

Study Session1

Unit 1-The Law of Contract

Study Session Outline

- i. Meaning of law of contract Purposes of contract law
- ii. Elements of Valid contract
- iii. Void and voidable contracts
- iv. Effects of Illegality

Study Session Duration

You may need 2 hours of formal study time to cover this study session.

INTRODUCTION

Dear learners, welcome to the first session of this module. Under this session, you will define the term contract and law of contract, learn how contracts are formed and what the validity requirements are in order to form a contract. Moreover, this session deals with some basic principles of law of contract.

Enjoy attending this session!

Learning Outcomes of Study Session 1

After completing this study unit, you are expected to

- Discuss the meaning and purpose of contract law
- Appreciate Contract formation and aspects of contract.
- identify the general rights/entitlements and duties/obligations of contracting parties that emanates out of the agreements
- Explore the validity requirements of contract

Unit 1 -The law of contract

1.1 Introduction

Our daily life is full of contracts. We conclude contractual agreements whether consciously or unconsciously. However, most of the contracts we conclude may lack formality. Contract of law is thus a set of rules that governs how contracts should be concluded and enforced under the law. Hence, completing this unit enables learners to appreciate how contracts are formed, the rights and obligations of the parties to a contract and how contractual agreements are enforced.

1.2 Definition

A contract is a legally binding act/judicial act of proprietary nature concluded between two or more people (Bassyouni, 2021), (*Chen-Wishart, 2012*). All contracts can be considered as agreements, but it doesn't mean that all agreements are contracts. Contracts may be concluded either in a written form or orally. Some contract requires they be concluded in a written form for evidentiary purpose and other legal purposes. While some contracts may be concluded orally. For example, the contract of sale of a house is concluded in a written form. However, you may not need to write a contract while buying a soap from a shop.

1.3 Purposes of contract law

Contract law's primary objective is to promote cooperation in human behavior, most notably in exchange of goods and services. According to Roscoe Pound, 'wealth in a commercial society is essentially composed of promises.' (Kahsay Debesu, 2009) Hence, Law of contract in addition to facilitation of daily transactions, promotes the accumulation of wealth by protecting the property rights of individuals. In a nutshell, law of contract is vital in the promotion of economic transaction. Law of contract also helps in the promotion and facilitation of business by creating a predictable business environment and. the other purpose of law of contract is that it provides freedom for contracting parties to stipulate rights and duties based on their free will. Hence freedom of contract is another advantage that we get from a contract. If rights and duties are freely stipulated under the contract by contracting parties it will be easier to enforce the obligations/object of the contract. Of course, freedom of contract may be limited for the reasons of social fairness, peace, and tranquility (*Chen-Wishart, 2012*).

Hence, we can infer from this, that contracts also help us in order to easily enforce rights and duties. This by itself helps in the reduction of time and cost of unnecessary litigations. Therefore,

law of contract, has several purposes in a society from helping the economic transaction, to facilitation of trade, investment, and from justice perspective, easy enforcement of rights and obligations and builds trust and confidence among society. (Chen-Wishart, 2012).

Moreover, Contracts serve as a record of commitments for both parties. Once concluded contracts may stay for longer period of time. Hence the stipulations provided under the contract may be refereed from that record even after several times.

Contracts can also help in order to avert disputes and lessen risk. Since Contracts regularly undergo a negotiating procedure in order to ensure that contracting parties get the best bargain possible, mutually beneficial outcome would result out of the continues negotiations and this helps in minimizing conflict

1.4 The Elements of a valid Contract

1.4.1 Object

The object of a contract refers to the rights and obligations of the parties to agreements embodied under the agreement. The object of a contract is the action or inaction agreed upon by the person receiving the consideration. The Object of a contract should be **possible, Legal and moral**. This means impossible duties and rights should not be included under the contract. For example, the object of a contract should not be to bring sand from the moon which is impossible under normal circumstances. The other requirement of the object is that it should be legal, that means parties to a contract cannot agree to perform an illegal act under the laws of a country by which they are bound. For example, a contract concluded in order to commit a crime. The last requirement of the Object of a contract is that contracts should not contradict with the moral standards of a certain community. For example, in Ethiopia, Somalia and Sudan Prostitution is immoral. Therefore, concluding contracts in order to perform prostitution may be immoral taking the moral values of the society. Hence such contracts may not be enforced. In a similar manner drug, alcohol dealing is immoral and illegal under the context of Somalia, and Sudan. Therefore the object of a contract in the above countries shouldn't include illegal, immoral and impossible obligations.

1.4.2 Offer and Acceptance

The essential ingredients of a valid contract is free consent, expressed through a legitimate offer and acceptance.

Offer-Offer is defined as a clear expression of one party's intention to contract with another. The one who provides offer is known as the “offeror” and the “offeree” is the party to whom the intention is manifested.

Dear learners can we see the following illustration of an offer

- A bicycle assembly company provides offer to another company that distributes the bicycles
- Auction bidding, as in *Harris v. Nickerson*.
- Tender submission
- Employment application

The above illustrations can be considered as example of offer.

Dear learners, you need to see the difference between offer and mere invitation to treat, which is just a party's invitation to another or others to make an offer or bargain. The invited party, the ‘invitee’ assumes the role of the offeror, while the inviter assumes the role of the offeree. In a nut shell we can consider that ‘offer ‘is a positive answer to an invitation to treat. Examples of invitations to treat include the following:

- i. Advertisement of sale by auction
- ii. Sale by display
- iii. Self-service sales.

Acceptance -This is the offeree's external indicator of agreement. It results in the creation of contract between the parties. According to legal principle, an agreement is formed when the parties' thoughts meet. This is known as the ‘*consensus ad idem moment*’ (meeting of minds). However, for the agreement to occur, the offeree's subjectivity must be externally established. Acceptance may be expressed orally, in written form , or may be implied from the offeree's behavior.

1.4.3. Capacity

The other essential element of a contractual agreement is the capacity of parties. Capacity may be defined as the ability or capability of parties to enter in to a contract or perform legally binding acts. In order to enforce a contract, the parties to the contract should possess the necessary capacity. Generally, every individual possesses the power to enter into any contractual

arrangement. Even though in principle everyone is entitled to conclude a contract, in exceptional circumstances some persons, natural or artificial, may be prohibited from concluding contracts on their individual capacity. Those include:

- a. *Minors/under age*
- b. *Persons with unsound mind.*
- c. *Bankrupt Corporations.*

Dear Learners: what do you think the reasons for excluding the above categories of persons from concluding contracts by themselves?

- The main reason for excluding the above categories of persons is that they are assumed to lack the necessary capabilities to analyze the outcome/consequences of their juridical acts.

1.4.4 Consent to create legally binding relations

Intent to be bound by the agreement, is another essential component of contract. The parties' intent must have been to create binding relations. Unless the intent of parties is to create a binding agreement between them, it will be difficult to enforce the contract.

Dear Learners, how do you establish/confirm the intent of parties to be bound by the contract?

In order to confirm the intent of parties to be bound by a contract, courts need to evaluate the following aspects when establishing whether parties intended to establish legal relations: 1. The characteristics or type of agreement, 2. The circumstances that surround the agreement's conclusion. These above two elements establish whether the parties wanted to enter into a contract and be bound by the agreement.

Adhesion contract

Some contracts are concluded without negotiating on the contents of the contract. Such kinds of contracts are called Contract of Adhesion or adhesion contract. Most of the time banks, insurances and some other service giving organs priority prepare contract forms and offer the forms to you. As a service recipient or party to the agreement, you have the right to negotiate on the content of the contract, however, such forms don't allow you to negotiate on the contents and terms of the contract. This sort of contract is often assumed to be advantageous for some parties because to it is convenient to induce the weaker party to comply with the contract's provisions (Brietzke, 1974).

Agreements of Mortgage, lease contract, online purchase agreements, and so on are all examples. In some instances, courts may use their discretionary power in order to balance the unequal bargaining power of the parties.

1.4.5 Consideration - Consideration additional element of contracts in addition to capacity, consent, and object. Consideration is assumed to be the bargaining element of a contractual relationship. In order to enforce a contract, consideration plays a vital role. It can also be defined as the reciprocity element of a contract. It is described as "an act or promise made by one party and accepted by the other as the price for the other party's pledge."(Mulgeta Mengist ,2008)

Dear Learners can you demonstrate the concept of consideration by providing examples?

Illustration-: Mr. X enters in to a contract of sale with company ‘Y’ in order to buy a car for 2000 USDs. From this transaction the consideration for Mr. X could be that he has agreed to pay 2000USDs, and the consideration for company is that he has agreed to deliver the car in the specified order.

1.5 Void and voidable contracts

1.5.1 voidable contracts -Voidable contracts are contracts that are concluded with defective consent. Defects in consent may occur, if the contract was concluded for example by exerting duress on either party. That means the contract concluded under the threat of force or duress may be invalidated upon the request of the party whose consent was affected by duress. The other manifestation of a defective consent is when a fraudulent contract is concluded between parties. Since the object of the contract is affected by deceit or fraudulent acts of either party, this kind of contract can also be invalidated when the disadvantaged party applies for invalidation. For example, if the agreement was about sale of a leather jacket and the seller delivers a synthetic jacket instead, concealing that it was a leather jacket. Some contracts can also be invalidated if there is fundamental mistake under the contents/objects of the contract. For example, mistakes in amount, mistakes in quality of products etc.

The other ground by which a contract may be invalidated is ‘*Undue influence*’. Undue influence refers to a situation in which a person takes advantage of his or her position of authority over another person. This inequality in bargaining strength may affect the consent of the weaker party.

Dear Learners can you give some more examples of avoidable contracts from your own experiences?

1.5.2 Void Contracts- void contracts are illegal/immoral contracts that don't exit from the beginning (void *ab initio*) because they are illegal, cannot be enforced, or are totally impossible contracts. Parties who concluded a voidable contract cannot enforce the rights and duties stipulated under the contract.

The following are some of the manifestations of voidable contracts

Contracts concluded to commit a crime, or fraud.

Such contracts are illegal, contravenes to public order and safety and cannot be enforced since it is against public policy to conduct crimes, or fraud/deception. In the case of *Bigos v. Boustead*, where the contract's stated purpose was to breach 'English Exchange Control Legislation', the contract was found to be void and unenforceable.

Contracts to defraud state revenue.

In *Karlinski v. Miller* it was established that a contract whose purpose is to deprive the state, be it central or local, of revenue through tax evasion is illegal and unenforceable.

Contracts that promote public corruption

Corruption is a crime and it contravenes public policy of a nation. In the case of *Parkinson v. College of Ambulance and Another*, 'a philanthropic organization's secretary told the plaintiff that the organization was on to him. The complainant contributed £3,000 but was not knighted because the title could only be bestowed by the King. In an effort to recover the money, it was determined that it was unrecoverable due to the illegality of the contract.' (Parkinson v. College of Ambulance)

Contracts that encourage sexual immorality

Such contracts contradict with the good morality of the wider society in the world. Such contracts cannot be enforced because they promote immorality. (Pearce v. Brooks)

Contracts that cannot be enforced- contracts that are difficult or impossible to enforce are also treated as void contract. As we mentioned above, a good example is a contract concluded between two parties where the obligation of the other party is to construct a house constructed out of sand brought from the moon.

Dear Learners can you give some more examples of void contracts from your own country's legal point of view?

1.6 Effects of Illegality

A contract that is regarded as void or voidable by a competent authority is said to be "outside the light of the law." Such a contract cannot be enforced because it creates no rights or duties on the parties. Either of the parties is under no obligation to perform. In this scenario, the law doesn't recognize the transaction of parties, and is not obligated to enforce the contract.

Unit Summary

Dear learners, we have seen the meaning, formation, and purposes of law of contract. The primary goal of contract law is to ensure collaboration in human behavior, notably in exchange. Contract law ultimately provides the necessary underpinning to sustain the entire credit institution and outlines the roles and responsibilities of each party in a contract. A contract may be concluded by the agreement of propriety nature of two or more parties. A contract may be concluded in a written form or orally. We have also seen the fundamental elements in the formation of contracts. a contract must contain an object, offer, acceptance, consideration, capacity, intention, and legality in order to be enforceable. And finally, we have seen voidable and void contracts where void contracts are not enforceable because they are illegal, immoral or contradict the public peace, policy and order.

Unit Quizzes

1. “An agreement between the parties is an essential element of a contract, but every such agreement does not form a valid contract”. Do you agree with this statement? Justify your answer with reference to the Law of Contract.
2. Mention the essential elements of a binding contract?
3. Read and make notes on the case of *Bigos v. Boustea*
4. What is an offer in a contract?
5. Is it necessary to put a contract in writing?
6. What is a “breach of contract” and what should I do if this occurs?
7. Are there any defenses for breaching a contract?
8. Can I change my mind after entering into a contract?
9. Explain the differences between voidable and void contracts by giving example?