CLATalogue
The Home of Law Aspirants

BLOGS

Fraud and Misrepresentation under Indian Contract Act

Ruchika Mohapatra · 11 Sep 2024

Introduction

Fraud and misrepresentation are crucial concepts under the Indian Contract Act, 1872, governing the formation and enforceability of contracts in India. Fraud involves intentional deception or misleading conduct by one party towards another, inducing the latter to enter into a contract under false pretenses. Misrepresentation, on the other hand, occurs when false information is communicated innocently or negligently, leading the other party to form a contract based on incorrect assumptions.

Section 19 of the Indian Contract Act pertains to the voidability of agreements due to lack of free consent. If a contract incorporates any of the elements delineated in Sections 15 to 18 of the Indian Contract Act, rendering consent compromised, the affected party holds the prerogative to declare the agreement voidable.

Fraud under Section 17 of the Indian Contract Act

Fraud is defined as any act committed by a party with the intent to deceive another party or to induce them to enter into a contract. It includes the concealment of material facts known to the party making the statement.

A contract induced by fraud is voidable at the option of the innocent party. The innocent party has the right to rescind the contract and claim damages for any losses suffered as a result of the fraudulent misrepresentation.

Elements of Fraud

1. The fraudulent party must have a specific intention to deceive the other party. This involves a deliberate and conscious effort to mislead or defraud.
2. The misrepresentation must concern a material fact, which is crucial and likely to influence the other party's decision to enter into the contract.
3. The deceived party must have reasonably relied on the false representation or concealment of facts, resulting in their entering into the contract and suffering damages as a consequence.

Illustrations

- A knowingly and falsely represents to B that a property is free from all encumbrances, whereas there is a pending mortgage on the property.
- A conceals the fact that a business is on the verge of bankruptcy while enticing B to invest in it.

Does staying silent constitute fraud?

Under the Indian Contract Act of 1872, silence alone typically does not constitute fraud. However, Section 17 of the Act provides conditions under which silence can be construed as fraudulent. These exceptions include:

1. Duty to Speak: When one party places trust and reliance on the other, a duty to disclose material facts arises. Failure to do so can amount to fraud.
2. Duty to Disclose Changes: If circumstances change after a statement is made, rendering the original statement false or misleading, the party who made the statement must disclose these changes to the other party.
3. Silence is Misleading: Silence may amount to fraud if it misleads the other party, especially when the silence could reasonably be expected to be disclosed through ordinary diligence or investigation.
4. Half-Truths: Fraud can occur when a party voluntarily discloses part of the truth but omits other material facts necessary for the other party to make an informed decision.

Misrepresentation under Indian Contract Act

Misrepresentation is addressed under Sections 18 and 19 of the Indian Contract Act. It occurs when one party innocently or negligently makes a false statement or assertion that leads the other party to form a contract based on incorrect information.

Section 18: Misrepresentation

Section 18 defines misrepresentation as a false statement of fact made innocently or without knowledge of its falsehood, which induces one party to enter into a contract. It occurs when a party makes a statement believing it to be true, without any intention to deceive.

A contract entered into based on innocent misrepresentation is voidable at the option of the innocent party. The innocent party has the right to rescind the contract and seek compensation for any losses suffered due to the misrepresentation.

For example, A, a seller, innocently misstates the production capacity of a machine to B, a buyer, who relies on this information in deciding to purchase the machine. If the actual capacity is significantly lower, B may rescind the contract.

In ***M.C. Chacko v. State Bank of Travancore***, the Supreme Court held that false assurances by a bank manager about the approval of a loan, inducing the borrower to make payments under a contract, constituted fraudulent misrepresentation due to the bank's negligence.

The House of Lords established in the case of ***Derry v. Peek*** that fraudulent misrepresentation requires the maker's knowledge of the statement's falsity or reckless disregard for its truth, and it must be proven to have induced the other party to act.

Section 19: Effect of Fraudulent Misrepresentation

Section 19 deals with fraudulent misrepresentation, where a false statement of fact is made knowingly or with reckless disregard for its truth, with the intent to deceive another party and induce them to enter into a contract. It involves a deliberate intention to deceive or mislead the other party.

A contract induced by fraudulent misrepresentation is voidable at the option of the innocent party. The innocent party may rescind the contract and claim damages for any losses suffered due to the fraud.

A, a property owner, falsely represents to B that there are no legal disputes pending against the property, knowing well that there is an ongoing litigation. B, relying on A's misrepresentation, purchases the property. B can rescind the contract upon discovering the truth.

Differences between Fraud and Misrepresentation

Edit **AspectsFraudMisrepresentation Intent Fraud requires a deliberate intent to deceive. Misrepresentation can occur innocently or negligently. Legal ConsequencesContracts induced by fraud are voidable, but may also lead to criminal liability under certain circumstances.Contracts induced by innocent misrepresentation are both voidable. ProofFraud requires stricter proof of intention to deceive.Misrepresentation can be proven through showing negligence or innocence in making false statements.**

Conclusion

Under the Indian Contract Act, 1872, fraud and misrepresentation are distinct concepts, each with its own legal implications and requirements. While both fraud and misrepresentation involve false statements leading to contractual obligations, the key distinction lies in the intent and level of knowledge behind the false representation.