

CONTRACTUAL CAPACITY

- **Contractual Capacity:** The minimum mental capacity the law requires to bind a party who enters into a contract.

- The law presumes that the following classes of persons **lacked contractual capacity** when they entered into a contract to bind them to a contract they wish to avoid:
 - (1) persons who were **minors**;

 - (2) persons who were **mentally impaired**, including those whose impairment was due to voluntarily consuming alcohol or drugs;

 - (3) persons who were **mentally incompetent**, but had not been adjudged incompetent and were not under the care of a legal guardian.

- Unlike a ***void*** contract, which the law will not enforce, a ***voidable*** contract is enforceable unless the party with the right to avoid it elects to do so.

- **Disaffirmance:** A person with the option to avoid a contract due to lack of capacity may do so by **manifesting**, by words or actions, his **intent not to be bound**.

- Disaffirmance must be **timely**.

MINORITY

- Subject to certain exceptions, an **unmarried** legal minor (in most states, someone less than 18 years old) may avoid a contract that would bind him if he were an adult.

- Contracts entered into by **young children** and contracts for something the law permits **only for adults** (*e.g.*, a contract to purchase cigarettes or alcohol) are generally *void*, rather than voidable.

- **Right to Disaffirm:** Generally speaking, a minor may **disaffirm** a contract **at any time during** minority or for a **reasonable time after** he comes of age.
 - When a minor disaffirms a contract, he can recover **all property** that he has **transferred as consideration** – even if it was subsequently transferred to a third party.
 - The minor must disaffirm the contract in its **entirety**.
 - Only the minor may disaffirm; any **adult party** to the contract **remains bound** unless and until the minor's disaffirmance releases her.

MINORITY: EXCEPTIONS

- **Marriage:** In most states, marriage makes a person a legal adult for purposes of contracting.
- **Emancipation:** A minor may lose his right to disaffirm due to his age if, before he entered into the contract,
 - (1) a court or other state official empowered to do so **divested** his parents or guardian of legal control,
 - (2) his parents or legal guardian voluntarily **relinquished** legal control, or
 - (3) he **engaged in business as an adult**.
- **Misrepresentations Regarding Age:** Most states permit disaffirmance *even if the minor misrepresented his age* when entering into a contract. However, some states prohibit disaffirmance in such instances, while other states allow disaffirmance but subject the minor to **tort liability** for her misrepresentation.
- **Liability for Necessaries:** A minor who enters into a contract to purchase food, shelter, clothing, medical attention, or other goods or services necessary to maintain his well-being will generally be liable for the **reasonable value** of those goods and services even if he disaffirms the contract.

MINORS' AND PARENTS' LIABILITY

- **The Minor's Obligations on Disaffirmance:** Upon disaffirmance, a majority of states require only that the minor **return any goods or other consideration in his possession.**

- However, a growing number of states further require that the minor take whatever additional steps are required to **restore the adult to the position he was in prior to entering the contract.**

- **Parental Liability:** As a general rule, a parent is not liable for the contracts made by his minor children unless:
 - (1) the parent **co-signs** the contract, and thereby assumes personal liability for its performance, even if his minor child disaffirms the contract; or

 - (2) the minor child committed some wrongful act associated with the contract **at the direction of** a parent.

INTOXICATION

- If a party was so intoxicated when he entered into a contract that he **lacked the ability to comprehend the legal consequences of entering into the contract**, then he may **avoid** the contract, *even if his intoxication was purely voluntary*.
- Obviously, proving someone's degree of intoxication or sobriety at some time in the past is much more difficult than proving age. Most courts look for **objective indications** that the allegedly intoxicated party possessed or lacked the necessary capacity (*e.g.*, negotiating the terms of the contract, committing it to writing, etc.).
- **Right to Disaffirm:** A person entitled to avoid a contract due to intoxication must disaffirm while still intoxicated or within a reasonable time after becoming sober following the episode of intoxication during which he entered into the contract he wishes to disaffirm.
- **Duty to Disgorge:** A person who timely disaffirms on the basis of intoxication will likely have to return any goods or money received from the other party or fully compensate the other party for any goods or money he cannot return.

MENTAL INCOMPETENCE

- Contracts made by mentally incompetent parties may be void, voidable, or valid, depending on the circumstances.
- **Void Contract:** A party who has been **adjudged** mentally incompetent by a court of law **prior to** entering into a contract, and who has a **court-appointed guardian**, cannot enter into a legally binding contract – only the guardian may enter into binding contracts on behalf of the incompetent party.
- **Voidable Contract:** A party who has not been adjudged mentally incompetent by a court of law may, nonetheless, avoid a contract if, at the time of contracting, he (1) did not know he was entering into a contract or (2) lacked the mental capacity to understand its nature, purpose, and consequences.
 - Only the incompetent party has the option of disaffirming his contractual obligations; **any competent party to the contract remains bound** unless released by the incompetent party's disaffirmance.
- **Valid Contract:** An otherwise incompetent party who understood the nature, purpose, and consequences of entering into the contract is bound by it.

RATIFICATION

- **Ratification:** Accepting and giving legal force to an obligation that previously was (1) not enforceable or (2) voidable. Ratification may be either *express* or *implied*.

- **Express Ratification:** A person lacking contractual capacity at the time they formed a contract may, upon (re-)gaining the necessary capacity to do so, expressly ratify the contract by **stating, orally or in writing, that they intend to be bound** by the contract.

- **Implied Ratification:** Likewise, a person lacking contractual capacity at the time they formed a contract may, upon (re-)gaining the necessary capacity to do so, impliedly ratify the contract
 - (1) by acting in a manner that is **clearly inconsistent with disaffirmance or avoidance**, or
 - (2) in the case of a minor, by **failing to disaffirm within a reasonable time** after reaching the age of majority, or
 - (3) in the case of an intoxicated person, by **failing to disaffirm within a reasonable time** after regaining sobriety.

CONTRACTS CONTRARY TO STATUTE

- Statutes sometimes **proscribe** certain types of contracts or contractual provisions. For example:
 - **Criminal Activity:** A contract to commit a crime is void and unenforceable.
 - **Usury:** Virtually every state has a statute that sets the maximum rate of interest that can legally be charged for different types of transactions, including ordinary loans. Usurious contracts are illegal, and may be void in their entirety, although most states simply limit the interest the lender is permitted to collect.
 - **Gambling:** Most gambling contracts are illegal and unenforceable, even in states where certain forms of regulated gambling are permitted. In 2006, Congress banned electronic payments to Internet gambling sites.
 - **Licensure:** All states require that certain professionals (*e.g.*, attorneys, doctors, architects) obtain a license from the state; many states also license skilled workers (*e.g.*, dental hygienists, electricians, plumbers). A contract with an unlicensed individual may be void, voidable, or , depending on a particular state's statutes, public policy, or case law.

CONTRACTS IN RESTRAINT OF TRADE

- **Contracts in Restraint of Trade:** Contracts that tend to reduce competition for the provision of goods or services in a market (*e.g.*, covenants not to compete).

- **Restrictive Covenants in the Sale of a Business:** Many agreements for the sale of an ongoing business require the seller not to open a competing business within a specified area including the business being sold. To be enforceable, the geographic restriction must be reasonable, and must be effective only for a reasonable period of time after the sale is completed.

- **Restrictive Covenants in Employment Contracts:** Many employment agreements, likewise, require the employee to refrain from working for a competitor or starting a new business in competition with the employer for a reasonable period of time, and within a reasonably defined geographic area, after the employment relationship ends.

- A restrictive covenant is generally permitted when it is *ancillary* to an otherwise enforceable contract. If it is not ancillary to an otherwise enforceable contract, or if the terms of the covenant are too restrictive, the covenant will be *void*.

OTHER CONTRACTS CONTRARY TO PUBLIC POLICY

- **Unconscionable Contracts:** Contracts that contain terms that unfairly burden one party and unfairly benefit the other.
- **Procedural Unconscionability:** Arises when one party to the contract lacks or is deprived of any meaningful choice regarding the terms of the contract due to inconspicuous print, unintelligible language, lack of opportunity to read the contract before signing, or lack of bargaining power.
- **Substantive Unconscionability:** Arises when the contract contains terms that deprive one party of the benefit of its bargain or of any meaningful remedy in the event of breach by the other party.
- **Exculpatory Clauses:** A contractual provision releasing a party from liability, regardless of fault.
- Other contracts contrary to public policy include contracts to:
(1) **discriminate** based on race, color, national origin, religion, gender, age, or disability; (2) **commit a tort**; (3) **interfere with public service**; and (4) **delay, prevent, or obstruct legal process**.

EFFECT OF ILLEGALITY

- A contract that is contrary to statute or to public policy is generally *void*, and therefore unenforceable. In most cases, both parties to a void contract are considered to be **equally at fault** (*in pari delicto*), and therefore cannot enforce the contract against the other party. There are some exceptions:
 - **Justifiable Ignorance:** When one of the parties to an illegal contract has no knowledge or any reason to know that the contract is illegal, that party will be entitled to be restored to its pre-contractual situation.
 - **Protected Classes:** When a statute protects a class of people, a member of that class may enforce an otherwise illegal contract, even though the other party cannot.
 - **Withdrawing from an Illegal Agreement:** If a party withdraws from a partial agreement before any illegality occurs, she may recover its value to her.
 - A party induced to enter an illegal contract by **fraud, duress, or undue influence** may either enforce the contract or recover its value to her.
- **Severability/Divisibility:** If the contract can be divided into legal and illegal parts, a court may enforce the legal parts but not the illegal ones.