

CHAPTER 1 - INDIAN CONTRACT ACT, 1872

UNIT 1: NATURE OF CONTRACT

INTRODUCTION

It received its assent on 25th April, 1872 and was introduced on 1st September, 1872.

It is applicable to whole of India except Jammu and Kashmir

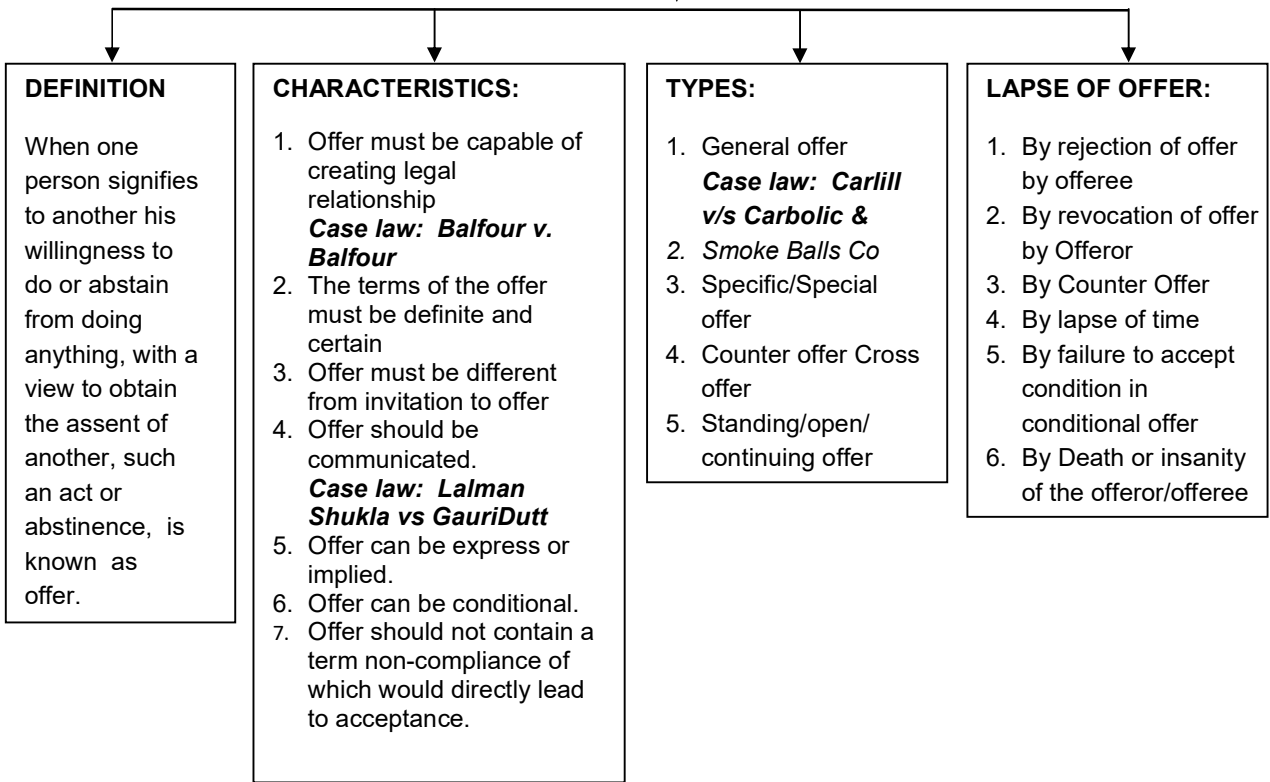
Contract = Agreement + Enforceable by law

Agreement:

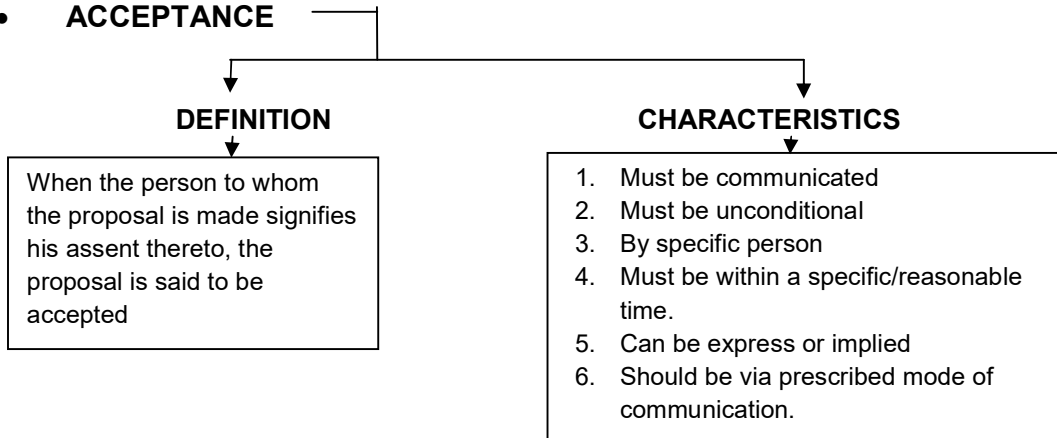
“Every promise and every set of promises forming the consideration for each other, is an agreement.”

All Contracts are agreements but all agreements are not contracts.

OFFER

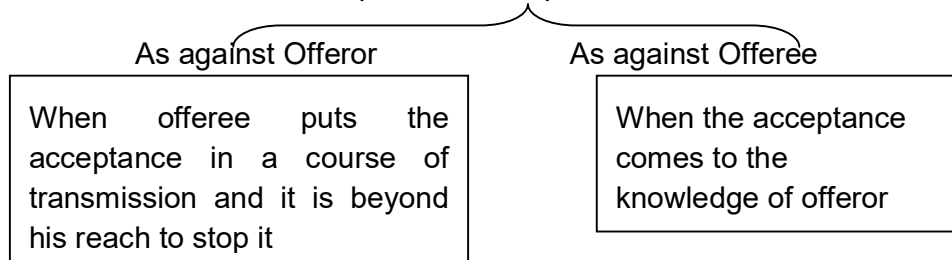


• **ACCEPTANCE**



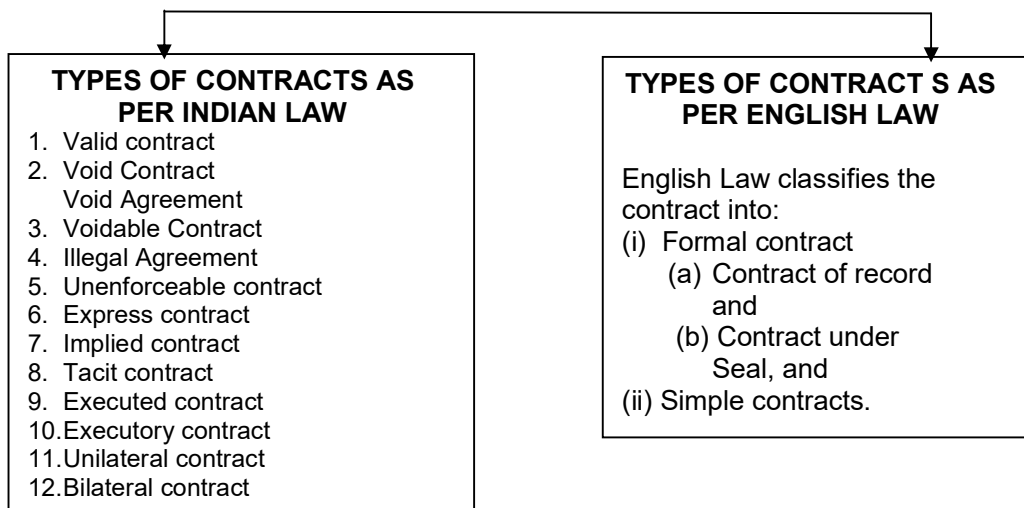
• **COMMUNICATION OF OFFER & ACCEPTANCE AND REVOCATION OF OFFER & ACCEPTANCE**

1. Communication of offer is complete when it comes to the knowledge of offeree.
2. Communication of acceptance is complete



3. Revocation of offer is valid before offeree puts the acceptance in course of transmission and it is out of his reach to stop it.
4. Revocation of acceptance is valid before acceptance comes to the knowledge of offeror.

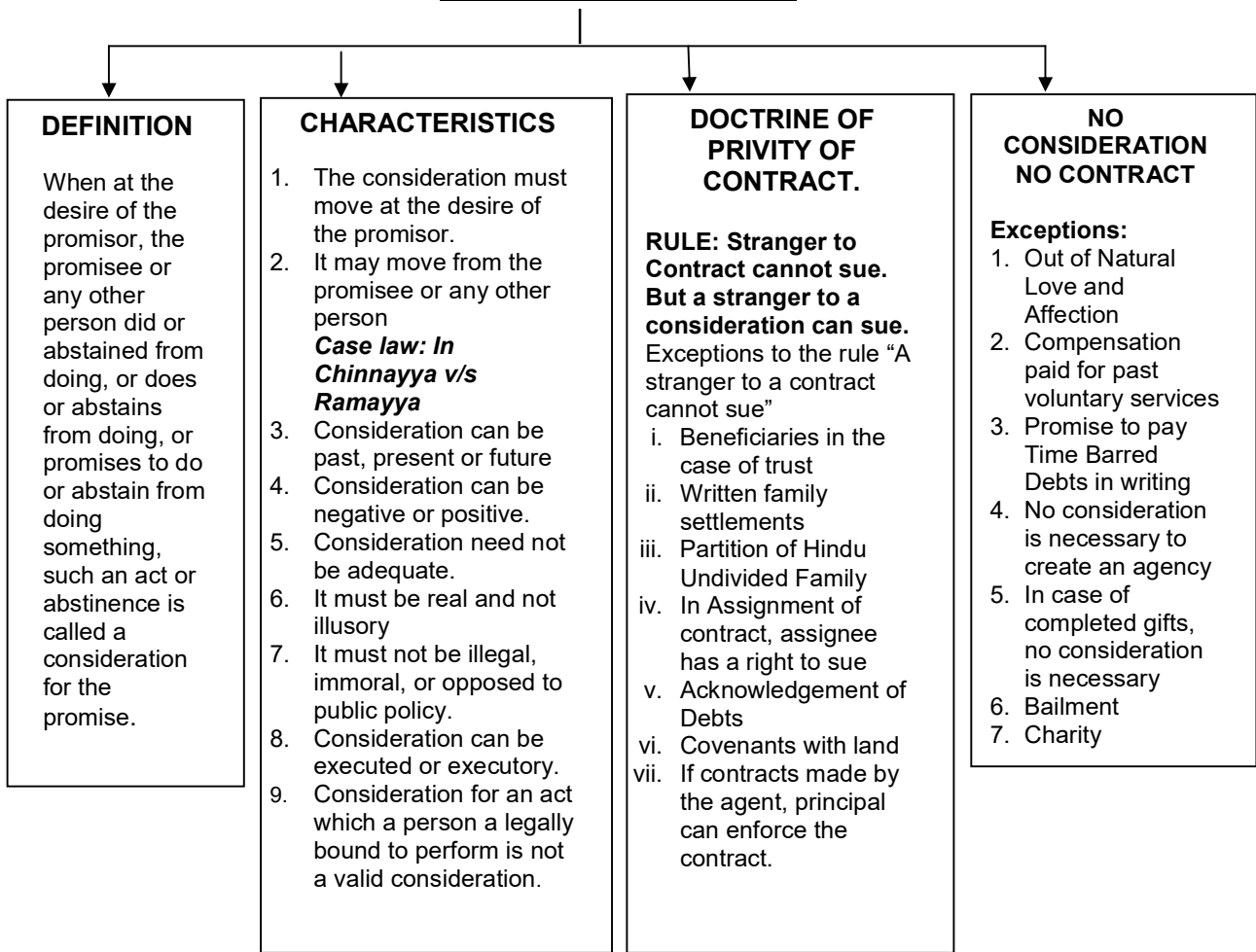
• **TYPES OF CONTRACTS**



• **ESSENTIAL ELEMENTS OF A VALID CONTRACT**

1. There must be an offer and its acceptance and intention to create a legal relationship.
2. There must be capacity of parties.
3. There must be free consent and consensus-ad-idem.
4. There must be lawful object and lawful consideration.
5. The performance must not be impossible.
6. The performance must not be uncertain. The agreement must not be declared to be void.

UNIT 2: CONSIDERATION



UNIT 3: OTHER ESSENTIAL ELEMENTS OF A VALID CONTRACT

• CAPACITY OF PARTIES

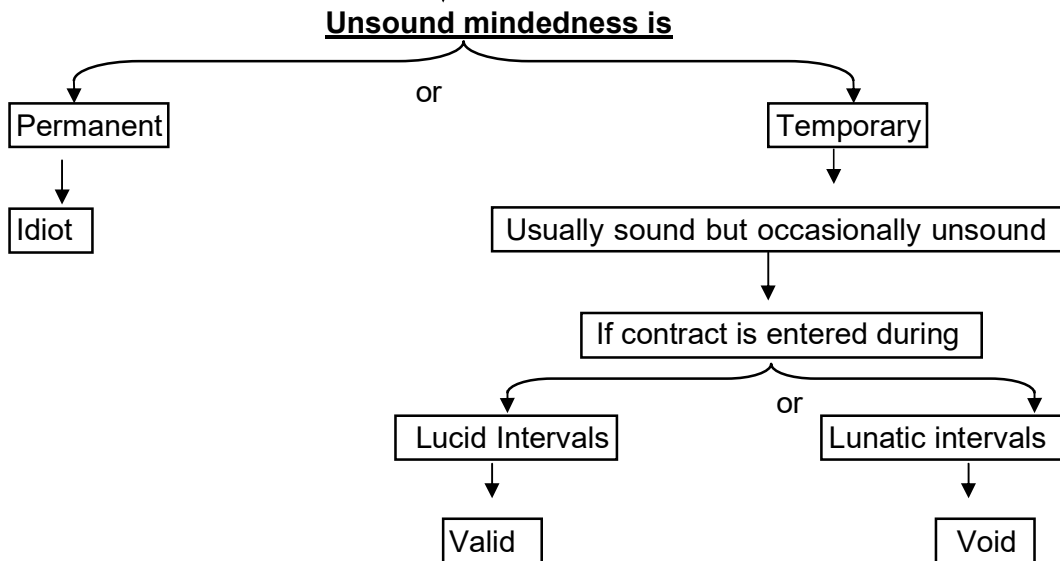
An agreement will be valid and enforceable only if the parties to it are legally competent to enter into contract.

Following persons are not competent to contract :

1. Minor

- ✓ A minor is a person who is below the age of eighteen years.
- ✓ An agreement with a minor is void ab initio
- ✓ The minor's contracts do not impose any liability on his parents or guardians.
- ✓ Parents/Guardians can enter into a contract on behalf of minor for his benefits.
- ✓ Parents/Guardian cannot bind a minor in a contract to purchase immovable properties
- ✓ If minor falsely represents his age, still the contract is void-ab-initio as he can always plead minority.
- ✓ Minor cannot ratify the agreement after attaining majority
- ✓ If any necessities of life (food, clothing, shelter, education, health) are supplied to a minor, he is not personally liable but only his property is liable.
- ✓ A minor can be appointed as an agent but he is not liable for his acts as an agent
- ✓ Case law: In *Mohiri Bibee vs. Dharmodas Ghose*

2. Person of unsound mind:



3. Persons disqualified by law.

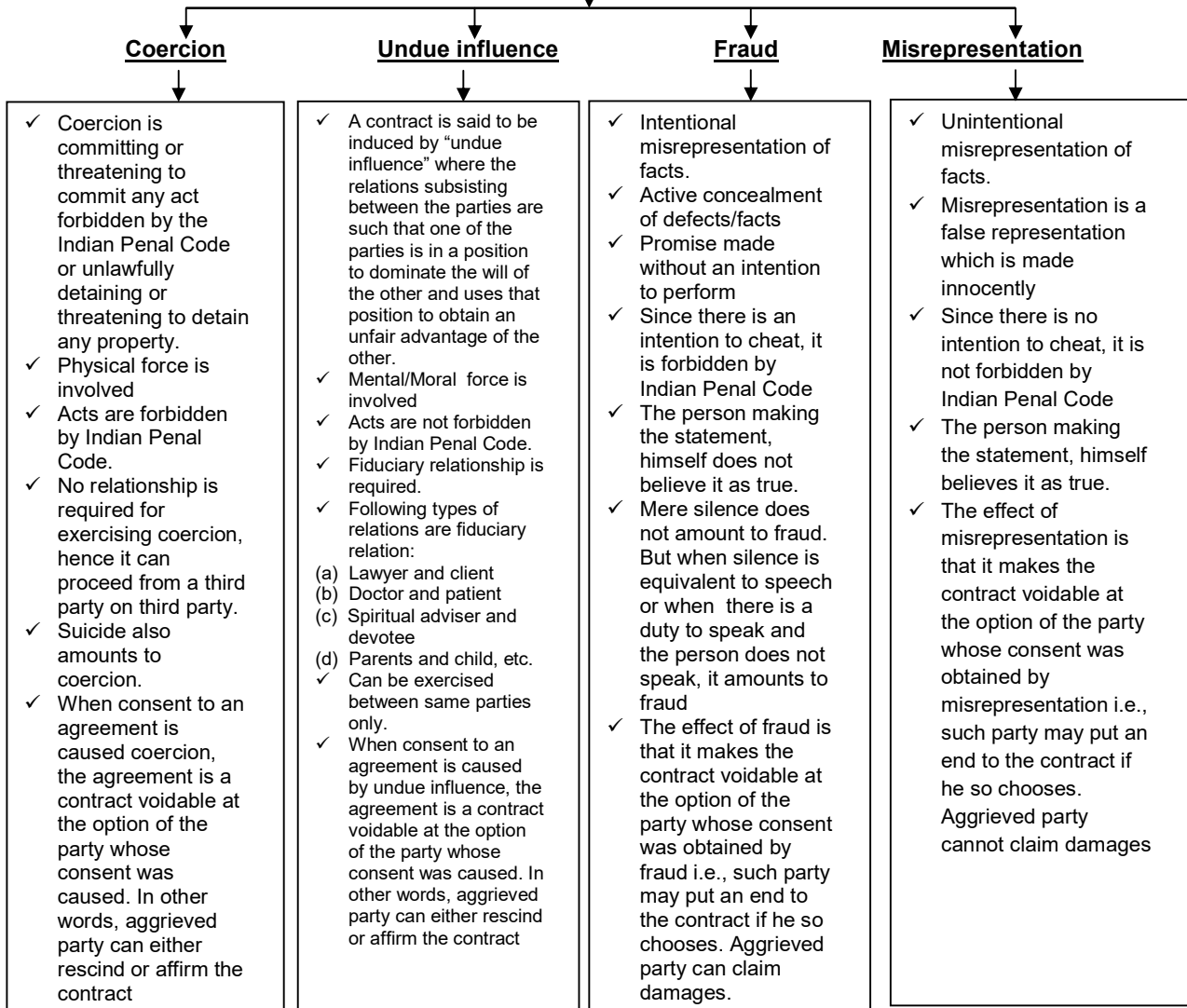
- (i) Alien enemies
- (ii) Insolvents
- (iii) Convicts
- (iv) Foreign sovereigns, diplomatic staff, and accredited representatives of foreign states
- (v) Corporation and a company

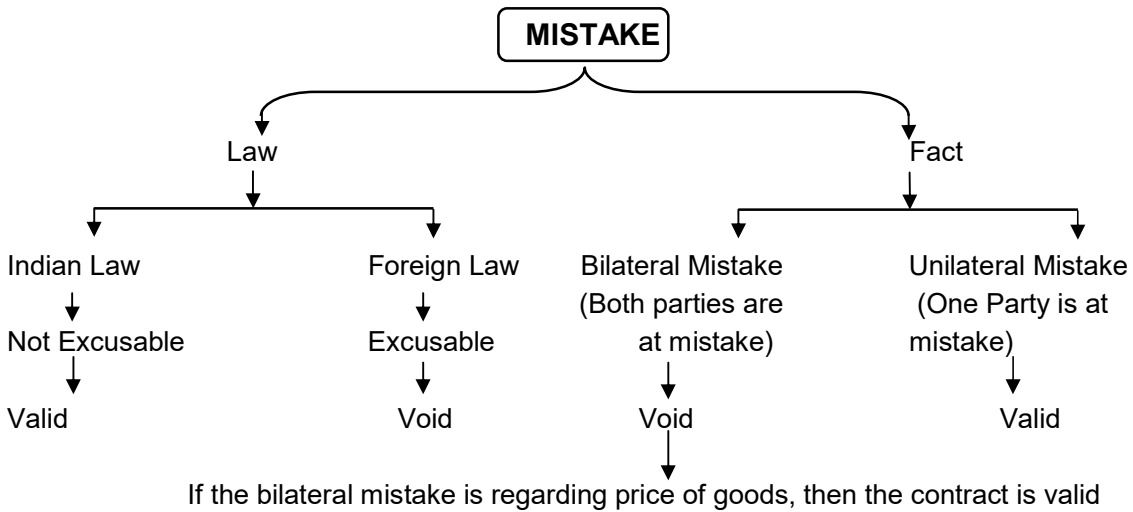
CONSENSUS-AD- IDEM

Two or more persons are said to consent when they agree upon the same thing in the same sense. It is also known as consensus ad idem (i.e., meetings of the minds). For the creation of contract, there must be consensus ad idem

FREE CONSENT

Consent is said to be free if it is **not induced** by:





UNLAWFUL OBJECT & UNLAWFUL CONSIDERATION

1. Agreement forbidden by law
2. Agreement defeating the provisions of law
3. Agreement causing injury to a person or loss of property.
4. Where consideration is immoral.
5. Agreement has a fraudulent object.
6. Agreement interfering with course of law and justice
7. Where consideration is opposed to public policy.
 - a) Stifling Prosecution
 - b) Maintenance and Champerty
 - c) Trading with an enemy
 - d) Trafficking in public offices
 - e) Marriage brokerage contracts
 - f) Interest against obligation
 - g) Agreement for the creation of monopolies

UNIT 4: PERFORMANCE OF CONTRACTS

• **CONTRACT WILL BE PERFORMED BY:**

1. Promisor himself
2. Legal Representative
However, if the contract involves personal skills and if the promisor dies, the contract becomes void.
3. Agent
4. Third persons, if promise permits

• **REQUISITES OF A VALID PERFORMANCE**

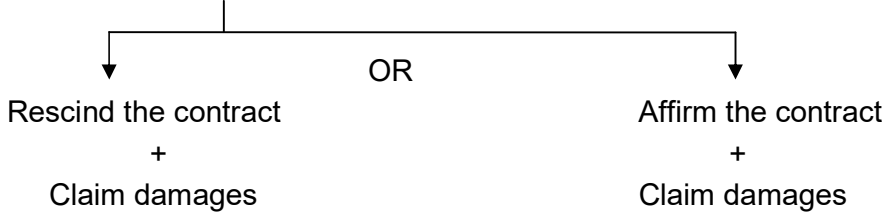
A performance to be valid must fulfil the following conditions otherwise promisor will be liable non-performance:

1. It must be unconditional
2. Performance must be at a proper time and place
3. Performance must be within reasonable time.
4. Performance must give reasonable opportunity for inspection

• **EFFECT OF REFUSAL OF A PARTY TO PERFORM**

If Promisor fails to perform the contract,

Promisee can



• **DISTINCTION BETWEEN SUCCESSION AND ASSIGNMENT**

- ✓ **Succession**
When the benefits of a contract are succeeded by a process of law, both the ASSET and the LIABILITY would be transferred to the legal heir.
- ✓ **Assignment:** Assignment is voluntary transfer of right. Unlike succession, the assignor can assign only the assets to the assignee and not the liabilities.

• **LIABILITY OF JOINT PROMISERS**

- ✓ Liability of joint promisor is joint and several
- ✓ If any joint promisor dies, his legal representatives must jointly with the surviving promisors fulfil the promise.
- ✓ On the death of all the joint promisors, the representatives of all of them must jointly fulfil the promise.
- ✓ The promisee may compel anyone of the joint promisor to perform the promise
- ✓ Where a promisee releases one of the joint promisors, the release of one promisor does not discharge the other joint promisors

• **RIGHTS OF JOINT PROMISEES**

- ✓ Rights of joint promises is only joint and not joint & several

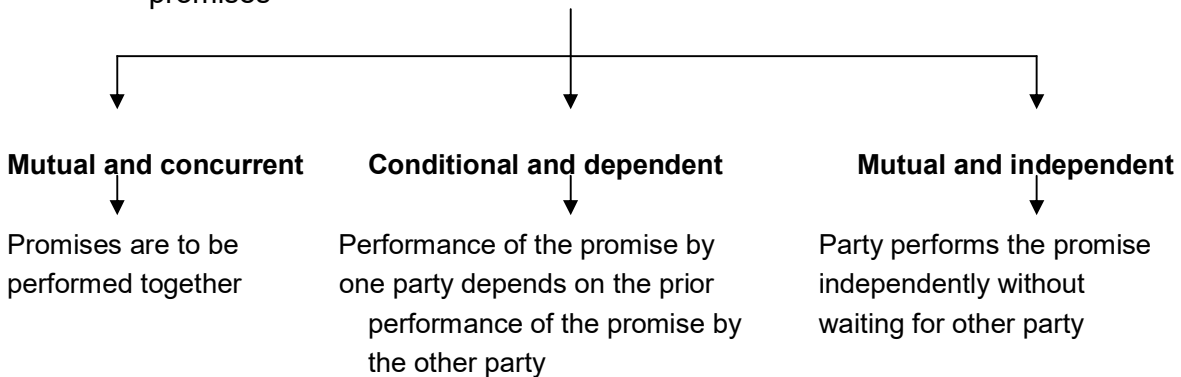
- ✓ If any joint promisee dies, his legal representative must jointly with the surviving promisees claim the performance.
- ✓ On the death of all the joint promisees, the legal representatives of all of them must jointly claim the performance.

• **TIME AND PLACE FOR PERFORMANCE**

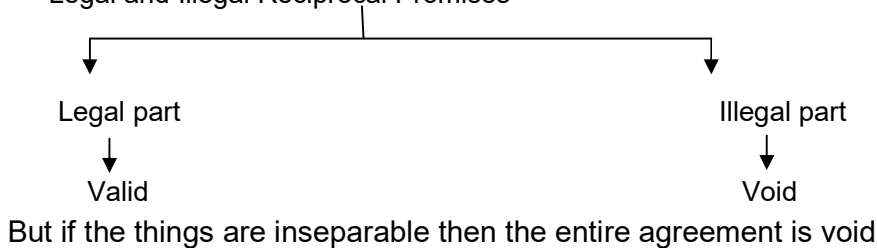
- ✓ Where the day for performance is not specified → promisor has to perform within reasonable time
- ✓ Where the time for performance is not specified → promisor has to perform during business hours
- ✓ Promisee has to specify day, time and place for performance.
- ✓ Where the place for performance is not specified → promisor has to apply to promise to appoint the place
- ✓ Performance is after reasonable time, business hour or at a place other than appointed place → Performance is valid if promise accepts or demands it.

• **RECIPROCAL PROMISES**

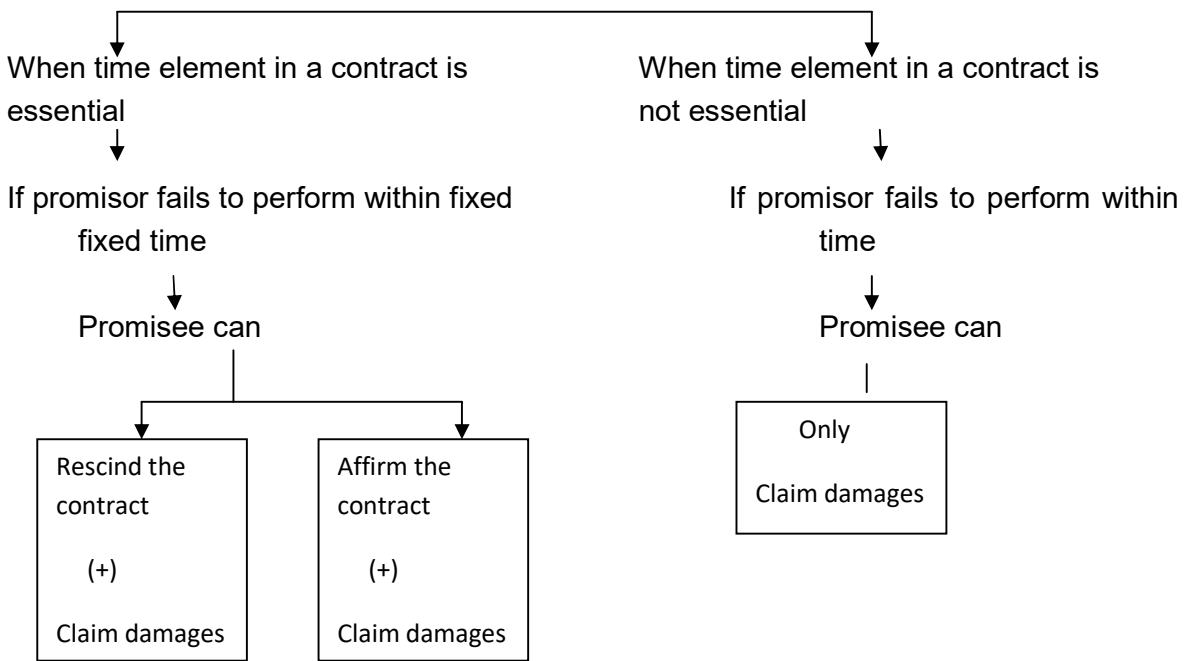
- ✓ Promises which form the consideration for each other are called reciprocal promises



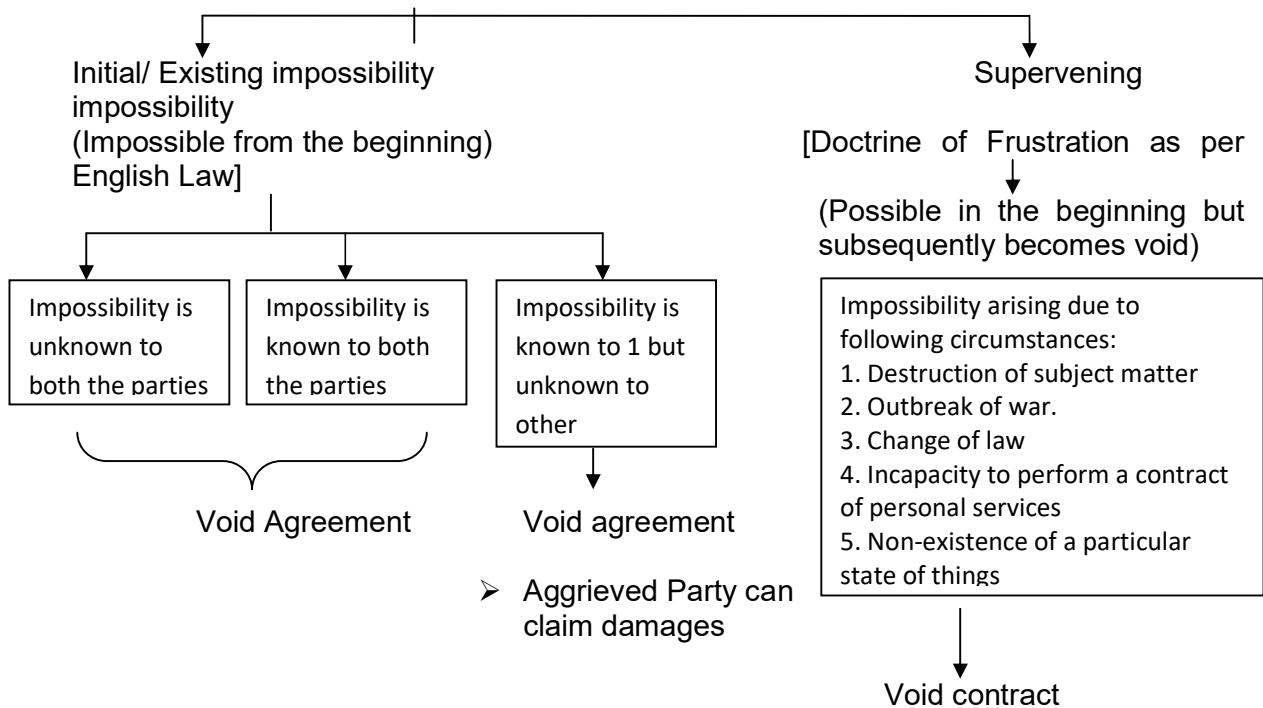
- ✓ Where one party to a reciprocal promise prevents the other party from performing his promise, the contract becomes voidable at the option of the party who is so prevented. And the aggrieved party can also recover compensation.
- ✓ Legal and Illegal Reciprocal Promises

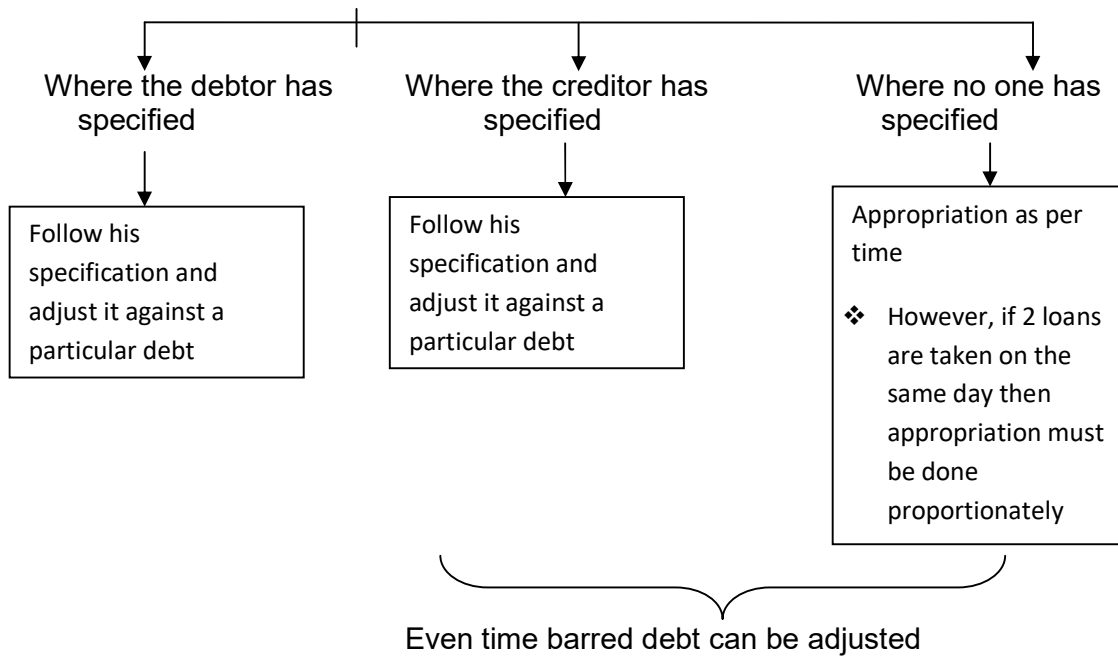


• **EFFECTS OF FAILURE TO PERFORM AT A TIME FIXED IN A CONTRACT IN WHICH TIME IS ESSENTIAL**



• **IMPOSSIBILITY OF PERFORMANCE**



➤ **APPROPRIATION OF PAYMENTS**➤ **CONTRACTS WHICH NEED NOT BE PERFORMED**

1. **Novation:** Cancellation of old contract and substitution of new contract. It must be with the mutual consent of all the parties.
2. **Alteration:** It means change in one or more terms of the contract. It must be with the mutual consent of all the parties.
3. **Rescission:** It means the cancellation of the contract.
4. **Remission :** It means the acceptance of lesser fulfilment of the terms of the promise.

➤ **QUANTUM MERUIT**

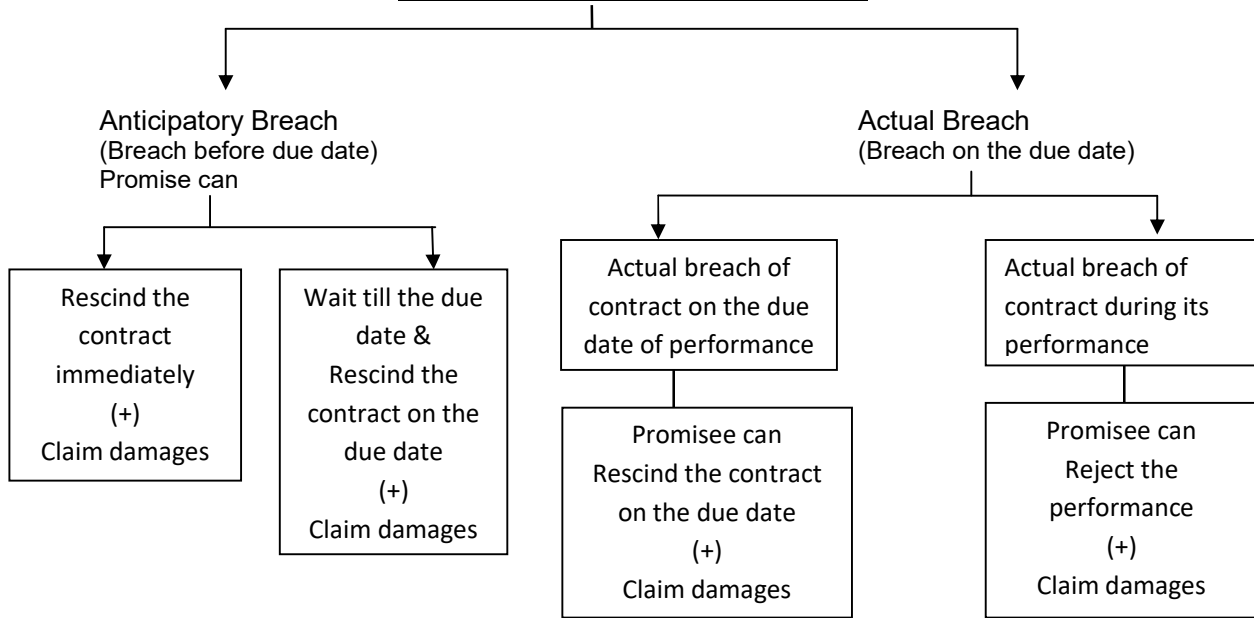
(as much as is earned)

- ✓ Any benefit received under voidable contract which is subsequently avoided is to be returned back .
- ✓ Any benefit received under void contract is to be returned back.

➤ **EFFECTS OF NEGLIGENCE OF PROMISEE**

If any promisee neglects or refuses to afford the promisor facilities for the performance of a promise, the promisor is excused from the performance of his promise.

UNIT 5- BREACH OF CONTRACT



DAMAGES FOR BREACH OF CONTRACT

- 1) Ordinary/ Usual damages: Market Value-Contract Price
- 2) Liquidated damages: Pre-estimated damages which shall arise in ordinary breach circumstances.
- 3) Special damages: Pre-estimated damages which shall arise in special circumstances.
- 4) Exemplary/ Vindictive/ Punitive damages: Here intention of the party is not to recover loss but to punish the other party. It can be claimed in following cases:
 - a) Where a banker wrongfully dishonours customer's cheque
 - b) Where there is a breach of a promise to marry
- 5) Nominal damages: Here intention of the parties to establish a right to sue. Such damages are awarded by court. Such damages are for nominal amounts like ten rupees or even ten paise.
- 6) Damages for deterioration caused by delay: Such damages are recovered for damages or 'deterioration' caused to goods on account of delay by carriers
- 7) Remote or indirect damages: The remote damages are not recoverable.

LIQUIDATED DAMAGES AND PENALTY

- ✓ Liquidated damages: Pre-estimated damages which shall arise in ordinary breach circumstances. Intention of parties is to recover the loss. Its genuine calculation of loss.
- ✓ Penalty: Pre-estimated penalty which shall arise in ordinary breach circumstances.
- ✓ Intention of parties is to punish the other party. Its not genuine calculation but its a random amount
- ✓ As per Indian law, there is no difference between Liquidated damages and Penalty but English Law recognizes the difference between the two.
- ✓ Only court can reduce the amount of Liquidated damages/Penalty if it is found unreasonable. However even court cannot increase the amount.
- ✓ A party who rightfully rescinds the contract only can claim damages.

DISCHARGE OF CONTRACT

Discharge of contract and discharge of party are different.

1. Discharge by performance
2. Discharge by mutual agreement
3. Discharge by impossibility of performance
4. Discharge by lapse of time
5. Discharge by operation of law
6. Discharge by breach of contract
7. Discharge by remission
8. When a promise neglects or refuses to provide reasonable facilities for the performance, promisor and contract is discharged.

ADDITIONAL REMEDIES AVAILABLE IN CASE OF BREACH OF CONTRACT:

Apart from claiming damages, following remedies are available in case of breach of contract:-

1. Rescission of contract**2. Suit for Quantum Meruit****3. Suit for Specific Performance:**

Where (i) The damages are not an adequate remedy or

(ii) The damages cannot be estimated or

(iii) The subject matter of contract is unique in nature,

Then the aggrieved party can file a suit for specific performance in the court. However it is at the discretion of the court.

Specific performance cannot be ordered if

(i) Performance of contract is continuous in nature

(ii) Performance of contract involves personal skills

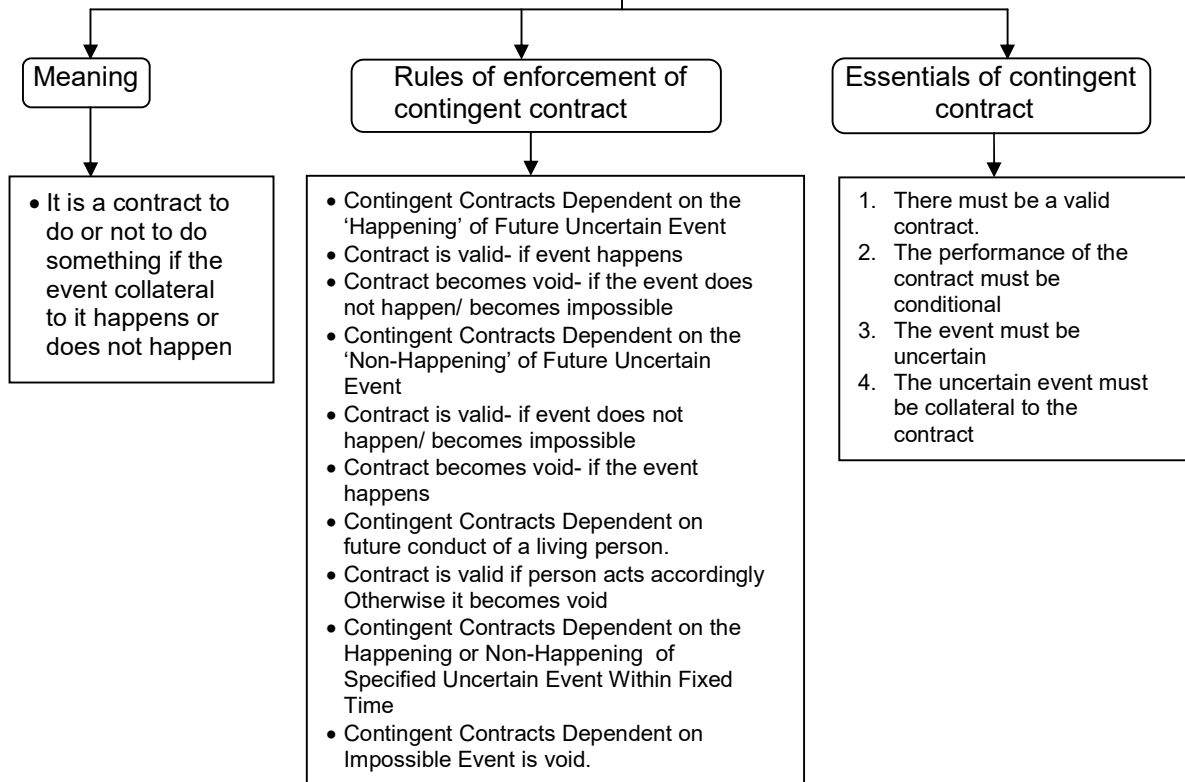
4. Suit for Injunction:

Injunction is an order of the courts restraining a person from doing something which he promised not to do. In this case also, the courts are at discretion to issue an injunction order.

Case Law: *Lumely v/s Wagner*

UNIT 6: CONTINGENT AND QUASI CONTRACT

CONTINGENT CONTRACTS



QUASI CONTRACTS

INTRODUCTION

It is an implied contract.
It is based on the principle of "Prevention of unjust enrichment at the expense of other"

CIRCUMSTANCES (OR CASES) OF QUASI CONTRACTS

1. Supply of necessaries to persons who are incompetent to contract
2. Payment by a Person Having Some Interest in Payment
Conditions:
 - (i) The person making the payment must have some interest in paying the amount.
 - (ii) The person making the payment must not be bound by law to pay the amount.
 - (iii) The other person from whom the money is sought to be recovered must be legally bound to pay the money.
3. Claim for any benefit received under a non-gratuitous act
Conditions:
 - (a) The person must lawfully do something for another person or deliver something to him.
 - (b) The person doing some act or delivering something must not intend to act gratuitously
 - (c) The other person must voluntarily accept the acts or goods and he must have enjoyed their benefits
4. Finder of goods
5. Payment of Money or Delivery of Goods by Mistake or Under Coercion

TOPIC : Indian Contract Act (Nature of Contracts, Consideration, Other Essential Elements of a Valid Contract)

QUESTION NO.1

A. Distinction between Void and Illegal Agreements. **(5 MARKS)**

B. Mr. Singh, an old man, by a registered deed of gift granted certain landed property to A, his daughter. By the terms of the deed, it was stipulated that an annuity of Rs. 2,000 should be paid every year to B, who was the brother of Mr. Singh. On the same day A made a promise to B and executed in his favour an agreement to give effect to the stipulation. A failed to pay the stipulated sum. In an action against her by B, as he contended that since B had not furnished any consideration, he has no right of action.

Examining the provisions to the Indian Contract Act, 1872, decide whether the contention of A is valid ? **(5 MARKS)**

QUESTION NO.2

A. Sohan induced Suraj to buy his motorcycle saying that it was in a very good condition. After taking the motorcycle, Suraj complained that there were many defects in the motorcycle. Sohan proposed to get it repaired and promised to pay 40% cost of repairs. After a few days, the motorcycle did not work at all. Now Suraj wants to rescind the contract. Decide giving reasons.

(4 MARKS)

B. Define the term "Acceptance". Discuss the legal provisions relating to communication of acceptance.

(6 MARKS)

QUESTION NO.3

A. What are the exceptions to the Doctrine of privity of Contract. **(6 MARKS)**

B. Mere silence does not amount to fraud." Discuss. **(4 MARKS)**

QUESTION NO.4

A. "Acceptance is to proposal what a lighted match – stick is to train of gun – powder."- Explain. **(4 MARKS)**

B. "No consideration, no contract" Comment **(6 MARKS)**



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ANSWER-1

ANSWER-A

Void and Illegal Agreements : According to Section 2(g) of the Indian Contract Act, an agreement not enforceable by law is void. The Act has specified various factors due to which an agreement may be considered as void agreement. One of these factors is unlawfulness of object and consideration of the contract i.e. illegality of the contract which makes it void. Despite the similarity between an illegal and a void agreement that in either case the agreement is void and cannot be enforced by law, the two differ from each other in the following respects :

(1 MARK)

- (i) **Scope** : An illegal agreement is always void while a void agreement may not be illegal being void due to some other factors e.g. an agreement the terms of which are uncertain is void but not illegal.
- (ii) **Effect on collateral transaction** : If an agreement is merely void and not illegal, the collateral transactions to the agreement may be enforced for execution but collateral transaction to an illegal agreement also becomes illegal and hence cannot be enforced.
- (iii) **Punishment** : Unlike illegal agreements, there is no punishment to the parties to a void agreement.
- (iv) **Void ab – initio** : Illegal agreements are void from the very beginning but sometimes valid contracts may subsequently become void.

(4*1 = 4 MARKS)

ANSWER-B

As per Section 2(d) of the Indian Contract Act, 1872, consideration is defined as “When at the desire of the promisor, the promisee or any other person did or abstained from doing, or does or abstains from doing, or promises to do or abstain from doing something, such act or abstinence is called a consideration for the promise”.

It is not necessary that consideration should be furnished by the promise only. A promise is enforceable if there is some consideration for it and it is quite immaterial whether it moves from the promise or any other person. The leading authority in the decision of the Chinnaya Vs. Ramayya, held that the consideration can legitimately move from a third party and it is an accepted principle of law in India. In the given problem. Mr. Singh has entered into a contract with A, but Mr. B has not given any consideration to A but the consideration did flow from Mr. Singh to A and such consideration from third party is sufficient to the enforce the promise of A, the daughter, to pay an annuity to B. Further the deed of gift and the promise made by A to B to pay the annuity were executed simultaneously and therefore they should be regarded as one transaction and there was sufficient consideration for it. **Thus, a stranger to the contract cannot enforce the contract but a stranger to the consideration may enforce it.**

ANSWER-2

ANSWER-A

According to Section 18 of the Indian Contract Act, 1872, misrepresentation is present :

1. When a **person positively asserts that a fact is true when his information does not warrant** it to be so, though he believes it to be true.
2. When there is **any breach of duty by a person, which brings an advantage to the person committing it by misleading another to his prejudice.**
3. When a party causes, however, innocently, the other party to the agreement to make a mistake as to the substance of the thing which is the subject of the agreement.

(3*1 = 3 MARKS)

The aggrieved party, in case of misrepresentation by the other party, can avoid or rescind the contract [Section 19, Indian Contract Act, 1872]. **The aggrieved party loses the right to rescind the contract if he, after becoming aware of the misrepresentation,** takes a benefit under the contract or in some way affirms it. Accordingly in the given case, **Suraj could not rescind the contract, as his acceptance to the offer of Sohan to bear 40% of the cost of repairs impliedly amounts to final acceptance of the sale.**

(1 MARK)

ANSWER-B

According to Section 2(b), the term 'acceptance' is defined as follows :

"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."

An acceptance in order to be valid must be absolute, unqualified, accepted according to the mode if any prescribed within reasonable time and communicated to offeror. Acceptance can also be made by way of conduct.

The **legal provisions relating to communication of acceptance are contained in Section 4.**

The **communication of an acceptance is complete** :

- (a) as against the proposer, when it is put in a course of transmission to him, so as to be out of power of the acceptor ;
- (b) as against the acceptor, when it comes to the knowledge of the proposer.

Example : A proposes, by letter, to sell a house to B at a certain price :

- (1) The communication is complete when B receives the letter.
- (2) B accepts the proposal by a letter sent by post. The communication is complete :
as against A, when letter is posted.

As against B when the letter is received by A.

Section 3 of the Act prescribes, in general terms, two modes of communication, namely :

- (1) **by any act** or
- (2) **by omission intending thereby communicate to the other** or which has the effect of communicating it to the other.

The first method would include any conduct and words whether written or oral. Written words would include letters, telegrams, text messages, advertisements, etc. Oral words would include telephone messages. Any conduct would include positive acts or signs so that the other person understands what the person acting or making signs means to say or convey. Omission would exclude silence but include such conduct or forbearance on one's part that the other person takes it as his willingness or assent. These are not the only modes of communication of the intention of the parties. There are other means as well, e.g., if you as the owner, deliver the goods to me as the buyer thereof at a certain price, this transaction will be understood by everyone, as acceptance by act or conduct, unless there is an indication to the contrary.

The phrase appearing in **Section 3 "which has the effect of communicating it,"** clearly refers to an **act or omission or conduct which may be indirect but which results in communicating an acceptance or non – acceptance.** However, a mere mental but unilateral act of assent in one's own mind does not tantamount to communication, since it cannot have the effect of communicating it to the other.

(6 MARKS)

ANSWER-3

ANSWER-A

Situation	Example
a) Trust or Charge : Beneficiary of a Trust or other interest in specific immovable property, can enforce it even if he is not a party named in the Trust Deed.	A agree to transfer certain properties to be held by T in trust for the benefit of B. B can enforce the agreement even though he is not a party to the agreement. [MK Rapai vs John]
b) Marriage Settlement, Partition and other Family Arrangements, and such agreement is reduced to writing.	Two brothers, on partition of joint properties, agreed to invest in equal shares a certain sum of money for the maintenance of their mother. Held she was entitled to require her sons to make the investment. [Shuppu Ammal vs Subramaniyam]
c) Acknowledgement of liability, or by past performance thereof	X receives money from Y for paying it to Z. X admits the receipt of that amount to Z. Z can recover the amount from X, even though the money is due from Y.
d) Assignment of a contract : Where a benefit under a Contract has been assigned, the assignee can enforce the Contract subject to all equities between the original parties to the Contract.	The assignee of an Insurance Policy.
e) Contracts entered into through an Agent	Where the agent has acted within his capacity and in the name of his principal.
f) Covenants running with land	In cases of transfer of immovable property,

the purchaser of land who has notice that the owner of the land is bound by certain conditions or covenants created by an agreement affecting the land, shall be bound by such conditions, even though he is not a party to the original agreement containing those conditions or covenants.

(6*1 = 6 MARKS)

ANSWER-B

Mere silence not amounting to fraud : Mere silence as to facts likely to affect the willingness of a person to enter into a contract is no fraud; but where it is duty of a person to speak, or his silence is equivalent to speech, silence amounts to fraud.

It is a rule of law that mere silence does not amount to fraud. **A contracting party is not duty bound to disclose the whole truth to the other party or to give him the whole information in his possession affecting the subject matter of the contract.**

The rule is contained in explanation to Section 17 of the Indian Contract Act which clearly states the position that mere silence as to facts likely to affect the willingness of a person to enter into a contract is not fraud.

(2 MARKS)

Exceptions to this rule :

- (i) Where the circumstances of the case are such that, regard being had to them, it is the **duty of the person keeping silence to speak**. Duty to speak arises when one contracting party reposes trust and confidence in the other or where one party has to depend upon the good sense of the other (e.g. Insurance Contract).
- (ii) **Where the silence is, in itself, equivalent to speech.**

(2*1 = 2 MARKS)

ANSWER-4

ANSWER-A

1. According to **William Anson**, Offer may be compared to a Train of Gun Powder and Acceptance to a Lighted Match – Stick. The moment, a lighted match – stick reaches a train of gun – powder, the train of gun – powder catches fire and leaves no trail but ash. But the train may move before the match stick reaches it.
2. If Acceptance (match – stick) reaches Offer (gun – powder), it culminates in a Contract, leaving as such no more Offer or Acceptance. But Offer can be revoked before acceptance reaches the Offeree.
3. Offer by itself is inert, it materialises into a Contract only when it is accepted, i.e., the train catches fire only when the match – stick reaches it. Thus, Once an Offer is accepted, it

becomes a Contract, and there can be no revocation as legal relationship is established between the parties.

4. But in the Indian context, revocation may be made even after sending letter of acceptance, but before it reaches the offeror. Hence, this statement has limited applicability to the Indian Contract Law.

(4*1 = 4 MARKS)

ANSWER-B

No consideration, no contract : Every agreement, to be enforceable by law must be supported by valid consideration. An agreement made without any consideration is void. **A gratuitous promise may form a subject of a moral obligation and may be binding in honour but it does not cause a legal responsibility**. For example, A promises to pay Rs. 100 to B. This promise cannot be enforced by B because he is not giving anything to A for this promise. No consideration, no contract is a general rule. However Section 25 of the Indian Contract Act provides some exceptions to this rule, where an agreement without consideration will be valid and binding. These exceptions are as follows :

(1 MARK)

- (i) **Agreement made on account of natural love and affection** : Section 25(1) provides that if an agreement is (i) **in writing** (ii) **registered under the law** and (iii) **made on account of natural love and affection** (iv) **between the parties standing in a near relation to each other**, it will be enforceable at law even if there is no consideration. Thus, where A, for natural love and affection, promises to give his son, B, Rs. 10,000 in writing and registers it. This is a valid contract.
- (ii) **Compensation for services voluntarily rendered** : Section 25(2) provides that something which the promisor was legally compelled to do; (iii) and the promisor was in existence at the time when the act was done whether he was competent to contract or not (iv) the promisor must agree now to compensate the promise. Thus when A finds B's purse and gives it to him and B promises to give A Rs. 50, this is a valid contract.
- (iii) **Promise to pay time – barred debts (Section . 25(3))** : Where there is an agreement, made in **writing and signed by the debtor or by his agent, to pay wholly or in part a time barred debt, the agreement is valid and binding even though there is no consideration**. If A owes B Rs. 1,000 but the debt is lapsed due to time – bar and A further makes a written promise to pay Rs. 500 on account of this debt, it constitutes a valid contract.
- (iv) **Contract of agency (Section. 185)** : No consideration is necessary to create an agency.
- (v) **Completed gift (Explanation 1 to Section 25)** : A completed gift needs no consideration. Thus if a person transfers some property by a duly written and registered deed as a gift he cannot claim back the property subsequently on the ground of lack of consideration.

(5*1 = 5 MARKS)

TOPICS : Indian Contract Act (Performance of Contract, Breach of Contract and its Remedies, Contingent & Quasi Contracts)

QUESTION NO.1

- A. Discuss the effect of accepting performance third person. **(4 MARKS)**
- B. Explain the – term 'Quasi Contracts' and state their characteristics. **(6 MARKS)**

QUESTION NO.2

- A. "Liquidated damage is a genuine pre – estimate of compensation of damages for certain anticipated breach of contract whereas Penalty on the other hand is an extravagant amount stipulated and is clearly unconscionable and has no comparison to the loss suffered by the parties." Explain. **(5 MARKS)**
- B. Suppose, time is of the essence of the contract but yet promisor does not perform the promise within the stipulated time. But five days after the expiry of the stipulated time, the promisor offers to perform his promise. Can the promisee accept such performance and at the same time claim compensation from the promisor for the delay ? **(5 MARKS)**

QUESTION NO.3

- A. Explain the meaning of 'Contingent Contracts' and state the rules relating to such contracts. **(7 MARKS)**
- B. "When a contract has been broken, the party who suffers by such a breach is entitled to receive compensation for any loss or damage caused to him". Discuss. **(3 MARKS)**

QUESTION NO.4

- A. "The basic rule is that the promisor must perform exactly what he has promised to perform." Explain stating the obligation of parties to contracts. **(5 MARKS)**
- B. "An anticipatory breach of contract is a breach of contract occurring before the time fixed for performance has arrived". Discuss stating also the effect of anticipatory breach on contracts. **(5 MARKS)**

QUESTION NO.5

- A. A, an Indian, contracts to marry B. A is already married – a – fact of which B was unaware. A breaks his promise in course of time. Thereupon B brings a suit against A for a breach of contract. A pleads that his promise is impossible of being performed as the law of the country does not permit polygamy. Can A get away with plea ?

(5 MARKS)

B. 'A, 'B' and 'C are partners in a firm. They jointly promise to pay Rs. 1,50,000 to 'P'. C became insolvent and his private assets are sufficient to pay only $1/5^{\text{th}}$ of his share of debts. A is compelled to pay the whole amount to P. Examining the provisions of the Indian Contract Act, 1872, decide the extent to which A can recover the amount from B. **(5 MARKS)**



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ANSWER-1

ANSWER-A

Effect of accepting performance from third person (Section 41)

When a promisee accepts performance of the promise from a third person, he cannot afterwards enforce it against the promisor.

That is, performance by a stranger, if accepted by the promisee, this results in discharging the promisor, although the latter has neither authorised nor ratified the act of the third party.

(2 MARKS)

Example : A received certain goods from B promising to pay Rs. 1,00,000/-. Later on, A expressed his inability to make payment. C, who is known to A, pays Rs. 60,000/- to B on behalf of A. However, A was not aware of the payment. Now B is intending to sue A for the amount of Rs. 1,00,000/- whether he can do so ? Advice.

As per Section 41 of the Indian Contract Act, 1872, when a promisee accepts performance of the promise from a third person, he cannot afterwards enforce it against the promisor. That is, performance by a stranger, accepted by the promisee, produces the result of discharging the promisor, although the latter has neither authorised nor ratified the act of the third party. Therefore, in the present instance, B can sue only for the balance amount i.e., Rs. 40,000/- and not for the whole amount.

(2 MARKS)

ANSWER-B

Quasi Contracts : Under certain special circumstances obligation resembling those created by a contract are imposed by law although the parties have never entered into a contract. Such obligations imposed by law are referred to as 'Quasi – contracts'. Such a contract resembles with a contract so far as result or effect is concerned but it has little or no affinity with a contract in respect of mode of creation. These contracts are based on the doctrine that a person shall not be allowed to enrich himself unjustly at the expense of another. The salient features of a quasi – contract are :

(1 MARK)

1. It does not arise from any agreement of the parties concerned but is imposed by law.
2. Duty and not promise is the basis of such contract.
3. The right under it is always a right to money and generally though not always to a liquidated sum of money.
4. Such a right is available against specific person(s) and not against the whole world.
5. A suit for its breach may be filed in the same way as in case of a complete contract.

(5*1 = 5 MARKS)

ANSWER-2

ANSWER-A

Liquidated damage is a **genuine pre – estimate of compensation of damages for certain anticipated breach of contract.** This estimate is agreed to between parties to avoid at a later date detailed calculations and the necessity to convince outside parties.

Penalty on the other hand is an extravagant amount stipulated and is clearly unconscionable and has no comparison to the loss suffered by the parties.

In terms of Section 74 of the Act “where a contract has been broken, if a sum is named in the contract as the amount to be paid in case of such breach, or if the contract contains any other stipulation by way of penalty, the party complaining of the breach is entitled, whether or not actual damages or loss is proved to have been caused thereby, to receive from the other party who has broken the contract, a reasonable compensation not exceeding the amount so named, or as the case may be the penalty stipulated for.

(3 MARKS)

Explanation to Section 74

A stipulation for increased interest from the date of default may be a stipulation by way of penalty.

In terms of Section 74, courts are empowered to reduce the sum payable on breach whether it is ‘penalty’ or “liquidated damages” provided the sum appears to be unreasonably high.

Sri Chunnilal vs. Mehta & Sons Ltd.(Supreme Court)

Supreme Court laid down the ratio that the aggrieved party should not be allowed to claim a sum greater than what is specific in the written agreement. But even then the court has powers to reduce the amount if it considers it reasonable to reduce.

(2 MARKS)

ANSWER-B

As per **Section 55 of Indian Contract Act, 1872, where the intention of the parties is that the time should be of the essence of the contract the contract must be performed within the fixed time.**

And if the party, who is bound to perform his promise within the fixed time, fails to do so then the contract becomes voidable at the option of the other party. Thus, the innocent party may put an end to the contract if he so chooses and he can also claim damages.

In the given question, **time is of the essence of the contract but yet promisor does not perform the promise within the stipulated time.** But five days after the expiry of the stipulated time, the promisor offers to perform his promise. With respect to above provisions, **promise can accept such performance and at the same time claim compensation from the promisor for the delay.**

(5 MARKS)

ANSWER-3

ANSWER-A

Essential characteristics of a contingent contract : A **contract may be absolute or contingent**. A **contract is said to be absolute when the promisor undertakes to perform the contract in all events. A contingent contract, on the other hand” is a contract to do or not to do something, if some event, collateral to such contract does or does not happening** (Section 31). It is a contract in which the performance becomes due only upon the happening of some event which may or may not happen.

For example, A contracts to pay B Rs. 10,000 if he is elected President of a particular association. This is a contingent contract. The essential characteristics of a contingent contract may be listed as follows :

- (i) There must be a **contract to do or not to do something**,
- (ii) The performance of the contract must **depend upon the happening or non – happening of some event**.
- (iii) The **happening of the event is uncertain**.
- (iv) The **event on which the performance is made to depend upon is an event collateral to the contract** i.e. it does not form part of the reciprocal promises which constitute the contract. The event should neither be a performance promised, nor the consideration for the promise.
- (v) The contingent event **should not be the mere will of the promisor**. However, where the event is within the promisor’s will, but not merely his will, it may be a contingent contract.

(5 MARKS)

The rules regarding the contingent contract are as follows “

- (1) Contingent contract dependent on the happening of an uncertain future cannot be enforced until the event has happened. If the event becomes impossible, such contracts become void. **(Sec. 32)**.
- (2) Where a contingent contract is to be **performed if a particular event does not happening performance can be enforced only when happening of that event becomes impossible** (Sec. **33**).
- (3) If a contract is contingent upon, how a person will act at an unspecified time the event shall be considered to become impossible ; **when such person does anything which renders it impossible that he should so act within any definite time or otherwise than under further contingencies. (Section 34,35)**.
- (4) The **contingent contracts to do or not to do anything if an impossible happens, are void whether or not the fact is known to the parties** (Sec. 36).

(0.5*4 = 2 MARKS)

ANSWER-B

Compensation for loss or damage caused by breach of contract (Section 73)

When a contract has been broken, the party who suffers by such a breach is entitled to receive, from the party who has broken the contract, compensation for any loss or damage caused to him thereby, which naturally arose in the usual course of things from such breach, or which the parties knew, when they made the contract, to be likely to result from the breach of it.

Such compensation is not to be given for any remote and indirect loss or damage sustained by reason of the breach.

In view of above, the statement given in the question seems to be incorrect.

(3 MARKS)

ANSWER-4

ANSWER-A

1. **Obligations of parties to contracts (Section 37)**

The parties to a contract must either perform, or offer to perform, their respective promises unless such performance is dispensed with or excused under the provisions of the Contract Act or of any other law.

Promises bind the representatives of the promisor in case of death of such promisor before performance, unless a contrary intention appears from the contract.

Example 1 : A promises to deliver goods to B on a certain day on payment of 1,00,000. A dies before that day. A's representatives are bound to deliver the goods to B, and B is bound to pay 1,00,000 to A's representatives.

Example 2 : A promises to paint a picture for B by a certain day, at a certain price. A dies before the day. The contract cannot be enforced either by A's representative or by B because it involves use of personal skill.

Analysis of Section 37

A contract being an agreement enforceable by law, creates a legal obligation, which subsists until discharged. Performance of the promise or promises remaining to be performed is the principal and most usual mode of discharge.

The basic rule is that the promisor must perform exactly what he has promised to perform. The obligation to perform is absolute. Thus, it may be noted that it is necessary for a party who wants to enforce the promise made to him, to perform his promise for himself or offer to perform his promise. Only after that he can ask the other party to carry out his promise. This is the principle which is enshrined in Section 37.

Thus, it is the primary duty of each party to a contract to either perform or offer to perform his promise. He is absolved from such a responsibility only when under a provision of law or an act of the other party to the contract, the performance can be dispensed with or excused.

ANSWER-B

An anticipatory breach of contract is a breach of contract occurring before the time fixed for performance has arrived. **When the promisor refuses altogether to perform his promise and signifies his unwillingness even before the time for performance has arrived, it is called Anticipatory Breach.** The law in this regard has very well summed up in **Frost v. Knight and Hochster v. DelaTour :**

Section 39 of the Indian Contract Act deals with anticipatory breach of contract and provides as follows : “When a party to a contract has refused to perform or disable himself from performing, his promise in its entirety, the promise may put an end to the contract, unless he has signified, but words or conduct, his acquiescence in its continuance.”

(3 MARKS)

Effect of anticipatory breach : The promise is excused from performance or from further performance. Further he gets an option :

- (1) To either **treat the contract as “rescinded and sue the other party for damages** from breach of contract immediately without waiting until the due date of performance; or
- (2) He may elect not to rescind but to **treat the contract as still operative, and wait for the time of performance** and then hold the other party responsible for the consequences of non – performance. But in this case, he will keep the contract alive for the benefit of the other party as well as his own, and the guilty party, if he so decides on re – consideration, may still perform his part of the, contract and can also take advantage of any supervening impossibility which may have the effect of discharging the contract.

(2*1 = 2 MARKS)

ANSWER-5**ANSWER-A**

As per Section 73 of Indian Contract Act, 1872, **the vindictive damages are claim with the intention of punishing the party in default.** As a general rule, the exemplary damages are not awarded for the breach of contract as they are punitive in nature. However, in following case, the court may award exemplary damages :

Where there is a breach of a promise to marry : In such cases, the damages will include compensation for loss to the feelings and reputation of the aggrieved party.

In the given question, A, an Indian, contracts to marry B. A is already married – a – fact of which B was unaware. A breaks his promise in course of time. Thereupon B brings a suit against A for a breach of contract. A pleads that his promise is impossible of being performed as the law of the country does not permit polygamy.

A can get away with the plea as the marriage cannot be forced upon. However, he is liable to vindictive damages as stated above.

(5 MARKS)

ANSWER-B

As per Section 43 of the Indian Contract Act, 1872, when two or more persons make a joint promise, the promise may in the absence of express agreement to the contrary, compel anyone or more of such joint promisors to perform the whole of the promise. In such a situation the performing promisor can enforce contribution from other joint promisors. If anyone or more joint promisors make default in such contribution, the remaining joint promisors must bear the loss arising from such default in equal share. Hence in the instant case, A is entitled to receive (a) from C's assets –

Rs. 10,000 ($\frac{1}{5}^{\text{th}}$ of Rs. 50,000) and (Rs. 50,000 is the amount to be contributed by C being $\frac{1}{3}^{\text{rd}}$ of Rs. 1,50,000), (b) from b – Rs. 70,000 (Rs. 50,000 being his own share + $\frac{1}{2}$ (50,000 – 10,000) i.e. Rs. 20,000 being one half share of total loss of Rs. 40,000 due to C's insolvency). A can recover Rs. 70,000 from B.

(5 MARKS)

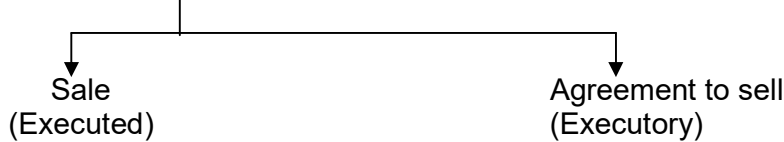
CHAPTER 2 - SALE OF GOODS ACT

UNIT 1 : FORMATION OF CONTRACT OF SALE

• **INTRODUCTION**

- Introduced on 1st of July, 1930
- Applicable to whole of India except Jammu & Kashmir
- This law was previously part of Indian Contract Act, 1872
- Where the Sale of Goods Act is silent on any point, the Indian Contract Act is applicable.

• **CONTRACT OF SALE**

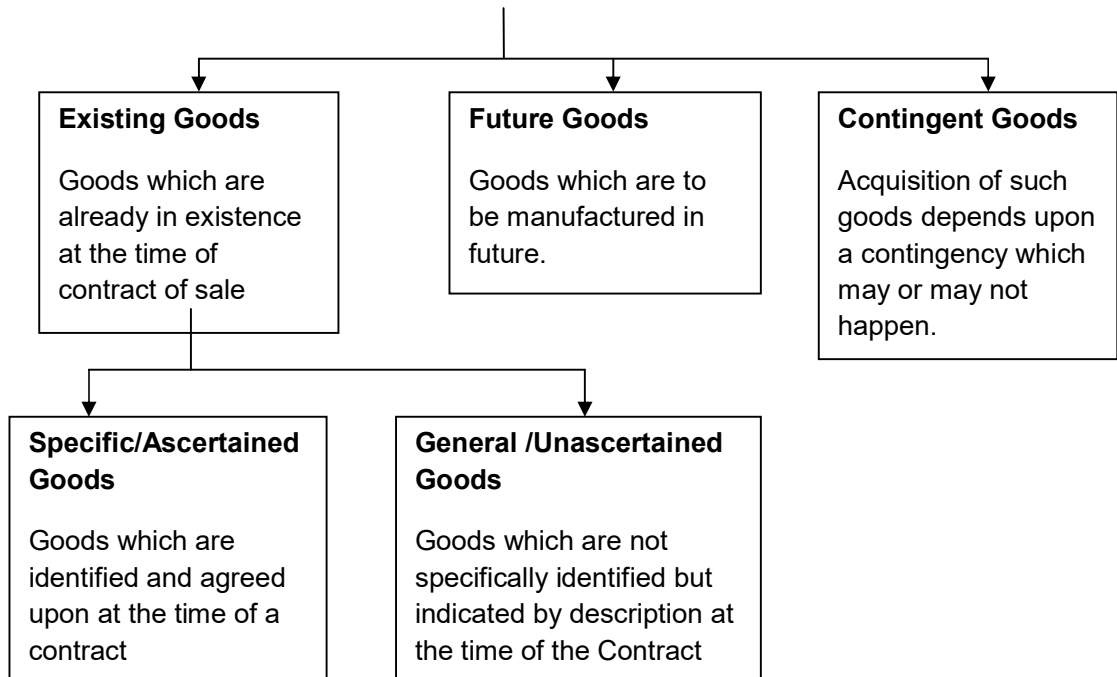


“A contract of sale of goods is a contract whereby the seller transfers or agrees to transfer the property in the goods to the buyer for a price

• **DEFINITIONS**

1. Buyer: Buyer means a person who buys or agrees to buy goods.
2. Seller: Seller means person who sells or agrees to sell goods.
3. Goods: Any movable asset, except money and actionable claims, including stocks and shares, including growing crops, grass and things attached to or forming part of the land which are can be severed before the contract of sale.

Classification of Goods



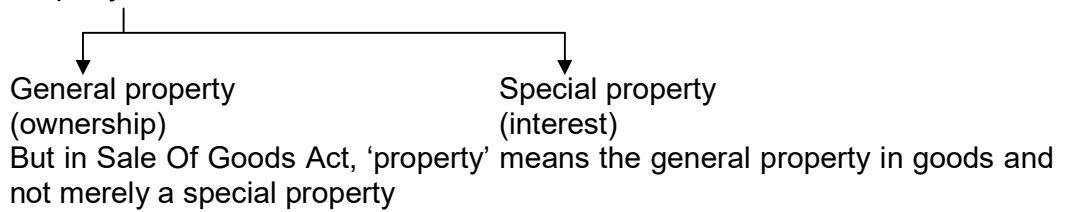
- ✓ Money here means legal tender of money, i.e. the recognised circulation in the country; but not old rare coins.
- ✓ Things attached to the earth are not movables, but trees, growing crops which can be easily severed from the earth before sale. Fruits, vegetables and flowers which can be separated from the trees, are included in 'goods'.
- ✓ Livestock i.e. cows, buffaloes, cats etc are 'goods'.
- ✓ Patents, copyrights, goodwill, trade-marks, are all considered goods which can be the subject matter of a contract.
- ✓ Water, gas and electricity are goods
- ✓ As per English law, "shares and stock" are not treated as "goods".
- ✓ To conclude, everything movable is goods, except the following:-
 1. Money
 2. Actionable Claims
 3. Immovable assets
 4. Services
 5. Human Beings

4. Price

= Money Consideration of the goods

- Gift of Goods ≠ Sale Of Goods Act
- Exchange of goods for goods i.e Barter ≠ Sale Of Goods Act
- Exchange of goods for goods + Price = Sale Of Goods Act

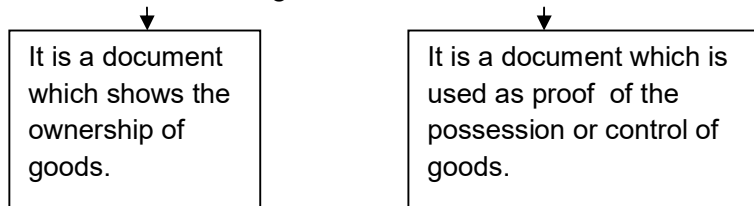
5. Property



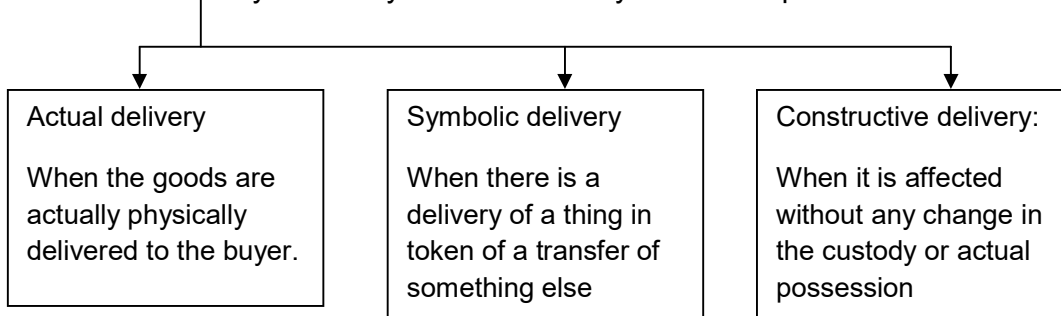
6. Mercantile Agent

Mercantile Agent means an agent having authority to sell goods, or to consign goods for the purpose of sale, or, to buy goods, or to raise money on the security of goods.

7. Documents showing Title to Goods/ Documents of Title to Goods



8. Delivery: Delivery means voluntary transfer of possession



- **ESSENTIAL ELEMENTS OF A VALID CONTRACT OF SALE**
 1. All the requirements of a valid contract must be fulfilled
 2. There must be two parties to the contract of sale
 3. There must be some goods as a subject-matter
 4. The general property in the goods must be transferred to the buyer
 5. There must be some price for the goods
 6. A contract of sale can be absolute or conditional

- **DISTINGUISH BETWEEN**

1. **Sale and Bailment**

Sale	Bailment
1. The ownership in goods is transferred from the seller to the buyer.	1. There is only transfer of possession of goods from the bailor to the bailee
2. The return of goods in contract of sale is not possible.	2. The bailee must return the goods to the bailor on the fulfilment of the purpose for which the bailment was made.
3. The consideration is the price in terms of money.	3. The consideration may be gratuitous or non-gratuitous.

2. **Sale and Agreement to sell**

Sale	Agreement to sell
1. Ownership and risk are immediately transferred	1. Ownership and risk are transferred at some future time
2. A sale is an executed contract	2. An agreement to sell is an executory contract
3. Consequences of Breach by buyer : In a sale, if the buyer fails to pay for the goods, the seller can: (i) File a suit for recovery of price (ii) Claim damages.	3. Consequences of Breach by buyer : In an agreement to sell, if the buyer fails to pay for the goods, the seller can only claim damages for breach of contract
4. Consequences of Breach by seller : In a sale, if the seller defaults, i.e. commits a breach, the buyer can: (i) sue for damages (ii) claim the goods back from third party	4. Consequences of Breach by seller : In the case of an agreement to sell, if the seller commits a breach, the buyer can only claim damages.
5. A subsequent loss or destruction of the goods is the liability of the buyer	5. Such loss or destruction is the liability of the seller.

3. Sale and Hire Purchase

Sale	Hire Purchase
1. Ownership is transferred immediately	1. The ownership in goods passes to the hirer upon payment of the last instalment.
2. The position of the buyer is that of the owner of the goods.	2. The position of the hirer is that of a bailee till he pays the last
3. The return of goods in contract of sale is not possible.	3. The hirer may, if he so likes, terminate the contract by returning the goods to its owner without any liability to pay the remaining instalments.
4. If buyer becomes insolvent, seller takes the risk	4. The owner takes no such risk, for if the hirer fails to pay an instalment the owner has right to take back the goods.
5. The buyer can resell the goods.	5. The hirer cannot resell the goods
6. Tax is levied at the time of the contract.	6. Tax is not leviable until it eventually converted into a sale.

- **CONTRACT FOR WORK AND LABOUR**

In contract for work and labour or materials, the contract is for the exercise of the skill and labour, and delivery of goods is only subsidiary.

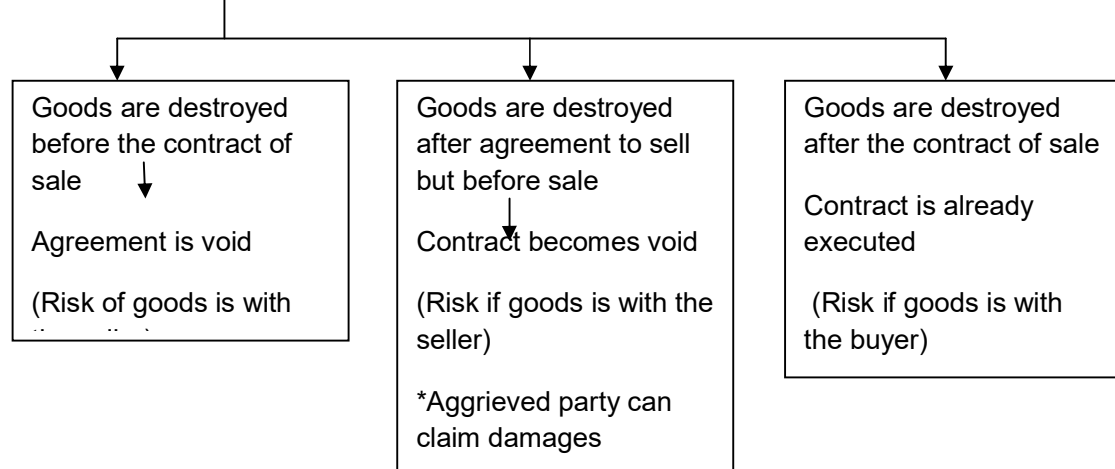
- **FORMATION AND MODES OF A CONTRACT OF SALE**

A contract of sale may be made in anyone of the following modes:

1. There may be immediate delivery of goods, but the price to be paid at some future date.
2. There may be immediate payment of price, but the delivery to be made at some future date.
3. There may be immediate payment of price and the immediate delivery of goods.
4. The price and delivery of the goods may be postponed.
5. The price and delivery of the goods may be agreed to be made in instalments.

A contract of sale may be made (a) in writing, or (b) by words of mouth , or (c) partly in writing and partly by words of mouth, or (d) may be implied from the conduct of the parties. However, if any particular mode is prescribed by any law, then the contract of sale must be made in that particular mode

- **EFFECT OF DESTRUCTION OF GOODS**



- **PRICE AND MODES OF FIXING THE PRICE**

Price may be fixed in any of the following modes:

1. The fixation of price by the contract of sale
 2. The fixation of price in a manner provided in the contract of sale [
 3. The fixation of price by course of dealings
 4. The fixation of a reasonable price
 5. The fixation of price by third party:
- ✓ However, if such third party fails to make the valuation, the contract becomes void. But if the buyer has received the goods and has appropriated them, he becomes bound to pay reasonable price to the seller.
 - ✓ Sometime, the third party is influenced or prevented by the buyer or the seller from fixing the price. In such cases, the innocent party may recover damages from the defaulting party.

UNIT 2: CONDITIONS AND WARRANTIES

Conditions & Warranties

Stipulations

- ✓ Condition: Stipulation essential to the main purpose of the contract
In Breach of Condition, buyer can
 - (i) 3Rs → Rescind the contract, Return the goods, claim Refund
 - (ii) Claim damages
- ✓ Warranty: Stipulation collateral to the main purpose of the contract
In Breach of Warranty, buyer can
 - (i) Only claim damages

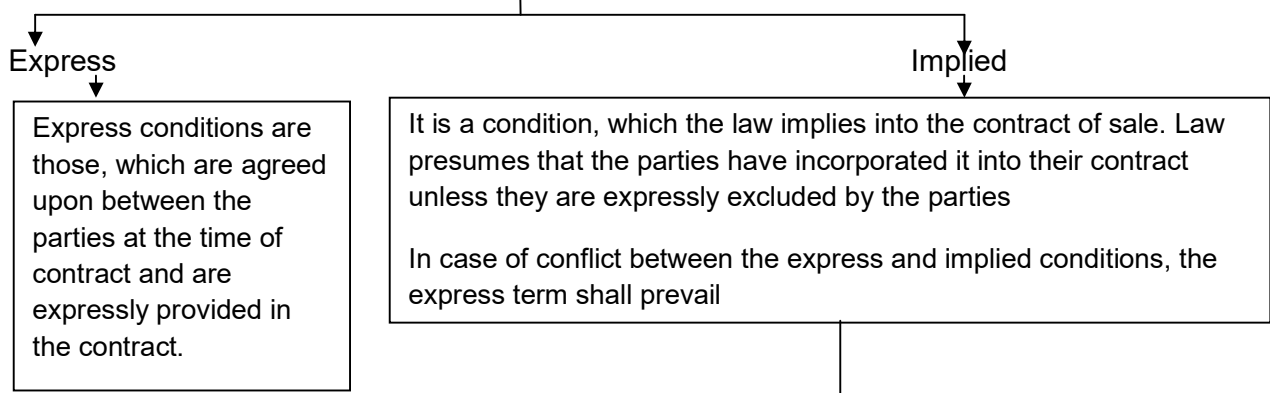
✓ **DISTINCTION BETWEEN CONDITION AND WARRANTY**

CONDITION	WARRANTY
1. A condition is a stipulation which is essential to the main purpose of the contract.	1. It is only collateral to the main purpose of the contract.
2. In Breach of Condition, buyer can <ul style="list-style-type: none"> i. 3Rs → Rescind the contract, Return the goods, claim Refund ii. Claim damages 	In Breach of Warranty, buyer can <ul style="list-style-type: none"> i. Only claim damages
3. A breach of condition may be treated as a breach of warranty	3. A breach of warranty cannot be treated as a breach of condition

✓ **WHEN A CONDITION CAN BE TREATED AS A WARRANTY:**

1. Voluntary waiver of condition by buyer
2. Buyer treats the breach of the condition as breach of warranty
3. Waiver by law as to impossibility
4. Where a contract of a sale is not severable and the buyer has accepted the goods or part thereof, then buyer cannot reject the goods and can only claim damages.

CONDITION



1. Conditions as to title: It is presumed that the seller has a valid title to the goods, i.e., he has the right to sell the goods. If later on, the buyer comes to know that the seller had no valid right to sell the goods, then he may reject the goods and claim the refund of the price, if already paid

2. Condition as to sample: In case of sale of goods by showing the sample to the buyer, there is an implied condition that the goods delivered shall correspond with the quality of the sample.

3. Condition as to description: When the goods are sold by description, there is an implied condition is that the goods shall correspond with the description.

4. Condition as to sample as well as description:When the seller shows sample of the goods to the buyer and also gives him their description, there is an implied condition is that the goods shall correspond with both, the sample as well as description.

5. Condition as to quality or fitness for buyer's purpose: Ordinarily, there is, no implied condition that the goods shall be fit for the particular purpose of the buyer as seller is not responsible in following cases:

- (i) To know the particular purpose of buyer.
 - (ii) If buyer chooses the goods negligently.
- However in following exceptions, seller is responsible to the buyer:
- (i) If the buyer makes his purpose clear to the seller.
 - (ii) If the buyer buys the goods 'relying upon his skill and judgment'.

6. Condition as to merchantability:The term 'merchantability' has not been defined in the Sale of Goods Act.

Goods are purchased for

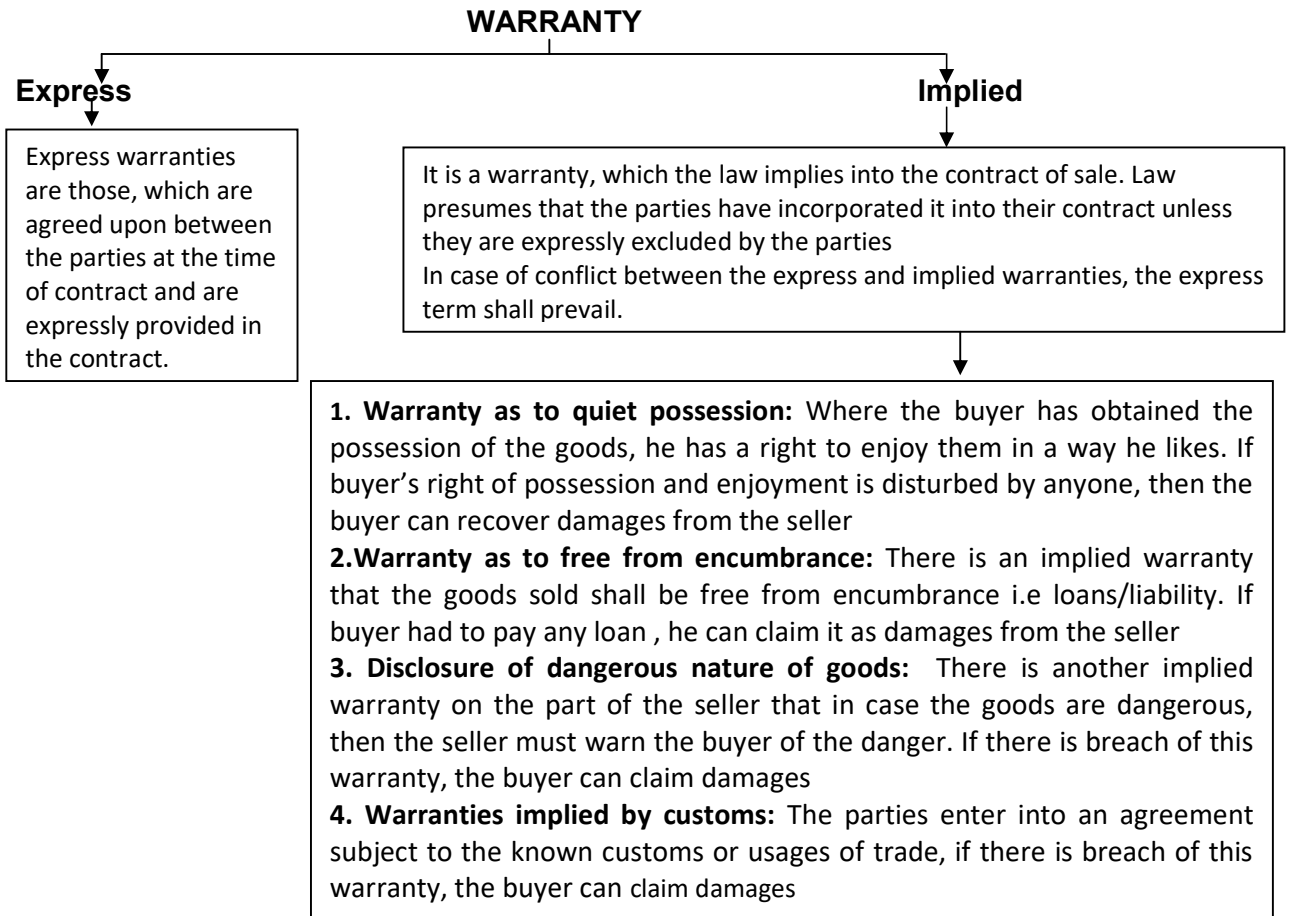
Self use

Then they should be reasonably fit for the purpose for which they are generally used

Resale

Then they should be immediately re-saleable in the market under their description

7. Condition as to wholesomeness: As per this condition, foodstuffs/eatables sold must be fit for human consumption.



✓ **DOCTRINE OF CAVEAT EMPTOR (BUYER BEWARE)**

✓ The Doctrine states generally seller is not responsible for bad goods. This Doctrine takes the side of the seller.

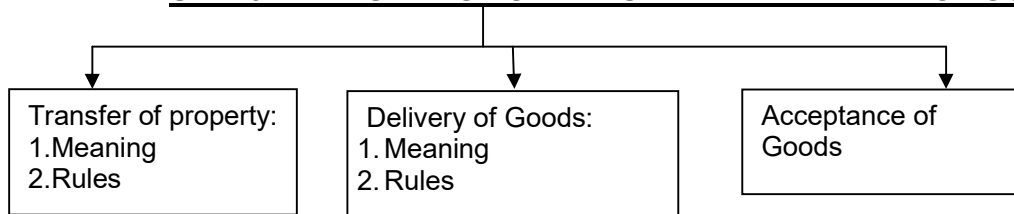
Seller is not responsible in following cases:-

- (i) To know the particular purpose of buyer.
- (ii) If buyer chooses the goods negligently
- (iii) If the goods are defective and the defect is patent (i.e defect which can be discovered by mere inspection)

✓ Exceptions : The exceptions to the doctrine of Caveat Emptor; which are mentioned below (i.e in the following seller is responsible) :

1. Where the buyer specifies the particular purpose for which the goods are required to the seller.
2. Where buyer relies on the seller's skill or judgment.
3. Where there is contract of sale by sample, the rule of caveat emptor will not apply if the goods do not correspond with sample
4. Where goods are bought by description, the goods shall correspond with the description.
5. If the goods are bought both by sample as well as by description this rule will not apply if goods do not correspond with both sample and description.
6. There is an implied condition that the goods shall be of merchantable quality
7. When the seller actively conceals some defect in the goods so that the same could not be discovered by the buyer on a reasonable examination, then the rule of Caveat Emptor will not apply.
8. When the goods are purchased under some brand name.

UNIT 3: TRANSFER OF OWNERSHIP AND DELIVERY OF GOODS



✓ **TRANSFER OF PROPERTY**

Meaning: The term 'property in the goods' may be defined as the legal ownership of the goods.

Transfer of Ownership means transfer of Risk, Rights and Returns pertaining to the goods

Rules:

1. The ownership is transferred at the time of making the contract if the following conditions' are fulfilled:
 - a) The sale must be of specific/ascertained goods
 - b) The goods must be in a deliverable state
 - c) The contract of sale must be unconditional

2. Transfer of ownership in case of sale of unascertained goods
 - (a) When the goods are ascertained and
 - (b) When the goods are appropriated to the contract: Appropriation is the process by which the goods to be delivered under the contract are identified and set apart with the mutual consent of the seller as well as buyer.

3. Where the specific goods are to be put in a deliverable state by the seller , the ownership is transferred as soon as the seller has put the goods in a deliverable state and the buyer comes to know about the act of the seller.

4. Where the specific goods in a deliverable state are to be weighed or measured by the seller to ascertain the price, the ownership is transferred to the buyer as soon as the seller has done the act of ascertaining the price and the buyer comes to know about this act of the seller.

5. However, parties may decide to pass the ownership as per the contract.

6. Transfer of ownership in case of sale on approval
 - ✓ The ownership of goods is with seller and the possession of goods is with buyer
 - ✓ The buy er has an option to return the goods.
 - ✓ The ownership is transferred to the buyer in any of the following three ways:
 - a) When the buyer accepts the goods
 - b) When the buyer adopts the transaction by doing some act which shows that he has accepted the goods
 - c) Where the buyer fails to return the goods within fixed or reasonable time

7. Reservation of right of disposal
 - ✓ The seller may like to retain the ownership of the goods until some later date, e.g., until the price is paid or some conditions are fulfilled. The seller may do so by reserving his right of disposal.

- ✓ In the following two circumstances the seller is presumed to have reserved the right of disposal :
 1. By taking the documents showing title in his own name or his agent's name
 2. By sending the bill of exchange for the price, to the buyer, along with the documents of title

- 8. Risk passes with the ownership
 - ✓ The risk and the ownership of the goods go together. In other words, the goods are at the risk of the party who has the ownership of the goods.
 - ✓ Exceptions:
 - a) Agreement between the parties: The risk and the ownership may be separated by an agreement between the seller and the buyer.
 - b) Goods are at the risk of the party in default
 - c) Trade customs : The risk and the ownership may also be separated by the trade customs

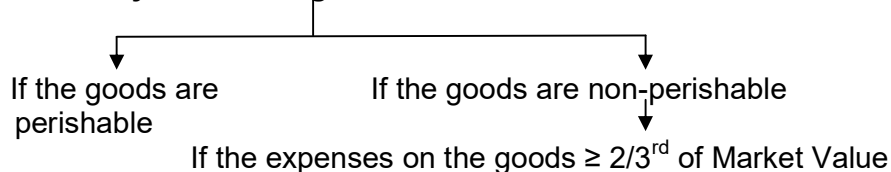
9. Transfer of title by non-owners

- ✓ "Nemo dat quod non-habet": This means that 'no one can transfer a better title than he himself has'. Thus, the buyer cannot get a better title than that of the seller. If the seller's own title is defective, the buyer's title will also be defective.

✓ **Exceptions:**

In the following exceptional circumstances a non-owner can transfer a valid title to a bonafide buyer:

- 1) **Sale by a mercantile agent**
- 2) **Sale by a joint owner:** When the joint owner is in the sole possession of the goods, and he sells them to a person who buys in a good faith, the buyer gets a valid title to the goods.
- 3) **Sale by estoppel:** When the owner of goods, by his conduct or by statement, wilfully leads the buyer to believe that the seller has the authority to sell, then he is estopped (i.e., prevented) from denying the seller's authority to sell
- 4) **Sale by unpaid seller:** To be done in Unit 4
- 5) **Sale by a seller in possession of goods after their sale :** If the seller continues to have the possession of the goods even after their sale and if he resells the same goods to a new buyer then in such cases, the second buyer gets a valid title to the goods if he buys them in a good faith
- 6) **Sale by a buyer in possession of goods after their sale:** If the buyer obtains the possession of the goods which he has bought or agreed to buy from the seller and the seller still has some lien or other rights over the goods. If the buyer resells the same goods to a new person. In such cases, the second buyer gets a valid title free.
- 7) **Sale by a finder of goods:**



- 8) **Sale by a person in possession under a voidable contract:** The buyer gets a valid title only if the following conditions are satisfied:-
 - a. A person must obtain the possession of the goods by coercion, undue influence, fraud or misrepresentation.

- b. The seller must have obtained the possession of the goods under a voidable contract and not under a void contract.
 - c. The contract must not have been rescinded (i.e., put to an end) at the time of sale
 - d. The buyer must act in a good faith.
- 9) Sale Under the Provision of Other Acts :**
- a. Sale by an Official Receiver or Liquidator of the Company will give a valid title to the purchaser.
 - b. Sale by a pawnee/pledgee under default of pawnor in repayment of debt will give valid title to the purchaser.
 - ❖ In case of hire-purchase, hirer cannot pass a good title even to a bonafide buyer.

✓ **DELIVERY OF GOODS**

Meaning: "Delivery" means a voluntary transfer of possession from one person to another.

Delivery of goods may be actual, symbolic or constructive.

Rules:

1. Buyer in position to access the goods:

The delivery of the goods may be made in any of the modes, but it must have the effect of putting the goods in the possession of the buyer or his agent.

2. Demand for delivery of goods:

It is seller's duty to put the goods in deliverable state and inform the buyer regarding same. It is buyer's duty to make a demand for the delivery of the goods.

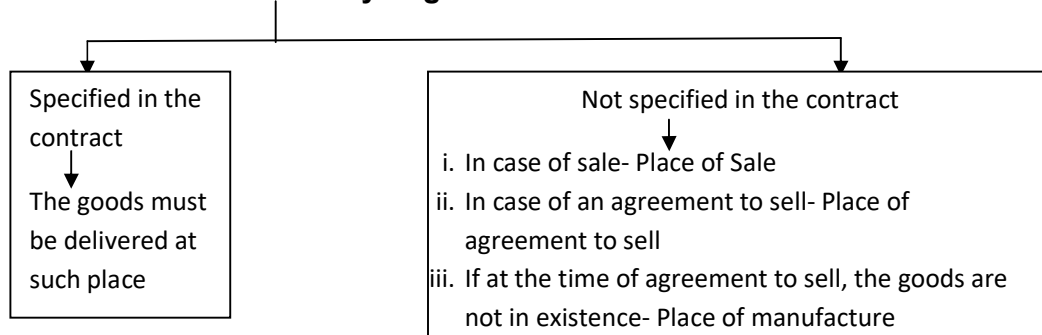
3. Goods in the possession of a third person:

Sometimes, at the time of sale, the goods are in the possession of a third person. In such cases, the effective delivery takes place when such person acknowledges to (i.e., inform) the buyer, that he holds the goods on his (buyer's) behalf.

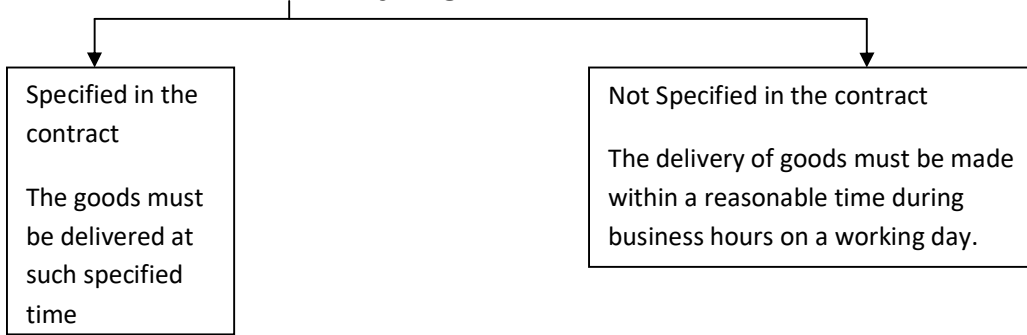
4. Delivery to a carrier or wharfinger:

Where the sold goods are delivered to a carrier/wharfinger for the purpose of transmission to the buyer or safe custody, the delivery of goods to the carrier/wharfinger is treated as a delivery to the buyer.

5. Place for the delivery of goods:



6. Time for the delivery of goods:



7. Time for demand or tender of delivery:

The demand of delivery by the buyer must be made within reasonable time during business hours and on a working day.

8. Expenses for the delivery of goods:

The expenses of putting the goods into a deliverable state are borne by the seller. And the expenses of receiving the goods are borne by the buyer. However, the seller and the buyer may also agree otherwise

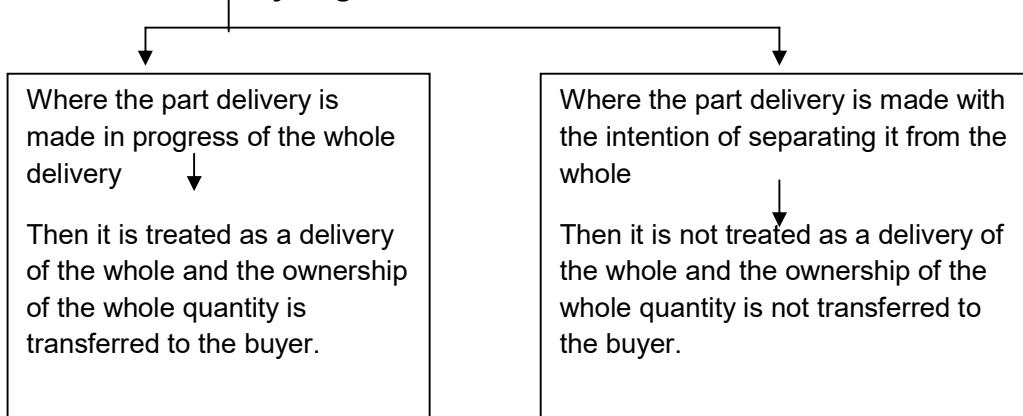
9. Deterioration of goods during transit:

The buyer shall bear the loss of deterioration of goods which is incidental i.e. natural in transit.

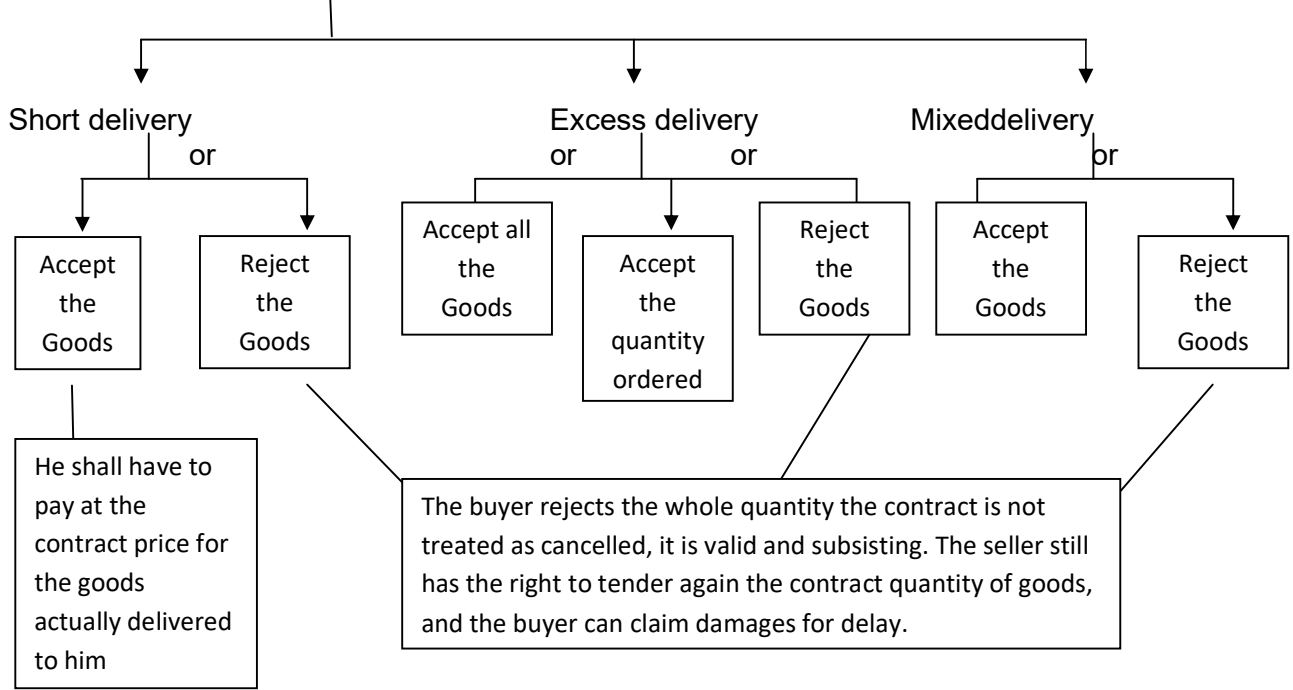
10. Delivery of goods by instalments:

As a rule, the delivery of goods by instalments is not considered as a good delivery and the buyer is not bound to accept the goods delivered to him by instalments, unless otherwise agreed.

11. Part delivery of goods:



12. Delivery of wrong quantity:



✓ **ACCEPTANCE OF DELIVERY OF GOODS**

Acceptance is deemed to take place when the buyer-

- (a) intimates to the seller that he had accepted the goods; or
- (b) does any act to the goods, which is inconsistent with the ownership of the seller i.e when the buyer adopts the transaction by doing some act which shows that he has accepted the goods; or
- (c) retains the goods after the lapse of a reasonable time, without intimating to the seller that he has rejected them

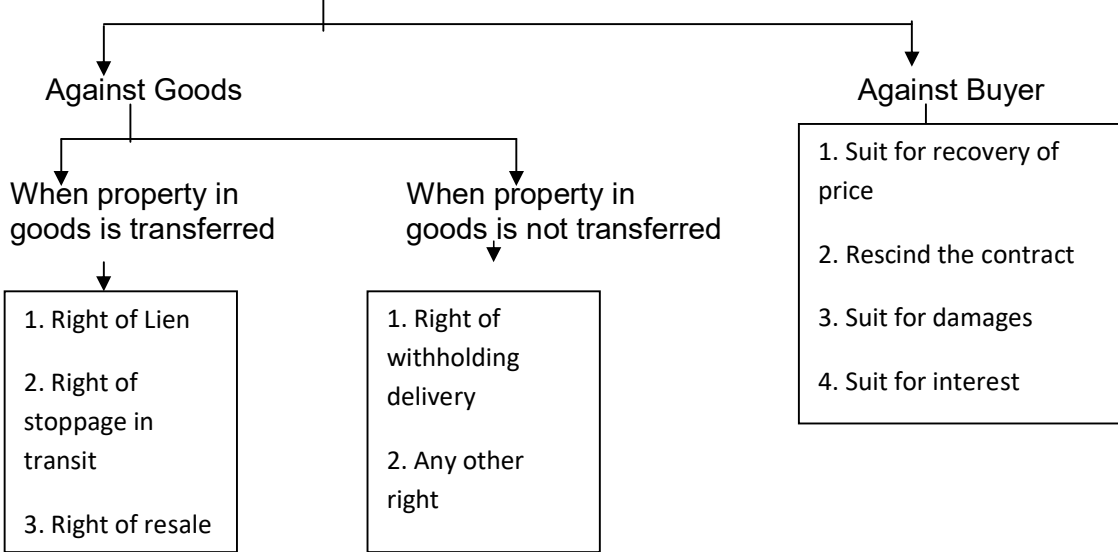
UNIT 4: UNPAID SELLER

✓ **MEANING OF UNPAID SELLER:**

A seller will be called 'unpaid' if the following conditions are fulfilled:

- (1) The whole or part of the price has not been paid or tendered and that the seller has immediate right of action for the price.
- (2) A bill of exchange or other negotiable instrument has been received but the same has been dishonoured.

✓ **RIGHTS OF UNPAID SELLER**



(A) Rights Against the Goods:

1. Where the ownership of the goods has transferred to the buyer: In this case, the unpaid seller has the following rights:

(a) Right of lien

- The right of lien is the right to retain possession of the goods.
- This right can be exercised only when the possession of goods is with the seller.
- The unpaid seller of goods can retain his possession of goods until payment of the price in following cases:
 - a) Where the goods are not sold on credit.
 - b) Where the goods have been sold on credit, but the term of credit has expired
 - c) Where the buyer becomes insolvent.
- The unpaid seller can retain the goods only for the payment of the price of the goods: He cannot retain the goods for any other charges, e.g., maintenance, charges for storage of goods during the exercise of lien etc.
- The right of lien is indivisible in nature.
- Termination of Lien:
 - a) By delivery of goods to the carrier
 - b) By delivery of goods to the buyer
 - c) By waiver of the lien
 - d) By payment of price by the buyer

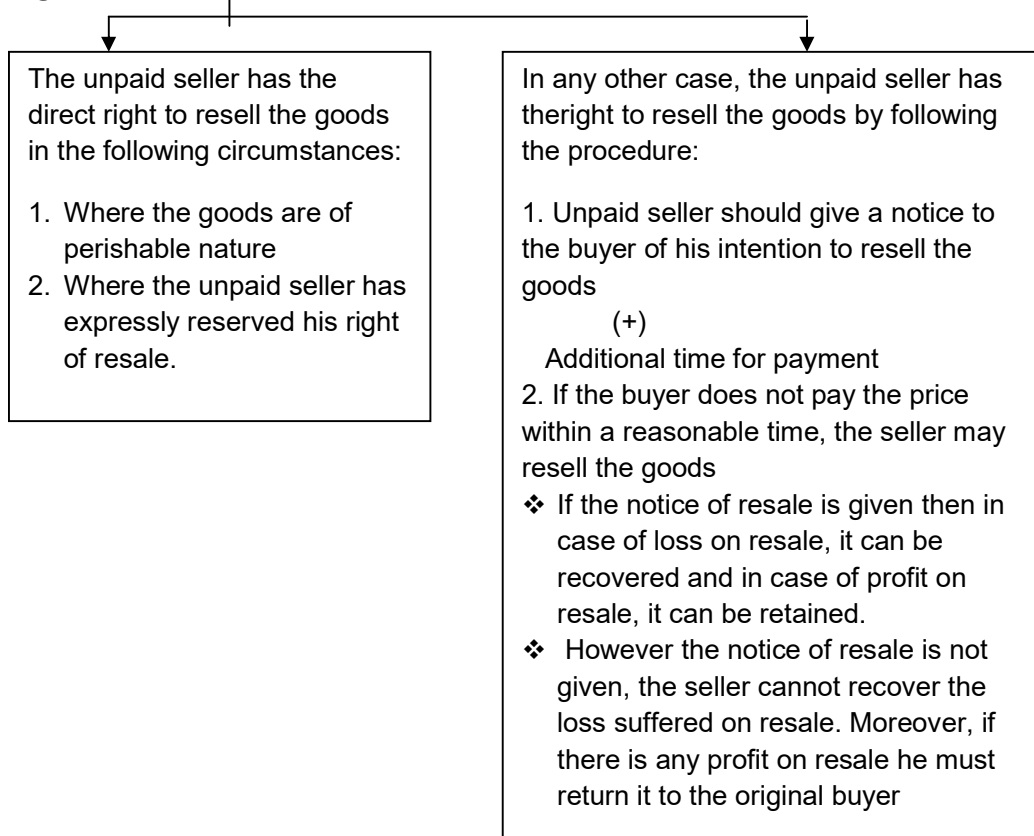
(b) Right of stoppage in transit

- The right of stoppage in transit is the right to regain possession of the goods.
- This right can be exercised only when,

- (i) Seller should have parted with the possession
- (ii) Possession should be with a carrier, &
- (iii) Buyer has not acquired the possession.
- The right of stoppage in transit can be exercised if the buyer has become insolvent.
- The unpaid seller can stop the goods in transit only for the payment of the price of the goods.
- Distinction between Right of Lien and Right of Stoppage in transit

Right of Lien	Right of stoppage in transit
1. The essence of a right of lien is to retain possession	1. The essence of stoppage in transit is to regain possession
2. Seller should be in possession of goods under lien	2. In stoppage in transit, (i) seller should have parted with the possession (ii) possession should be with a carrier, & (iii) buyer has not acquired the possession.
3. Right of lien can be exercised even when the buyer is not insolvent.	3. Right of stoppage in transit can be exercised only when buyer becomes insolvent
4. Right of lien precedes right of stoppage in transit.	4. Right of stoppage in transit begins when the right of lien ends

(C) Right of Resale



2. Where the ownership of the goods has not been transferred to the buyer:

(a) Right of Withholding Delivery

When the ownership of the goods sold is not transferred to the buyer, if the buyer fails to pay the price, the unpaid seller may refuse to deliver the goods to the buyer. Such right is known as right of withholding the delivery of the goods.

(b) Any other right

Since ownership and possession of goods is with the seller, seller can use, gift, resell the goods, etc.

(B) Rights against the Buyer

1. Suit for recovery of price

Where the buyer takes the ownership as well as possession of goods and the buyer fails to pay the price of the goods, the seller can file a suit against the buyer for recovery of the price.

2. Rescind the contract

By not paying the price, the buyer has breached the contract. So the unpaid seller can rescind the contract.

3. Suit for damages

The seller may bring a legal action against the buyer for the recovery of damages suffered.

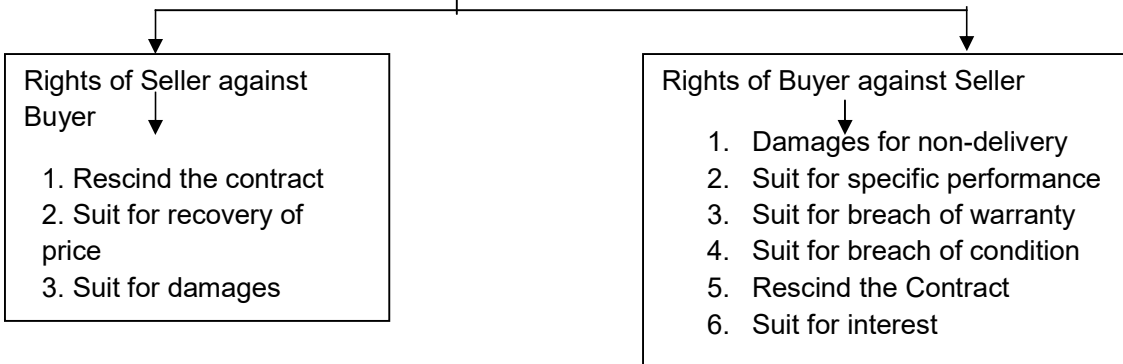
4. Suit for interest

The court may award the interest from the date of tender of the goods or from the date when the price is payable. The rate of interest to be awarded is at the discretion of the court.

• EFFECTS OF SUB-SALE OR PLEDGE BY BUYER

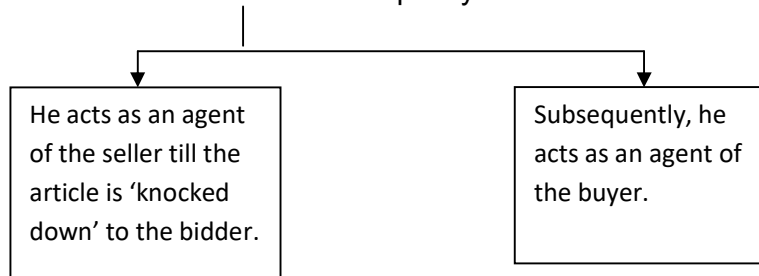
- ✓ The right of lien or stoppage in transit is not affected by the buyer selling or pledging the goods unless the seller has assented to it.
- ✓ Exceptions:
 - (a) When the seller has assented to the sale, mortgage or other disposition of the goods made by the buyer.
 - (b) When a document showing title to goods has been transferred to the buyer and the buyer transfers the documents to a person who has bought goods in good faith and for value.

• RIGHTS OF PARTIES IN BREACH OF CONTRACT



- **AUCTION SALES**

- ✓ An auction sale is a sale at which the auctioneer, as agent for the seller, invites persons present to bid for goods sold.
- ✓ Auctioneer acts in a dual capacity



- ✓ **Rules regarding Auction Sales:**
 - (i) Where goods are put up for sale in lots, they are deemed to be sold in lots.
 - (ii) The sale is complete and ownership is transferred when the auctioneer announces its completion by the fall of the hammer or in any other customary manner.
 - (iii) Bidder may retract his bid anytime before auction sale is complete.
 - (iv) The sale may be notified to be subject to a 'reserve price' or 'upset price.' When the sale is notified to be subject to a 'reserve price', the bidding and knocking down of the article to the highest bidder are all subject to the condition that the 'reserve price' should be reached.
 - (v) If the seller makes use of pretended bidding to raise the price, the sale is voidable at the option of the buyer.
 - (vi) A right to bid may be 'reserved' expressly by or on behalf of the seller and, where such right is expressly so reserved, but not otherwise, the seller or any other person on his behalf, may bid at the auction.
 - (vii) Implied warranties in auction sale: In an auction sale, the auctioneer warrants the following :
 1. that he has an authority to sell;
 2. that he is not aware of any defect in the title of the principal;
 3. that he undertakes to handover the quite possession of the goods as soon as the price is paid to him.

Ques 1:

(A) Define "GOODS" & discuss the types of Goods. **(7 Marks)**

(B) State which of the following are goods as defined under the sale of goods act, 1930.

(i) Goodwill

(ii) Trees

(iii) Rivers

(iv) Money

(v) Plants

(3 Marks)

Ques 2:

(A) Define delivery of Goods and its types/forms. **(5 Marks)**

(B) Give difference between Sale and Hire Purchase. **(5 Marks)**

Ques 3:

(A) Discuss Destruction of Goods-Consequences

(B) Define and discuss Conditions and warranties along with their difference, in the light of provisions of the Sale of goods Act, 1930.

Ques 4:

(A) When can an unpaid seller of goods exercise his right of lien over the goods under the Sale of Goods Act? Can he exercise his right of lien even if the property in goods has passed to the buyer? When such a right is terminated? Can he exercise his right even after he has obtained a decree for the price of goods from the court? **(5 Marks)**

(B) What are the rules related to Acceptance of Delivery of Goods? **(5 Marks)**

Ques 5:

(A) Risk prima facie passes along with ownership-Discuss **(3 Marks)**

(B) State the rules relating to the Delivery of goods. **(7 Marks)**

Ans 1:(A)

“Goods” means every kind of movable property other than actionable claims and money; and includes stock and shares, growing crops, grass, and things attached to or forming part of the land, which are agreed to be severed before sale or under the contract of sale. [Section 2(7)] This is a wider definition than contained in the English law, which does not consider ‘stock’ and ‘shares’ as goods, though it includes a ship. ‘Actionable claims’ are claims, which can be enforced only by an action or suit, e.g., debt. A debt is not a movable property or goods. Even the Fixed Deposit Receipts (FDR) are considered as goods under Section 176 of the Indian Contract Act read with Section 2(7) of the Sales of Goods Act.

Types of Goods Goods Future Goods Existing Goods Contingent Goods Unascertained Ascertained Specific

(i) **EXISTING GOODS** are such goods as are in existence at the time of the contract of sale, i.e., those owned or possessed by the seller at the time of contract of sale (Section 6).

The existing goods may be of following kinds:

(a) **Specific goods means goods identified and agreed upon at the time a contract of sale is made [Section 2(14)].**

Example: Any specified and finally decided goods like a Samsung Galaxy S7 Edge, Whirlpool washing machine of 7 kg etc.

(b) **Ascertained Goods** are those goods which are identified in accordance with the agreement after the contract of sale is made. In actual practice the term ‘ascertained goods’ is used in the same sense as ‘specific goods.’ When from a lot or out of large quantity of unascertained goods, the number or quantity contracted for is identified, such identified goods are called ascertained goods. **Example:** A wholesaler of cotton has 100 bales in his godown. He agrees to sell 50 bales and these bales were selected and set aside. On selection the goods becomes ascertained.

(c) **Unascertained goods** are the goods which are not specifically identified or ascertained at the time of making of the contract. They are indicated or defined only by description or sample.

Example: If A agrees to sell to B one packet of salt out of the lot of one hundred packets lying in his shop, it is a sale of unascertained goods because it is not known which packet is to be delivered. As soon as a particular packet is separated from the lot, it becomes ascertained or specific goods.

(ii) **FUTURE GOODS means goods to be manufactured or produced or acquired by the seller after making the contract of sale [Section 2 (6)].**

A contract for the sale of future goods is always an agreement to sell. It is never actual sale because a man cannot transfer what is not in existence.

Example : P agrees to sell to Q all the milk that his cow may yield during the coming year. This is a contract for the sale of future goods.

(iii) **CONTINGENT GOODS:** The acquisition of which by the seller depends upon an uncertain contingency (uncertain event) are called ‘contingent goods’ [Section 6(2)]. **Example:** A agrees to sell to B a Picasso painting provided he is able to purchase it from its present owner. This is a contract for the sale of contingent goods.

Ans 1: (B)

- (i) Goodwill : it is related to firm or business, it is intangible and hence covered under the Sale of Goods as Goods.
- (ii) Trees: They are not Goods as attached to land and therefore immovable.
- (iii) Rivers: They are not Goods as attached to land and therefore immovable, water of river is movable.
- (iv) Money: It is a medium by itself, but not Goods.
- (v) Plants: As in pots, movable and therefore Goods.

Ans 2 (A)

Delivery : Delivery means voluntary transfer of possession from one person to another [Section 2(2)]. As a general rule, delivery of goods may be made by doing anything, which has the effect of putting the goods in the possession of the buyer, or any person authorized to hold them on his behalf.

Forms of delivery: Following are the kinds of delivery for transfer of possession: Delivery of goods Actual delivery Constructive delivery Symbolic delivery

- (i) **Actual delivery:** When the goods are physically delivered to the buyer.
- (ii) **Constructive delivery:** When it is effected without any change in the custody or actual possession of the thing as in the case of delivery by attornment (acknowledgement) e.g., where a warehouseman holding the goods of A agrees to hold them on behalf of B, at A's request.
- (iii) **Symbolic delivery:** When there is a delivery of a thing in token of a transfer of something else, i.e., delivery of goods in the course of transit may be made by handing over documents of title to goods, like bill of lading or railway receipt or delivery orders or the key of a warehouse containing the goods is handed over to buyer.

Ans 2: (B)

Sale and Hire Purchase: Contract of sale resembles with contracts of hire purchase very closely, and indeed the real object of a contract of hire purchase is the sale of the goods ultimately. Hire purchase agreements are governed by the Hire-purchase Act, 1972. Term "hire-purchase agreement" means an agreement under which goods are let on hire and under which the hirer has an option to purchase them in accordance with the terms of the agreement and includes an agreement under which—

- (a) Possession of goods is delivered by the owner thereof to a person on condition that such person pays the agreed amount in periodical instalments, and
- (b) The property in the goods is to pass to such person on the payment of the last of such instalments, and
- (c) Such person has a right to terminate the agreement at any time before the property so passes; None the less a sale has to be distinguished from a hire purchase as their legal incidents are quite different.

The main points of distinction between the 'sale' and 'hire-purchase' are as follows:

1. **Time of passing property:** Property in the goods is transferred to the buyer immediately at the time of contract. The property in goods passes to the hirer upon payment of the last installment.
2. **Position of the party:** The position of the buyer is that of the owner of the goods. The position of the hirer is that of a bailee till he pays the last installment.
3. **Termination of contract:** The buyer cannot terminate the contract and is bound to pay the price of the goods. The hirer may, if he so likes, terminate the contract by returning the goods to its owner without any liability to pay the remaining installments.

4. **Burden of Risk of insolvency of the buyer:** The seller takes the risk of any loss resulting from the insolvency of the buyer. The owner takes no such risk, for if the hirer fails to pay an installment, the owner has right to take back the goods.
5. **Transfer of title:** The buyer can pass a good title to a *bonafide purchaser* from him. The hirer cannot pass any title even to a bonafide purchaser.
6. **Resale:** The buyer in sale can resell the goods The hire purchaser cannot resell unless he has paid all the installments.

Ans 3 (A)

Destruction of Goods-Consequences:

- (i) In accordance with the provisions of the Sale of Goods Act, 1930 as contained in Section 7, a contract for the sale of specific goods is void if at the time when the contract was made; the goods without the knowledge of the seller, perished or become so damaged as no longer to answer to their description in the contract, then the contract is void ab initio. This section is based on the rule that where both the parties to a contract are under a mistake as to a matter of fact essential to a contract, the contract is void.
- (ii) In a similar way Section 8 provides that an agreement to sell specific goods becomes void if subsequently the goods, without any fault on the party of the seller or buyer, perish or become so damaged as no longer to answer to their description in agreement before the risk passes to the buyer. This rule is also based on the ground of impossibility of performance as stated above. It may, however, be noted that section 7 & 8 apply only to specific goods and not to unascertained goods. If the agreement is to sell a certain quantity of unascertained goods, the perishing of even the whole quantity of such goods in the possession of the seller will not relieve him of his obligation to deliver the goods.

Ans 3 (B)

Condition and warranty (Section 12): A stipulation in a contract of sale with reference to goods which are the subject thereof may be a condition or a warranty. [Sub-section (1)]

“A **condition** is a stipulation essential to the main purpose of the contract, the breach of which gives rise to a right to treat the contract as repudiated”. [Sub-section (2)]

Example: Ram consults Shyam, a motor-car dealer for a car suitable for touring purposes to promote the sale of his product. Shyam suggests ‘Maruti’ and Ram accordingly buys it from Shyam. The car turns out to be unit for touring purposes. Here the term that the ‘car should be suitable for touring purposes’ is a condition of the contract. It is so vital that its non-fulfillment defeats the very purpose for which Ram purchases the car. Ram is therefore entitled to reject the car and have refund of the price.

“A **warranty** is a stipulation collateral to the main purpose of the contract, the breach of which gives rise to a claim for damages but not to a right to reject the goods and treat the contract as repudiated”. [Sub-section (3)]

Example: Ram buys a new Maruti car from the show room and the car is guaranteed against any manufacturing defect under normal usage for a period of one year from the date of original purchase and in the event of any manufacturing defect there is a warranty for replacement of defective part if it cannot be properly repaired. After six months Ram finds that the horn of the car is not working, here in this case he cannot terminate the contract. The manufacturer can either get it repaired or replaced it with a new horn. Ram gets a right to claim for damages, if any, suffered by him but not the right of repudiation.

The following are important differences between conditions and warranties.

1. Meaning : A condition is essential to the main purpose of the contract. While warranty is, only collateral to the main purpose of the contract.

2. Right in case of breach: The aggrieved party can repudiate the contract or claim damages or both in the case of breach of condition. The aggrieved party can claim only damages in case of breach of warranty.
3. Conversion of stipulations: A breach of condition may be treated as a breach of warranty. A breach of warranty cannot be treated as a breach of condition.

Ans 4 (A)

A lien is a right to retain possession of goods until the payment of the price. It is available to the unpaid seller of the goods who is in possession of them where-

- (i) the goods have been sold without any stipulation as to credit;
- (ii) the goods have been sold on credit, but the term of credit has expired;
- (iii) the buyer becomes insolvent.

The unpaid seller can exercise 'his right of lien even if the property in goods has passed on to the buyer. He can exercise his right even if he is in possession of the goods as agent or bailee for the buyer.

Termination of lien: An unpaid seller loses his right of lien thereon-

- (i) When he delivers the goods to a carrier or other bailee for the purpose of transmission to the buyer without reserving the right of disposal of the goods;
- (ii) When the buyer or his agent lawfully obtains possession of the goods;

Ans 4 (B)

Rule related to Acceptance of Delivery of Goods (Section 42): The buyer is deemed to have accepted the goods when the buyer-

- (a) intimates to the seller that he had accepted the goods; or
- (b) does any act to the goods, which is inconsistent with the ownership of the seller; or
- (c) retains the goods after the lapse of a reasonable time, without intimating to the seller that he has rejected them.

Buyer not bound to return rejected goods (Section 43): Unless otherwise agreed, where goods are delivered to the buyer and he refuses to accept them, having the right so to do, he is not bound to return them to the seller, but it is sufficient if he intimates to the seller that he refuses to accept them.

Liability of buyer for neglecting or refusing delivery of goods (Section 44): When the seller is ready and willing to deliver the goods and requests the buyer to take delivery, and the buyer does not within a reasonable time after such request take delivery of the goods, he is liable to the seller for any loss occasioned by his neglect or refusal to take delivery and also for a reasonable charge for the care and custody of the goods.

Ans 5(A)

Risk prima facie passes with ownership:

The general rule is, "unless otherwise agreed, the goods remain at the seller's risk until the property therein is transferred to the buyer, but when the property therein is transferred to the buyer, the goods are at the buyer's risk whether delivery has been made or not".

Example: A bids for an antique painting at a sale by auction. After the bid, when the auctioneer struck his hammer to signify acceptance of the bid, he hit the antique which gets damaged. The loss will have to be borne by the seller, because the ownership of goods has not yet passed from the seller to the buyer.

The aforesaid rule is, however, subject to two exceptions:

- (i) If delivery has been delayed by the fault of the seller or the buyer, the goods shall be at the risk of the party in default, as regards loss which might not have arisen but for the default.

- (ii) The duties and liabilities of the seller or the buyer as bailee of goods for the other party remain unaffected even when the risk has passed generally.

However, the parties may by special agreement stipulate that 'risk' will pass sometime after or before the 'property' has passed.

Ans 5 (B)

- (i) **Delivery (Section 33):** Delivery of goods sold may be made by doing anything which the parties agree shall be treated as delivery or which has the effect of putting the goods in the possession of the buyer or of any person authorised to hold them on his behalf.
- (ii) **Buyer to apply for delivery:** Apart from any express contract, the seller of goods is not bound to deliver them until the buyer applies for delivery.
- (iii) **Effect of part delivery:** A delivery of part of goods, in progress of the delivery of the whole has the same effect, for the purpose of passing the property in such goods, as a delivery of the whole; but a delivery of part of the goods, with an intention of separating it from the whole, does not operate as a delivery of the remainder.
- (iv) **Place of delivery:** Goods sold are to be delivered at the place at which they are at the time of the sale, and goods agreed to be sold are to be delivered at the place at which they are at the time of the agreement to sell or if not then in existence, at the place at which they are manufactured or produced.
- (v) **Time of delivery:** Where under the contract of sale the seller is bound to send the goods to the buyer, but no time for sending them is fixed, the seller is bound to send them within a reasonable time.
- (vi) **Goods in possession of a third party:** Where the goods at the time of sale are in possession of a third person and if such third party holding the goods, acknowledges to the buyer that he holds the goods on his behalf, goods are said to be delivered to buyer.
- (vii) **Time for tender of delivery:** Demand or tender of delivery may be made at a reasonable hour. What is reasonable hour is a question of fact in each case.
- (viii) **Expenses for delivery:** The expenses of and incidental to putting the goods into a deliverable state must be borne by the seller in the absence of a contract to the contrary.
- (ix) **Delivery of wrong quantity:** Where the seller delivers to the buyer a quantity of goods less than he contracted to sell, the buyer may reject them, but if the buyer accepts the goods so delivered he shall pay for them at the contract rate.
Where the seller delivers to the buyer a quantity of goods larger than he contracted to sell, the buyer may accept the goods included in the contract and reject the rest, or he may reject the whole. If the buyer accepts the whole of the goods so delivered, he shall pay for them at the contract rate.
Where the seller delivers to the buyer the goods he contracted to sell mixed with goods of a different description not included in the contract, the buyer may accept the goods which are in accordance with the contract and reject, or may reject the whole.
- (x) **Instalment deliveries:** the buyer is not bound to accept delivery in instalments. The rights and liabilities in cases of delivery by instalments and payments thereon may be determined by the parties of contract.
- (xi) **Delivery to carrier:** The delivery of the goods to the carrier for transmission to the buyer, is *prima facie* deemed to be delivery to the buyer.
- (xii) **Deterioration during transit:** Where goods are delivered at a distant place, the liability for deterioration necessarily incidental to the course of transit will fall on the buyer, though the seller agrees to deliver at his own risk.
- (xiii) **Buyer's right to examine the goods:** Where goods are delivered to the buyer, who has not previously examined them, he is entitled to a reasonable opportunity of examining them in order to ascertain whether they are in conformity with the contract.

Ques: 1:

- (A) Ram sells 200 bales of cloth to Shyam and sends 100 bales by lorry and 100 bales by Railway. Shyam receives delivery of 100 bales sent by lorry, but before he receives the delivery of the bales sent by railway, he becomes bankrupt. Ram being still unpaid, stops the goods in transit. The official receiver, on Shyam's insolvency claims the goods.

Decide the case with reference to the provisions of the Sale of Goods Act, 1930.

(5 marks)

- (B) Distinguish between a 'Condition' and a 'Warranty' in a contract of sale. When shall a 'breach of condition' be treated as 'breach of warranty' under the provisions of the Sale of Goods Act, 1930? **Explain.**

(5 marks)

Ques: 2:

- (A) When can an unpaid seller of goods exercise his right of lien over the goods under the Sale of Goods Act? Can he exercise his right of lien even if the property in goods has passed to the buyer? **When such a right is terminated? Can he exercise his right** even after he has obtained a decree for the price of goods from the court? **(5 marks)**

- (B) State difference between "Sale" and "Agreement to Sell". **(5 marks)**

Ques: 3:

- (A) "Nemo Dat Quod Non Habet" – "None can give or transfer goods what he does not himself own." Example the rule and state the cases in which the rule does not apply under the provisions of the Sale of Goods Act, 1930. **(5 marks)**

- (B) During world cup matches, P buys a TV set from R. R agrees to deliver the same to P after some days. In meanwhile R sells the same to S, at a higher price, who buys in good faith and without knowledge about the previous sale. Will S get a good title? **(5 marks)**

Ques: 4:

- (A) A entered into a contract to sell cartons in possession of a what finger to B and agreed with B that the price will be paid to A from the sale proceeds recovered from his customers. Now B sold goods to C and C duly paid to B. But anyhow B failed to make the payment to A. A wanted to exercise his right of lien and ordered the what finger not to make delivery to C. Can he do so? **(5 marks)**

- (B) State the Remedies available to Seller against Buyer in case of breach of contract of sale. **(5 marks)**

Ques: 5:

- (A) Explain the term delivery and its form under the Sale Of Goods Act, 1930. **(5 marks)**

- (B) What do you understand by "Caveat-Emptor" under the Sale of Goods Act, 1930? What are the exceptions to this rule? **(5 marks)**

Answer 1:

(A)

Right of stoppage of goods in transit: The problem is based on section 50 of the Sale of Goods Act, 1930 dealing with the **right of stoppage of the goods in transit available to an unpaid seller**. The section states that the right is exercisable by the seller **only** if the following conditions are fulfilled.

- (i) The seller must be unpaid
- (ii) He must have parted with the possession of goods
- (iii) The goods must be in transit
- (iv) The buyer must have become insolvent
- (v) The right is subject to the provisions of the Act.

Applying the provisions to the given case, Ram being still unpaid, can stop the 100 bales of cloth sent by railway as these goods are still in transit. **(5 marks)**

(B)

Difference between Condition and Warranty

- (i) A condition is a **stipulation essential to the main purpose** of the contract whereas a warranty is a **stipulation collateral to the main purpose** of the contract.
- (ii) **Breach of condition** gives rise to a **right to treat the contract as repudiated** whereas in case of **breach of warranty**, the aggrieved party can **claim damage only**.
- (iii) Breach of condition may be treated as breach of warranty, whereas a breach of warranty cannot be treated as breach of condition.

According to Section 13 of the Sale of Goods Act, 1930 a breach of condition may be treated as breach of warranty in following circumstances:

- (i) Where a contract of sale is subject to any condition to be fulfilled by the seller, the buyer may waive the condition,
- (ii) Where the buyer elects to treat the breach of condition as breach of a warranty.
- (iii) Where the contract of sale is non-severable and the buyer has accepted the whole goods or any part thereof.
- (iv) Where the fulfillment of any condition or warranty is excused by law by reason of impossibility or otherwise. **(5 marks)**

Answer 2:

(A)

A lien is a right to retain possession of goods until the payment of the price. It is available to the unpaid seller of the goods who is in possession of them where –

- (i) The goods have been sold without any stipulation as to credit ;
- (ii) The goods have been sold on credit, but the term of credit has expired;
- (iii) The buyer becomes insolvent.

The **unpaid seller can exercise 'his right of lien' even if the property in goods has passed on to the buyer**. He can exercise his right even if he is in possession of the goods as agent or bailee for the buyer. **(3 marks)**

Termination of lien : An unpaid seller loses his right of lien thereon –

- (i) When he delivers the goods to a carrier or other bailee for the purpose of transmission to the buyer without reserving the right of disposal of the goods;
- (ii) When the buyer or his agent lawfully obtains possession of the goods.

(2 mark)

Answer 2(B) Particulars	Sale	Agreement to Sell
1. Meaning	Where under a contract of sale, the property (ownership) in the Goods is transferred from the Seller to the Buyer, it is called a Sale.	Where under a contract of sale, the transfer of the property (ownership) in the Goods is to take place at a future time or subject to some condition thereafter to be fulfilled is said to be Agreement to sell.
2. Example	Ram sells 20 bags of rice to Hari for a sum of Rs. 10,000. It is a sale since the ownership in 20 bags of rice has been transferred from Ram to Hari for a consideration of Rs. 10,000.	Mani agrees to buy 1,000 kgs of cement to arrive by a certain ship on a future date. The property in Goods (cement) will pass to the Buyer only when Goods arrive. Also the agreement is subject to condition that the ship arrives in the port with Goods.
3. Transfer of Risk	Buyer becomes the owner of Goods as soon as the contract is made. Hence the Buyer bears the risk.	Seller continues to be the owner till the agreement to sell becomes sale and hence the risk lies with him only.
4. Rights created	Creates a right in rem (right against property).	Creates a right in personam (right against a person).
5. Type of Goods	A Sale can be made only in respect of specific and ascertained Goods.	An agreement to sell may be made for Future and Contingent Goods.
6. Type of Contract	Generally, executed contract.	Executory contract.
7. Remedies available for breach of contract	Buyer's breach : Seller can (i) sue for price of Goods even if Goods are in his own possession (ii) resell the Goods, (iii) exercise right of lien and (iv) exercise right of stoppage of Goods in transit, if necessary. Seller's breach : Buyer has double remedy, (i) suit for damages against the Seller, and (ii) recovering of Goods from third parties who bought them.	Buyer's breach : The Seller can sue only for damages and not for Price. Seller's breach : The buyer can sue the Seller for damages and sue the third party who bought those Goods.

8. Rights of Buyer	The Buyer can sue the Seller for non – delivery of Goods, when he has paid the price for it.	The aggrieved party can sue for damages only and not for the price, unless the price was payable at a stated date.
9. Risk of loss of Goods	Risk being associated with ownership lies with the Buyer and hence any loss shall be borne by the Buyer only, even though the Goods lie with Seller.	Since risk associated with ownership is not transferred, loss shall be borne by Seller, even though the Goods lie with Buyer.
10. Insolvency of Seller after buyer has paid the price	Buyer can claim the Goods from the Official Receiver or Assignee.	Buyer can claim only a rateable dividend for price paid and cannot claim the Goods, since the property has not passed to him.
11. Sales Tax	A Sale is liable to Sales Tax.	An agreement to sell is not liable to sales tax, unless it becomes a “Sale.”
12. Rights to Re – sell	Once an effective sale is made, Seller cannot resell the Goods, as the property vests in the Buyer. However, if subsequent Buyer has purchased the Goods in good faith, for value, and without knowledge of prior sale, he gets a good title to such Goods.	Where Seller makes a re – sale, the subsequent Buyer, who takes the Goods for consideration and without notice of the prior agreement, gets a good title. The remedy available to the original Buyer is that he can sue for damages.

Answer 3:

(A) Exceptions to the Rule Nemo dat Quod Non Habet :

The term means, “none can give or transfer goods what he does not himself own.” Exceptions to the rule and the cases in which the Rule does not apply under the provisions of the Sale of Goods Act, 1930 are enumerated below :

- (i) **Sale by a Mercantile Agent** : A sale made by a mercantile agent of the goods or document of title to goods would pass a good title to the buyer in the following circumstances, namely;
 - (a) if he was in possession of the goods or documents with the consent of the owner;
 - (b) if the sale was made by him when acting in the ordinary course of business as a mercantile agent; and
 - (c) if the buyer had acted in good faith and has at the time of the contract of sale, no notice of the fact that the seller had no authority to sell. (Proviso to Sec27).
- (ii) **Sale by one of the joint owners** : If one of the several joint owners of goods has the sole possession of them with the permission of the others the property in the goods may be transferred to any person who buys them from such a joint owner in good faith and does not at the time of the contract of sale have notice that the seller has no authority to sell. (Section 28)
- (iii) **Sale by a person in possession under voidable contract** : A buyer would acquire a good title to the goods sold to him by seller who had obtained possession of the goods under a contract voidable on the ground of coercion, fraud, misrepresentation or undue influence provided that the contract had not been rescinded until the time of the sale (Section 29).

- (iv) **Sale by one who has already sold the goods but continues in possession thereof :** If a person has sold goods but continues to be in possession of them or of the documents of title to them, he may sell them to a third person, and if such person obtains the delivery thereof in good faith without notice of the previous sale, he would have good title to them, although the property in the goods had passed to the first buyer earlier. A pledge or other deposition of the goods or documents of title by the seller in possession are equally valid. [Section 30(1)].
- (v) **Sale by buyer obtaining possession before the property in the goods has vested in him :**
Where a buyer with the consent of seller obtains possession of the goods before the property in them has passed to him, he may sell, pledge or otherwise dispose of the goods to a third person, and if such person obtains delivery of the goods in good faith and without notice of the lien or other right of the original seller in respect of the goods in good faith and without notice of the lien or other right of the original seller in respect of the goods, he would get a good title to them. [Section 30(2)].
- (vi) **Sale by an unpaid seller :** Where an unpaid seller who had exercised his right of lien or stoppage in transit resells the goods, the buyer acquires a good title to the goods as against the original buyer [Section 54(3)].
- (vii) **Sale under the provisions of other Acts :**
- (i) Sale by an official Receiver or liquidator of the company will give the purchaser a valid title.
 - (ii) Purchase of goods from a finder of goods will get a valid title under circumstances.
 - (iii) Sale by a pawnee under default of pawnor will give valid title to the purchaser.

Answer 3

(B) As per section 27 of Sale of Goods Act, 1930, where goods are sold by a person who is not the owner thereof and who does not sell them under the authority or with the consent of the owner, the buyer acquires no better title to the goods than the seller had. However, if a person has sold goods but continues to be in possession of them, he may sell them to a third person, and if such person obtains the delivery thereof in good faith and without notice of the previous sale, he would have good title to them, although the property in the goods had passed to the first buyer earlier.

In the given questions, P buys a TV set from R. R agrees to deliver the same to P after some days. In meanwhile R sells the same to S, at a higher price, who buys in good faith without knowledge about the previous sale.

Hence, S will get a good title.

Answer 4

(A) As per section 53 of Sale of Goods Act 1930, the right of lien or stoppage in transit is not affected by the buyer selling or pledging the goods unless the seller has assented to it. This is based on the principle that a second buyer cannot stand in a better position than his seller. However, when the seller has assented to the sale, mortgage or other disposition of the goods made by the buyer, his right of lien or stoppage in transit is defeated. In the given question, A entered into a contract to sell cartons in possession of a wharfinger to B and agreed with B that the price will be paid to A from the sale proceeds recovered from his customers. Now if B failed to make payment, the seller cannot exercise his right of lien as he had assented to the resale of the goods by the buyer to the sub – buyers. Therefore, he cannot exercise his right of lien.

ANSWER-B

An unpaid seller has the following rights against the Buyer –

1. Suit for price (Sec. 55(1)):

- (a) Where under a contract of sale the property in Goods has passed to Buyer, and Buyer wrongfully, neglects or refuses to pay the price, the Seller can sue the Buyer for the price of goods.

- (b) When under the contract of sale, price is payable on a certain day irrespective of delivery and Buyer wrongfully neglects or refuses to pay the price, seller may sue him for the price. Unpaid Seller has this right even though property has not passed to the Buyer and Goods have not been appropriated to the contract.

(2 MARKS)

2. Damages for non – acceptance [Sec. 56]: Where the Buyer wrongfully neglects or refuses to accept and pay for goods, the seller may sue him for damages for non – acceptance.

(1 MARK)

3. Repudiation of contract before due date [Sec. 60] : Where the Buyer repudiates a contract before the date of delivery, the Seller may (i) treat the contract as subsisting and wait till the date of delivery or (ii) treat the contract as rescinded and sue the Buyer for damages for the breach on his part.

(1 MARK)

4. Interest by way of damages and special damages [Sec. 61]:

- (a) When under a contract of sale, the Seller tenders goods to the buyer who wrongfully refuses or neglects to accept and pay the price, the Seller has a further right to claim interest on the amount of price.
- (b) Unpaid Seller can claim interest only when he can recover the price, i.e., if the Seller's remedy is to claim damages, then he cannot claim interest.
- (c) The interest may be calculated from the date of tender of Goods or from the date on which the price was payable.
- (d) The rate of interest to be awarded is at the discretion of the Court.

(4*0.5 = 2 MARKS)

ANSWER-5

(A)

1. **Meaning [Sec. 2]:** Delivery means voluntary transfer of possession from one person to another.
2. **Duty of Seller [Sec. 31] :** It is the duty of the Seller to deliver the goods and of the buyer to accept and pay for them in accordance with the contract of Sale.
3. **Mode of delivery – Sec. 33 :** Delivery of Goods sold may be made by –
- (a) doing anything which the parties agree shall be treated as delivery, or
- (b) Which has the effect of putting the Goods in the possession of the Buyer or of any person authorized to hold them on his behalf.

(3 MARKS)

Types of Delivery

Actual Delivery : Goods are **physically handed over to the Buyer or his authorized agent** i.e. actual transfer of physical custody.

Constructive Delivery : i.e. **by causing a change in the possession of Goods without any actual change in the actual and visible custody.**

Example : A sells to B 100 bags of wheat lying in C's warehouse. A makes a delivery order to C to transfer the wheat to B. C transfers and holds the 100 bags on behalf of B and by making necessary entries in his books. There is constructive delivery of goods from A to B.

Symbolic Delivery : Where **Goods are bulky/ heavy and it is not possible to physically hand over them to the Buyer, some symbol which carries with it the real possession or control over the Goods is handed over to the Buyer.**

Example: Delivery of godown keys where Goods are lying, or endorsing bill of lading or railway receipt to the Buyer.

Forward Delivery : Where delivery is to be made in future, and not at the time contract is entered into.

(4*1.25 = 5 MARKS)

Answer 5

(B) Caveat Emptor' means "let the buyer beware", i.e. in sale of goods the seller is under no duty to reveal unflattering truths about the goods sold. Therefore, when a person buys some goods, he must examine them thoroughly. If the goods turn out to be defective or do not suit his purpose, or if he depends upon his skill and judgment and makes a bad selection, he cannot blame anybody excepting himself.

The rule is enunciated in the opening words of section 16 of the Sale of Goods Act, 1930 which runs thus: "Subject to the provisions of this Act and of any other law for the time being in force, there is no implied warranty or condition as to the quality or fitness for any particular purpose of goods supplied under a contract of sale"

The rule of caveat emptor does not apply in the following cases:

- (i) *Fitness for buyer's purpose:* Where the buyer, expressly or by implication, makes known to the seller the particular purpose for which he requires the goods and relies on the seller's skill or judgment and the goods are of a description which it is in the course of the seller's business to supply, the seller must supply the goods which shall be fit for the buyer's purpose. [Section 16(1)].
- (ii) *Sale under a patent or trade name:* In the case of a contract for the sale of a specified article under its patent or other trade name, there is no implied condition that the goods shall be reasonably fit for any particular purpose [Section 16(1)].
- (iii) *Merchantable quality:* Where goods are bought by description from a seller who deals in goods of that description (whether he is the manufacturer or producer or not), there is an implied condition that the goods shall be of merchantable quality. But if the buyer has examined the goods, there is no implied condition as regards defects which such examination ought to have revealed. [Section 16(2)].
- (iv) *Usage of trade:* An implied warranty or condition as to quality or fitness for a particular purpose may be annexed by the usage of trade. [Section 16(3)].
- (v) *Consent by fraud:* Where the consent of the buyer, in a contract of sale, is obtained by the seller by fraud or where the seller knowingly conceals a defect which could not be discovered on a reasonable examination, the doctrine of caveat emptor does not apply.

CHAPTER 3 - INDIAN PARTNERSHIP ACT

UNIT 1: NATURE OF PARTNERSHIP

- **INTRODUCTION**

- ✓ Introduced on 1st of October, 1932
- ✓ Applicable to whole of India except Jammu & Kashmir
- ✓ This law was previously part of Indian Contract Act, 1872
- ✓ Where the Indian Partnership Act is silent on any point, the Indian Contract Act is applicable.

- **PARTNERSHIP**

Partnership is the relation between two or more persons who have agreed to share profits of a business carried on by all or any of them acting for all.

- **PARTNER**

Person who enters into partnership

- **FIRM**

Partners are collectively known as firm

- **ESSENTIAL ELEMENTS OF PARTNERSHIP**

1. **It is an association of two or more persons**

- ✓ There must be at least two persons to form a partnership. Maximum number of partners, IPA is silent. But Companies Act 2013 specifies it as 50. If number of partners fall below it ceases to be partnership. If it goes beyond 50, it will become an illegal association.
- ✓ The persons can be natural or artificial. Hence 2 companies can be partners. But a firm cannot enter into a contract for partnership though their partners can become partners.
- ✓ All such persons must be competent to contract. According to Indian Contract Act every person except the following:
 - i Minor
 - ii Person of unsound mind
 - iii Person disqualified by any law to which they are subject (alien, insolvents etc)

2. **There must be an agreement**

- ✓ Partnership comes into existence by agreement and not by status (like by birth in HUF) or by operation of law (like law of inheritance).
- ✓ The agreement may be express or implied, oral or written. However the partnership deed must be in written.
- ✓ All the essential elements of a valid contract must be satisfied.

3. There must be business.

- ✓ Business means any trade, occupation and profession carried on with an intention to make profits.
- ✓ When two or more people agree to share income from a joint property it does not amount to partnership because there does not exist any business. Any charitable trust, NGO, etc cannot be considered as a partnership firm.

4. Sharing of Profits:

- ✓ Sharing of profits is essential but sharing of losses is not essential. Partner can share profits & losses or only profits but never only losses.
- ✓ It is not necessary that every person sharing profits is a partner. Following persons are getting profits but are not partners:
 - i Money Lender
 - li Employee/Manager
 - lii Seller of Goodwill
 - iv Retiring partner sharing profits pending settlement of accounts.
 - v Legal Representative of deceased partner sharing profits pending settlement of accounts.
 - vi Minor
- ✓ Just because a person is sharing profits, he is not a partner. But if a person is a partner, he will definitely get share in profits.

5. Mutual Agency

- ✓ It's the most essential element of Partnership. It determines the true test of partnership.
- ✓ There must exist a mutual agency relationship among the partners.
- ✓ It means every partner is a

Agent of the firm

Principal for other partners acts

- **DISTINCTION BETWEEN**

1. **Partnership and Co-ownership:**

Partnership	Co-ownership
1. It arises from an agreement.	1. It may arise from agreement or operation of law.
2. It is formed to carry on business.	2. It may or may not involve carrying on a business.
3. It involves profit or loss.	3. It may or may not involve profit or loss
4. Partners have a mutual agency relationship.	4. Co-owners do not have a mutual agency agreement.
5. Maximum partners can be 50.	5. No such limit is applicable here.
6. A partner cannot transfer his share to a stranger without the consent of any other business.	6. A co-owner can transfer his share to a stranger without the consent of other owners.
7. A partner has no right to claim partition of property.	7. A co-owner has the right to claim partition of property.

2. **Partnership and HUF:**

Partnership	HUF
1. It arises from agreement	1. It arises by status.
2. Governed by Indian Partnership Act, 1932.	2. It is governed by Hindu Law.
3. Maximum partners can be 50.	3. No such limit is applicable here.
4. A person can be admitted by the consent of the other existing partners.	4. A male person becomes a member merely by his birth.
5. A minor can be admitted only to the benefits of the firm.	5. A male minor becomes a member merely by his birth.
6. Each partner is implied authority to bind the firm for the actions done by him in the daily course of business.	6. Only Karta has such authority.
7. Unlimited liability.	7. Karta's liability is unlimited and the coparcener's liability is limited to their share in the family property
8. Each partner has the right to ask for the books of accounts and also for the profits and losses.	8. The coparceners have no such right
9. In case of death of a partner, partnership is dissolved unless otherwise agreed.	9. HUF continues to operate even after death of a coparcener.

3. Partnership and Company:

Partnership	Company
1. A firm does not enjoy separate legal entity i.e. separate legal existence.	1. It has a separate legal existence.
2. The liability of the partner is unlimited.	2. Limited to the value of shares held by the members.
3. It does not enjoy a long lease of life because of dissolution due to different reasons.	3. It enjoys a perpetual existence.
4. Maximum partners can be 50.	4. In case of private limited company, Minimum members-2, maximum members -200 In case of public limited company, Minimum members -7, maximum members - no limit
5. A partner cannot transfer his share without the consent of other partners.	5. A member can transfer his share as and when he wishes to.
6. There is mutual agency amongst the partners	6. There is no mutual agency amongst the members
7. Distribution of profits is compulsory as per the partnership deed	7. No such compulsion of distributing the profits.
8. The ownership & management lies with all the partners.	8. Ownership is with shareholders and the management is with board of directors
9. Property of the firm is the joint property of all the partners.	9. The property of company is not the joint property of the members.
10. The creditors of the firm can proceed against the partners jointly and severally.	10. The creditors of a company can proceed only against the company.
11. No compulsory Audit	11. Its compulsory

4. Partnership and Club:

Partnership	Club
1. Business oriented objects	1. Not aimed at making profits entirely.
2. Maximum partners can be 50.	2. No such limit is applicable here.
3. Does not enjoy long lease of life	3. Enjoys a long lease of life
4. There is mutual agency amongst the partners	4. There is no mutual agency amongst the members

- **TYPES OF PARTNERS**

1. **Active/Actual Partner :**

- ✓ A partner who is actively engaged in the conduct of the business of the partnership is known as 'active partner'.
- ✓ When an active partner retires from the firm, he has to give a public notice. Otherwise, he will be liable on the principle of 'holding out'.
- ✓ He is liable for acts of firm

2. Sleeping or Dormant Partner :

- ✓ A 'Sleeping partner' is one who does not take any active part in the business.
- ✓ Such partner joins the firm by agreement and invests capital and shares in the profit of the business like the other partners.
- ✓ A sleeping partner need not give public notice of his retirement from the firm.
- ✓ He is liable for acts of firm

3. Nominal Partner :

- ✓ A partner, who simply lends his name to the firm, without having any real interest in it, is called a nominal partner.
- ✓ He neither invests nor shares in the profits or takes part in the management of the business.
- ✓ He, along with other partners, is liable to outsiders for all the debts of the firm.
- ✓ Difference between sleeping and nominal partner: A nominal partner is known to the outside world as a partner of the firm but in reality does not share in the profit of the firm. A dormant partner on the other hand, even though not known as a partner to the world at large but in fact shares in the profits of the business.

4. Partner for profits only :

- ✓ Partners may agree that a particular partner shall get a share of the profits only but he will not be called upon to contribute towards the losses. Such a partner is known as 'partner for profits only'.
- ✓ He continues to be liable to third parties for all acts of the firm.

5. Sub-Partner :

- ✓ When a partner agrees to share his profits divided from the firm with a third person, that third person is known as 'sub-partner'.
- ✓ He cannot represent the firm and bind the firm by his acts. He has no right against the firm nor is he liable for the acts of the firm.

6. Partner by Holding Out or by Estoppel :

- ✓ To hold a person liable as a partner by holding out, it is necessary to establish the following :
 1. He represented himself or knowingly permitted himself to be represented as a partner.
 2. Such representation occurred by words spoken or written or by conduct.
 3. The other party on the faith of that representation gave credit to the firm.
- ✓ Once he poses himself as a partner, though he is not a partner, he is estopped from saying that he is not a partner in a firm.

7. Incoming Partner:

A person who is admitted as a partner into an already existing firm with the consent of all the existing partners is called as "incoming partner".

8. Outgoing Partner:

A partner who leaves a firm in which the rest of the partners continue to carry on business is called an outgoing partner.

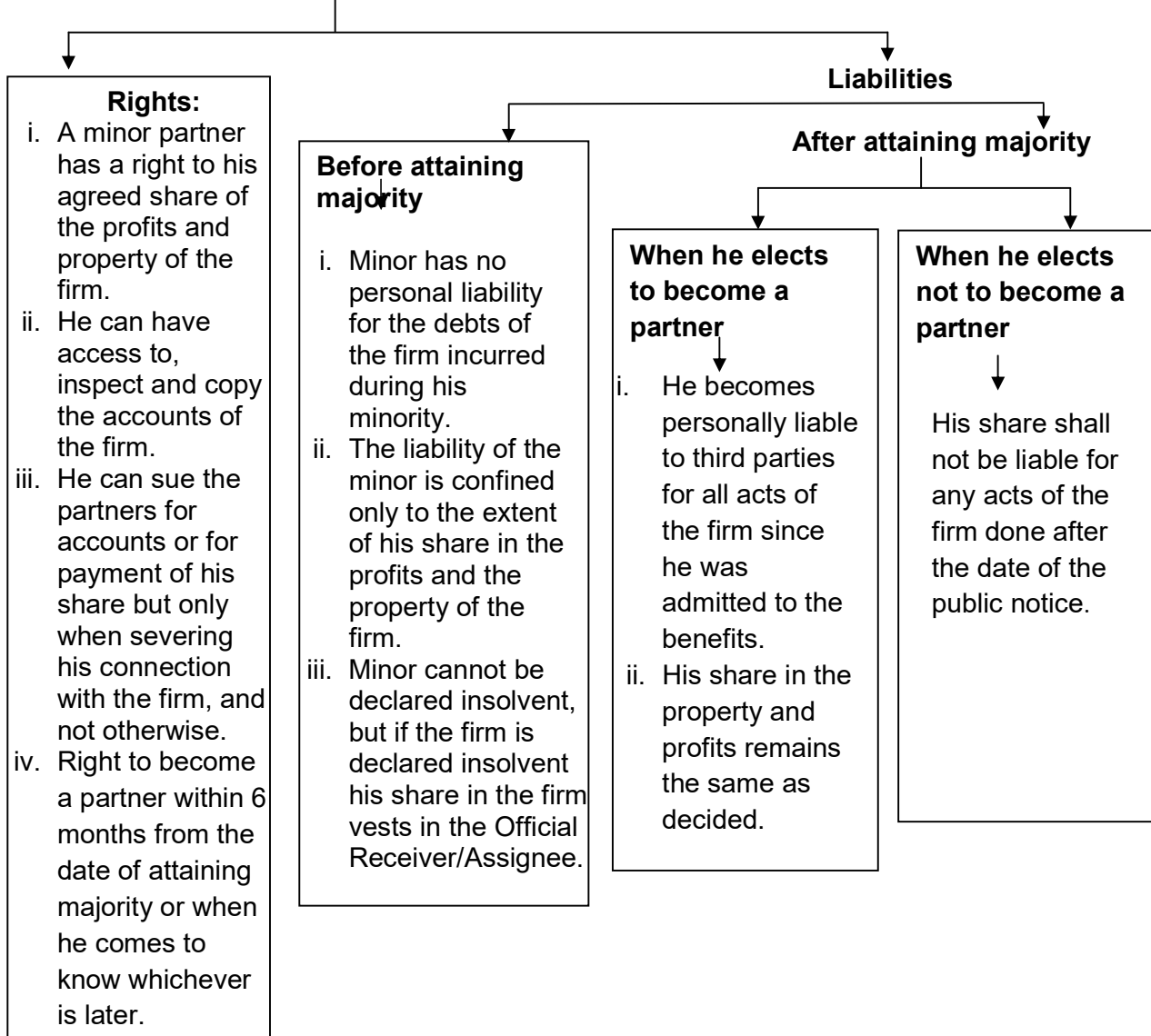
- **TYPES OF PARTNERSHIP**
 1. **Particular Partnership :**
 - ✓ When a partnership is started for a particular purpose or period, it ends only when the purpose or period is completed.
 - ✓ If the partnership is carried even after the completion of the target then it is deemed to be partnership at will.
 2. **Partnership at will :**
 - ✓ When no provision is made by contract between the partners for the duration of their partnership, or for the determination (termination) of their partnership, the partnership is “Partnership at will”.
 - ✓ Where the partnership is at will, the firm may be dissolved by any partner giving notice in writing to all the other partners of his intention to dissolve the firm.
 - ✓ The firm is dissolved as from the date mentioned in the notice as the date of dissolution or if no date is mentioned, then from the date of the communication of the notice.
- **REGISTRATION OF FIRM**
 1. The registration of a firm is not compulsory. It is optional for the firm either to get itself registered or not. There is no penalty for non-registration of a firm. The registration can be done anytime, either in the beginning or during the continuance of business.
 2. Procedure:
 1. Step 1- Obtain a statement in the form from the office of the Registrar.
 2. Step 2- State the following information:
 - Name of the firm
 - Principal place of the firm
 - Name of the other places where the firm carries its business
 - Date when each partner joined
 - Name in full and permanent address of each partner
 - Duration of the firm.
 3. Step 3- Get the statement of duly verified and signed by all the partners or their agents.
 4. Step 4- File the statement along with prescribed fees
 5. Step 5- Obtain a certificate or registration from the Registrar.
 3. The registration becomes effective from date of filing of duly signed and verified documents and not from the date of issue since the act of the Registrar in recording an entry of the statement in the firm is only a clerical act.
 4. Consequences of non-registration:
 1. The partners cannot file a suit against the firm or other partners
 2. The firm cannot file a suit against third parties
 3. The partner of the firm or the firm cannot claim a set-off over `100
 5. Following are not the disabilities of an unregistered firm:
 1. The third party can file a suit against the firm even if the firm is unregistered.
 2. The partners of an unregistered firm can file a suit for:
 - The dissolution of the firm,
 - The accounts of the dissolved firm, and
 - Realisation of the property of the dissolved firm

3. The partner of an unregistered firm/unregistered firm can sue for rights which arise otherwise than out of a contract.

• **MINOR’S POSITION IN PARTNERSHIP FIRM**

✓ A minor cannot become a partner in a firm because partnership is founded on a contract and contract with a minor is void-ab-initio. Though a minor cannot be a partner in a firm, he can be admitted to the benefits of partnership with the consent of all the partners.

✓ **Rights and liabilities of minor**

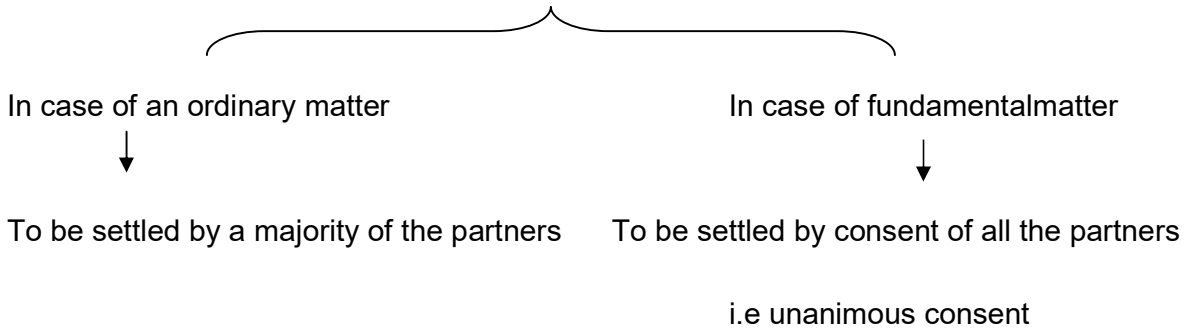


UNIT 2: RELATIONS OF PARTNER

• **RIGHTS OF PARTNERS**

1. **Right to take part in business:** However, the partners may provide, by a contract, that this right shall not be available to some partners.
2. **Right to be consulted:**

In case of difference of opinion, matter will be settled in following way:



3. **Right to have access to books:** However, the partners may provide, by a contract, that this right shall not be available to some partners.
4. **Right to share profits:** No agreement between the partners can restrict this right.
5. **Right to interest on capital and on advance:**
Interest on capital: It can be claimed only if partnership agreement specifies and only out of profits.
Interest on loans and advances: It is payable @6% per annum whether there are profits as well as losses.
6. **Right to indemnity:**
The partners have a right to recover expenses incurred and payments made by him in ordinary course of business or in emergency. No agreement between the partners can restrict this right.
7. **Right to use the partnership property for the purpose of the partnership business.**
8. **Right to be consulted at the time of admission of a new partner.**
9. **Right to retire from the firm.**
10. **Right not to be expelled by majority of partners.**
11. **Right to remuneration** if the partnership agreement expressly provides for the payment of remuneration to working partners.
12. **Right to dissolve the firm.**

• **DUTIES OF PARTNERS**

1. Duty of good faith
2. Duty to carry on the firm business to the greatest common advantage
3. Duty to render true, accounts
4. Duty to give full information
5. Duty to indemnify for loss caused by fraud
6. Duty to attend diligently

7. Duty to share losses
8. Duty to account for personal profits
 - (a) Personal profits from any transaction of the firm.
 - (b) Personal profits from the use of the property of the firm.
 - (c) Personal profits from the business connection of the firm.
 - (d) Personal profits from the use of the name of the firm.

However, the above duty is subject to a contract between the partners
9. Duty to account for profits of a competing business
10. Duty to use firm property exclusively for firm.

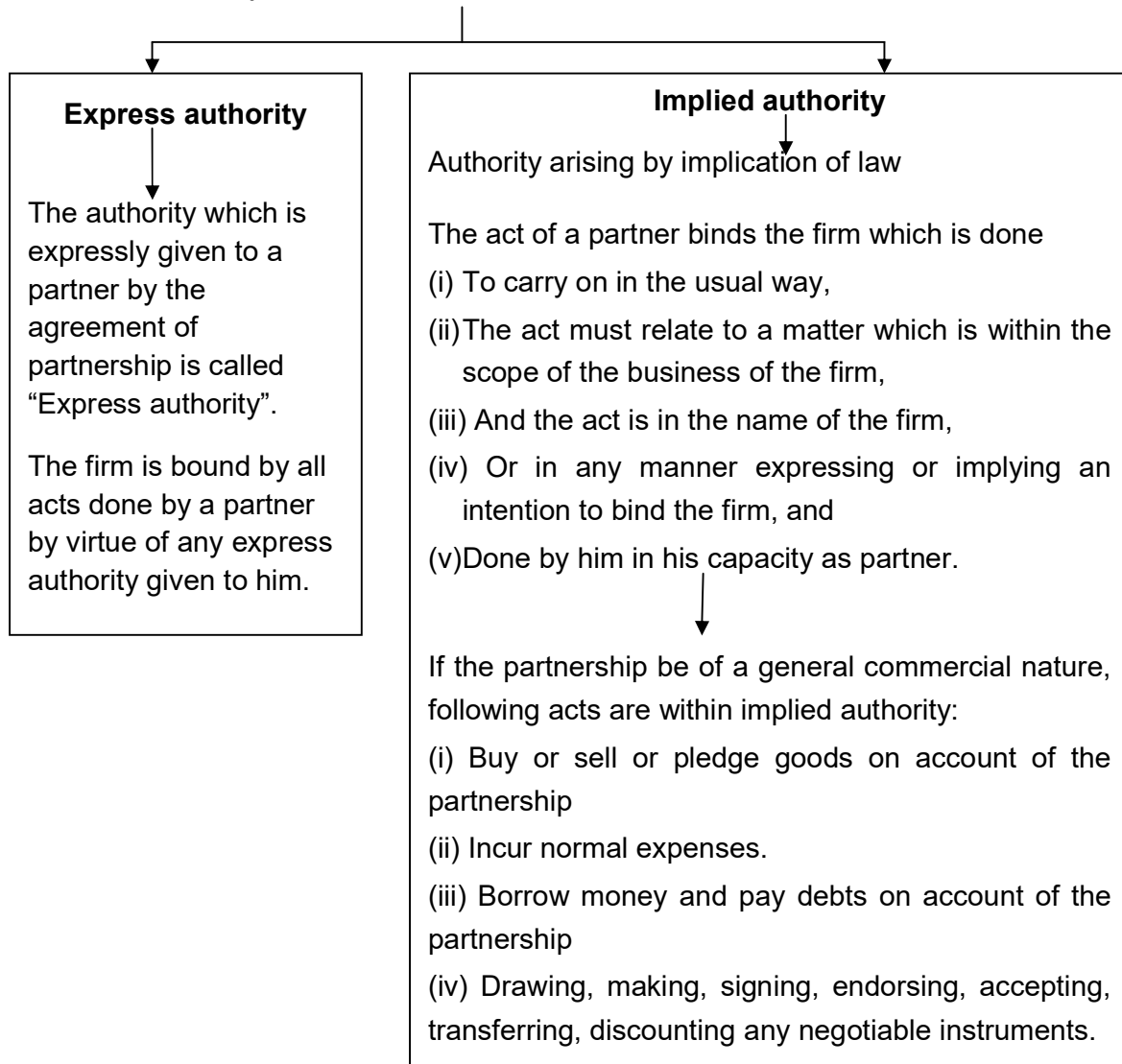
• **PROPERTY OF THE FIRM**

1. Property and rights brought into the firm by the partners
2. Property and rights purchased by the firm
3. Property and rights acquired otherwise
4. Goodwill of the firm

• **AUTHORITY OF A PARTNER**

- ✓ Authority means the right of a partner to bind the firm by his own acts.

Authority



- ✓ **Limitations of Partner's Implied Authority :**

The implied authority of a partner does not empower him to

 - (a) Submit a dispute relating to the business of the firm to arbitration,
 - (b) Withdraw a suit or proceeding filed on behalf of the firm,
 - (c) Compromise or relinquish any claim or portion of a claim by the firm,
 - (d) Admit any liability in a suit or proceeding against the firm,
 - (e) Transfer immovable property belonging to the firm,
 - (f) Acquire immovable property on behalf of the firm.
 - (g) Open a banking account on behalf of the firm in his own name or
 - (h) Enter into partnership on behalf the firm.

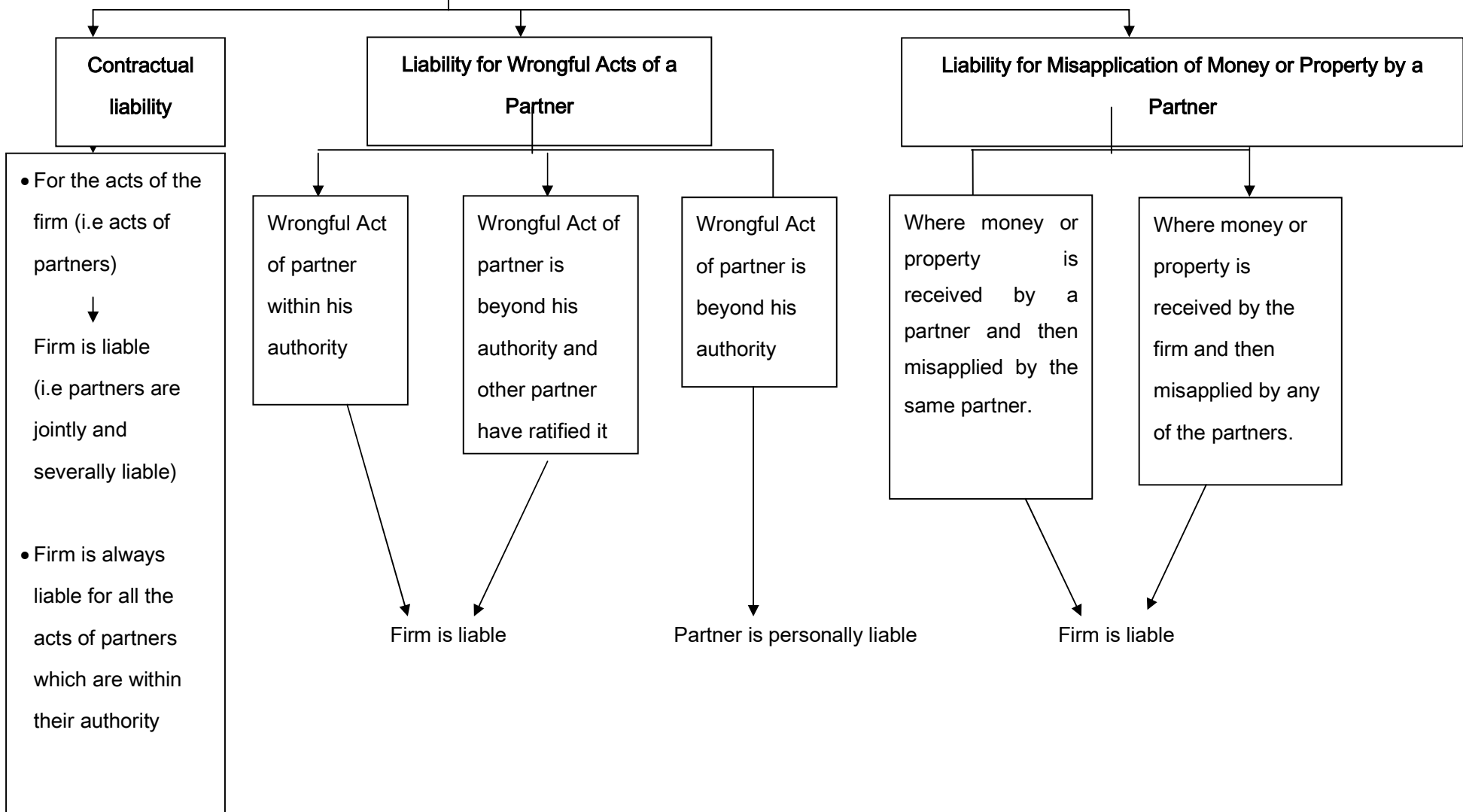
- ✓ The partners in a firm may, by contract between the partners, extend or restrict the implied authority of any partner.

- ✓ If any partner does an act which is beyond his authority but in emergency and good faith then the firm is liable.

- ✓ An admission or representation (i.e. statement of facts) made by a partner concerning the affairs of the firm makes the firm liable.

- ✓ Notice to a partner = Notice to the firm
 - (i) Such notice must relate to the affairs of the business
 - (ii) Such notice must be given to a working partner and not a sleeping partner
 - (iii) There must not be any fraud committed by the partner and third party against the firm.

• LIABILITY OF A FIRM AND ITS PARTNERS TO A THIRD PARTY



- **RECONSTITUTION OF A FIRM**
(Dissolution of partnership)

The reconstitution of a firm means a change in the constitution i.e., composition of the firm and it takes place in the following cases :

- (1) Admission of a new partner
- (2) Retirement of a partner
- (3) Expulsion of a partner
- (4) Rights of outgoing partner
- (5) Insolvency of a partner
- (6) Death of a partner
- (7) Transfer of a partner's interest
- (8) Revocation of continuing guarantee

(1) Admission of a Partner

- ✓ A new partner can be admitted into an existing firm in any of the following ways
 - (a) With the consent of all the partners.
 - (b) In accordance with a contract already entered into between the partners for the admission of a new partner.
- ✓ The liability of an incoming partner may be discussed as under :
 1. Liability for the acts of the firm done before admission :
An incoming partner is not liable for the acts of the firm done before his admission into the firm.
 2. Liability for the acts of the firm done after admission :
He is liable for all the acts of the firm done after he became a partner in the firm.
 3. If the incoming partner agrees to bear the past liabilities, then for past liabilities he shall not be liable to third parties as he is a stranger to contract but he shall be liable to other partners.

(2) Retirement of a Partner

- ✓ A partner may retire from the firm in any one of the following three modes :
 - (i) By consent. A partner may retire, at any time with the consent of all other partners.
 - (ii) By agreement. The partners may enter into an express agreement about the retirement of a partner. In such cases, a partner may retire according to the terms of the agreement.
 - (iii) By notice. In case of partnership at will, a partner may retire by given a written notice of retirement to all other partners.
- ✓ A retiring partner continues to be liable to third parties for the acts of the firm done even after his retirement until a public notice of his retirement is given.

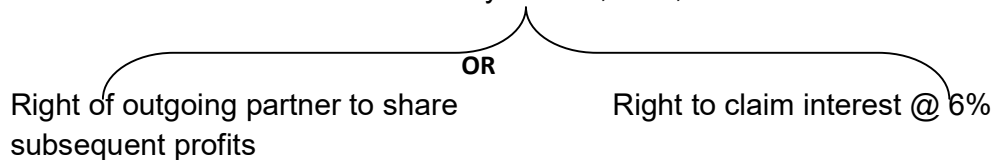
(3) Expulsion of a Partner

- ✓ He can be expelled only if the following conditions are satisfied:
 - (a) The power of expulsion should be given to the partners by an express contract between them.
 - (b) The power of expulsion should be exercised by majority of partners.
 - (c) The power of expulsion should be exercised in absolute good faith.
The test of good faith includes three things:
 - (i) that the expulsion must be advantageous to the firm and not to the partners personally.
 - (ii) that the partner to be expelled is given a notice to that effect
 - (iii) that he was given an opportunity of being heard.

- ✓ It these conditions are not fulfilled the expulsion is null and void and the expelled partner can demand re-instatement in the firm
- ✓ An expelled partner continues to be liable to third parties for the acts of the firm done even after his retirement until a public notice of his retirement is given.
- ✓ The public notice can be given either by the expelled partner himself or by the firm.

(4) Rights of outgoing partner

- ✓ To carry on competing business :
An outgoing partner may carry on a business, but it can be restricted by an agreement (below mentioned).
However he cannot
 - (a) Use the firm name.
 - (b) Represent himself as carrying on the business of the firm, or
 - (c) Solicit the custom of persons who were dealing with the firm before he ceased to be a partner.
 But he can advertise his business.
 Restraint of trade agreement:
 A partner may make an agreement with his partners that on ceasing to be a partner he will not carry on any business similar to that of the firm within a specified period or within specified local limits, such agreement shall be valid if the restrictions imposed are reasonable (Indian Contract Act, 1872).
- ✓ If settlement of accounts is not yet done, then,

**(5) Insolvency of a Partner**

- (i) The partner declared an insolvent, ceases to be a partner on the date on which the order of adjudication is made.
- (ii) The firm is dissolved on the date of the order of insolvency unless there is a contract to the contrary.
- (iii) The estate of the insolvent is not liable for any act of the firm after the date of the order of insolvency.
- (iv) The firm cannot be held liable for any acts of the insolvent partner after the date of the order of insolvency.

(6) Death of a Partner

- ✓ The firm is automatically dissolved on the death of a partner. However, the partners may specifically provide in their agreement that the firm shall not be dissolved, and the remaining partners shall continue the firm's business.
- ✓ Where the firm is not dissolved by the death of a partner, the estate of a deceased partner is not liable for any acts of the firm which are done after his death

(7) Transfer of Partner's Interest

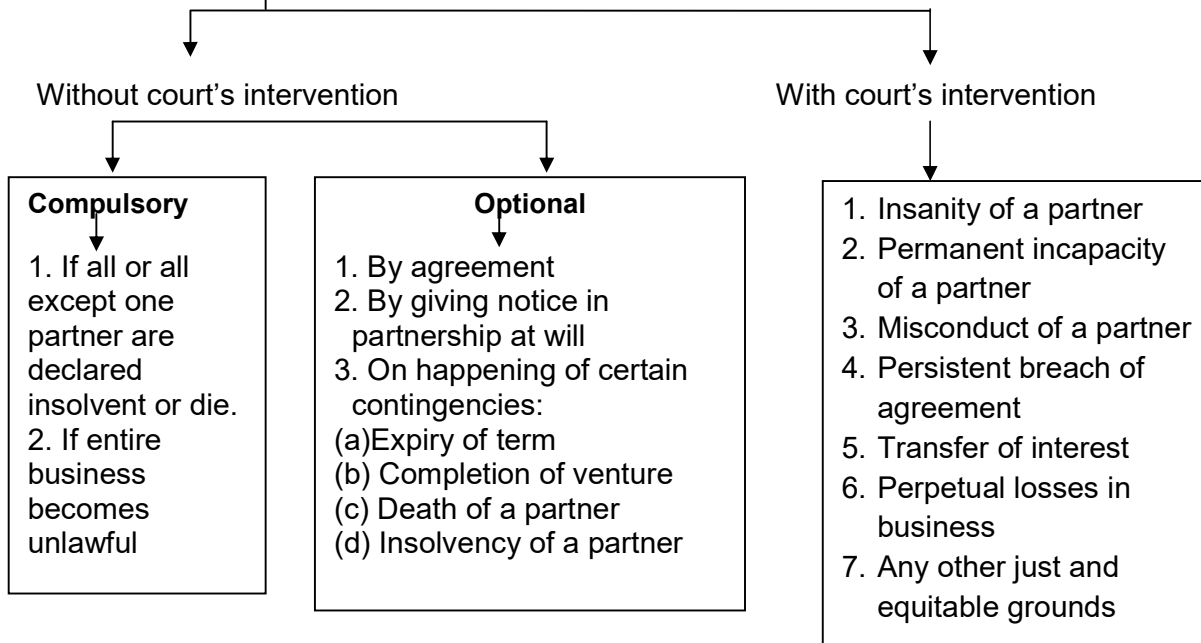
- ✓ A partner can transfer his share only with the consent of other partners.
- ✓ The transferee thereby does not become a partner of the firm,
- ✓ A transferee of a partner's interest cannot do the following, during the continuance of the partnership
 - Interfere in the conduct of the business; or
 - Inspect or take a copy of accounts
- ✓ On the dissolution of the firm, the transferee will be entitled,
 - To receive the share of the assets of the firm to which the transferring partner was entitled, and
 - For the purpose of ascertaining the share, he is entitled to an account as from the date of the dissolution.

(8) Revocation of continuing guarantee

A continuing guarantee given to a firm, or by a third party in respect of the transaction of a firm, is in the absence of agreement to the contrary, revoked as to future transactions from the date of any change in the constitution of the firm.

UNIT 3: DISSOLUTION OF FIRM

• **DISSOLUTION OF FIRM**



• **CONSEQUENCES OF DISSOLUTION**

1. Liabilities for the acts done after dissolution:

On the dissolution of a firm, partners have to give a public notice of the dissolution. If it is not given, the partners shall remain liable to the third party for their acts done even after the dissolution of the firm

2. Continuing Authority for Winding Up:

On the dissolution of a firm, the authority of each partner to bind the firm continues for the following purpose:

- (a) If it is necessary to wind up the affairs of the firm, and
- (b) If it is necessary to complete the transactions started but not completed at the time of dissolution.

3. Partner's Right for Utilisation of Assets

On the dissolution of the firm, each partner is entitled to the following rights:

- (a) He is entitled to have the property of the firm utilised in payment of its debts and liabilities.
- (b) He is entitled to have the surplus distributed among all the partners according to their rights.

4. Mode of Settlement of Accounts:

✓ **Utilization of assets:**

The assets of the firm, including any sums contributed by the partners to make up deficiencies of capital, shall be utilized in the following manner:

- (a) First of all, the assets shall be utilized in paying the debts of the firm to the third parties.
- (b) If there is any surplus, the same shall be utilized in paying each partner the amount of loan advanced to the firm other than the capital.
- (c) If there is still any surplus, the same shall be utilized in paying each partner towards the amount of his capital.

- (d) If there is still any surplus, the same shall be divided among all the partners in proportion to their share in the profits of firm.

✓ **Payment of losses:**

The losses of the firm, including the deficiencies of capitals shall be paid in the following manner:

- (a) First of all, the losses shall be paid out of the profits.
- (b) If the profits, are not sufficient to pay the losses, then the balance of loss shall be paid out of capital, and
- (c) If still some balance of losses remains, it shall be paid by the partners individually in the proportion in which they were entitled to share profits.

5. Payment of firm's debts and Partner's Private Debts:

- 1) Firm's property shall be applied first in payment of firm's debts then the surplus, if any, shall be applied for payment of partner's private debts to the extent in which the concerned partner is entitled to the surplus.
- 2) Partner's private property shall be applied first in the payment of his debts and the surplus, if any, shall be used in payment of firm's debts.

6. Return on premium of partnership's premature dissolution:

In the case of dissolution of partnership earlier than the period fixed for it, the partner paying the premium is entitled to the return of the premium of such part thereof as may be reasonable except when the partnership is dissolved:

- (i) By the death of one of the partners;
- (ii) When the dissolution is mainly due to the misconduct of the partner who paid the premium
- (iii) The dissolution is according to an agreement which had no provision for the return of premium or any part thereof.

7. Treatment of Loss Arising due to Insolvency of a Partner:

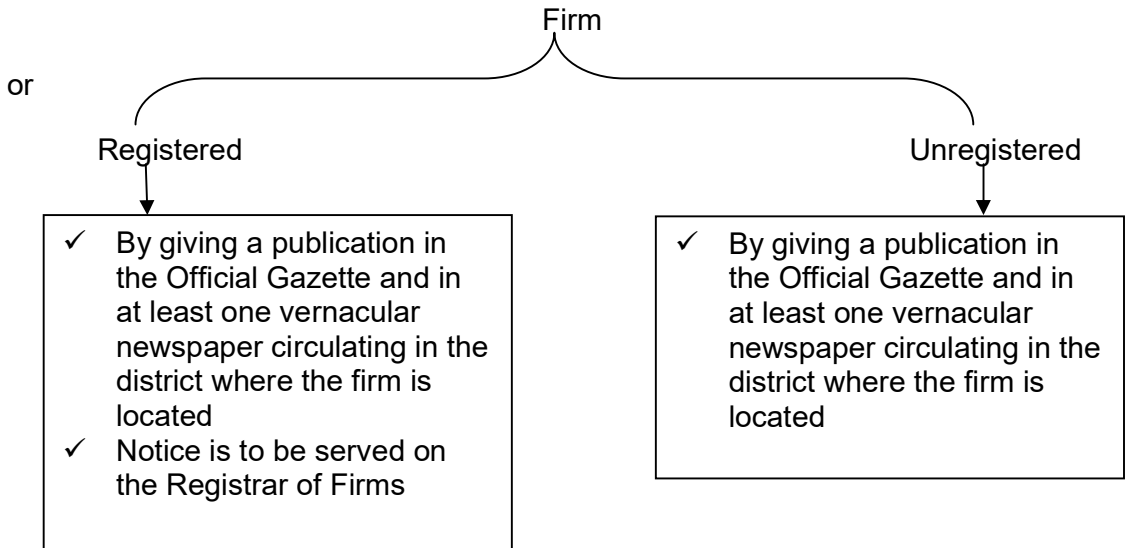
Unless otherwise agreed it requires that:

- 1) The solvent partners should bring in cash equal to their shares of the loss on realization
- 2) The solvent partners should bear the loss arising due to the insolvency of a partner in the ration of their Last Agreed Capitals.

8. Rights of a partner in case of Dissolution on Account of Fraud and Misrepresentation:

- 1) He has a right of lien on the surplus assets after the payment of firm's debts, for any sum paid by him for purchase of a share in the firm
- 2) He is entitled to rank as a creditor of the firm in respect of any payment made by him towards firm's debts
- 3) He is entitled to be indemnified by the partner guilty of fraud or misrepresentation against all the debts of the firm

• **MODE OF GIVING PUBLIC NOTICE**



- ✓ When public notice is required to be given
 - a) On retirement or expulsion of a partner
 - b) On the dissolution of the firm
 - c) On the election to become or not to become a partner by a minor on attaining his majority.
- ✓ When a public notice is not required
 - a) On the death of a partner
 - b) On the insolvency of partner

- Q.1. A, B & C were partners in a firm of drapers. The partnership deed authorised the expulsion of a partner when he was found guilty of flagrant breach of duty. A was convicted of travelling without ticket. On this ground, he was expelled by the other partners B & C. Is expulsion justified?
- Q.2. A, B & C are partners in a firm. As per terms of the partnership deed, A is entitled to 20% of the partnership property & profits. A retires from the firm & dies after 15 days. B & C continue business of the firm without settling accounts. What are the rights of A's legal representatives against firm under the Indian Partnership Act 1932?
- Q.3. Mayur and Nupur purchased a taxi to ply it in partnership. They had done business for about a year when Mayur, without consent of Nupur, disposed off the taxi. Nupur brought an action to recover his share in the sale proceeds. Mayur's only defence was that the firm was not registered. Will Nupur succeed in her suit?
- Q.4. Explain Liability of minor partnership.
- Q.5. What is Partnership Deed? Discuss contents of Partnership Deed?
- Q.6. Write a short note on effects of dissolution of partnership firm.
- Q.7. What test would apply for determining the existence of partnership?
- Q.8. X and Y were partners carrying on banking business. X had committed adultery on several women in the city and his wife had left on this ground. Y applied to Court for dissolution of the firm on this ground. Will he succeed?
- Q.9. What are the partners by estoppel or holding out?
- Q.10. Discuss the provisions of dissolution of Partnership Firm.

Q.1. Answer

A partner cannot be ordinarily expelled from the firm. However, in certain exceptional cases, he can be expelled by following a prescribed procedure.

He can be expelled only if the following conditions are satisfied:

- (a) The power of expulsion should be given to the partners by an express contract between them.
- (b) The power of expulsion should be exercised by majority of partners.
- (c) The power of expulsion should be exercised in absolute good faith.

The test of good faith includes three things :

- (1) That the expulsion must be in the interest of the partnership
- (2) That the partner to be expelled is given a notice to that effect
- (3) That he was given an opportunity of being heard. If these conditions are not fulfilled the expulsion is null and void and the expelled partner can demand re-instatement in the firm

In the given question, yes, expulsion is justified. In this case, the partnership deed authorised expulsion on the grounds of flagrant breach of duty. Doing an act which brings a partner within penalties of criminal law is flagrant breach of duty. Also, the expulsion decision was taken by majority of the partners.

Q.2. Answer

Section 37 of India Partnership Act provides that where a partner dies or otherwise ceases to be a partner and there is no final settlement of accounts between the legal representatives of the deceased partner or the firms with the property of the firm, then in absence of contract to the contrary, the legal representative of the deceased partner or retired partner entitled to claim either.

- a) Such share of profits earned after death or retirement of the partner which attribute to the use of his share in the property of the firm, or
- b) Interest at the rate of 6% per annum on the amount of his share in the property

Based on the aforesaid provisions of section 37 of India Partnership Act in the given problem A's representative at his option can claim

- i. The 20% share of profits as per partnership deed or
- ii. Interest at the rate of 6% per annum on the amount of A's shares in the property.

Q.3. Answer

Section 69(3) of Indian Partnership Act, the term set off may be defined as adjustments of debts by one party due to him from the other party who files a suit against him. It is another disability of the partners and of an unregistered firm that it cannot claim set off when a suit is filed against it. Yes, Nupur will succeed in her suit. As the business had been closed on the sale of taxi, the suit in the question is for claiming share of the assets of the dissolved firm. Section 69(3) specially protects the right of a partner of an unregistered firm to sue for the realisation of the property of a dissolved firm.

Q.4. Answer

Liabilities of Minor

1. His Share in Liability

A minor partner's liability is confined only to the extent of his share in the firm. Section 30(3) provides that a minor's share is liable for the acts of the firm. But a minor is not personally liable in any such act. Thus, he is neither personally liable nor is his private estate liable for the acts of the firm.

2. Personal Liabilities

Where a minor on attaining majority, elects to become a partner, he becomes personally liable as other partners to the third parties for all the acts of the firm done since he was admitted to the benefits of partnership.

Election by Minor

A minor who was admitted to the benefits during his minority within six months of his attaining the age of majority or when he comes to know of his being so admitted (whichever date is later), he has to elect whether he wants to become a partner, or sever his connection with the firm. He may give public notice of his election to continue or repudiate, but if he fails to give any public notice within the period stated above, he will be deemed to have elected to become a partner in the firm. [Section 30(5)]

If he becomes or elects to become a partner, his position will be as under:

1. His rights and liabilities will be similar to those of a full-fledged partner.
2. He will be personally liable for all the acts of the firm, done since he was first admitted to the benefits of the partnership.
3. His share of profits and property remains the same as was before, unless altered by agreement.

If he elects not to become a partner, then:

1. His rights and liabilities shall continue to be those of a minor upto the date of his giving public notice.
2. His share shall not be liable for any acts of the firm done after the date of the public notice.
3. He is entitled to sue the partners for his share of the property and profits in the firm. [Section 30(8)]

Q.5. Answer

Formation of Partnership

According to the definition of partnership under the Indian Partnership Act, 1932, there must be an agreement between the partners of a partnership firm. The partnership agreement must comply with all the essentials of a valid contract. There must be free consent of the parties who must be competent to contract and the object of partnership should not be forbidden by law or immoral or opposed to public policy. Two exceptions, however, may be noted:

- (i) A minor may be admitted to the benefits of a partnership with the consent of all other partners.
- (ii) As relations of partners inter se are that of agency, no consideration is required to create the partnership.

Partnership Deed

- The agreement of partnership may be oral but to avoid future disputes it is always advisable to have it in writing.
- The mutual rights and obligations of partners must be discussed in detail and should be put into writing in the shape of a 'Partnership Deed', before the partnership is actually started.

- Thus, the written document which contains the mutual rights and obligations of partners is known as partnership deed. (The partnership deed is also called as 'Partnership Agreement', 'Constitution of Partnership', 'Articles of Partnership' etc.).
- The deed must be properly drafted and stamped according to the provisions of the Indian Stamp Act.
- Each partner should be given a copy of the deed and if the firm is to be registered, a copy of the deed should be filed with the Registrar of Firms at the time of such legislation.
- The partnership deed is not a public document and therefore binds only third parties so far as they have notice of it.

Contents of Partnership Deed

The exact terms of the partnership deed (or agreement) will depend upon the circumstances but generally a partnership deed contains the following covenants:

- (i) The firm name and business to be carried on under that name.
- (ii) Names and addresses of partners.
- (ii) Nature and scope of business and address(s) of business place(s).
- (iv) Commencement and duration of partnership.
- (v) The capital and the contribution made by each partner.
- (vi) Provision for further capital and loans by partners to the firm.
- (vii) Partner's drawings.
- (viii) Interest on capital, loans, drawings and current account.
- (ix) Salaries, commission and remuneration to partners,
- (x) Profit (or loss) sharing ratio of partners.
- (xi) The keeping of proper books of accounts, inspection and audit, Bank Accounts and their operation.
- (xii) The accounting period and the date on which that accounts are to be prepared.
- (xiii) Rights, powers and duties of the partners.
- (xiv) Whether and in what circumstances, notice of retirement or dissolution can be given by a partner.
- (xv) Provision that death or retirement of a partner will not bring about dissolution of partnership,
- (xvi) Valuation of goodwill on retirement, death, dissolution etc.
- (xvii) The method of valuation of assets (and liabilities) on retirement or death of any partner.
- (xviii) Provision for expulsion of a partner.
- (xix) Provision regarding the allocation of business activities to be performed by individual partners.
- (xx) The arbitration clause for the settlement of disputes. The terms contained in the partnership deed may be varied with the consent of all the parties, and such consent may be express or implied by a course of dealing.

Q.6. Answer

Effect of Dissolution:

Continuing authority of partners

- The authority of partners to bind the firm continues so long as is necessary to wind up the business, provided that the firm is in no case bound by the acts of a partner who has been adjudged an insolvent except on the principle of holding out. (Section 47)
- Also each partner has an equitable lien over the firm's assets entitling him to have them applied in payment of the firm's debts, and in payment of whatever is due to partner. This lien can be enforced by injunction forbidding unfair distribution. (Section 46)

Continuing liability of partners

- The partners continue to be liable to outsiders for any act done by any of them which would have been an act of the firm if done before the dissolution, unless a public notice is given of the dissolution. After dissolution, the rights and obligations of partners continue in all things necessary for the winding up of the business. The partners may complete unfinished transactions. But this authority is only for the winding up of the affairs of the firm and not for new transactions.

Right to Return of Premium

To buy entry into an existing firm, a new partner sometimes has to pay a premium to the existing partners in addition to any investment of capital. On dissolution, he is entitled to demand the return of a proportion of the premium if the partnership was for a fixed term and was dissolved before the expiry of that term, unless dissolution was caused by (i) agreement, or (ii) misconduct of the party seeking return of the premium, or (iii) death of a partner. (Section 51)

Settlement of Accounts on Dissolution

Section 48 of the Act provides that in settling accounts between the partners after a dissolution of partnership, the following rules shall, subject to any agreement, be observed:

- (a) Losses, including deficiencies of capital shall be paid first out of undistributed profits, next out of capital, and lastly, if necessary, by the partners individually in the proportion in which they were entitled to share profits
- (b) The assets of the firm, including the sums, contributed by the partners to make up losses or deficiencies of capital shall be applied in the following manner and order:
 - (i) in paying outside creditors;
 - (ii) in repaying advances made by partners (distinct from investment of capital);
 - (iii) in repaying capital to partners; and
 - (iv) the ultimate residue, if any, shall be divided among the partners in the proportions in which profits are divisible.

Where the assets are not sufficient, the partners have to bear the loss in equal shares. After they have contributed their share of the deficiency they will be paid rateably the amount due to them by way of their capital (The Rule followed in the case of *Garner v. Murray*, 1904 73 L.J. Ch. 66).

Loss due to insolvency of partners

In case a partner is insolvent and is not able to contribute towards the deficiency, the principle laid down in the case of *Garner vs. Murray* will be applicable.

It holds that:

- (a) The solvent partners will contribute only their share of deficiency in cash
- (b) The available assets should be distributed among the solvent partners in proportion to their capital.
- (c) Thus, the deficiency of capital of the insolvent partners will be distributed among the solvent partners in the ratio of their respective capitals.

Q.7. Answer

These elements are discussed below in detail:

(1) Association of two or more persons

There must be a contract between two or more persons. Therefore unless there are at least two persons there cannot be a partnership. Persons must be competent to enter into a contract. They may all be natural or artificial or some natural and other artificial. Thus a corporation or limited partnership may itself be a partner in a general partnership.

(2) Agreement

Existence of an agreement is essential of partnership. Section 5 of the Act states that the relation of partnership arises from contract and not from status; and in particular, the

members of a Hindu Undivided Family carrying on a family business as such, or a Burmese Buddhist Husband and wife carrying on business as such are not partners in such business. Such an agreement between the partners may be express or implied. Further, the agreement must be a valid agreement and for a lawful object and purpose and between the persons competent to contract.

(3) Business

Partnership implies business and when there is no association to carry on business there is no partnership. The term “business” is, however, used in the widest sense to cover trade, occupation and profession. As per Section 2(b) of the Act the term “business” includes every trade, occupation and profession. In the definition of partnership the word “business” is used in the sense of “carrying on business” which suggests continuity or repetition of acts. But it does not mean that it should be confined to lengthy operations, it may consist of a single adventure of a single undertaking, if there is continued participation of two or more persons for acquisition of gains.

(4) Sharing of Profits

To constitute a partnership, the parties must have agreed to carry on a business and to share profits in common. “Profits” mean the excess of returns over advances, the excess of what is obtained over the cost of obtaining it. Sharing of profits also involves sharing of losses. But whereas the sharing of profit is an essential element of partnership, the sharing of losses is not. It is open to one or more partners to bear all the losses of the business. It follows that the sharing of profits is an essential ingredient of partnership and there would be no partnership where only one of the partners is entitled to the whole of the profits of the business. But it is open to the partners to agree to share the profits in any way they like. They may agree to share the profits either in specific proportions or in specific sums.

(5) Mutual Agency The True Test

Mutual agency is the foundation of partner’s liability. Each partner is both an agent and principal for himself and others; that is the significance of the phrase “carried on by all or any of them acting for all”. Each partner is an agent binding the other partners who are his principal and each partner is again a principal, who in turn is bound by the acts of the other partners. In other words, there must be facts or circumstances from which it can be inferred that each of the persons alleged to be partners was the agent, real or implied of another. What is essential is that the partner who conducts the business of the firm not only acts for himself but for the other partners also.

The true test, therefore, in determining whether a partnership exists, is to see whether the relation of principal and agent exists between the parties and not merely whether the parties share the profits or the business is carried on for the benefit of all. It is this relation of agency among partners which distinguishes a partnership from a single co-ownership on the one hand and the agreement to share profits on the other. The existence of this relation of agency can be gathered from the real intention of the parties and the circumstances of the case. The question of intention must be decided on the basis of the conduct of parties and of all the surrounding circumstances. The law of partnership is the extension of the law of agency therefore every partner is liable for the act of other partner if within authority upto unlimited extent. The relation of mutual agency is the conclusive test of partnership.

Q.8. Answer:

Section 44(c) of Indian Partnership Act states, a partner is guilty of misconduct when the Court is satisfied that the misconduct adversely affect the partnership business then the Court may allow dissolution of the firm. Y will not succeed. In this case, though X is guilty of misconduct but his misconduct does not have any adverse effect on their business as bankers [**Snow vs Milform**].

Q.9. Answer

- If the behaviour of a person arouses misunderstanding that he is a partner in a firm (when actually he is not), such a person is estopped from later on denying the liabilities for the acts of the firm. Such person is called partner by estoppel and is liable to all third parties.
- Similarly, if a person who is declared to be a partner (when actually he is not) does not deny the fact that he is a partner, he being held out as a partner is responsible for all liability of the business.
- The law relating to partners by holding out is contained in Section 28 of the Act which lays down thus: "Anyone who by words, spoken or written or by conduct represents himself, or knowingly permits himself to be represented to be a partner in a firm, is liable as a partner in that firm to anyone who has on the faith of any such representation given credit to the firm, whether the person representing himself or represented to be a partner does or does not know that the representation has reached the person so giving credit".
- The rule as to holding out is based on the doctrine of estoppel as contained in Section 115 of the Indian Evidence Act.
- Holding Out means "to represent". Strangers, who hold themselves out or represent themselves to be partners in a firm, whereby they induce others to give credit to the partnership are called "Partners by Holding Out".
- In case of "Partnership by Estoppel", the representation is made by partners about a stranger within his knowledge and hearing and he does not contradict it. He is then held liable as a partner.

Effects of Holding out

- The Holding Out partner becomes personally and individually liable for the acts of the firm. But he does not become a partner in the firm and is not entitled to any rights or claim upon the firm. An outsider, who has given credit to the firm thinking him to be a partner, can hold him liable as if he is a partner in that firm. As the liability of the partners is joint and several he can be held liable to pay the entire amount. But under the doctrine of subrogation as well as on the basis of quasi-contract, he can recover the amount so paid from the partners of the firm, if they are solvent.

Q.10. Answer

Dissolution

- According to Section 39 "The dissolution of partnership between all the partners of a firm" is called the "Dissolution of the Firm".
- A dissolution does not necessarily follow because the partnership has ceased to do business, for the partnership may continue for the purpose of realising the assets.
- The Partnership Act makes a distinction between the "dissolution of partnership" and "dissolution of firm".
- Where there is dissolution of partnership between all the partners of a firm, it is a dissolution of the firm (Section 39).
- Where there is an extinction of relationship between some of the partners only, it is a dissolution of partnership.
- So the dissolution of a partnership may or may not include the dissolution of the firm, but the dissolution of the firm necessarily means the dissolution of the partnership as well.

Dissolution of Partnership

The dissolution of partnership takes place (even when there is no dissolution of the firm) in the following circumstances:

- (a) By the expiry of the fixed term for which the partnership was formed. [Section 42(a)]
- (b) By the completion of the adventure. [Section 42(b)]
- (c) By the death of a partner. [Section 42(c)]

(d) By the insolvency of a partner. [Section 42(d)]

(e) By the retirement of a partner. [Section 42(e)]

In all the above cases, the remaining partners may continue the firm in pursuance of an agreement to that effect. If they do not continue then the dissolution of the firm takes place automatically.

Dissolution of the Firm

In the following cases there is necessarily a breaking up or extinction of the relationship between all the partners of the firm, and closing up of the business:

(a) By mutual agreement: A firm may be dissolved where all the partners agree that it shall be dissolved. (Section 40)

(b) By the insolvency of all the partners but one: If all the partners except one become insolvent, the firm must come to an end, as a partnership firm with one partner cannot continue. [Section 41(a)]

(c) By business becoming illegal: If the business of the firm becomes illegal because of some subsequent events, such as change of law, it is automatically or compulsorily dissolved by the operation of law. [Section 41(b)]

(d) By notice of dissolution: Where the partnership is at will, the firm may be dissolved at any time, by any partner giving notice in writing of his intention to dissolve the firm, to all the other partners. The dissolution will take place from the date mentioned in the notice or, if no such date is mentioned, as from the date of the communication of the notice. (Section 43)

Dissolution of the Firm through Court

Unlike a partnership at will, the partnership for a fixed period cannot be dissolved by a notice. It could only be dissolved by Court in a suit by a partner. Though remedy of dissolution by a suit is available in case of all kinds of partnership, it is of practical importance in case of partnership for a fixed period.

As per Section 44, the Court may order dissolution of the firm in the following circumstances:

(a) When a partner becomes of unsound mind: As the insanity of a partner does not automatically dissolve the firm, either the lunatic through his guardian or other partners may file a suit for the dissolution of the firm, in either case the Court may order dissolution which will take effect from the date of the order.

(b) Permanent incapacity of a partner: Where a partner has become permanently incapable of performing his duties as a partner, e.g., he becomes blind, paralytic, etc., the Court may, at the instance of any of the other partners, order the dissolution of the firm.

(c) Misconduct of a partner affecting the business: Where a partner is guilty of misconduct, which is likely to affect prejudicially the business of the firm, the Court may dissolve the firm at the instance of any of the other partners. Gambling by a partner or conviction of a partner for travelling without ticket would be sufficient ground for dissolution.

(d) Persistent disregard of partnership agreement by a partner: Where a partner frequently commits breaches of the partnership agreement and the other partners find it impossible to carry on the business, the Court may order dissolution at the instance of the other partners.

(e) Transfer of interest or share by a partner: A partner is not entitled to assign away his interest so as to introduce a new partner into the firm. Where a partner has transferred the whole of his interest to a third person or where his interest has been attached under a decree or sold under a process of law, the other partners may sue for dissolution.

(f) Business working at a loss: The Court may dissolve a partnership firm where it is satisfied that the business of the firm cannot be carried on except at a loss.

(g) Where just and equitable: As the grounds mentioned are not exhaustive, the Court may dissolve a firm on any other ground if it is satisfied that it would be just and equitable to dissolve the firm. The Court may order dissolution where the sub-stratum of the partnership firm has gone or where there is a complete deadlock and destruction of confidence between the partners [re. Yenidje Tobacco Co. Ltd. (1916) 2 Ch. 426].

- Q.1. Arun, Varun and Tarun started Kirana business in Chennai on 1st January 2012, for a period of five years. The business resulted in a loss of Rs.20,000 in the first year, Rs. 25,000 in the second year and Rs.35,000 in the third year. Varun and Tarun wish to dissolve the firm while Arun wants to continue the business. Advise Varun and Traun. **[6 marks]**
- Q.2. Akash, Ashish and Anil were partners in a firm. By his wilful neglect and misconduct Anil caused serious loss to the business of the firm. After several warranting to Anil, Akash and Ashish passed resolution expelling Anil from the firm. By another resolution admitted Abhishek as a partner in place of Anil. Anil objects to his expulsion as also to the admission of Abhishek. Is he justified in his objections? **[6 marks]**
- Q.3. What is Partnership Property? **[6 marks]**
- Q.4. Statutory duties of partners under Partnership Act 1932. **[7 marks]**
- Q.5. Write a short note on Limitations of Partner's Authority. **[6 marks]**
- Q.6. What changes are contemplated in partnership firm? **[6 marks]**
- Q.7. What are the Rights of partner. **[7 marks]**
- Q.8. Write short note on Liability of an Outgoing or Retiring Partner. **[6 marks]**

Q.1. Answer

As per section 44 of India Partnership Act, Varun and Tarun are advised to make a petition to the Court for the dissolution of the firm on the ground that the firm cannot be carried on except at a loss. Since the firm was constituted for fixed term of five years it cannot be dissolved without the consent of all the partners and as such Varun and Tarun cannot compel Arun to dissolve the firm.

Q.2. Answer

A partner may be expelled from a firm by majority of the partner's only if

- a) The power to expel has been conferred by contract between the partners and
- b) Such a power has been exercised in good faith and for the benefit of the firm

The partner who is being expelled must be given reasonable notice and opportunity to explain his position and to remove the cause of his expulsion. Yes, Anil is justified in his objections.

In the absence of an express agreement authorizing expulsion, the expulsion of a partner is not proper and is without any legal effect. Section 33(1). Anil's objection to the admission of Abhishek is also justified as a new partner can only be admitted with the consent of all the partners. Section 33(1).

Q.3. Answer

It is open to the partners to agree among themselves as to what is to be treated as the property of the firm, and what is to be separate property of one or more partners, although employed for the purposes of the firm.

In the absence of any such agreement, express or implied, the property of the firm is deemed to include:

- (a) all property, rights and interests which have been brought into the common stock for the purposes of the partnership by individual partners, whether at the commencement of the business or subsequently added thereto;
- (b) those acquired in the course of the business with money belonging to the firm; and
- (c) the goodwill of the business. (Section 14)

The property of the firm belongs to the firm and not to the individual partner or partners. The ownership belongs to the firm, and no partner can deal with specific properties as if the properties are his own, nor does the partner possess any assignable interest in such property (Narayanappa v. Bhaskaia Krishnappa, AIR 1966 SC 1300). What is meant by the share of a partner is his proportion of the partnership assets after they are all realised and converted into money, and all the partnership debts and liabilities have been paid and discharged. If certain partners jointly own immovable property which they use for the purposes of the partnership business, the mere use of such property does not make such property as partnership property. Whether such property is or is not partnership property depends upon the agreement between the partners (Lachhman Dass v. Mrs. Gulab Devi, AIR 1936 ALL. 270). The ultimate test to determine the property of the firm is the real intention of the partners and the Court can take into consideration the following facts:

- (1) The source of the purchase money.
- (2) The reason due to which the property was purchased or acquired.

- (3) The object for which the property was purchased or acquired.
- (4) The mode in which the property was obtained.
- (5) The mode in which the property was dealt with.
- (6) The use to which the property was put to.

All such facts are matter of evidence and depend on the facts of each case. These facts indicate the intention of the parties but are not conclusive to make a property as partnership property. These facts can be established by entries in the books of account of the firm and of the partners, correspondence, the deed of partnership, etc.

Q.4. Answer

Duties of Partners

Apart from any duties imposed by the partnership articles, the following statutory duties are implied:

- (a) Every partner is bound to carry on the business of the firm to the greatest common advantage. (Section 9)
- (b) Every partner must be just and faithful to other partners. (Section 9)
- (c) A partner is bound to keep and render true, proper and correct accounts of the partnership. (Section 9)
- (d) Utmost good faith between the partners is the rule and one partner must not take advantage of the other. As an agent of other partners, every partner is bound to communicate full information to them. (Section 9)
- (e) Every partner must account for any benefits derived from the partnership business without the consent of the other partners, i.e., a partner must not make "secret profits". [Section 16(a)]
- (f) A partner must not compete with the firm, without the consent of the other partners. Any profits made by such unauthorised competition can be claimed by the firm. [Section 16(b)]
- (g) Every partner is bound to attend diligently to the business of the firm and in the absence of any agreement to the contrary, he is not entitled to receive any remuneration. [Section 12(b) and 13(a)]
- (h) In the absence of an agreement to the contrary, every partner is bound to share losses equally with the others. [Section 13(b)]
- (i) Every partner must hold and use the partnership property exclusively for the firm. (Section 15)
- (j) Every partner is bound to indemnify the firm for any loss caused by fraud in the conduct of the business. (Section 10)
- (k) A partner who is guilty of wilful neglect in the conduct of the business and the firm suffers loss in consequence, is bound to make compensation to the firm and other partners. [Section 13(f)]
- (l) No partner can assign or transfer his partnership interest to any other person, so as to make him a partner in the business. (Section 29)
- (m) But a partner may assign the profits and share in the partnership assets. But the assignee or transferee will have no right to ask for the accounts or to interfere in the management of the business; he would be entitled only to share the actual profits. On dissolution of the firm, he will be entitled to the share of the assets and also to accounts but only from the date of dissolution. (Section 29)
- (n) Every partner is bound to act within the scope of his actual authority. If he exceeds his authority, he shall compensate the other partners for loss unless they ratify his act.

Q.5. Answer

Acts beyond Implied Authority

Section 19(2) states that in the absence of any usage or custom or trade to the contrary, the implied authority of a partner does not empower him to:

- (a) submit a dispute relating to the business of the firm to arbitration;
- (b) open a banking account on behalf of the firm in his own name;
- (c) compromise or relinquish any claim or portion of a claim by the firm;
- (d) withdraw a suit or proceeding filed on behalf of the firm;
- (e) admit any liability in a suit or proceedings against the firm;
- (f) acquire immovable property on behalf of the firm;
- (g) transfer immovable property belonging to the firm; and
- (h) enter into a partnership on behalf of the firm.

Q.6. Answer

The Indian Partnership Act, 1932, contemplates the following changes in a partnership firm:

- (1) Changes in the constitution of a firm.
- (2) Changes in the nature of a business or undertakings.
- (3) Changes in the duration of a firm.

A change in the constitution of a firm takes place when:

- (a) a new partner is introduced as a partner in a firm; (Section 31)
- (b) a partner retires from a firm; (Section 32),
- (c) a partner is expelled from a firm; (Section 33),
- (d) a partner is adjudicated as an insolvent; (Section 34) and
- (e) a partner dies. (Section 35)

A change in the nature of the business can only be brought about by the consent of all the partners. Thus, a partnership formed for a definite purpose, agreed upon at the time of formation of the partnership, cannot depart from the agreed purpose without the consent of all the partners [Section 12(c)].

Section 17(c) provides for a case whether a partnership firm is formed for a particular undertaking or undertakings, it proceeds to carry on other undertaking or undertakings, in that event the mutual rights and duties of the partners in respect of the other adventures or undertakings are the same as those in respect of the original adventures of undertakings.

Q.7. Answer

Rights of Partners

Unless otherwise agreed by the partners, the following rules apply:

- (a) Every partner has a right to take part in the conduct and management of the business. [Section 12(a)]
- (b) Every partner whether active or dormant, has a right of free access to all records, books and accounts of the business and also to examine and copy them. [Section 12(d)]
- (c) Every partner is entitled to share in the profits equally, unless different proportions are stipulated. [Section 13(b)]
- (d) A partner who has contributed more than the share of the capital for the purpose of the business is entitled to an interest at a rate agreed upon, and where no rate is stipulated for, at six per cent per annum. But a partner cannot claim interest on capital, unless there is an agreement to pay it. [Section 13(d)]
- (e) A partner is entitled to be indemnified by the firm for all expenses incurred by him in the course of the business, for all payments made by him in respect of partnership debts or

liabilities and disbursements made in an emergency for protecting the firm from loss. [Section 13(e)]

- (f) Every partner is, as a rule, a joint owner of the partnership property, and have it applied exclusively for the purposes of the partnership. (Section 15)
- (g) A partner has power to act in an emergency for protecting the firm from loss. (Section 21)
- (h) Every partner is entitled to prevent the introduction of a new partner into the firm without his consent. (Section 31)
- (i) Every partner has a right to retire by giving notice where the partnership is at will. [Section 32(1)(c)]
- (j) Every partner has a right to continue in the partnership and not to be expelled from it. [Section 33(1)]
- (k) An incoming partner will not be liable for any debts or liabilities of the firm before he becomes a partner. [Section 31(2)] (l)
- (l) Every outgoing partner has a right to carry on a competitive business under certain conditions. (Section 36)

Q.8. Answer

Liability of an Outgoing or Retiring Partner

- An outgoing partner remains liable for the partnership debts contracted while he was a partner. He may, however, be discharged by novation, i.e., by an agreement between himself, the new firm and the creditors.
- He may also continue to be liable after retirement if he allows himself to be held out as a partner, e.g. by allowing his name to remain the firm name.
- To protect himself from his liability, he should give express notice of his retirement to the persons who were dealing with the firm before his retirement or give public notice in the manner as laid down in Section 72 of the Act, that is to say, by publishing it in the Official Gazette and in at least one vernacular newspaper where the firm carries on the business.

CHAPTER 4 - THE LIMITED LIABILITY PARTNERSHIP ACT, 2008

• BACKGROUND AND AIM OF THE ACT

- The Parliament passed the Limited Liability Partnership Bill on 12th December, 2008 and the President of India has assented the Bill on 7th January, 2009 and called as the Limited Liability Partnership Act, 2008, and many of its sections got enforced from **31st March 2009**.
- This Act have been enacted to make provisions for the formation and regulation of Limited Liability Partnerships and for matters connected there with or incidental thereto.
- The LLP Act, 2008 has **81 sections and 4 schedules**.
- The **First Schedule** deals with **mutual rights and duties of partners**, as well limited liability partnership and its partners where there is absence of formal agreement with respect to them.
- The **Second Schedule** deals with **conversion of a firm into LLP**.
- The **Third Schedule** deals with **conversion of a private company into LLP**.
- The **Fourth Schedule** deals with **conversion of unlisted public company into LLP**.
- The Ministry of Corporate Affairs (MCA) and the Registrar of Companies (ROC) are entrusted with the task of administrating the LLP Act, 2008.
- It is also to be noted that '**The Indian Partnership Act, 1932 is not applicable to LLPs**.'

• MEANING OF LLP

- A LLP is a new form of legal business entity with limited liability.
- The LLP is a separate legal entity and, while the LLP itself will be liable for the full extent of its assets, the liability of the partners will be limited.
- Since LLP contains elements of both 'a corporate structure' as well as 'a partnership firm structure' LLP is called a hybrid between a company and a partnership.

• CHARACTERISTICS OF LLP

Following are the characteristics of a LLP:

1. **LLP is a body corporate**
2. **Perpetual Succession**
3. **Separate Legal Entity**
4. **No mutual Agency**
5. **LLP Agreement:** The LLP Act, 2008 provides flexibility to partner to devise the agreement as per their choice. In the absence of any such agreement, the mutual rights and duties shall be governed by the provisions of the LLP Act, 2008.
6. **Artificial Legal Person**
7. **Common Seal:** It is not mandatory for a LLP to have a common seal. It shall remain under the custody of some responsible official and it shall be affixed in the presence of at least 2 designated partners of the LLP.

8. **Limited Liability**
 9. **Management of Business:** The partners in the LLP are entitled to manage the business of LLP. But only the designated partners are responsible for legal compliances.
 10. **Minimum and Maximum number of Partners:** Every LLP shall have least two partners and shall also have at least 2 individuals as designated partners, of whom at least one shall be resident in India. There is no maximum limit on the partners in LLP.
 11. **Business for Profit Only**
 12. **Investigation:** The Central Government shall have powers to investigate the affairs of an LLP by appointment of competence authority for the purpose.
 13. **Compromise or Arrangement:** Any compromise or arrangement including merger and amalgamation of LLPs shall be in accordance with the provisions of the LLP Act, 2008.
 14. **Conversion into LLP:** A firm, private company or an unlisted public company would be allowed to be converted into LLP in accordance with the provisions of LLP Act, 2008.
 15. **E-Filing of Documents.**
 16. **Foreign LLPs:** Section 2(1)(m) defines foreign limited liability partnership "as a limited liability partnership formed, incorporated, or registered outside India which established a place of business within India". Foreign LLP can become a partner in an Indian LLP.
- **INCORPORATION OF LLP**
 - Essential elements to incorporate LLP - Under the LLP Act, 2008, the following elements are very essential to form a LLP in India:
 - (i) To complete and submit incorporation document in the form prescribed with the Registrar electronically;
 - (ii) To have at least two partners for incorporation of LLP [Individual or body corporate];
 - (iii) To have registered office in India to which all communications will be made and received;
 - (iv) To appoint minimum two individuals as designated partners who will be responsible for number of duties including doing of all acts, matters and things as are required to be done by the LLP. Atleast one of them should be resident in India.
 - (v) A person or nominee of body corporate intending to be appointed as designated partner of LLP should hold a Designated Partner Identification Number (DPIN) allotted by MCA.
 - (vi) To execute a partnership agreement between the partners inter se or between the LLP and its partners. In the absence of any agreement the provisions as set out in First Schedule of LLP Act, 2008 will be applied.
 - (vii) LLP Name.
 - Limited Liability Partnerships are bodies corporate and must be registered with the Registrar of LLP after following the provisions specified in the LLP Act, in a

similar way of setting up a company with distinct name. The LLP cannot have the same name with any other LLP, Partnership Firm or Company.

To create a LLP proper formation documents must be filed with the registrar along with the necessary filing fees.

➤ **Process:**

Deciding partners and designated partners



Obtaining DPIN and Digital Signature Certificate (DSC)



Checking the availability of names

The applicant has to file e-Form1, for ascertaining availability and reservation of the name of a LLP business (upto 6 choices can be indicated)



Drafting of LLP Agreement

Contents of LLP Agreements:

1. Name of LLP
2. Name & address of Partners & Designated Partners.
3. Form of contribution & interest on contribution
4. Profit sharing ratio
5. Remuneration of Partners
6. Rights & Duties of Partners
7. Proposed Business
8. Rules for governing LLP.



Electronic filing of some documents

After reserving a name, user has to file e-Form2 for incorporating a new LLP. e-Form2 contains the details of LLP proposed to be incorporated, partners and designated partners details and consent of the partners and designated partners to act as and designated partners



Issuing Certificate of Incorporation along with LLPIN (Limited Liability Partnership Identification Number)

- Execution of LLP Agreement is mandatory as per Section 23 of the Act. LLP Agreement is required to be filed with the registrar in e-Form3 within 30 days of incorporation of LLP

• **DISTINCTION BETWEEN LLP AND PARTNERSHIP**

	Basis	LLP	Partnership firm
1.	Regulating Act	The Limited Liability Partnership Act, 2008.	The Indian Partnership Act, 1932.
2.	Body corporate	It is a body corporate.	It is not a body corporate.
3.	Separate legal entity	It is a legal entity separate from its members.	It is a group of persons with no separate legal entity.
4.	Creation	It is created by a legal process called registration under the LLP Act, 2008.	It is created by an agreement between the partners.
5.	Registration	Registration is mandatory. LLP can sue and be sued in its own name.	Registration is voluntary. Only the registered partnership firm can sue the partners and outsiders
6.	Perpetual succession	The death, insanity, Retirement or insolvency of the partner(s) does not affect its existence of LLP. Members may join or leave But its existence continues	The death, insanity retirement or insolvency of the partner(s) may affect its existence. It has no perpetual succession.
7.	Name	Name of the LLP to contain the word limited liability partners (LLP) as suffix.	No guidelines. The partners can have any name as per their choice.
8.	Liability	Liability of each partner limited to the extent to agreed contribution except in case of willful fraud.	Liability of each partner is unlimited. It can be extended upto the personal assets of the partners.
9.	Mutual agency	Each partner can bind the LLP by his own acts but not the other partners.	Each partner can bind the firm as well as other partners by his own acts.
10.	Designated partners	At least two designated partners and atleast one of them shall be resident in India	There is no provision for such partners under the Indian partnership Act, 1932.
11.	Common seal	It may have its common seal as its official signatures.	There is no such concept in partnership
12.	Legal compliances	Only designated partners are responsible for all the compliances and penalties under this Act.	All partners are responsible for all the compliances and penalties under the Act.
13.	Annual filing documents	LLP is required to file: (a) Annual statement of accounts (b) Statement of solvency (c) Annual return with the registration of LLP every year.	Partnership firm is not required to file any annual document with the registrar of firms.
14.	Foreign partnership	Foreign nationals can become a partner in a LLP.	Foreign nationals cannot become a partner in a Partnership firm.
15.	Minor as partner	Minor cannot be admitted to the benefits of LLP.	Minor can be admitted to the Benefits of the partnership with the prior consent of the existing partners.

- DISTINCTION BETWEEN LLP AND LIMITED LIABILITY COMPANY (LLC)**

	Basis	LLP	LLC
1.	Regulating Act	The LLP Act, 2008.	The Companies Act, 2013.
2.	Members / Partners	The persons who contribute to LLP are known as partners of the LLP.	The persons who invest the money in the shares are known as members of the company.
3.	Internal governance structure	The internal governance structure of a LLP is governed by agreement between the partners.	The internal governance structure of a company is regulated by statute (i.e., Companies Act, 2013).
4.	Name	Name of the LLP to contain the word "Limited liability partnership" or "LLP" as suffix.	Name of the public company to contain the word "limited" and Private company to contain the word "Private limited"
5.	Number of members/ partners	Minimum - 2 members Maximum - No such limit on the members in the Act. The members of the LLP can be individuals/or body corporate through the nominees.	Private company: Minimum - 2 members Maximum - 200 members Public company: Minimum - 7 members Maximum - No such limit on the members.
6.	Liability of members/ partners	Liability of a partners is limited to the extent of agreed contribution except in case of wilful fraud.	Liability of a member is limited to the amount unpaid on the shares held by them.
7.	Management	The business of the company managed by the partners including the designated partners authorized in the agreement.	The affairs of the company are managed by board of directors elected shareholders.
8.	Minimum number of directors/ partners	Minimum 2 partners.	Private Co. - 2 directors Public Co. - 3 directors

-
1. What are the Advantages of LLP? **(6 MARKS)**
 2. What are the disqualifications of a designated partner? **(6 MARKS)**
 3. Difference between LLP and private limited company? **(8 MARKS)**
 4. Briefly define the nature and characteristics of LLP **(6 MARKS)**
 5. Explain the procedure to register a limited liability partnership **(8 MARKS)**
 6. Is change of name of a LLP is allow? If so then what are the procedure? **(6 MARKS)**

ANSWERS

Q.1. Answer:

1. Easy to form – forming an LLP is an easy process. it is less complicated and time consuming unlike the process of formation of a company.
2. Liability – the partners of the LLP is having limited liability which means partners are not liable to pay the debts of the company from their person assets. No partner is responsible for any other partner's misconduct
3. Perpetual succession – the life of the limited liability partnership is not affected by death, retirement or insolvency of the partner. The LLP will get wound up only as per provisions of the LLP act
4. Management of the company – an LLP has partners, who own and manage the business. This is different from a private limited company, whose directors may be different from shareholders.
5. Easy transferability of ownership – there is no restriction upon joining and leaving the LLP. It is easy to admit as a partner and to leave the firm or to easily transfer the ownership to others
6. Taxation – an LLP is not subject to dividend distribution tax (DDT). Distributed profits in the hands of the partners is not taxable. For income tax purposes, LLP is treated on par with partnership firms.
7. No compulsory audit required – every business has to appoint an auditor for checking the internal management of the company and its accounts. However, in the case of LLP, there is no mandatory audit required. The audit is required only in those cases where the turnover of the company exceeds Rs.40 lakhs and where the contribution exceeds Rs.25 lakhs
8. Fewer compliance requirements – an LLP is much easier and cheaper to run than a private limited company as there are just three compliances per year. On the other hand, a private limited company has a lot of compliances to fulfill and has to compulsorily conduct an audit of its books of accounts
9. Flexible agreement – the partners are free to draft the agreement as they please, with regard to their rights and duties
10. Easy to wind-up – not only is it easy to start, it is also easier to wind up an LLP, as compared to a private limited company

Q.2. Answer

Disqualification of a designated partner if he –

- a) Has at any time within the preceding five years been adjudged insolvent; or
- b) suspends, or has at any time within the preceding live years suspended payment to his creditors and has not at any time within the preceding five years made, a composition with them
- c) has been convicted by a Tribunal for any offence involving moral turpitude and sentenced in respect thereof to imprisonment for not less than six months; or
- d) has been convicted by a Tribunal for an offence involving section 30 of the act. (Section 30 deals with punishment for carrying out acts by the LLP or its partners with intent to defraud its creditors or for a fraudulent purpose)

Q.3. Answer

Particular	LLP	Private Limited Company
Registration under law	Registration under Limited liability partnership act 2008 is mandatory	Registration under companies act 2013 is mandatory
Proof of registration	Certificate of incorporation issued by registrar of companies	Certificate of incorporation issued by registrar of companies
Name	Name to end with "LLP" Limited Liability Partnership	Name of a public company to end with the word "Limited" and a private company with the words "private limited"
Capital contribution	Not specified in the law	Private company should have a minimum authorize capital of Rs.1 lakh and Rs.5 lakh for a public limited company. however, there is no requirement of paid up capital
Liability of shareholders / partners	Partners liability is limited to the extent of the contribution to the LLP	Shareholders liability is limited to the extent of the unpaid capital
No. of shareholders / partners	Minimum Of 2 no maximum limit	Private limited – minimum 2 shareholder and maximum of 200 shareholders. Public limited – minimum 2 shareholder and no upper limit of shareholders
Foreign nationals as shareholder / partner	Foreign nationals can be partners	Foreign nationals can be shareholders

Q.4. Answer – following are the features of a LLP

- a. LLP is a body corporate with distinct legal entity and perpetual succession
- b. LLP is applicable to any trade or business
- c. LLP is created and registered under limited liability partnership act, 2008
- d. LLP can be created by minimum 2 partners
- e. LLP act is administered by ministry o corporate affairs
- f. For registration, incorporation document is required to be filed to registrar of companies
- g. Every partner is the agent of the LLP
- h. Liability of partner is limited except in case of fraud and negligence
- i. Any person can become partner / member by subscribing to the incorporation document or by an agreement with existing partners / members
- j. Right and duties of partners are governed by an agreement between partners or between LLP and its partners

Q.5. Answer

Step 1 – digital signature certificate (DSC)

Before initiating the process of registration, you must apply for the digital signature of the designated partners of the proposed LLP. This is because all the documents for LLP are filed online and are required to be digitally signed.

Step 2 – director identification number (DIN)

You have to apply for the DIN of all the designated partners or those intending to be designated partner of the proposed LLP

Step 3 – reservation of name

Form 1 is filed for the reservation of name of proposed LLP, but before quoting the name in the form, it is recommended that you use the free name search facility on MCA portal. The system will provide the list of closely resembling names of existing companies / LLPs based on the search criteria filled up. This will help you in choosing names not similar to already existing names. You need to provide six names in the order of preference in form 1.

Step 4 – incorporation of LLP

Form 2 is the application form for the incorporation of the LLP. You must keep in mind many important points while filing form 2

Step 5 – file limited liability partnership agreement

LLP agreement governs the mutual rights and duties amongst the partners and also between the LLP and its partners

LLP agreement must be filed in form 3 online on MCA portal

Form 3 for LLP agreement has to be filed within 30 days of the date of incorporation

The LLP agreement has to be printed on stamp paper. The value of stamp paper is different for every state.

Steps to form a limited liability partnership

Step 1 – obtain DSC

Step 2 – Apply for DIN

Step 3 – name approval

Step 4 – incorporation of LLP

Step 5 – file LLP agreement

Q.6. Answer

The procedure for the name change is governed by provisions of section 19 of the limited liability partnership act, 2008. A limited liability partnership (LLP) that is registered in India may, under certain circumstances, need to change its name

The reasons can be business related or on account of certain directives from the central government (if the name of the LLP is considered undesirable or similar to an already existing LLP, the government can ask for a name change and failure to comply with the directives could attract a penalty of up to Rs.5 lakhs for the business and up to Rs.1 lakh for each partner)

An application for changing the name of the LLP should be, first submitted to the ministry of corporate affairs. The application must have maximum six name preferences.

One must ensure that the preferences are in tandem with the LLP naming guidelines that have been laid out in India. You can also check out the availability of a name on the MCA portal and then finalize a name.

CHAPTER 5 - THE COMPANIES ACT, 2013

- **BACKGROUND AND AIM OF THE ACT**

- It came into existence at once from the date of notification in the Official Gazette i.e., from **30th August, 2013**, however, the remaining provisions of the Act shall come into force on such date as the Central Government may specify. It extends to the **whole of India**.
- Structure of the Act: The Companies Act, 2013 has 470 Sections (covered in 29 Chapters) and 7 Schedules as against 658 Sections (covered in 13 Parts) and 15 Schedules of the Companies Act, 1956.

- **MEANING OF COMPANY**

The word '**company**' is derived from the Latin words (**com= with or together; and panis = bread or meal**); and originally referred to an association of persons who took their meals together.

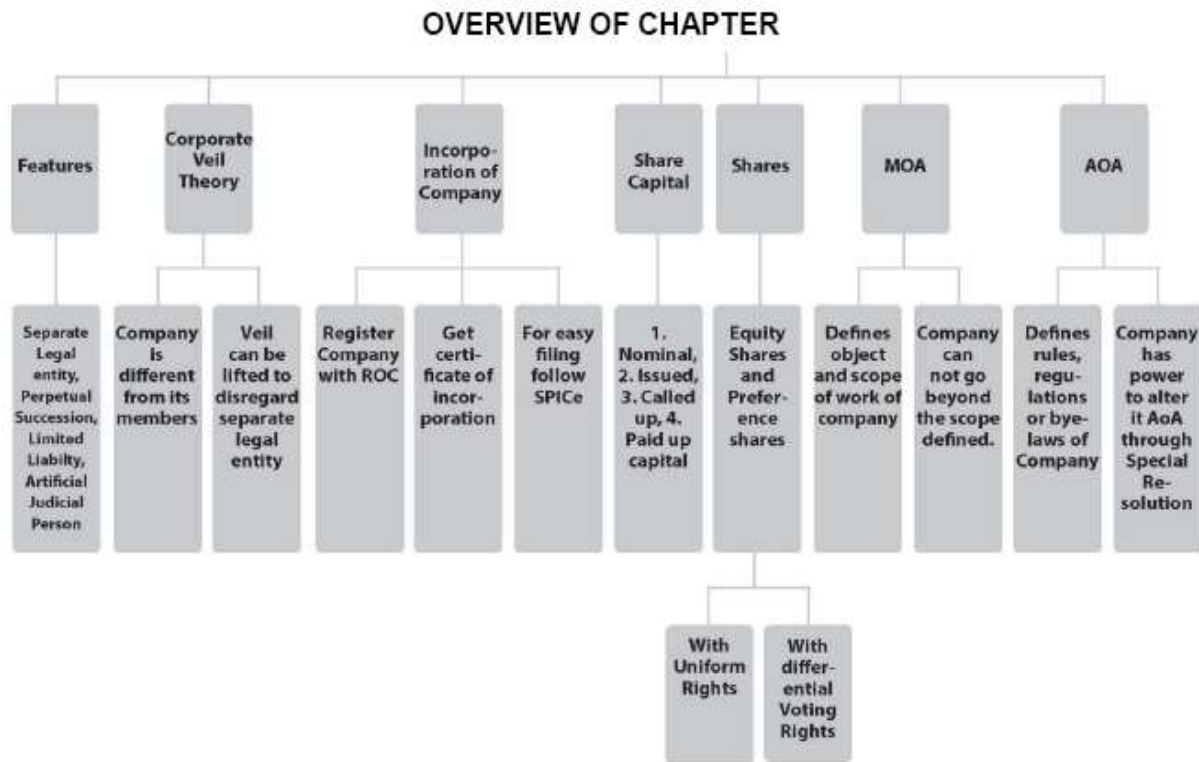
- **DEFINITION OF COMPANY**

The term '**company**' has been defined under Section 2(20) of the Companies Act, 2013. As per this, '**company**' means a company incorporated under Companies Act, 2013 or under any of the previous laws relating to companies.

- **ACT APPLICABLE TO:**

The provisions of this Act shall apply to-

1. Companies incorporated under this Act or under any previous company law.
2. Insurance companies, except in so far as the said provisions are inconsistent with the provisions of the Insurance Act, 1938 or the Insurance Regulatory and Development Authority Act, 1999;
3. Banking companies, except in so far as the said provisions are inconsistent with the provisions of the Banking Regulation Act, 1949;
4. Companies engaged in the generation or supply of electricity, except in so far as the said provisions are inconsistent with the provisions of the Electricity Act, 2003;
5. Any other company governed by any special Act for the time being in force, except in so far as the said provisions are inconsistent with the provisions of such special Act, and
6. Such body corporate, incorporated by any Act for the time being in force, as the Central Government may, by notification, specify in this behalf, subject to such exceptions, modifications or adaptation, as may be specified in the notification. Example: Food Corporation of India (FCI), National Highway Authority of India (NHAI) etc.



• **CHARACTERISTICS OF COMPANY**

Following are the characteristics of a company:

1. Separate legal entity
Case law: Salomon v. Salomon & Co. Ltd.
2. Limited liability
3. Perpetual Succession
4. Separate Property
Case law: Macaura vs. Northern Assurance Co. Ltd.
5. Transferability of Shares
6. Common Seal:

The Companies (Amendment) Act, 2015 has made the common seal optional **This amendment provides that the documents which need to be authenticated by a common seal will be required to be so done, only if the company opts to have a common seal. In case a company does not have a common seal, the authorization shall be made by two directors or by a director and the Company Secretary, wherever the company has appointed a Company Secretary.**

7. Capacity to sue and be sued
8. Separate Management
9. Voluntary Association for Profit

• **IS COMPANY A CITIZEN?**

Although, a company is regarded as a legal person (though artificial), it is not a citizen either under the Constitution of India or the Citizenship Act, 1955.

• **HAS COMPANY A NATIONALITY AND RESIDENCE?**

It is established through judicial decisions that a company cannot be a citizen, yet it has nationality, domicile and residence.

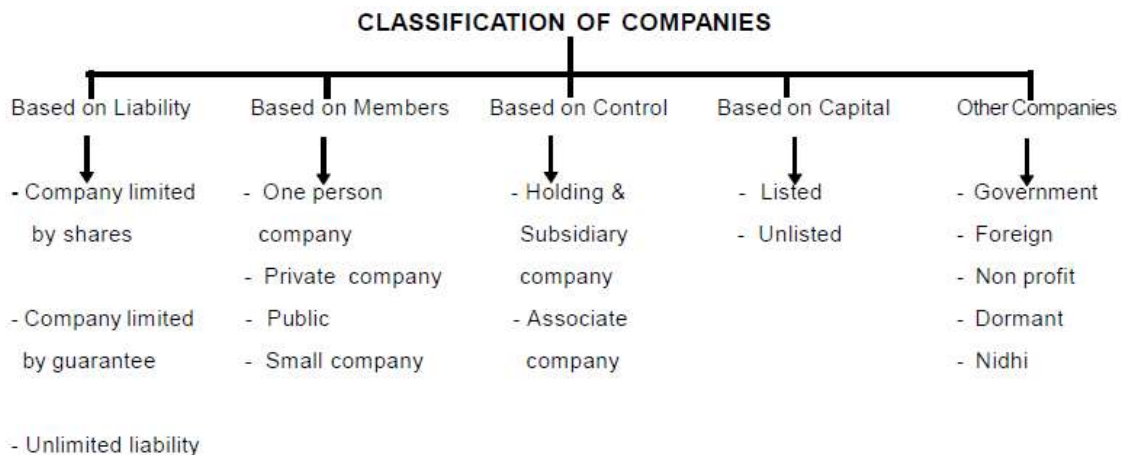
• **LIFTING OR PIERCING THE CORPORATE VEIL**

- **Corporate veil:** It refers to a separate legal existence enjoyed by the company which is distinct from people who own & manage it. It is an artificial curtain created by law which separates the company from the people who own and manage it.
- **Effect of corporate veil:** Only company is liable for the acts/defaults done in name of company, even though directors/employees acted on behalf of company.
- **Lifting of corporate veil:** It means looking behind the company as a legal person, i.e., disregarding the corporate entity and paying regard, instead, to the realities behind the legal facade. Only in appropriate circumstances, the **Courts shall lift the corporate veil.**

The following are the cases where company law disregards the principle of corporate personality or the principle that the company is a legal entity distinct and separate from its shareholders or members:

1. **Where the device of incorporation is adopted for some illegal or improper purpose, e.g., to defeat law, to defraud creditors or to avoid legal obligations.**
Case law: *Gilford Motor Co. v. Homes*
2. **For determining residence and character :** The Courts also look behind the facade of the company and its place of registration in order to determine its residence for the purposes of taxation or the character of the company, for example whether it is enemy.
Case law: *Daimler Co. Ltd. vs. Continental Tyre & Rubber Co.*
3. **Formation of Companies to divide income and avoid tax or avoid any welfare laws:**
Case law: (i) *Sir Dinshaw Maneckjee Petit*
(ii) *Workmen employed in Associated Rubber Industries Ltd v. Associated Rubber Industries Ltd*
4. **Where companies form other companies as their subsidiaries to act as their agent.**
Case law: *Merchandise Transport Limited vs. British Transport Commission*

CLASSIFICATION OF COMPANY



A. BASED ON LIABILITY

1. **Company limited by shares:** As per Section 2(22), A company limited by shares is a registered company having the liability of its members limited to the amount, if any, unpaid on the shares respectively held by them. If his shares are fully paid - up, he has nothing more to pay.

2. **Company limited by guarantee:**
 - As per Section 2(21), a company limited by guarantee or a "guarantee company" is a company having the liability of its members limited to such an amount as the members may respectively thereby undertake, by the memorandum of association of the company, to contribute to the assets of the company.
 - The liability of members to pay their guaranteed amounts arises only when the company has gone into liquidation and not when it is a going concern.
 - Clubs, trade associations and societies for promoting different objects are examples of companies limited by guarantee.
 - If a guarantee company has share capital, the shareholders have two-fold liability; to pay the amount which remains unpaid on their share whenever called upon to pay, and secondly, to pay the amount payable under the guarantee when the company goes into liquidation.

3. **Unlimited Company:**
 - As per Section 2(92), unlimited company is a company not having any limit on the liability of its members. In such a company the liability of a member ceases when he ceases to be a member.
 - The members of an unlimited company are not liable directly to the creditors of the company, unlike in the case of partners of a firm. The liability of the members is only towards the company, so long it is a going concern; and in the event of its being wound up, only the Liquidator can ask the members to contribute to the assets of the company.

B. BASED ON MEMBERS**1. Private Company:**

- As per Section 2(68), private company is a company which by its articles,—
 - (i) restricts the right to transfer its shares;
 - (ii) limits the number of its members to two hundred (except in case of One Person Company):

The clause provides that where two or more persons hold one or more shares in a company jointly, they shall be treated as a single member:
However following shall not be included in the number of members:

 - ◆ Employees
 - ◆ Past employees
 - (iii) prohibits any invitation to the public to subscribe for any securities of the company.

- There should be at least two persons to form a private company i.e., the minimum no. of members in a private company is two. A private company should have at least two directors. The name of a private limited company must end with the words "Private Limited".

2. Public Company:

- As per Section 2(71), public company is a company which-
 - ◆ is not a private company
 - ◆ Seven or more members are required to form the company.
 - ◆ a private company which is a subsidiary of a public company shall also be deemed to be a public company for the purposes of this Act, even where such subsidiary company continues to be a private company in its articles (three restrictions).
- There should be at least seven persons to form a public company i.e., the minimum no. of members in a public company is seven. A public company should have at least three directors. The name of a public limited company must end with the word "Limited".

3. One Person Company:

- **Definition:** As per Section 2(62), one person company is a company which-

One Person Company' means a company which has only one person as a member.

It is basically a private company with some unique features.

As regards the name of a One Person Company, the Act provides that the words "One Person Company" or 'OPC' shall be mentioned in brackets below the name of such Company, wherever its name is printed, affixed or engraved.
- **Important points:**
 - ◆ Only one person as member.
 - ◆ Minimum paid up capital - no limit prescribed.
 - ◆ The memorandum of OPC shall indicate the name of the other person, who shall, in the event of the subscriber's death or his incapacity to contract, become the member of the company.
 - ◆ The other person whose name is given in the memorandum shall give his prior written consent in prescribed form and the same shall be filed with Registrar of companies at the time of incorporation.
 - ◆ Such other person may be given the right to withdraw his consent.
 - ◆ The member of OPC may at any time change the name of such other person by giving notice to the company and the company shall intimate the same to the Registrar.
 - ◆ Only a natural person who is an Indian citizen and resident in India (person who has stayed in India for a period of not less than 182 days during the immediately preceding one calendar year)-
 - shall be eligible to incorporate a OPC;
 - shall be a nominee for the sole member of a OPC.
 - ◆ No person shall be eligible to incorporate more than one OPC or become nominee in more than one such company.
 - ◆ No minor shall become member or nominee of the OPC or can hold share with beneficial interest.

- ◆ Such Company cannot be incorporated or converted into a company under section 8 of the Act. Though it may be converted to private or public companies in certain cases.
- ◆ Such Company cannot carry out Non-Banking Financial Investment activities including investment in securities of anybody corporate.
- ◆ OPC cannot convert voluntarily into any kind of company unless two years have expired from the date of incorporation, except where the paid up share capital is increased beyond fifty lakh rupees or its average annual turnover during the relevant period exceeds two crore rupees.

4. Small Company:

- **Definition:** As per Section 2(85), small company means a company, **other than a public company,-**
 - (i) paid-up share capital of which **does not exceed fifty lakh rupees** or such higher amount as may be prescribed which shall not be more than five crore rupees;
 - and
 - (ii) turnover of which as per its last profit and loss account **does not exceed two crore rupees** or such higher amount as may be prescribed which shall not be more than twenty crore rupees:
 - **Provided that nothing in this clause shall apply to--**
 - (i) a holding company or a subsidiary company;
 - (ii) a company registered under section 8; or
 - (iii) a company or body corporate governed by any special Act.
- It is basically a private company meeting prescribed threshold.

C. BASED ON CONTROL

1. Holding & Subsidiary Company

A company is a holding company in relation to one or more other companies, means a company of which such companies are subsidiary companies.

[Section 2(46)]

Whereas section 2(87) defines "subsidiary company" in relation to any other company (that is to say the holding company), means a company in which the holding company—

- (i) controls the composition of the Board of Directors; or
- (ii) exercises or controls more than one-half of the total share capital either at its own or together with one or more of its subsidiary companies
- (iii) Subsidiary's subsidiary.

For the purposes of this section —

- (I) a company shall be deemed to be a subsidiary company of the holding company even if the control referred to in sub-clause (i) or sub-clause (ii) is of another subsidiary company of the holding company;
- (II) the composition of a company's Board of Directors shall be deemed to be controlled by another company if that other company by exercise of some power exercisable by it at its discretion can appoint or remove all or a majority of the directors;

2. Associate company

- As per Section 2(6), In relation to another company, means a company in which that other company has a significant influence, but which is not a subsidiary company of the company having such influence and includes a joint venture company.
- The term “significant influence” means control of at least 20% of total share capital, or of business decisions under an agreement

D. BASED ON CAPITAL**1. Listed company:**

As per the definition given in the section 2(52), it is a company which has any of its securities listed on any recognised stock exchange.

2. Unlisted company: Means a company other than listed company.**E. OTHER COMPANIES****1. Government Company**

- As per Section 2(45), government company means any company in which not less than fifty- one per cent. of the paid-up share capital is held by-
 - (i) the Central Government, or
 - (ii) by any State Government or Governments, or
 - (iii) partly by the Central Government and partly by one or more State Governments,
- And the section includes a company which is a subsidiary company of such a Government company;

2. Foreign Company

As per Section 2(42), foreign company means any company or body corporate incorporated outside India which-

- (i) has a place of business in India whether by itself or through an agent, physically or through electronic mode; and
- (ii) conducts any business activity in India in any other manner

3. Company not for profit/Non-Profit companies

- **Object of formation of Section 8 Company:** Section 8 of the Companies Act, 2013 deals with the formation of companies which are formed to promote the charitable objects of commerce, art, science, sports, education, research, social welfare, religion, charity, protection of environment etc.
- **Restrictions on such company:**
 - (i) Such company is prohibited from declaring any dividend to its members
 - (ii) Such company has to apply its surplus only in promoting its objects
- **Power of Central government to issue the license-**

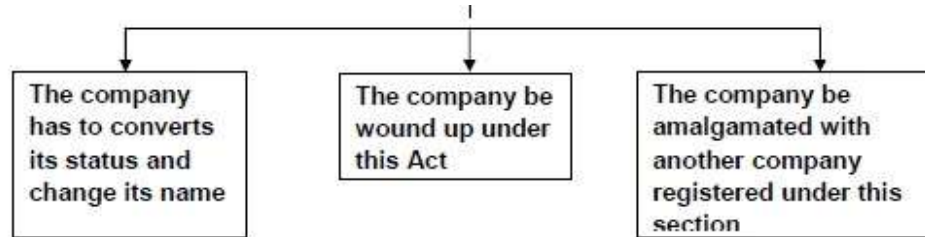
Section 8 allows the Central Government to register such person or association of persons as a company with limited liability without the addition of words 'Limited' or 'Private limited' to its name, by issuing licence on such conditions as it deems fit. The registrar shall on application register such person or association of persons as a company under this section

On registration the company shall enjoy same privileges and obligations as of a limited company.
- **Privileges of Limited Company:** On registration the company shall enjoy same privileges and obligations as of a limited company.
- **Revocation of license:** The Central Government may by order revoke the licence of the company where the company contravenes any of the requirements or the conditions of this section.

But before such revocation, the Central Government must give it a written notice of its intention to revoke the licence and opportunity to be heard in the matter.

➤ **Order of the Central Government:**

Where a licence is revoked, the Central Government may, by order, if it is satisfied that it is essential in the public interest, direct that:



4. Dormant company:

- Where a company is formed and registered under this Act for a future project or to hold an asset or intellectual property and has no significant accounting transaction, such a company or an inactive company may make an application to the Registrar in such manner as may be prescribed for obtaining the status of a dormant company.
- "Significant accounting transaction" means any transaction other than—
 - (i) payment of fees by a company to the Registrar;
 - (ii) payments made by it to fulfil the requirements of this Act or any other law;
 - (iii) allotment of shares to fulfil the requirements of this Act; and
 - (iv) payments for maintenance of its office and records.

5. Nidhicompany:

As per Section 406, a company which has been incorporated as a nidhi with the object of cultivating the habit of thrift (cost cutting) and savings amongst its members, receiving deposits from, and lending to, its members only, for their mutual benefits and which complies with such rules as are prescribed by the Central Government for regulation of such class of companies.

6. Public financial institutions

As per Section 2(72), following institutions are to be regarded as public financial institutions.

- (i) the Life Insurance Corporation of India, established under the Life Insurance Corporation Act, 1956;
- (ii) the Infrastructure Development Finance Company Limited,
- (iii) specified company referred to in the Unit Trust of India (Transfer of Undertaking and Repeal) Act, 2002;
- (iv) institutions notified by the Central Government under section 4A(2) of the Companies Act, 1956 so repealed under section 465 of this Act;
- (v) such other institution as may be notified by the Central Government in consultation with the Reserve Bank of India:

Provided that no institution shall be so notified unless—

- (A) it has been established or constituted by or under any Central or State Act; or
- (B) not less than fifty-one per cent of the paid-up share capital is held or

Governments or partly by the Central Government and partly by one or more State Governments.

- **MODE OF REGISTRATION/ INCORPORATION OF COMPANY**

PROMOTERS: Persons who form the company are known as promoters. It is they who conceive the idea of forming the company. They take all necessary steps for its registration. It should, however, be noted that persons acting only in a professional capacity e.g., the solicitor, banker, accountant etc. are not regarded as promoters.

The Companies Act, 2013 defines the term "Promoter" under section 2(69) which means a person—

- (a) who has been named as such in a prospectus or is identified by the company in the annual return referred to in section 92; or
- (b) who has control over the affairs of the company, directly or indirectly whether as a shareholder, director or otherwise; or
- (c) in accordance with whose advice, directions or instructions the Board of Directors of the company is accustomed to act.

- **INCORPORATION OF COMPANIES**

[SECTION 7 READ WITH COMPANIES (INCORPORATION) RULES, 2014]

Following is the procedure, in brief, for the incorporation of a company:-

- I. **Selection of the type of company:** The promoters of a company may however select the type of a company as they wish to form themselves into viz, One person company, private company, public company, non-profit company, etc.
- II. **Preliminary Requirements:**
All the directors of the proposed company must ensure that they are having Director's Identification Number (DIN). Out of all the directors of the proposed company, at least one director should have digital signature to digitally sign the incorporation and other related documents.
- III. **Reservation of Name:**
Any of the promoters should apply to the Registrar of Companies (ROC) regarding the reservation of name.
- IV. **Preparation of the Memorandum of Association and Articles of Association:**
Drafting of the MOA and AOA is generally a step subsequent to the reservation of name made by the Registrar. MOA and AOA shall be in the respective forms as specified in Schedule -1..
- V. **Filing of the documents with the Registrar of Companies:**
An application shall be filed, with the Registrar of Companies within whose jurisdiction the registered office of the company is proposed to be situated, in **Form No. INC.2 (for One Person Company)** along with the following documents, along with the fees for registration of a company, within 20 days from the date of intimation regarding the reservation of name :-
 - (i) **The memorandum and articles of the company** duly signed by all the subscribers to the memorandum;

- (ii) **A declaration by an advocate or chartered accountant or cost accountant or company secretary in practice**, that all the requirements of this Act and the rules made there under in respect of registration have been complied with;
- (iii) An **declaration in Form INC-9** by each of the subscribers to the Memorandum and by all the persons named as the first directors, if any, in the articles that they are not convicted of any offence in last 5 years.
- (iv) The **address for correspondence** till its registered office is established;
- (v) **Certain prescribed particulars of every subscriber** to the memorandum along with proof of identity;
- (vi) The **particulars of the interests of the persons** mentioned in the articles as the first directors of the company in other firms
- (vii) **Verification of the location of the registered office.**

VI. Certificate of Incorporation and allotment of Corporate Identity Number:

If the Registrar of Companies is satisfied that everything has been complied with in regard to incorporation of companies, he shall issue a certificate of incorporation in Form No. INC.11, normally within 7 days of the receipt of documents, to the company signed & dated under his hand.

VII. Effect of Registration [Sec. 9]:

Section 9 provides that from the date of incorporation, the subscribers become the members of the company. The company shall be a body corporate with a name, capable of exercising all the functions of an incorporated company under this Act.

VIII. Commencement of Business [Sec. 11]:

A company (both public and private) having a share capital shall not commence any business or exercise any borrowing powers, unless the following documents are filed with the ROC:

- (i) a declaration by a director in the prescribed form that every subscriber to the memorandum has paid the value of shares taken by him (minimum five lakh rupees for public company and minimum one lakh rupees for private company); and
- (ii) The verification of its registered office.

Where no declaration has been filed with the Registrar within a period of 180 days of the date of incorporation of the company and the Registrar has reasonable cause to believe that the company is not carrying on business or operations, he may remove the name of the company from the register of companies.

Order of the Tribunal :

Where a company has been got incorporated by furnishing false or incorrect information or representation or by suppressing any material fact or information in any of the documents or declaration filed or made for incorporating such company or by any fraudulent action, the Tribunal may, on an application made to it, on being satisfied that the situation so warrants,—

- (a) pass such orders, as it may think fit, for regulation of the management of the company including changes, if any, in its memorandum and articles, in public interest or in the interest of the company and its members and creditors; or
- (b) direct that liability of the members shall be unlimited; or
- (c) direct removal of the name of the company from the register of companies; or

- (d) pass an order for the winding up of the company; or
- (e) pass such other orders as it may deem fit:

Provided that before making any order,—

- ◆ the company shall be given a reasonable opportunity of being heard in the matter; and
- ◆ the Tribunal shall take into consideration the transactions entered into by the company, including the obligations, if any, contracted or payment of any liability.

- **SIMPLIFIED PROFORMA FOR INCORPORATING COMPANY ELECTRONICALLY (SPICe)**

The Ministry of Corporate Affairs has taken various initiatives for ease of business. MCA has simplified the process of filing of forms of incorporation of company through Simplified Proforma For Incorporating Company ELECTRONICALLY (SPICe)

- **MEMORANDUM OF ASSOCIATION**
“Fundamental Document”

➤ Memorandum of Association is the fundamental condition upon which alone is allowed to incorporate.

<p>➤ Definition and Meaning of Memorandum: Section 2(56) of the Companies Act, 2013.</p>	<p>"memorandum" means memorandum of association of a company as originally framed or as altered from time to time in pursuance of any previous companies law or of this Act.</p>
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Memorandum of association is a document, which contains the fundamental provisions of the company's constitution. It defines as well as confines the powers of the company. It not only shows the objects of formation but also determines the utmost possible scope of its operations beyond which its action cannot go.

<p>Purpose of Memorandum:</p>	<p>The purpose of memorandum is two-fold.</p> <ol style="list-style-type: none"> 1. The Prospective shareholder who contemplates the investment of his savings, should know the field in, or the purpose for which it is going to be used and what risk he is taking in making the investment. 2. Outsiders or Creditors dealing with the company will know without reasonable doubt whether the contractual relation into which he contemplates entering with the company is one relating to a matter within its corporate objects.
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<p>Form of Memorandum [Section 4]:</p>	<ul style="list-style-type: none"> • Table A is applicable to companies limited by shares; • Table B is applicable to companies limited by guarantee and not having a share capital; • Table C is applicable to the companies limited by guarantee and having a share capital; • Table D is applicable to unlimited companies and not having a share capital; • Table E is applicable to unlimited companies and having a share capital.
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- The memorandum must be printed, divided into paragraphs, numbered consecutively, and signed by at least seven persons (two in the case of a private company and one in the case of One Person Company) in the presence of at least one witness, who will attest the signatures.
- The Memorandum of Association of a company cannot contain anything contrary to the provisions of the Companies Act. If it does, the same shall be devoid of any legal effect. Similarly, all other documents of the company must comply with the provisions of the Memorandum.
- **Contents of Memorandum:** Section 4 of the Companies Act provides that the memorandum of association of every company must contain the following clauses:-

1. Name clause	<ul style="list-style-type: none"> • The first clause in the memorandum must state the name by which a company is known. • The name of the company with the last word "Limited" in the case of a public limited company, or the last words "Private Limited" in the case of a private limited company. This clause is not applicable on the companies formed under section 8 of the Act. • The name including phrase 'Electoral Trust' may be allowed for Registration of companies to be formed under section 8 of the Act, in accordance with the Electoral Trusts Scheme, 2013 notified by the Central Board of Direct Taxes (CBDT). For the Companies under section 8 of the Act, the name shall include the words foundation, Forum, Association, Federation, Chambers, Confederation, council, Electoral trust and will constitute an offence under any law.
2. Situation or registered office clause	<ul style="list-style-type: none"> • The name of the State in which the registered office of the company is to be situated must be given in the memorandum. But the exact address of the registered office is not required to be stated therein.
3. Object clause	<ul style="list-style-type: none"> • The objects for which the company is proposed to be incorporated and any matter considered necessary in furtherance thereof; • If any company has changed its activities which are not reflected in its name, it shall change its name in line with its activities within a period of six months from the change of activities after complying with all the provisions as applicable to change of name.
4. Liability Clause:	<p>The liability of members of the company, whether limited or unlimited, and also state,—</p> <ul style="list-style-type: none"> • in the case of a company limited by shares, that the liability of its members is limited to the amount unpaid, if any, on the shares held by them; and • in the case of a company limited by guarantee, the amount up to which each member undertakes to contribute.
5. Capital Clause (only in the case of a company having a share capital):	<p>The amount of authorized capital divided into share of fixed amounts and the number of shares with the subscribers to the memorandum have agreed to take, indicated opposite their names, which shall not be less than one share. A company not having share capital need not have this clause.</p>

6. Association Clause and Subscription:	In this clause, the persons (includes a body corporate) subscribing to the memorandum declare their desire to be formed into a company and agree to take the shares indicated opposite their respective names.
7. Succession Clause (only in the case of OPC):	This clause shall state the name of the person who, in the event of the death of the subscriber, shall become the member of the company.

The above clauses of the Memorandum are called compulsory clauses, or "Conditions". In addition to these a memorandum may contain other provisions, for example rights attached to various classes of shares.

- **ARTICLES OF ASSOCIATION**

Definition and Meaning of Articles Section 2(5) of the Companies Act, 2013	'articles' means the articles of association of a company as originally framed or as altered from time to time in pursuance of any previous companies law or of this Act.
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The articles of a company are its bye — laws or rules and regulations that govern the management of its internal affairs and the conduct of its business. The articles of a company are sub—ordinate to and are controlled by the memorandum of association..

Section 5 of the Companies Act, 2013 seeks to provide the contents and model of articles of association. The section lays the following law-

- (1) **Contains regulations:** The articles of a company shall contain the regulations for management of the company.
- (2) **Inclusion of matters:** The articles shall also contain such matters, as are prescribed under the rules. However, a company may also include such additional matters in its articles as may be considered necessary for its management.
- (3) **Contain provisions for entrenchment:** The articles may contain provisions for entrenchment (to protect something) to the effect that specified provisions of the articles may be altered only if conditions or procedures as that are more restrictive than those applicable in the case of a special resolution, are met or complied with.
- (4) **Manner of inclusion of the entrenchment provision:** The provisions for entrenchment shall only be made either on formation of a company, or by an amendment in the articles agreed to by all the members of the company in the case of a private company and by a special resolution in the case of a public company.
- (5) **Notice to the registrar of the entrenchment provision:** Where the articles contain provisions for entrenchment, whether made on formation or by amendment, the company shall give notice to the Registrar of such provisions in such form and manner as may be prescribed.
- (6) **Forms of articles:** The articles of a company shall be in respective forms specified in Tables, F, G, H, I and J in Schedule I as may be applicable to such company.
- (7) **Model articles:** A company may adopt all or any of the regulations contained in the model articles applicable to such company.
- (8) **Company registered after the commencement of this Act:** In case of any company, which is registered after the commencement of this Act, in so far as the registered articles of such company do not exclude or modify the regulations

contained in the model articles applicable to such company, those regulations shall, so far as applicable, be the regulations of that company in the same manner and to the extent as if they were contained in the duly registered articles of the company.

The following are the key differences between the Memorandum of Association vs. Articles of Association:

1. Objectives: Memorandum of Association defines and delimits the objectives of the company whereas the Articles of association lays down the rules and regulations for the internal management of the company. Articles determine how the objectives of the company are to be achieved.
2. Relationship: Memorandum defines the relationship of the company with the outside world and Articles define the relationship between the company and its members.
3. Alteration: Memorandum of association can be altered only under certain circumstances and in the manner provided for in the Act. In most cases permission of the Regional Director, or the Tribunal is required. The articles can be altered simply by passing a special resolution.
4. Ultra Vires: Acts done by the company beyond the scope of the memorandum are ultra-vires and void. These cannot be ratified even by the unanimous consent of all the shareholders. The acts ultra-vires the articles can be ratified by a special resolution of the shareholders, provided they are not beyond the provisions of the memorandum.

- **EFFECT OF MEMORANDUM AND ARTICLES:**

As per section 10 of the Companies Act, 2013, where the memorandum and articles when registered, shall bind the company and the members thereof to the same extent as if they respectively had been signed by the company and by each member, and an agreement to observe all the provisions of the memorandum and of the articles.

- **DOCTRINE OF ULTRA VIRES**

- The meaning of the term 'ultra vires' is 'beyond the powers of. Anything which is outside the specified objects and powers or not reasonably incidental to or necessary for the attainment of objects of the company is ultra vires the company and therefore is void-ab-initio.
- No rights and liabilities, on the part of the company, arise out of such transactions and it remains nullity even if every member assents to it.
- Consequently, an act, which is ultra vires the company, does not bind the company and neither the company nor the other contracting party can sue on it.
- An act which is ultra vires the company being void, cannot be ratified by the shareholders of the company. Sometimes, act which is ultra vires can be regularised by ratifying it subsequently. For instance, if the act is ultra vires the power of the directors, the shareholders can ratify it; if it is ultra vires the articles of the company, the company can alter the articles; if the act is within the power of the company but is done irregularly, shareholder can validate it.
- Case law: ***Ashbury Railway Carriage and Iron Company Limited v. Riche***

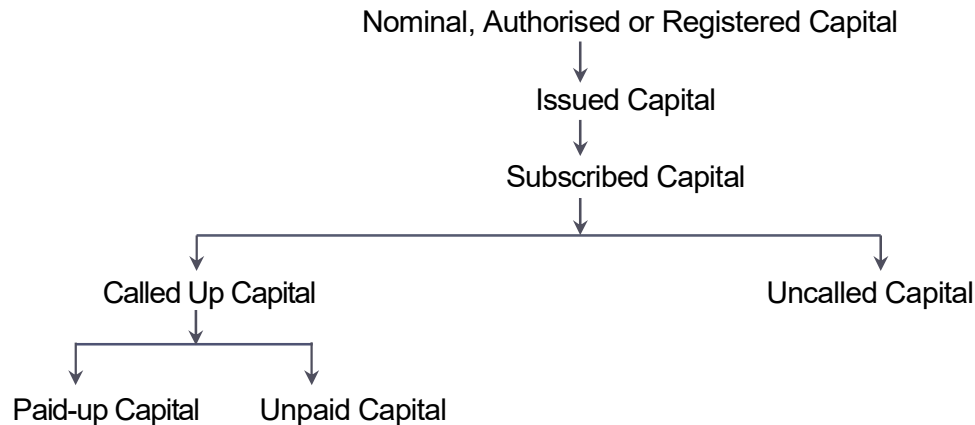
- **DOCTRINE OF CONSTRUCTIVE NOTICE**

- When the memorandum and articles of association of a company are registered, they become public documents and are open to inspection by anyone on payment of nominal fee. Hence, every person dealing with the company is under an obligation to know the contents of these documents.

- Whether a person reads the documents or not, he is presumed to have knowledge of the contents of the documents. He is not only presumed to have read the documents but also understood them in their true perspective, Thus, if a person enters into a contract which is beyond the powers of the company as defined in the memorandum, or outside the authority of directors as per memorandum or articles, he cannot acquire any rights under the contract against the company.
- **DOCTRINE OF INDOOR MANAGEMENT**
 - While persons dealing with a company are presumed to have read the public documents and understood their contents and ascertain that the transaction is not inconsistent therewith, they are entitled to assume that the PROVISIONS of the articles have been observed by the officers of the company. It is no part of the duty of an outsider to see how the company carries out its own internal proceedings or indoor management. He can assume that all is being done regularly.
 - The doctrine of indoor management, thus, imposes an important restriction on the scope of doctrine of constructive "notice. While the doctrine of "constructive notice" seeks to protect the company against the outsiders, the principle of indoor management operates to protect the outsiders against the company.
 - Case law: **The Royal British Bank vs. Turquand**
 - **Exceptions:** The doctrine of indoor management is subject to the following exceptions or limitations:-
 1. **Actual or constructive knowledge of irregularity:** The rule does not protect any person when the person dealing with the company has notice, whether actual or constructive, of the irregularity.
 2. **Suspicion of Irregularity:** Where the person dealing with the company is put upon an inquiry, for example, where the transaction is unusual or nothing the ordinary course of business, it is the duty of the outsider to make the necessary enquiry.
 3. **Forgery:** The doctrine of indoor management applies only to irregularities which might otherwise affect a transaction but it cannot apply to forgery which must be regarded as nullity.
- **SHARE**
 - **Definition and Meaning of Share:** Section 2(84) of the Companies Act, 2013 defines the term "share". As per this, share means a share in the share capital of a company and includes stock.
 - By its nature, a **share is not a sum of money but a bundle of rights and liabilities**. A share is a right to participate in the profits of a company, while it is a going concern and declares dividend; and a right to participate in the assets of the company, when it is wound up.
 - The shares or debentures or other interests of any member in a company shall be movable property transferable in the manner provided by the articles of the company [Section 44 of the Companies Act, 2013]. Every share in a company having a share capital, shall be distinguished by its distinctive number [Section 45]. This shall not apply to a share held by a person whose name is entered as holder of beneficial interest in such share in the records of a depository.

• **CLASSIFICATION OF SHARE CAPITAL**

The share capital of a company can be classified as :



- According to **Section 2(8)** “**authorised capital**” or “nominal capital” means such capital as is authorised by the memorandum of a company to be the maximum amount of share capital of the company.
- Whereas **Section 2(86)** “**subscribed capital**” means such part of the capital which is for the time being subscribed by the members of a company.
- As per **Section 2(15)** “**Called-up capital**” means such part of the capital, which has been called for payment.
- **Section 2(64)** defines “**paid-up share capital**” or “share capital paid-up” means such aggregate amount of money credited as paid-up as is equivalent to the amount received as paid-up in respect of shares issued and also includes any amount credited as paid-up in respect of shares of the company, but does not include any other amount received in respect of such shares, by whatever name called.

• **KINDS OF SHARE CAPITAL**

Preference Share

Equity Share

With voting rights

With differential rights as to dividend, voting or otherwise

(A) PREFERENCE SHARE

A preference share is a share which fulfils the following two conditions:

- ♦ It carries preferential right in respect of payment of dividend; and It also carries preferential right in regard to repayment of capital.
- ♦ In simple terms, preference share capital must have priority both regards to dividend as well as capital.

(B) EQUITY SHARE

- “**Equity share capital**” with reference to any company limited by shares, means all share capital which is not preference share capital;
- Equity share capital —
 - (1) with voting rights; or

- (2) with differential rights as to dividend, voting or otherwise in accordance with prescribed rules;
- **Example:** It is to be noted that, **Tata Motors in 2008 introduced equity shares with differential voting rights** called 'A' equity shares in its rights issue. In the issue, every 10 'A' equity shares carried only one voting right but would get 5 percentage points more dividend than that declared on each of the ordinary shares.
- Since 'A' equity share did not carry the similar voting rights, it was being traded at discount to other common shares having full voting. Other companies which have issued equity shares with differential voting rights (popularly called DVRs) are Future Retail, Jain Irrigation among others.

Q.1 Comment on the following (3 Marks each)

1. Corporate personality of a company is absolute in nature.
2. Small company and OPC can be a company limited by shares or by guarantee as well.
3. MOA serves as the charter of the company.
4. Doctrine of Indoor Management saves the company from outsiders.
5. Entrenchment provision in AOA is a bulwark against oppression.

Q.2 Define the following (2 Marks each)

1. Company
2. Government Company
3. Foreign Company
4. Private Company
5. Small company.

Q.3 Analyse the case laws (4 Marks each)

1. Mr. Raju wants to incorporate an OPC and make it a wholly owned subsidiary of his another company Avenue Ltd. The legal advisor consented to his decision. For a second opinion Raju approaches you. Being a CA advise.
2. Vijay advanced a debt to Anand Ltd without referring MOA which was silent as to the borrowing powers. Advise whether Vijay can claim repayment referring a case law.
3. Narang Ind. Ltd. has approached you for the following.
 - a. Can it make an IPO?
 - b. Can it have more than 200 Members?
 - c. Can the members of company transfer shares freely?
4. Members of a sec 8 co want the company to declare dividend as the company has surplus reserves. You are required to rectify or ratify their wants referring the provision of the Act.
5. Mr. and Mrs. Shetty the only directors as well as members of a company died in a car accident. Advise as to the status of the company.

Q.4 Answer any one of the following (5 Marks)

1. Certificate of Incorporation is a conclusive evidence of Incorporation of the company. Justify the statement
2. There were 2 Members in ABC Pvt. Ltd. One died leaving only 1 Member in the company. The sole Member undertook a contract in the name of the company. Advise as to the liability of the member on the contract.

Q.1 Comment on the following

(3 Marks each)

1. Corporate personality of a company is absolute in nature.

Ans. Corporate personality means that the company is a separate person in the eyes of law (Salomon vs. Salomon & Co. Ltd).

Generally this statement is a valid statement but in certain circumstances the courts dissolve the corporate personality of company. This phenomenon is known as Lifting of Corporate Veil. Hence, we can conclude that corporate personality of company is not absolute

2. Small company and OPC can be a company limited by shares or by guarantee as well.

Ans. As per the provisions of companies Act, 2013, a company can be Company Limited by share as well as guarantee. OPC is also a company features the same characteristics so we can conclude that the statement is right in law

3. MOA serves as the charter of the company.

Ans. As per section 2(56) Memorandum means the Memorandum of Association of the company as originally framed and as altered from time to time. It sets the constitution of the company upon which the company is formed.

It is the charter of the company which define its objects and powers. The company cannot exceed its MOA and if it exceeds the activity is void ab initio

4. Doctrine of Indoor Management saves the company from outsiders.

Ans. The doctrine if indoor management is an exception to the rule of constructive notice.

The outsider dealing with the companies are entitled to assume that as far as the internal proceedings of the company are concerned everything has been done regularly done. He is not required to do examine whether the internal proceedings have been complied with or not. They need not inquire into the regularity of the internal proceedings. The can presume that all is done regularly

Thus we can say that Doctrine of Indoor management saves the interest of outsiders against the company. (Royal British Bank vs. TURQUAND)

5. Entrenchment provision in AOA is a bulwark against oppression.

Ans. Article may contain provision for entrenchment (to protect something) to the effect that specified provision of the articles may be altered only if condition or procedures as that are more restrictive than those applicable in the case of special resolution are met

The provision for entrenchment shall only be made either on formation of company or by amendment in AOA agreed by all the members of private company and by special resolution in case of public company. Thus Entrenchment protects interest of Minority and stands a bulwark against their exploitation

Q.2 Define the following**(2 Marks each)**

1. **Company:** - Section 2 (20) of the 2013 Act defines the term “company” to mean “a Company incorporated under the Companies Act 2013 or any previous company law. The sub-section states that for the purposes of such definition, the expression company includes “Body corporate”.
2. **Government Company:** - A “Government Company” is defined under section 2(45) of the Companies Act, 2013 as “any company in which not less than 51% of the paid-up share capital is held by the central Government, or by any state government or Government, or partly by the central government and partly by one or more state governments, and includes a company which is a subsidiary company of such a government company”.
3. **Foreign Company:** - Section 2 (42) of the Companies Act, 2013 (the Act) defines foreign company (FC) as follows: Foreign Company means any company or body corporate incorporated outside India which, conducts any business activity in India in any other manner.
4. **Private Company:-** Section 2 (68) defines the private company the ‘private company’ means a company having a minimum paid-up share capital of one lakh rupees or such higher paid-up share capital as may be prescribed, and which by its articles -
 - (i) Restricts the right to transfer its shares.
 - (ii) Excepts in case of one Person Company, limits the number of its members to two hundred.

Provide that where two or more persons hold one or more shares in a company jointly, they shall, for the purposes of this clause, be treated as a single member:
Provide further that – (A) Persons who are in the employment of the company, and (B) Person who, having been formerly in the employment of the company, were members of the company while in that employment and have continued to be members after the employment ceased. Shall not be included in the number of members; and
 - (iii) Prohibits any invitation to the public to subscribe for any securities of the company.
5. **Small company:** - Section 2 (85) small companies as Companies Act 2013. Company can claim to be small company as per Act on fulfilling the following provisions: (1) Company should be private limited (2) Paid up capital should not be more than Rs. 50 lakh (3) Turnover should not exceed more than Rs. 2 Cr.

Q.3 Analyse the case laws**(4 Marks each)**

1. **Mr. Raju wants to incorporate an OPC and make it a wholly owned subsidiary of his another company Avenue Ltd. The legal advisor consented to his decision. For a second opinion Raju approaches you. Being a CA advise.**

Ans. As per section 2(62) OPC means a company with only 1 person as member.

Referring the provisions of Companies Act, 2013 it is to be noted that during Incorporation of a company the member of the OPC has to appoint a nominee taking his consent who shall be the member OPC in case the Member fails to act as such.

Eligibility to be a Member as well as Nominee: - The person should be an Individual, Resident of India and Citizen of India.

Noting the above we can conclude that Avenue Ltd cannot be Member of an OPC as it is not a natural person.

2. Vijay advanced a debt to Anand Ltd without referring MOA which was silent as to the borrowing powers. Advise whether Vijay can claim repayment referring a case law.

Ans. The memorandum and articles when registered with ROC become public document and can be inspected by anyone. Therefore any person who enters into a contract with the company is presumed to have read these documents before contracting. Thus the onus of loss is on the outsiders.

Hence, in the above case Vijay cannot recover his loan as the contract is void for both company as well as Vijay

3. Narang Ind. Ltd. has approached you for the following.

a. Can it make an IPO?

Ans. Yes, as a public company is not prohibited to invite public to subscribe for securities as under section 2(68) of companies Act, 2013

b. Can it have more than 200 Members?

Ans. Yes, as it is not subject to maximum no of members of 200 as in case of Private company under sec2(68)

c. Can the members of company transfer shares freely?

Ans. Yes, as there is no requirement of restriction on transfer of shares in AOA of the company.

4. Members of a sec 8 co want the company to declare dividend as the company has surplus reserves. You are required to rectify or ratify their wants referring the provision of the Act.

Ans. As per section 8 of Companies ACT, 2013, a license is to be derived from CG to work as NPO.

CG gives the license only on fulfillment of the 3 conditions

The company's main objects are profit motive

The company shall not declare dividend

The company shall utilize its income on attaining its main objects only

Referring point B we can conclude that Sec 8 Company cannot declare dividend to members even on unanimous consent

5. Mr. and Mrs. Shetty the only directors as well as members of a company died in a car accident. Advise as to the status of the company.

Ans. A company has a special feature known as perpetual succession which entails the company to enjoy a continuous life without having any effect due to the death of all members as well as shareholders.

It states that members may come and members may go but company stays forever.

Hence we conclude that death of Mr. and Mrs. Shetty shall not affect the status of company as a going concern

Q.4 Answer any one of the following

(5 Marks)

1. Certificate of Incorporation is a conclusive evidence of Incorporation of the company. Justify the statement

Ans. The certificate of incorporation given by the Registrar in respect of any association shall be conclusive evidence that all the requirements under the Companies Act, 2013 have been complied with respect to registration and matters precedent and incidental thereto have been duly complied with.

Therefore, the validity of the certificate of incorporation cannot be questioned on any ground.

The certificate of incorporation has been held to be conclusive on the following points

The requirements of the Act in respect of registration of matters precedent and incidental thereto have been complied with.

That the association is a company authorized to be registered and duly registered under the Act.

However, it does not render illegal activity legal.

2. There were 2 Members in ABC Pvt. Ltd. One died leaving only 1 Member in the company. The sole Member undertook a contract in the name of the company. Advise as to the liability of the member on the contract.

Ans. Companies Act, 2013 states that if the number of Members fall below statutory minimum, the existing members should appoint a new member within 6 months so as to comply with the statutory minimum number.

If the members fail to do the same and carry on business, every member knowing the fact shall be personally liable for contracts entered into after 6 months from cessation of member.

Here if the sole member doesn't appoint a new member within 6 months, he shall be personally liable for the contracts entered into after 6 months.

Q1. Discuss the case laws

(4 Marks each)

1. Arvind Ltd. received a certificate of Incorporation on 18th Jan 2019 mentioning the date 16th Jan 2019. The company issued shares on 17th Jan 2019. The company later made a call. Mr. X, one of the member refused the contention of the company. Being a CA advise.
2. A company undertook a contract of TV manufacturing with its objects in MOA as Fertilizer manufacturing. ALL the members later on ratified the contract. Can the company commence production?
3. Bombay Ind Ltd. holds 38% voting power in Jirag Ltd. Bombay Ind Ltd. Ltd holds 55% in Denver Ltd. Denver Ltd holds 17% voting power in Jirag Ltd. Being a CA advise whether Jirag Ltd is subsidiary of Bombay Ind Ltd.
4. Louis holds all the entire capital of Louis Ltd. The company purchased vehicle and machinery out of the money invested by Louis. During winding up, Louis claims the properties. Advise.
5. Mentioning the contents of affidavit by subscriber and directors during incorporation of a company advise whether the affidavit is to be given jointly or individually.

Q2. Define the following

(2 Marks each)

1. Dormant Company
2. Public Financial Institution
3. Subsidiary Company
4. Company Ltd by shares
5. Nidhi Company

Q3. Answer the following

1. State the procedure for incorporation of a company **(7 Marks)**
2. State the features of a company **(8 Marks)**
3. Define AOA AND MOA. Also justify the following
"AOA cannot exceed MOA and Companies Act" **(5 Marks)**

Q.1 Discuss the case laws (4 Marks each)

1. Arvind Ltd. received a certificate of Incorporation on 18th Jan 2019 mentioning the date 16th Jan 2019. The company issued shares on 17th Jan 2019. The company later made a call. Mr. X, one of the member refused the contention of the company. Being a CA advise.

Ans. The Date mentioned in the certificate of Incorporation is the date when the company is incorporated. In the present case, the date mentioned in the certificate is 16th Jan 2016 and the shares are issued on 17th Jan 2016.

Hence, the issue of shares is a valid issue and therefore the company's contention demanding call money is right in law.

2. A company undertook a contract of TV manufacturing with its objects in MOA as Fertilizer manufacturing. ALL the members later on ratified the contract. Can the company commence production?

Ans. Any contract undertaken by the company exceeding the MOA's object clause is void ab initio as per the doctrine of constructive notice which means that the contract is void from the beginning itself.

Referring to the explanation, we can conclude that not even all the shareholders can ratify retrospective ultra vires contracts as it is void ab initio and so cannot commence production of the TV sets

3. Bombay Ind Ltd. holds 38% voting power in Jirag Ltd. Bombay Ind Ltd. Ltd holds 55% in Denver Ltd. Denver Ltd holds 17% voting power in Jirag Ltd. Being a CA advise whether Jirag Ltd is Section 2 (87)

Ans. "Subsidiary Company" or "Subsidiary", in relation to any other company (that is to say the holding company), means a company in which the holding company –

(i) controls the composition of the board of directors; or (ii) exercise or controls more than one – half of the total share capital either at its own or together with one or more of its subsidiary companies:

Referring point (ii) Bombay Ind Ltd is a holding company of Jirag Ltd as Bombay Ind Ltd is holding more than one half of the paid up capital of Jirag Ltd along with its subsidiary Denver Ltd.

4. Louis holds all the entire capital of Louis Ltd. The company purchased vehicle and machinery out of the money invested by Louis. During winding up, Louis claims the properties. Advise.

Ans. The Company being a separate legal entity can own property, have banking account, raise loans, incur liabilities and enter into contracts.

Noting the above feature, we can conclude that company is the owner of its properties and no one else even if the entire share capital of the company is held by anyone else. In this case, Louis is not the owner of the properties but Louis Ltd is the owner.

5. Mentioning the contents of affidavit by subscriber and directors during incorporation of a company advise whether the affidavit is to be given jointly or individually.

Ans. The AFFIDAVIT CONTAINS:-

- Declaration from each of the subscribers to the memorandum and form persons named as the first directors, if any in the articles stating that -
 - He is not convicted of nay offence in connection with the promotion, formation or management of any company, or

He has not been found guilty of any fraud or misfeasance or of any breach of duty to any company under this Act or any pervious company law during the last five years.

As the statement mentions each of the subscribers and directors should give the declaration we can conclude that the affidavit is to be given individually.

Q.2 Define the following (2 Marks)

1. Dormant Company: - Where a company is formed and registered under this act for a future project or to hold an asset or intellectual property and has no significant accounting transaction, such a company or an inactive company may make an application to the registrar in such manner. As may be prescribed for obtaining the status of a dormant company. "Inactive company" means a company which has not been carrying on any business or operation, or has not made any significant accounting transaction.

2. Public Financial Institution: - Section2 (72) "Public Financial Institution' means –

- (i) The life insurance corporation of India established under section 3 of the life insurance corporation Act, 1956;
- (ii) The infrastructure development finance company limited, referred to in clause (vi) of sub – section (1) of section 4A of the companies Act, 1956 so repealed under section 465 of this Act;
- (iii) Specified company referred to in the unit trust of India (Transfer of undertaking and Repeal) Act, 2002;
- (iv) Institution notified by the central government under sub –section (2) of section 4A of the companies Act, 1956 so repealed under section 465 of this Act;
- (v) Such other institution as may be notified by the central government in consultation with the reserve bank of India:

Provided that no institution shall be so notified unless -

- (A) It has been established or constituted by or under any central or state Act; or
- (B) not less than fifty – one percent of the paid – up share capital is held or controlled by the central government or by any state government or governments or partly by the central government and partly by one or more state governments.

3. Subsidiary Company: - Section 2 (87) "Subsidiary Company" or "Subsidiary", in relation to any other company (that is to say the holding company), means a company in which the holding company –

- (i) Controls the composition of the board of directors; or (ii) exercise or controls more than one – half of the total share capital either at its own or together with one or more of its subsidiary companies:

Provided that such class or classes of holding companies as may be prescribed shall not have layers of subsidiaries beyond such numbers as may be prescribed.

4. **Company Ltd by shares:** - Section 2 (22) “Company Limited by share” means a company having the liability of its member limited by the memorandum to the amount, if any, unpaid on the shares respectively held by them.
5. **Nidhi Company:** - Company which has been incorporated as a Nidhi with object of cultivating the habit of thrift (cost cutting) and savings amongst its members, receiving deposits from, and lending to, its members only, for their mutual benefit and which complies with such rules as are prescribed by the central government for regulation of such class of companies. [Section 406 of companies Act, 2013]

Q.3 Answer the following

1. State the procedure for incorporation of a company (7 Marks)

Ans. Section 7 of the companies Act, 2013 provides for the procedure to be followed for incorporation of a company.

- Filing of the documents and information with the registrar :- For the registration of the company following documents and information are required to be filed with the registrar within whose jurisdiction the registered office of the company is proposed to be situated –
- The memorandum and articles of the company duly signed by all the subscribers to the memorandum.
- A declaration by person who is engaged in the formation of the company (an advocate, a chartered accountant, cost accountant or company secretary in practice), and by a person named articles (director, manager or secretary of the company), that all the requirement of this act and the rules made there under in respect of registration and matters precedent or incidental thereto have been complied with.
- Declaration from each of the subscribers to the memorandum and form persons named as the first directors, if any in the articles stating that -
 - He is not convicted of any offence in connection with the promotion, formation or management of any company, or
 - He has not been found guilty of any fraud or misfeasance or of any breach of duty to any company under this Act or any pervious company law during the last five years,
 - Details OF Registered Office and also the address for correspondence till its registered offices is established
 - Details of Director’s mentioning the Directors Identification number, residential address, Nationality, etc along with his consent to be the Director of the Company.

2. State the features of a company (8 Marks)

Ans. Following are the features of a company

1. **Separate Legal Entity:-** When a company is registered, it becomes a separated legal personality. It comes to have almost the same rights and powers as human being. It is a different person altogether from the subscribes to the memorandum of association. Its personality is distinct and separate from the personality of those who compose it. Case low C.L Salomon Vs. Salomon & Company Ltd.
2. **Perpetual Succession:** - A company has a continued existence and it can be wound up only as per law. Members may come & Members go but Company stays forever.
3. **Limited Liability:** - liability of Member is limited upto unpaid face value of shares or guaranteed.
4. **Separate Property:** - The Company being a separate legal entity can own property, have banking account, raise loans, incur liabilities and enter into contracts.

5. Common seal:- It is the official signature of the company. However Companies Amendment ACT, 2015 does not mandate common seal. So, a company's document without common seal is authenticated by 2 Directors if the company does not have company secretary in employment and by 1 Director and Company secretary if it has appointed company secretary.
6. Separation of ownership from management:- The shareholders who are the owners of the share capital of the company and they bear risk but they do not actually manage the company. The management is vested in the board of directors who are elected by the shareholders.
7. Can Sue and be sued:- A Company can sue other and it can be sued in its own name.
8. Transferability of shares:- The capital of a company is divided into shares. Share of a company are movable property, transferable subject to certain conditions which may be provided in the articles.

**3. Define AOA AND MOA. Also justify the following
"AOA cannot exceed MOA and Companies Act"**

(5 Marks)

Ans. As per section 2(56) Memorandum means the Memorandum of Association of the company as originally framed and as altered from time to time.

It is the charter of the company which define its objects and powers.

As per section 2(5) Articles means the Article of Association of the company as originally framed and as altered from time to time.

They are the regulation for the internal management of the company and are subsidiary to the memorandum.

MOA is derived from and is subsidiary to Companies Act, the same relation exists between AOA and MOA. As per section 6 companies Act, 2013 AOA and MAOA should be in conformity with companies Act.

But AOA can have stringent provisions compare to Companies Act 2013. Eg. A company can add entrenchment provisions in AOA which requires alteration of to be passed by unanimous voting rather than just special resolution