

CONTRACTS

Introduction

- 1 The purpose of this Note is to give a very brief overview of the law relating to contract and its application to local councils. This Note describes how contracts are created, different types of contractual obligations, and the consequences of breaching them.

The Creation of Contracts

- 2 There are four elements to a valid contract. These are:

- an intention to create legal relations;
- an offer;
- an acceptance; and
- consideration.

The Intention to Enter Into Legal Relations

- 3 This element requires all the parties to a contract to want the agreement to be a formal arrangement enforceable at law. The main purpose of this requirement is to distinguish contracts from other arrangements which are not intended by the parties to amount to a contract. A basic example of this principle is the type of arrangement that family members enter into on an informal basis. Parents may agree to pay their child £5 if he/she cuts the grass but the law would not treat the arrangement as an enforceable contract. Such an arrangement may well include all the other necessary elements of a contract but there would be no intention to enter into legal relations and, hence, no contract would be formed.
- 4 This principle is linked to another – namely that parties to a contract should be “of the same mind”. For the purpose of forming a contract, both parties must agree to the same terms. The importance of this requirement is that it distinguishes it from negotiations and statements showing a general willingness to enter into a contract at a later date.

The Offer and the Acceptance

- 5 The second element of a contract consists of an offer. For example, a council will make an offer if it offers a lease of land (which is a type of contract) to a prospective tenant. A contract is not made at the offer stage, however, and the prospective tenant will need to accept the offer before the contract comes into being.
- 6 The third element of a contract consists of a party's acceptance of an offer made by another party. If the recipient of the offer suggests changes to the agreement then that is a counter offer and there is no contract until the original party accepts that counter offer. Thus if a prospective tenant wants a longer lease, that is a counter offer and does not become a contract unless the council accept that counter offer. Also the original offer will no longer be available to the prospective tenant as their counter offer will have ended that original offer.

Consideration

- 7 Consideration is the final element of a contract. In the case *Currie v Misa* (1875) LR 1 App Cas 554, consideration was defined as "some right, interest, profit or benefit accruing to one party, or some forbearance, detriment, loss or responsibility given, suffered or undertaken by the other." A contract is a "bargain" in which each party receives a benefit (e.g. goods or a service) or suffers some form of detriment (e.g. payment) - this is referred to as the "consideration". In most contracts it is usually quite easy to identify the benefit to one of the parties and most often the detriment to the other party is the payment of money but there other forms including forbearance (refraining from enforcing a right) and loss. The issue of consideration becomes more important where it is absent. A lack of consideration tends to suggest that there is no contract.
- 8 A valid contract is made if the four elements above are present.

Contractual Terms

- 9 Many large companies only enter contracts which include their written standard terms and conditions. Such contracts are usually favourable to the party who created them and there is limited scope for a council to renegotiate standard terms and conditions (but see unfair contract terms below and LTN 36).

- 10 However in many other contracts entered into by councils, the important terms of a contract will need to be negotiated and agreed. Although contracts need not be in writing, councils are recommended to ensure that all their contracts are in writing to minimise the risk of uncertainty in the meaning of contractual obligations and subsequent disputes.
- 11 Councils will need to instruct solicitors to draft contracts that they wish to enter into. They may use the Law Society's online directory of solicitors to find a suitable firm of solicitors. The directory can be accessed via <http://www.lawsociety.org.uk/find-a-solicitor>.

Breach of contractual obligations and termination

- 12 The breach of a contractual obligation does not automatically bring the contract to an end. A breach of a contractual obligation may entitle the injured party to claim for damages (i.e. money) but the right to terminate the contract after a breach depends on whether the consequences of the breach are significant enough to warrant termination.
- 13 If a party is in breach of a contractual obligation which is ancillary or secondary to the major purpose of the contract (sometimes referred to as a warranty), the injured party may only be able to sue for damages. Damages aim to put the injured party in the position it would have been in had the contractual obligation been properly performed. Put another way, damages are designed to compensate for the loss suffered by the injured party in so far as that loss has been caused by the breach of a contractual obligation.
- 14 Where a party is acting, or about to act, in a way prohibited by the contract (e.g. use of confidential information), the court may grant an injunction (i.e. an order of the court) to prevent the party in breach from that action.
- 15 An order for "specific performance" compels a party in breach of contract to perform its obligations and may be granted in circumstances where damages or an injunction would be an inadequate remedy (such as where an item to be purchased is unique).
- 16 If a party is in breach of a contractual obligation which goes to the root of the contract (usually referred to as a condition), the injured party may then sue for damages and/ or to repudiate the contract. Repudiation entitles to injured party to treat the contract as having ended. Following the discharge of the parties' primary obligations, the injured party may seek compensation for any loss suffered.

- 17 Some contracts entered into by councils expressly require the parties to attempt to resolve disputes without commencing court proceedings. Such provisions may require resolution by a suitable arbitrator or by mediation.
- 18 A contract will normally provide a party with an option to terminate it if obligations are breached by the other party. A provision in a contract which permits a party to terminate will generally require notice to be given to the other party, a requirement that must be complied with for termination to take effect.
- 19 It is not always easy to ascertain (i) whether a contractual obligation is a warranty or a condition and, consequently, (ii) whether a breach of that obligation will entitle the party not in breach to sue for damages only, seek an injunction or to terminate the contract. Where there is a dispute relating to the performance of a contractual obligation, a council should seek legal advice. If a council has legal expenses insurance cover for contractual disputes, it may benefit from advice and representation from solicitors appointed by the council's insurer.

Unfair Contract Terms

- 20 The Unfair Contract Terms Act 1977 and the Consumer Rights Act 2015 outlaw terms in a contract that are either unreasonable or unfair. Please see LTN 36 for the details of this legislation.

Implied Terms

- 21 Certain terms are to be automatically read (i.e. implied) into consumer contracts or contracts made in the course of a business (which would include the activities of a local authority). This is done under a number of pieces of legislation including:
 - Consumer Rights Act 2015 (for consumer contracts) or
 - Sale of Goods Act 1979 and Supply of Goods and Services Act 1982 (for business to business contracts).
- 22 Many of the provisions are detailed and complex and it is not possible to give a comprehensive guide here but they include:
 - goods will meet the standard that a reasonable person would regard as satisfactory, taking account any description of the goods, the price and all the other relevant circumstances;

- goods sold by sample will match the sample; and
- the supplier of a service will use reasonable care and skill.

The *Ultra Vires* (beyond the powers) Doctrine

23 As with everything councils do, they must ensure that they have the appropriate power to enter into a contract. If a local council enters into a contract without the relevant power the contract will be unlawful. An example of an unlawful agreement is in the case of *Eastbourne Borough Council v James Foster* (2001) EWCA Civ 1091 where the council attempted to award one of its employees an enhanced redundancy payment in excess of the amount set out in The Local Government (Discretionary Payments) Regulations 1996 (now revoked). The court held that the payment was outside the council's powers *ultra vires* and void.

Other Legal Topic Notes (LTNs) relevant to this subject:

LTN	Title	Relevance
15	Legal Proceedings	Useful for threatened or actual legal proceedings about contract disputes.
23	Health and Safety	Gives further consideration to duties owed to and by independent contractors.
36	Unfair Contract Terms	Provides further information in respect of contract terms and non-contractual notices.
42	Occupiers' Liability	Gives further consideration to duties owed to and by independent contractors.
87	Procurement	Provides guidance about procuring contracts.

© NALC 2017

This Legal Topic Note is published by National Association of Local Councils
 109 Great Russell Street
 London WC1B 3LD
 Tel: 020 7637 1865
 Fax: 020 7436 7451
 E-mail: nalc@nalc.gov.uk
 Website: www.nalc.gov.uk

This LTN was last revised in July 2015.