



Advanced Contracts, Tendering and Public Procurement
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Lecture 11: Formation of Contract – Free Consent Part 02


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Free Consent: contd.



- Misrepresentation: innocent or negligent
 - *caveat emptor*
 - *Uberimae Fidei* [O Sareojam v UOI]
 - Conditions & Warranties
- Fraud
 - Ward v Hobbs,
- Whether silence amounts to fraud?
 - *Sykes v Rose and Shri Krishna v Kurukshetra University*; AIR 1976 SC 376
- Only 'serious allegation of fraud' will make the disputes non arbitral. [shareholder agreement: *Avitel Post Studios Limited v HSBC PI Holdings (Mauritius) Limited* Aug SC 2020: The court also drew a distinction between a contract which was obtained by fraud and performance of an otherwise valid contract being vitiated by fraud.]



The essentials of a contract include aspects that may affect free consent. Free consent is a crucial element, as the parties involved must agree on the same thing in the same sense, which is known as the principle of consensus ad idem. Once this agreement is reached, a contract is formed. The principle of consensus ad idem, or the meeting of the mind's theory, is a fundamental principle in contracts. Factors such as coercion, undue influence, and misrepresentation can affect the formation of a contract by compromising free consent.

Fraud is an interesting aspect that commonly arises in contracts and is often associated with a sense of being cheated or receiving an unfair deal. Fraud can occur in various types of contracts and is prevalent in exploitative markets. It is important to note that fraud is also covered under criminal law, with the Indian Penal Code addressing fraud, cheating, and related offenses that can result in imprisonment or fines.

Fraud is also addressed in personal laws, particularly in marriage laws. In cases where a person misrepresents their age, status, caste, or other relevant factors in a marriage, fraud can serve as a ground for annulment or divorce. It is worth noting that fraud is a form of misrepresentation, which can be categorized as innocent, negligent, or fraudulent.

The state of mind is crucial in these categories. Fraud involves deliberate and mischievous actions with the intention to deceive. The person making the fraudulent representation is fully aware that it is untrue, yet chooses to deceive the other party to obtain their consent in the contract. They possess knowledge of the market conditions and may have engaged in such deceptive practices in the past.

Intentional misrepresentation, deliberate misrepresentation, or reckless misrepresentation that jeopardizes the safety and rights of the other party can be considered as fraud. Fraud is a severe offense that infringes upon the rights of the other contracting party. If fraud is committed in a contract where your consent was sought, you have the right to challenge the contractual obligation in court and potentially seek damages if you have suffered significant harm to yourself or your property due to the fraudulent misrepresentation.

Courts treat fraud seriously, which underscores the importance of this aspect in contracts. It is also important to note that fraud can occur in government contracts, where false documents may be submitted during the tendering process. Companies and contractors sometimes attempt to qualify for government contracts despite not fulfilling the specified criteria in the tender documents. This can lead to the submission of false documents or errors, ultimately establishing a case of fraud. Negligent misrepresentation, on the other hand, may arise when there is a general misunderstanding of the documents to be submitted in a tender.

Overall, fraud is a significant concern in various contractual scenarios, and its detection and legal repercussions are treated seriously by the courts.

The distinction between negligent and fraudulent misrepresentation can be a gray area, but it is important to note that negligence occurs when someone fails to exercise caution in submitting tender documents, while fraud involves creating false documents or deliberately misrepresenting information. Intentional and deliberate actions to gain unfair advantages in the market contribute to the categorization of fraud as a distinct and serious offense.

An interesting case that sheds light on the evolution of misrepresentation and fraud is the case of *Ward v. Hops*, which revolves around the sale of pigs at a fair in a village. The seller advertised the pigs as "pigs with all faults." The buyer, despite being aware of this representation, decided to purchase the pigs, believing he could rectify any faults himself. However, the purchased pigs carried typhoid fever, which then spread to the buyer's existing pigs, resulting in significant damages.

The buyer, feeling aggrieved, sued the seller, claiming fraud and seeking to set aside the contract while also claiming damages for the loss suffered. The seller, in his defense, argued that he had clearly stated the pigs had faults and had not hidden any information. He asserted that the principle of *caveat emptor* (let the buyer beware) applied, suggesting that the buyer, being a pig farmer, should have verified the nature of the faults and taken appropriate precautions.

This case raises the question of whether the buyer can solely blame the seller and claim fraud. It is essential to recognize that while consumer protection laws exist, placing a responsibility on the seller, buyers also have their obligations. Pro-consumer legislation, such as the Sale of Goods Act of 1930, the Competition Act of 2002, and the recent Consumer Protection Act of 2019 (replacing the 1986 Act), aim to safeguard innocent consumers from exploitation in the market. However, it is not always appropriate to shift the entire burden onto the seller. Buyers also carry a certain level of responsibility.

While fraud and misrepresentation have distinct characteristics, buyers and sellers both have their roles and responsibilities in ensuring fair and transparent transactions.

The buyer could have potentially discovered the faults if they had been diligent and fulfilled their obligations in the contract. The issue at hand is not solely about representation or misrepresentation. The law acknowledges that if the buyer had the means to discover the truth but failed to do so, they are deemed to have contributed to the fault. Consequently, the buyer may not receive the remedies they seek from the court of law. In this case, the buyer did not fulfill their obligations and approached the court with unclean hands. The seller, on the other hand, fulfilled their obligation sufficiently to avoid liability, albeit cleverly or mischievously by stating "with all faults" without specifying the faults.

The court sided with the seller in this case, applying the principle of Caveat emptor, as the buyer was negligent. Seeking equity requires coming to the court with clean hands and not contributing to the breach. Therefore, the court upheld the principle of Caveat emptor.

It is important to note that Caveat emptor was prominent when consumer interests were not the primary focus. From a consumer perspective, the approach may differ. In contracts, it is crucial to distinguish between B2C contracts (business to consumer) and B2B contracts (business to business). In B2C contracts, the principle of Caveat emptor may predominantly apply, placing the burden on the seller. In B2B contracts, where both parties are presumed to have equal bargaining capacity, Caveat emptor may also apply. Courts have recognized that there is nothing inherently wrong with the principle of Caveat emptor in B2B contracts.

Furthermore, it is worth mentioning another relevant contract type for this course, which is B2G contracts (business to government). In B2G contracts, it is important to acknowledge that the government often holds a higher bargaining position. Therefore, it is inaccurate to solely attribute fraud to the contractor as the government has greater bargaining power in such cases.

Nevertheless, the government should be aware that it cannot solely hold contractors responsible when awarding contracts. The government also bears responsibility and must take note of these circumstances. For instance, the government should have diligently verified the authenticity of documents submitted, rather than claiming fraud without making any effort to discover the truth. It is the government's duty to exercise due diligence in contract tendering, including thorough verification and scrutiny. Failure to exercise this responsibility negates the possibility of fraud. This principle is clearly established in contract law.

Additionally, the question of whether silence can amount to fraud is worth considering. While representation typically involves positive statements, the act of remaining silent when one can speak can constitute fraud or misrepresentation. This concept is exemplified in cases such as *Shri Krishna versus Kurukshetra University* and *Skies versus Rose*.

In the *Shri Krishna* case, a student intentionally left a column regarding attendance requirements blank on an examination form. The university later discovered the student's attendance shortage and accused the student of fraud. However, the court noted that the university should have verified the information provided by the student, as they possess the attendance records. If the

university had the opportunity to uncover the alleged fraud but failed to do so, the fault lies with the university, not the student.

The Skies versus Rose case, an English case involving the sale of a house, further illustrates the issue of silence amounting to fraud. The buyers, after almost finalizing the purchase, asked the seller if there was any other information they should know about the property. The seller chose to remain silent and disclosed nothing. Subsequently, the buyers discovered that a gruesome murder had occurred in the house, information that significantly affected the value and desirability of the property. The buyers sought to void the contract and sued the seller, claiming that the seller's silence constituted fraud.

When the case reached the court, the principle of *caveat emptor*, or "let the buyer beware," was considered. Should buyers be responsible for investigating and uncovering such information before entering a contract? However, in this case, the buyers posed an extra question to the seller, specifically asking if there was any other information they should know. The seller's failure to disclose the murder in response to this question led the court to establish that silence can indeed amount to fraud when there is a duty to speak.

Therefore, in cases where the law imposes a duty to speak, such as in the sale of property or insurance contracts based on utmost good faith, non-disclosure or silence can constitute fraud. Sellers and parties in fiduciary relationships have an obligation to disclose any information that may adversely affect the buyer's rights or peaceful enjoyment of the property. Failure to do so knowingly and deliberately constitutes active concealment and amounts to fraud. It is crucial to evaluate the intention of the other party and the nature of the contractual relationship in determining whether allegations of fraud are justified.

Fraud is a significant ground for voiding contracts based on defective consent, and modern-day contracts often involve court intervention and examination of evidence to establish the presence of fraud.