CHAPTER III

UNDERSTANDING ELECTRONIC CONTRACTS

The Indian Law of Contract

Introduction

To understand electronic contracts, it is essential to understand the general principles of contract and also the law governing contracts in Indian context. Contracts are in essence an agreement between two or more parties to conduct any business transaction. Such a contract has to be valid and legally binding on the parties to mutually benefit their interest and transactions. Such contract can be oral or written as may be required by law in specific cases and is validated by the law. Before the evolution of the complex legal systems, agreements were oral and carried out by mutual trust. In community settings any breach of contract is settled through community adjudication system, which inquired into the breach and set right things. As the society grew complex and so were the complexity of the transactions. With the evolution of the legal system, contracts came to be governed by specific laws under the respective legal systems.

It can be stated that 'a contract is a agreement for a specified transaction between two or more parties for a specified consideration and is binding upon on the transacting parties.' The Contract, which could be oral or written, is arrived through a process of negotiation with offers/proposals, counter offer/counter proposals towards acceptance by the contracting parties. Such an acceptance gives rise to an agreement. Indian Contracts Act 2(h) states that 'an agreement enforceable by law is a contract.'

A Contract enforceable by Law

The Indian Contract Act 1872-s10 states:

S 10. What agreements are contracts: All agreements are contracts if they are made by the free consent of parties competent to contract, for a lawful consideration and with a lawful object, and are not hereby expressly declared to be void.

Nothing herein contained shall affect any law in force in India, and not hereby expressly repealed, by which any contract is required to be made in writing or in the presence of witnesses, or any law relating to the registration of documents.

Interpreting the section 10 of the Act the positive aspects can be enlisted as:

1. **Free and conscious consent of the parties to the contract:** In other words there should not be any coercion, undue influence, fraud, misrepresentation or mistake which will not be considered as free consent and will be considered as void.

2. **Persons entering to the contract should be competent:** In other words persons who are minors by law, persons with unsound mind are not competent and any contract entered with them is non-enforceable.

3. **Lawful Consideration :**In other words any contract which is violative of any other law or considerations which not legal will not be valid and will be void

4. **Lawful Object:** The purpose of any such contract has to be lawful in its object or else will be rendered as void.

From this one can infer that a contract enforceable by law is a process, which has a vital significance in any transaction whether it is manufacturing, trading or service. The significance of the contract assumes importance in the cyber world where anonymity and speed of transactions are key elements. E-Commerce can succeed only on these strengths and the sane could turn out to be a huge liability. In order to understand the electronic contracts and its special position let us look into the fundamentals of the contract in the Indian Contract Act.

Proper Law of Contract

The Indian Contract Act section 1. deals with the proper law of contract to create legally binding contract based on the agreement and such an agreement and the proper law takes its validity on the following:

    a. The place of contracting
    b. The place of performance
    c. The place of residence
    d. The subject Matter of Contract
    e. All other facts

Section 2 of the Act enumerates the following:

S 2 (a) – When one person signifies to another his willingness to do or abstain from doing anything, with a view to obtaining the assent of that other to such act or abstinence, he is said to be making a proposal.

S 2 (b) when the person to whom the proposal is made signifies his assent thereto, the proposal is said to be accepted. A proposal, when accepted, becomes a promise.

S 2 (c) The person making the proposal is called the 'promisor' and the person accepting the proposal is called the 'promisee'

S 2 (d) When, at the desire of the promisor, the promisee or any other person has done or abstained from doing, or does or abstains from doing, or promises to do or to abstain from doing, something, such act or abstinence or promise is called a consideration for the promise.

S 2 (e) every promise and every set of promises, forming the consideration for each other, is an agreement.

S 2(f) Promises, which form the consideration or part of the consideration for each other, are called reciprocal promises.

S 2(g) an agreement not enforceable by law is said to be void

S 2(h) an agreement enforceable by law is a contract

S 2 (I) An agreement that are enforceable by law at the option of one or more of the parties thereto, but not at the option of the other or others, is a voidable contract.

S 2(j) a contract that ceases to be enforceable by law becomes void when it ceases to be enforceable.

Communication and Acceptance in Contract

Section 4 of the act pertains to the communication in the contract and is as follows:

The communication of a proposal is complete when it comes to the knowledge of the person to whom it is made.

The Communication of an acceptance is complete-
As against the proposer, when it is put in a course of transmission to him so as to be out of the power of the acceptor, as against the acceptor, when it comes to the knowledge of the proposer.

The Communication of a revocation is complete- as against the person who makes it, when it is put into a course of transmission to the person to whom it is made, so as to be out of the power of the person who makes it;
As against the person to whom it is made, when it comes to his knowledge."

Section 5 – Revocation of Proposals and Acceptance:

A proposal may be revoked at any time before the communication of its acceptance is complete as against the proposer, but not afterwards.

An acceptance may be revoked at any time before the communication of the acceptance is complete as against the acceptor, but not afterwards."

The essence of the above sections is that of the binding force of the contract. It denotes the effect of the binding nature of the contract on acceptance in the mode prescribed by the offer and is deemed as accepted only on receipt where as it complete as for as the acceptance is done through post or telegram. It is in this context the internet is different in the sense the offer or acceptance depending on the position is instantaneous there is no scope for second though of revocation which is possible by a telegram before a post reaches or by personal letter before a telegram reaches.

Competence to Contract

S 11- every person is competent to contract:
Who is of age to majority according to the law to which he is subject; and
Who is of sound mind and is not disqualified from contracting by any law to which he is subject

S 12- a person who is usually of unsound mind, but occasionally of sound mind, make a contract when he is of sound mind.
A person, who is usually of sound mind, but occasionally of unsound mind, may not make a contract when he is unsound mind.

Consenting parties

S 13 Two or more parties are said to consent when they agree upon the same thing in the same sense. The mutual understanding is based on

    a. subject matter of the agreement

    b. the nature of transaction

    c. the language or expression used in recording the understanding

S 14- free consent is defined as one, which is not done through
S 15 coercion
S16 undue influence

S17 fraud
S 18 misrepresentation
S 20 mistake

Void Voidable agreements

S 19 – This section deals with the instance of an agreement which is concluded by coercion, fraud, or misrepresentation, the contract does not become void automatically but can is voidable at the option of the party whose consent was caused by those listed in section 14- 20.

To illustrate that A enters into an agreement with B to sell his business with misrepresenting the facts of profit and goodwill and later when B finds about the same, B has the choice to make the contract void or can still proceed with the contract for other extraneous reasons and thus the contract is not void but had the choice to be made voidable by B who choose not to do so.

Void Agreement

1. **s 20 – Both parties are under mistake as to the matte of facts**

2. **s 24 Consideration and objects are unlawful in part**

3. **s 25 Absence of consideration, except under certain cases**

4. **s 26 The agreement in restraint of marriage**

5. **s. 27**. The agreement in restraint of trade

6. **s 28** The agreement in restraint of legal proceedings

7. **s 29** The agreement in restraint of uncertainty

8. **s 30** Agreement based on wager/gambling

9. **s 56** Agreement becomes impossible to perform

Contingent Contract

S31- 36- speaks about the type of contracts entered which has to be performed or not to be performed based on the eventuality of an event to happen or not to happen and is enforceable accordingly. However the contingent contract would be void if the event becomes impossible to happen.

Breach of Contract

Section 73. – speaks about the breach of contract and appropriate remedies. This section enforces the binding nature of the contract and its legal validity. This section enumerates the loss or damage occurred to one party by the breach of contract of the other party, which is due to such breach of contract or prior knowledge of such consequence when the contract was entered to be compensated by the party who has breached it. In such calculation of loss or damage, the means of such consequence resulting from the non-performance of such contract has to be taken into account.

CONSTRUCTION OF ELECTRONIC CONTRACTS

Contracts in the traditional information technology prior to the Internet age pertained to

1. Manufacturing contracts of hardware products, accessories and peripherals

2. Contracts for software products

3. Contracts for service and maintenance

and post- online era brought in the

4. Electronic Contracts or Online contracts

With the emergence of internet and electronic commerce the contract of e-commerce in terms of Business to Business (B to B), Business to Consumer (B to C) and Consumer to Consumer (C to C) has assumed importance in terms of its complexity and reach. Electronic Banking, .Com ventures, Music download, E-books have spanned the usage of Internet and online -contracts have assumed significance.

Among these contracts the manufacturing contract of hardware is that of any other type of contract in manufacturing industry except that of the latest issue of monopoly or anti-trust where browsing software is bundled with that of the hardware to keep up the market share which shall be dealt latter.

On the software contracts the contracts assumed significance based on the type of software as
   a. Standard package software
   b. Bespoke software and
   c. Customized software

The standard software is the type of software written and produced to address mass consumers around the world. Microsoft Windows and its different versions fall under this category.

Bespoke software is the type of software specially commissioned and written to meet the needs of specific needs of varied clients. Many Indian software firms are involved in bespoke software production. E.g. an airline company may want bespoke software, which will suit its operations. Infosys in the early nineties did software for retailing Reebok shoes.
Customised software is a standard software package, which is altered to the needs of the clients. Many hospital and hotel administration software packages are standard software packages often modified to meet the variations of the customers. There are many networking packages, which are tinkered and tailored to meet client specific needs.

The contract of these software are dealt as manufacturing contracts where hardware manufacturers can bundle as standard software packages and the others like customized and bespoke software are dealt as contracts between parties based on the functionalities and thereby the terms of the contract. It is in this area care has to be taken in construction of contracts which will include offshore and on-site issues involved in developing such packages. On-site contracts need to take into account of not merely the technical aspects and delivery of the software but also

labour laws, gender laws and other accounting aspects of the country where the firm intends to operate in drawing up the contracts.

Electronic Contracts

Electronic contracts facilitate transactions and agreements electronically without the parties meeting each other. This means that the traditional contract process of offer, acceptance and agreement to transact through electronic mode than physical mode of paper. E-Commerce to succeed such contracts need to be validated legally an alternate mode of transaction through online using the latest technological developments. This is aimed at:

1. To create a secure atmosphere of transacting online with alternate mode to paper and writing.
2. To create a electronic documentation system which will safeguard the contracting parties on par with the traditional mode of contracts
3. To create statutory status and monitoring/verifying authorities for such electronic transaction
4. To check frauds intentional or unintentional transactions to promote and build confidence in genuine online transactions
5. To create necessary legal structures to oversee such transactions
6. To establish standard rules and regulation for smooth functioning of online transactions
7. To make Digital signature legally valid and incorporating the same with the existing legal regime of contracts, sale of goods, evidence and consumer acts.

Such electronic transactions will depend on the appropriate legal framework, which recognizes 'electronic records' or 'writings' or 'digital signatures'. It should facilitate for a secure system of such transactions and should create evidentiary value of such records. The Indian IT Act 2000 section 2 deals with various definitions involved in internet transaction and Chapter II and section 3 deals with the definition of digital signature and its authentication for legal purposes.

Section 4 of the IT Act 2000 reads as follows:

4. Legal recognition of electronic records. - Where any law provides that information or any other matter shall be in writing or in the typewritten or printed form, then notwithstanding anything contained in such law, such requirement shall be deemed to have been satisfied if such information or matter is—

(a) Rendered or made available in an electronic form; and
(b) Accessible so as to be usable for a subsequent reference

COMMENTS

If any information or matter is rendered or made available in an electronic form, and accessible so as to be usable for a subsequent reference shall be deemed to have satisfied the requirement of the law, which provides that information or any other matter shall be in writing or in the typewritten form.

5. **Legal recognition of digital signatures. -** Where any law provides that information or any other matter shall be authenticated by affixing the signature or any document should be signed or bear the signature of any person, then, notwithstanding anything contained in such law, such requirement shall be deemed to have been satisfied, if such information or matter is authenticated by means of digital signature affixed in such manner as may be prescribed by the Central Government.

Explanation. - For the purposes of this section, "signed", with its grammatical variations and cognate expressions, shall, with reference to a person, mean affixing of his hand written signature or any mark on any document and the expression "signature" shall be construed accordingly.

COMMENTS

If any information or any other matter is required by law to be authenticating by affixing the signature then such requirement shall be deemed to have been satisfied if such information or matter is authenticated by means of digital signature affixed in the prescribed manner.

Thus with the IT Act 2000 the necessary legal validity for electronics has been established. In this context the earlier Indian Contract Act has bee supplemented with the online transaction as a valid form of contract. In electronic contracts the twin aspects of time and place of dispatch assumes importance between the contracting parties. Online contracts whether it is B to B or B to C will to be validated the place of the dispatch and time factors are crucial. IT Act by section 11. -

11. -Attribution of electronic records. -
An electronic record shall be attributed to the originator-

(a) If it was sent by the originator himself;
(b) By a person who had the authority to act on behalf of the originator in Respect of that electronic record; or
(c) By an information system programmed by or on behalf of the originator to Operate automatically.

12. - Acknowledgment of receipt. -

(1) Where the originator has not agreed with the addressee that the acknowledgement of receipt of electronic record be given in a particular form or by a particular method, an acknowledgment may be given by-

(a) any communication by the addressee, automated or otherwise; or

(b) any conduct of the addressee, sufficient to indicate to the originator that the electronic record has been received.

(2) Where the originator has stipulated that the electronic record shall be binding only on receipt of an acknowledgment of such electronic record by him, then unless acknowledgment has been so received, the electronic record shall be deemed to have been never sent by the originator.

(3) Where the originator has not stipulated that the electronic record shall be binding only on receipt of such acknowledgment, and the acknowledgment has not been received by the originator within the time specified or agreed or, if no time has been specified or agreed to within a reasonable time, then the originator may give notice to the addressee stating that no acknowledgment has been received by him and specifying a reasonable time by which the acknowledgment must be received by him and if no acknowledgment is received within the aforesaid time limit he may after giving notice to the addressee, treat the electronic record as though it has never been sent.

In internet transactions the time and place of dispatch and receipt of electronic records will play a crucial role in the aspects of territorial jurisdiction, applicable laws, evidentiary issues, period of

limitation on initiation of litigations and other issues. To validate such contracts, section 13 of the IT Act has enabling provisions.

S 13. - Time and place of dispatch and receipt of electronic record. -

(1) Save as otherwise agreed to between the originator and the addressee, the dispatch of an electronic record occurs when it enters a computer resource outside the control of the originator.

(2) Save as otherwise agreed between the originator and the addressee, the time of receipt of an electronic record shall be determined as follows, namely: -

(a) If the addressee has designated a computer resource for the purpose of receiving electronic records, -

(i) Receipt occurs at the time when the electronic, record enters the designated computer resource; or

(ii) If the electronic record is sent to a computer resource of the addressee that is not the designated computer resource, receipt occurs at the time when the electronic record is retrieved by the addressee;

(b) If the addressee has not designated a computer resource along with specified timings, if any, receipt occurs when the electronic record enters the computer resource of the addressee.

(3) Save as otherwise agreed to between the originator and the addressee, an electronic record is deemed to be dispatched at the place where the originator has his place of business, and is deemed to be received at the place where the addressee has his place of business.

(4) The provisions of sub-section (2) shall apply notwithstanding that the place where the computer resource is located may be different from the place where the electronic record is deemed to have been received under sub-section (3).

(5) For the purposes of this section, -

(a) If the originator or the addressee has more than one place of business, the principal place of business, shall be the place of business;

(b) If the originator or the addressee does not have a place of business, his usual place of residence shall be deemed to be the place of business;

(c) "Usual place of residence", in relation to a body corporate, means the place where it is registered.

Section 12 and 13 read together is the online equivalent to the traditional contract act transaction aspects of offer and acceptance.

Issues of Security

In electronic commerce the issue of security and a statutory monitoring agency become crucial factors and the same will become crucial aspects of electronic contracts for the consumers to protect their interests and for the business establishments to conduct their business without costly legal battles. The essential security aspects of e-commerce, which need to be taken care in contracts, are:

a. Entity authentication (identifying with whom you are transacting)

b. Message integrity

c. Payment non-repudiation

d. Effective audit

e. Privacy

Such security requirements should also be affordable and the process requires uniform platforms in terms of scalability and transaction models backed by technology. These issues are crucial in drawing up the contracts, which are not part of the physical transaction contracts existing hitherto. As E-commerce means global business in volume and transactions anywhere at anytime with customers not known prior to transactions, it is crucial these aspects are taken care. The current IT Act provides for the security aspects through sections 14, 15 and 16.

14. -Secure electronic records. -

Where any security procedure has been applied to an electronic record at a specific point of time. then such record shall be deemed to be a secure electronic record from such point of time to the time of verification.

15. Secure digital signature. -
 If, by application of a security procedure agreed to by the parties concerned, it can be verified that a digital signature, at the time it was affixed, was-

(a) unique to the subscriber affixing it;

(b) capable of identifying such subscriber;

(c) created in a manner or using a means under the exclusive control of the subscriber and is linked to the electronic record to which it relates in such a manner that if the electronic record was altered the digital signature would be invalidated, then such digital signature shall be deemed to be a secure digital signature.

16. Security procedure. -

The Central Government shall for the purposes of this Act prescribe the security procedure having regard to commercial circumstances prevailing at the time when the procedure was used, including-

(a) the nature of the transaction;

(b) the level of sophistication of the parties with reference to their technological capacity;

(c) the volume of similar transactions engaged in by other parties;

(d) the availability of alternatives offered to but rejected by any party;

(e) the cost of alternative procedures; and

(f) the procedures in general use for similar types of transactions or communications.

Apart from these issues, the Act enables for a certifying authority and officers and functions in section 17 and they're of from section 18 to 34 on the various aspects of security and privacy issues.

17. Appointment of Controller and other officers. -

(1) The Central Government may, by notification in the Official Gazette, appoint a Controller of Certifying Authorities for the purposes of this Act and may also by the same or subsequent notification appoint such number of Deputy Controllers and Assistant Controllers as it deems fit.

(2) The Controller shall discharge his functions under this Act subject to the general control and directions of the Central Government.

(3) The Deputy Controllers and Assistant Controllers shall perform the functions assigned to them by the Controller under the general superintendence and control of the Controller.

(4) The qualifications, experience and terms and conditions of service of Controller, Deputy Controllers and Assistant Controllers shall be such as may be prescribed by the Central Government.

(5) The Head Office and Branch Office of the office of the Controller shall be at such places as the Central Government may specify, and these may be established at such places as the Central Government may think fit.

(6) There shall be a seal of the Office of the Controller.

Issues of Privacy

In Internet transactions, e-commerce to succeed the issue of privacy plays a crucial role. Apart from consumer transaction in terms of personal data, the application of internet in banking, privacy is very crucial if not maintained can lead to major financial loss and there of huge litigation costs both to establishments as well as the clients. Hence privacy plays strategic as well as other non-monetary aspects of business in e-commerce.

Contracts drawn in cyber world need to take care of the mutual interest of the establishments and the clients. This needs an adequate legal framework and the IT Act section 35- 39 deals on the digital signature and its various aspects which will be dealt in length in module 3 on e-banking. However the Act also specifies duties of subscribers which is of importance in contracts drawn from the point of the establishments under Chapter VIII as:

DUTIES OF SUBSCRIBERS
40. Generating key pair.

Where any Digital Signature Certificate, the public key of which corresponds to the private key of that subscriber which is to be listed in the Digital Signature Certificate has been accepted by a subscriber, then, the subscriber shall generate the key pair by applying the security procedure.

41.Acceptance of Digital Signature Certificate.

(1) A subscriber shall be deemed to have accepted a Digital Signature Certificate if he Publishes or authorises the publication of a Digital Signature Certificate-

(a) to one or more persons;

(c) in a repository, or otherwise demonstrates his approval of the Digital Signature Certificate in any manner.

(2) By accepting a Digital Signature Certificate the subscriber certifies to all who reasonably rely on the information contained in the Digital Signature Certificate that-

(a) the subscriber holds the private key corresponding to the public key listed in the Digital Signature Certificate and is entitled to hold the same;

(b) all representations made by the subscriber to the Certifying Authority and all material relevant to the information contained in the Digital Signature Certificate are true;

(b) all information in the Digital Signature Certificate that is within the knowledge of the subscriber is true.

42. Control of private key.

(1) Every subscriber shall exercise reasonable care to retain control of the private key corresponding to the public key listed in his Digital Signature Certificate and takes all steps to prevent its disclosure to a person not authorised to affix the digital signature of the subscriber.

(2) If the private key corresponding to the public key listed in the Digital Signature Certificate has been compromised, then, the subscriber shall communicate the same without any delay to the Certifying Authority in such manner as may be specified by .the regulations.

Explanation. -

For the removal of doubts, it is hereby declared that the subscriber shall be liable till he has informed the Certifying Authority that the private key has been compromised.