CONTRACTUAL CAPACITY

- **Contractual Capacity:** The minimum mental capacity required by law for a party who enters into a contractual agreement to be bound by it. Common law recognizes three classes of persons who are generally not considered to have sufficient capacity to be bound by their contracts:

  - **Minors:** In virtually all states, unmarried persons under the age of eighteen (18) are permitted to enter into any contract an adult can, provided that the contract is not one prohibited by law for minors (e.g., agreement to purchase cigarettes or alcohol). However, unlike those entered into by adults, contracts entered into by minors are generally **voidable** by the minor.

  - **Mentally Impaired or Incompetent Persons:** Likewise, contracts entered into by persons who are, at the time of contracting, intoxicated (voluntarily or not) or mentally incompetent are generally voidable.

  - Recall that, unlike a **void** contract, which is unenforceable on its face, a **voidable** contract is presumed to be enforceable but for the presence of some factor -- here, the contractual capacity which permits the incapacitated party to avoid his or her otherwise valid contractual obligations.
CONTRACTS WITH MINORS - PART I

- **Disaffirmance:** In order for a minor to avoid a contract, he or she need only manifest an intention not to be bound by it.

- This intent to avoid, or “disaffirm,” the contract may be manifested by words or actions.

- Generally speaking, a minor may disaffirm a contract at any time during minority or for a reasonable time after the minor comes of age.

- When a minor disaffirms a contract, all property that he or she has transferred as consideration can be recovered -- even if it was subsequently transferred to a third party.

- Disaffirmance must be timely.

- The contract must be disaffirmed in its entirety.

- Only the minor has the option of disaffirming his or her contractual obligations; any adult parties to the contract remain bound by it unless released by the minor’s disaffirmance.
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 or her possession.

However, a growing minority of states further requires that the minor take whatever additional steps are required to restore the adult to the position he or she was in prior to entering the contract.

Parents’ Liability: As a general rule, parents are not liable for the contracts made by their minor children unless:

(1) one or more parent(s) co-sign the contract, and thereby assume personal liability for its performance, even if their minor child disaffirms the contract; and/or

(2) the minor child committed some tort or other wrongful act associated with the contract at the direction of one or both parent(s).
CONTRACTS WITH MINORS - PART III

- **Misrepresentations Regarding Age:** Most states will permit disaffirmance *even if the minor misrepresented his or her age* when entering into the agreement. However,

  - some states prohibit disaffirmance in *all* cases where the minor misrepresented his or her age;
  
  - other states prohibit disaffirmance in cases where the minor has *engaged in business as an adult*;
  
  - some courts refuse to allow minors to disaffirm *fully performed* contracts *unless* they can return all consideration received; and
  
  - some courts permit disaffirmance but subject the minor to *tort liability* for his or her misrepresentation.

- **Liability for Necessaries:** A minor who enters into a contract to purchase food, shelter, clothing, medical attention, and/or other goods or services necessary to maintain the minor’s well-being will generally be liable for the *reasonable value* of those goods and services *even if* the minor disaffirms the contract.
RATIFICATION

- **Ratification**: Accepting and giving legal force to an obligation that previously was (1) not enforceable and/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.
MENTALLY INCOMPETENT

- **Void contracts:** If a person has been adjudged mentally incompetent and a **guardian** and/or **conservator** has been appointed by the court, then any subsequent contract made by the incompetent person is **void**.

- **Voidable contracts:** If a person not previously adjudged mentally incompetent enters into a contract, the contract may be **voidable**, if he or she is not able to comprehend the nature, purpose and consequences of the contract.
Contracts Contrary to Statute: Statutes sometimes proscribe certain types of contracts, contract terms, and/or contractual provisions. For example:

- **Usury Statutes:** 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 Statutes:** Most gambling contracts are illegal and void, even in states where certain forms of gambling are permitted, subject to governmental regulation.
ILLEGAL CONTRACTS
CONTRARY TO STATUTES
PART II

- **Blue Laws:** Some states and localities prohibit engaging in certain business activities on Sundays.

- **Licensing Statutes:** All states require those members of certain professions -- attorneys, doctors, and architects, to name a few -- be licensed by the state. Any contract with an unlicensed individual is illegal and may be unenforceable. However, a contract with an unlicensed party, where the licensing requirement is merely to raise revenue, may be enforceable.
ILLEGAL CONTRACTS
CONTRARY TO PUBLIC POLICY
PART I

- **Contracts Contrary to Public Policy:** Some contracts between private parties are void (i.e., not enforceable), because they are against public policy.

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

- **Exception** – Covenants not to compete are generally permitted when they are ancillary to an otherwise enforceable contract for the sale of a business or for employment.
ILLEGAL CONTRACTS
CONTRARY TO PUBLIC POLICY
PART II

■ **Unconscionable Contracts:** Contracts that require one party, as a consequence of disproportionate bargaining power, to accept terms that are unfairly burdensome to that party and unfairly beneficial to the party with greater bargaining power, are generally unenforceable.

■ **Exculpatory Clauses:** A contractual provision that releases a party from liability, regardless of fault.

■ Usually, public utilities, common carriers, and banks cannot enforce exculpatory clauses.
EFFECTS OF ILLEGAL CONTRACTS
PART I

- **Effect of Illegality:** An illegal contract -- one that is contrary to statute and/or to public policy -- is, generally, *void*.

- Recall that, unlike a *voidable* contract, which permits a party to avoid his or her otherwise valid contractual obligations, a *void* contract is unenforceable on its face.

- In most cases, both parties to a void contract are considered to be *equally at fault*, 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.
EFFECTS OF ILLEGAL CONTRACTS
PART II

Fraud, Duress, or Undue Influence: A party induced to enter an illegal contract by fraud, duress, or undue influence may either enforce the contract or recover its value to him or her.