7

Ronny, a retail trader, displayed goods in his shop with prices marked on them. Kelly a consumer asked to sell the goods at the prices mentioned on the goods. Ronny refused to sell the goods at that price by saying the prices had increased. Kelly demanded that Ronny sold the goods for the displayed prices; otherwise she would sue Ronny for breach of contract.

Which of the following statement(s) is / are correct?

- Kelly can sue Ronny for breach of contract
- Display of prices on goods amounts to a valid offer
- Display of prices on goods amounts to an invitation to make an offer
- Refusal to sell the goods at the prices mentioned on them will amount to breach of contract.

Answers to Self Examination Questions

Answer 1

An invitation to treat is merely an **invitation** to others **to make offers**. It is **not an offer**.

An offer is made when one party proposes to another that it should **buy a particular item** on particular terms, including:

- the precise nature of the item,
- the price to be paid,
- the mode of delivery
- the date of payment etc.

An offer must not be confused with an invitation to treat. An invitation to treat is intimation by one party to another that:

- It may be willing to do business in relation to a particular article on particular terms and
- The other party, **if interested** should **make the first party an offer in relation thereto**.

Hence, an invitation to treat if accepted by the other party does not form a contract.

Examples of common situations involving invitations to treat are:

The display of goods in a shop window: the classic case in this area is *Fisher v Bell* (1961), in which a shopkeeper was prosecuted for offering offensive weapons for sale, by having flick-knives on display in his window. It was held that the shopkeeper was not guilty as the **display in the shop window was not an offer for sale but only an invitation to treat**.

The display of goods on the shelf of a self-service shop: in *Pharmaceutical Society of Great Britain v Boots Cash Chemists* (1953), it was held that the display of goods on the shelf was only an invitation to treat and that in law, the customer offered to buy the goods at the cash desk.

Answer 2

An agreement may become void due to various reasons, such as:

- Object is not lawful
- Contract terms are vague
- No consideration is provided by the parties
- Consent to contract was caused by duress, undue influence or misrepresentation.

Void agreements are not necessarily illegal, for e.g., the agreements, the terms of which are uncertain, are void but not illegal.

A void agreement does not involve any punishment. It also does not invalidate the collateral transactions and the law may enforce them. An illegal agreement not only vitiates the primary transaction but also any collateral transactions.

Illegal agreements are **void abinitio** (i.e. void from the beginning) but, at times, valid contracts may subsequently become void for certain reasons.

Answer 3

Free consent is one of the essentials of valid contract. 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:

- i. Duress
- ii. Undue influence
- iii. Fraud
- iv. Misrepresentation

Answer 4

Yes, because all the elements for valid contract are present.

- i. The contract is made because of the offer by Alvin and acceptance by Charley
- ii. The object (the ownership of car) is lawful
- iii. Charley's promise to pay £1,500 is the consideration for Alvin's promise to sell the car and Alvin's promise to sell the car is the consideration for Charley's promise to pay £1,500.

Answer 5

Basis of distinction	Agreement	Contract
Meaning	Offer when accepted becomes an agreement	An agreement enforceable by law is a contract
One in another	All agreements are not contracts	All contracts are agreement
Enforceability	An agreement may or may not be enforceable by law	All contracts can be enforced by law

Answer 6

The areas cover in this case study are offer, counter-offer, revocation of offer, communication of revocation of offer by a reliable third party, etc.

Offer and counter-offer

John offered Merry to sell a piece of antique for £20,000. Merry made a counter-offer to buy the antique for £12,000. This counter-offer by Merry resulted in termination of the original offer. Then John again offered to sell the piece for £15,000. This counter-offer by John resulted in rejection of Merry's offer of £12,000.

In **Hyde v Wrench (1840) case**, Wrench offered a price of £1,000 to sell his farm. Hyde offered £950, which Wrench rejected. Hyde then informed Wrench that he accepted the original offer of £1,000. But Wrench refused to sell the farm to Hyde. It was held that there was no contract. Hyde's **counter-offer** had terminated the original offer and therefore the original offer was no longer open for acceptance. Hyde was now making an altogether new offer to buy Wrench's land for £1,000, and it was for Wrench to decide whether to accept the offer or reject it. The offeror and offeree has replaced each other.

Revocation of offer and communication of revocation of offer by a reliable third party

An offeror may revoke an offer at any time before its acceptance. Once revoked, it is no longer open to the offeree to accept the offer. John phoned Merry to inform her about the revocation of his offer to her. However as she was out, he informed the same to her assistant.

In **Dickinson v Dodds (1876)**, it was held that communication of revocation of offer may be made by a reliable **third party**.

The facts of this case are as follows:

Dodds offered to sell a property to Dickinson. He also told Dickinson that the offer would be left open until Friday. On Thursday, Dodds informed Dickson through a person who was acting as an intermediary that he intends to sell the property to someone else. Dickson still attempted to accept the offer on Friday. But the property was already sold before Friday.

It was held that the sale of the property amounted to revocation. The revocation communicated by the reliable third party amounts to effective communication of revocation.

In our case, it can be concluded that John has revoked his offer to Merry before she accepted it. This was successfully communicated to her through her assistant. Hence there was no contract between John and Merry for sale of antique. Merry, therefore, cannot force John to sell her the antique.

Answer 7

A contract basically evolves from an offer by one party and acceptance of the same by the other party. The offer needs to be clear, definite and complete. An offer should be differentiated from an invitation to make an offer. For example, a catalogue with prices indicated on it is not an offer to sell; it is an invitation to make an offer. A person interested in buying the product specified in the catalogue may make an offer to buy and it is left to the discretion of the seller to either accept or reject the same.

Kelly cannot insist that Ronny sells the goods for the prices mentioned on them. Ronny has not made an offer. He has only made an invitation to make an offer.

Therefore option (c) is a true statement



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