

DEFAULT RULE IN CASE OF AN INCOMPLETE CONTRACT

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Abstract

This manuscript is basically made as a project that is to give a default rule in a case of an incomplete contract. There are many cases of incomplete contracts but there is no such uniform default rule to deal with such situations. This is a small attempts towards drafting legislation along with its detailed explanation.

Questions presented -

Q.1. Is there requirement of parity of default rule in case of incomplete contracts in India ?

Ans. Yes, there is requirement of parity of default rule in case of incomplete contracts in India , as their are many cases in courts of incomplete contracts and for its decision it is fully depended on the judicial discretion , due to which unsatisfaction is their to one of the parties .To remove this flaw their must be a separate provision as “Default rule for an incomplete contract” , in the Indian Contract Act, 1872.

Q.2. Is there a need for a single default rule ?

Yes , there is a need of a single default rule in case of incomplete contracts because if their are multiple default rules then many contradiction will arise in the cases regarding incomplete contracts and again it would be fully on the discretion of the Judge on deciding the case.

Q.3 Why till now no such default rule have been formed by the legislature ?

Till now the legislature didn't felt the need for a default rule as the cases regarding it was decided by judicial discretion but now the legislate has realization and feels for having more

predicable laws regarding it so that the decisions of the Judge can be provided by reasonable ground.

Q.4 Will a single default rule in case of Incomplete contracts help in saving the time of the Judiciary ?

Ans. There are millions of cases pending in the Indian judiciary currently and also Indian judiciary is always criticized for its slow progress in cases and its disposal , according to stats one out of every 10 cases the suit is pending for more than 10 years. Thus, the single default rule in case of Incomplete contracts will somehow help the judiciary in saving its time and dispose the suits as quickly as possible , as the rule will help as a path for the Judge's and will help in decreasing judicial discretion.¹

FACTS

In an effort to reduce judicial discretion and create more predictable laws, the ministry would like to propose legislation mandating that all judges fill gaps in incomplete contracts by using a single type of default rule , and there is a high chance that legislation will pass , as their is need for a single default rule has been felt so that the decisions of the Judge can be provided by reasonable ground and for the satisfaction of the parties.

What is an incomplete contract ?

- Contracts are never fully complete , because some contractual incompleteness are always there. An incomplete contract is a contract which is not complete .A contract can be said incomplete when -:

- Its conditions are not fulfilled ;
- Its conditions are partly fulfilled ;
- Important points like time , date , etc, are missing in the contract ;
- Contingent contract ; etc.

¹ <http://www.firstpost.com/india/twenty-million-cases-still-pending-in-indias-district-courts-a-crisis-is-revealed-2712890.html>.

An incomplete contract can be defined as -

“An incomplete contract is an agreement that does not specify actions and payments for all possible contingencies. All but the simplest contracts are incomplete, containing 'gaps' that must be filled by negotiation, convention, or formal dispute resolution procedures such as courts and arbitration.”

Cases of incomplete contracts -

1. Gujarat Water Supply And Sewerage ... vs Heirs And L.R. Of Pravin bhai Patel on 21 February, 2002

Plaintiff filed aforesaid four suits to recover different amounts of compensation, on the ground that as original **contractor** failed to complete the execution of **contract** work, the plaintiff got that '**incomplete**' **contract** work 'completed' through a third agency and for getting such '**incomplete-contract** work' completed through the third party, the plaintiff had to pay excess amount to third party, and therefore, the plaintiff filed aforesaid four suits to recover compensation from the defendant.

2. Nair Service Society, ... vs R.M. Palat And Ors. on 13 December, 1965
(AIR 1966 Ker 311)

"In all sales it is evident that price is an essential ingredient, and that where this is neither ascertained nor rendered ascertainable, the contract is void for **incompleteness**, and incapable of enforcement.

Accordingly where A agreed to sell an estate to B for 1,500 pounds less than any other purchaser would give, the contract was held void: for if the estate was not to be sold to any other purchaser than B, it was impossible to know what such a purchaser would give for it. So again, where there was a contract to sell at a price to be fixed by two surveyors, and they made their valuation, but that did not sufficiently and finally ascertain the price, specific performance was refused; and the like was the result of a similar case, where the valuation was such as the

Court could not act on, by reason of circumstances of great impropriety on the part of one of the valuers, and the valuation being based on an erroneous view of the facts.

<https://indiankanoon.org/docfragment/1020720/?formInput=incomplete%20contracts>

What is default rule(s) ?

Default rule is a legal principle that fills a gap in a contract in the absence of an applicable express provision but remains subject to a contrary agreement. It can be overridden by a contract, trust, will, or other legally effective agreement.

Written contracts, of course, whether by design or by accident, do not always fully specify the parties' intentions. Indeed, there is a sense in which contracts never cover every conceivable contingency; all contracts, in other words, are on some level incomplete, which is where default rules come in. Default rules "fill the gaps in incomplete contracts; they govern unless the parties contract around them." As a result, a primary role for courts when applying contracts, for legislatures when enacting laws governing contractual relationships, as well as for scholars when writing about contract law is to identify the best default rules for various contractual situations. These will be the gap-filling rules that will apply where the parties fail to specify what they regard as the value maximizing outcome.

Default rule -

"Default rule in case of an incomplete contract -

A contract is not complete between the parties , then the following must be followed :-

- (a) complete performance of the promise(s) made ; or
- (b) Make necessary amendments in the contract ; or

Comments

The applying of the default rule in each case or if any contradictory arise during the case then it shall be solved by Judicial discretion.

In depth explanation of the rule

“Default rule in case of an incomplete contract -

A contract is not complete between the parties , then the following must be followed :-

- (a) complete performance of the promise(s) made ; or
- (b) Make necessary amendments in the contract ; or
- (c) Penalty for non-performance .”

Clause (a) of the default rule -

“complete performance of the promise(s) made;”

Promises are very important from both the sides of a contract. In a contract it is the obligation of both the parties of the contract to fulfill their promises made in the contract , if which is not fulfilled then the contract becomes an incomplete contract.

Exceptions to this -

1. Acceptance of partial performance-

Where one party freely agrees to accept partial performance then a sum is payable for the work completed. The main focus is on free acceptance

2. Substantial performance-

When the court is satisfied that substantial performance is present. The court may then award the contractually agreed price and deduct sums to reflect the amount not performed. If however, the performance is not held to amount to substantial performance the claimant is entitled to nothing. Difficulty arises as to what amounts to substantial performance. There is no precise limit set down but is to be determined on the facts of individual cases.

Bolton v. Mahadeva

[1972] 2 All ER 1322

(Substantial Performance of an obligation)

Defendant engaged plaintiff to install central heating system under a lump sum contract. However, the work was completed with many defects like: fumes from the boilers, inadequacy of warmth, etc. such that the total cost of repairing would have to be approximately 30% of the contract price. In these conditions defendant refused to pay the plaintiff any consideration for the work done and plaintiff sued for recovering the amount due for substantial performance.

Held:

There was neither an express term nor any implied term pleaded to make it obligatory upon defendant to pay for the work only after it has been done ‘precisely’ and ‘completely’ such that any claim for substantial performance was not rejected on sole grounds of the agreement being a ‘lump-sum’ contract.

But, the contract was to install a central heating system such that the heating system neither did produce adequate heat nor was usable for it emitted fumes that made the air uncomfortable; the costs to repair the defects was huge in proportion to the contract price. Under these circumstances, the performance whatsoever couldn’t be regarded as substantial enough so as to enable plaintiff to recover anything upon it.

3. Divisible Contracts

Complete performance applies where there exists an entire contract. Where it is possible to divide a contract into separate parts, eg. if a sum is agreed to be payable per week or hour, then the courts can award a sum for the separate parts of the contract which have been performed.

Ritchie V Atkinson (1808) 10 East 295

By contract the claimant agreed to carry a cargo of specified quantity of hemp and iron. The price agreed was £5 per ton for the hemp and 5 shillings per ton of iron. The claimant only carried part of the agreed quantity. The defendant argued the contract had not been fully performed and therefore no payment was due.

Held:

The contract could be divided into separate parts as the parties had agreed a price per ton. The claimant was thus entitled to payment for the amount carried although the defendant was entitled to damages for non performance in relation to the amount not carried.

4. Free consent-

When the consent is not taken freely because of which one party does not fulfill its obligation then this clause cannot be applied as a default rule.

Clause (b) of the rule -

“Make necessary amendments in the contract”

It means parties with their consent can make necessary amendment(s) in the contract accordingly . The amendment can be like making changes in the time essence of a contract or to a specific point but with the consent of both the parties.

Necessity of clause(b) of rule is free consent of both the parties of contract.

Clause (c) of the rule -

“Penalty for non- performance”

Penalty means the remedy or compensation that one party gets from other due to loss suffered , etc by their non - completion of the contract .

When there is a breach of contract by a party then this default can be applied.

The doubt here arises that how much and what penalty must be given, answer to this is judicial discretion. The penalty shall be given on the factual matrix of the individual cases.

In **Hadley v. Baxendale** a miller hired a carrier to transport a crankshaft. The carrier failed to deliver the crankshaft on time. The miller was unable to operate his mill for 5 days and lost profits that is, incurred consequential losses. The contract itself did not have a term that said what would happen if the crankshaft was delivered late whether, for example, the carrier should pay damages equal to the miller's losses, should refund the fee, or something else. Thus, the contract had a gap. The Hadley rule is, in essence, that the carrier does not have to pay damages for the consequential losses unless they are foreseeable or communicated in advance. However, if the parties choose, they may agree in the contract that the carrier should pay the consequential losses. Thus, the default rule is foreseeable losses; but the parties can opt out of the default that is, fill the gap by agreeing to liability for consequential losses at the time that they enter the contract.

Counterarguments

- ✧ No exception mentioned for frustration i.e. Change of circumstances after the contract is formed. Not in the hands of parties.

Condor V Baron Knights [1966]

A 16 year old agreed by contract to play the drums for the defendant band for 7 nights per week for 5 years. The claimant suffered a mental breakdown and was told by his doctor that he should not perform more than 4 nights per week. The band dismissed him. He brought a claim for wrongful dismissal.

Held:

The claimant's action was unsuccessful as his medical condition made it impossible for him to perform his contractual obligations and the contract was thus frustrated.

- ✧ The motive of making a single default was to reduce judicial discretion but still the rule which is formed needs a lot of judicial discretion .

Conclusion

The default rule in case of incomplete contract suggested is -

“Default rule in case of an incomplete contract -

A contract is not complete between the parties , then the following must be followed :-

- (a) complete performance of the promise(s) made ; or
- (b) Make necessary amendments in the contract ; or
- (c) Penalty for non-performance .”

Comments

The applying of the default rule in each case or if any contradictory arise during the case then it shall be solved by Judicial discretion.

This is the default rule which the ministry finds most appropriate in case of Incomplete contracts in India as it covers all the points , it’s main motive is to reduce judicial discretion and not to remove judicial discretion in cases of Incomplete contracts .

Also the need is to get predictable laws regarding incomplete contracts which this default rule fulfills.