

Sampurna (CA-Foundation)

The Indian Contract Act, 1872 – Part 1

Q. Bank

1. A sends an offer to B to sell his second-car for Rs. 1,40,000 with a condition that if B does not reply within a week, he (A) shall treat the offer as accepted. Is A correct in his proposition? What shall be the position if B communicates his acceptance after one week?

Sol. Acceptance to an offer cannot be implied merely from the silence of the offeree, even if it is expressly stated in the offer itself. Unless the offeree has by his previous conduct indicated that his silence amount to acceptance, it cannot be taken as valid acceptance. So, in the given problem, if B remains silent, it does not amount to acceptance.

The acceptance must be made within the time limit prescribed by the offer. The acceptance of an offer after the time prescribed by the offer or has elapsed will not avail to turn the offer into a contract. If B communicates his acceptance after one week it will not turn the offer into contract as the offer is already lapsed.

2. Shambhu Dayal started “self service” system in his shop. Smt. Prakash entered the shop, took a basket and after taking articles of her choice into the basket reached the cashier for payments. The cashier refuses to accept the price. Can Shambhu Dayal be compelled to sell the said articles to Smt. Prakash? Decide as per the provisions of the Indian Contract Act, 1872.

Sol. Invitation to offer: The offer should be distinguished from an invitation to offer. An offer is the final expression of willingness by the offer or to be bound by his offer should the party chooses to accept it. Where a party, without expressing his final willingness, proposes certain terms on which he is willing to negotiate, he does not make an offer, but invites only the other party to make an offer on those terms. This is the basic distinction between offer and invitation to offer.

The display of articles with a price in it in a self-service shop is merely an invitation to offer. It is in no sense an offer for sale, the acceptance of which constitutes a contract. In this case, Smt. Prakash by selecting some articles and approaching the cashier for payment simply made an offer to buy the articles

selected by her. If the cashier does not accept the price, the interested buyer cannot compel him to sell.

3. Define the term acceptance under the Indian Contract Act, 1872. Explain the legal rules regarding a valid acceptance

Sol. (a) Definition of Acceptance: In terms of Section 2(b) of the Indian Contract Act, 1872 the term acceptance is defined as “When the person to whom the proposal is made signifies his assent thereto, proposal is said to be accepted. The proposal, when accepted, becomes a promise”.

1. Legal Rules regarding a valid acceptance

Acceptance can be given only by the person to whom offer is made: In case of a specific offer, it can be accepted only by the person to whom it is made. In case of a general offer, it can be accepted by any person who has the knowledge of the offer.

2 Acceptance must be absolute and unqualified:

As per section 7 of the Act, acceptance is valid only when it is absolute and unqualified and is also expressed in some usual and reasonable manner unless the proposal prescribes the manner in which it must be accepted. If the proposal prescribes the manner in which it must be accepted, then it must be accepted accordingly.

3 The acceptance must be communicated: To conclude a contract between the parties, the acceptance must be communicated in some perceptible form. Further when a proposal is accepted, the offeree must have the knowledge of the offer made to him. If he does not have the knowledge, there can be no acceptance. The acceptance must relate specifically to the offer made. Then only it can materialize into a contract.

4 Acceptance must be in the prescribed mode: Where the mode of acceptance is prescribed in the proposal, it must be accepted in that manner. But if the proposer does not insist on the proposal

being accepted in the manner prescribed after it has been accepted otherwise, i.e., not in the prescribed manner, the proposer is presumed to have consented to the acceptance.

5 Time: Acceptance must be given within the specified time limit, if any, and if no time is stipulated, acceptance must be given within the reasonable time and before the offer lapses.

6 Mere silence is not acceptance: The acceptance of an offer cannot be implied from the silence of the offeree or his failure to answer, unless the offeree has in any previous conduct indicated that his silence is the evidence of acceptance.

7 Acceptance by conduct/Implied Acceptance: Section 8 of the Act lays down that “the performance of the conditions of a proposal, or the acceptance of any consideration for a reciprocal promise which may be offered with a proposal, constitutes an acceptance of the proposal. This section provides the acceptance of the proposal by conduct as against other modes of acceptance i.e. verbal or written communication.

Therefore, when a person performs the act intended by the proposer as the consideration for the promise offered by him, the performance of the act constitutes acceptance

4. A shop-keeper displayed a pair of dress in the show-room and a price tag of Rs. 2,000 was attached to the dress. Ms. Lovely looked to the tag and rushed to the cash counter. Then she asked the shop-keeper to receive the payment and pack up the dress. The shopkeeper refused to hand-over the dress to Ms. Lovely in consideration of the price stated in the price tag attached to the Ms. Lovely seeks your advice whether she can sue the shopkeeper for the above cause under the Indian Contract Act, 1872.

Sol. The offer should be distinguished from an invitation to offer. An offer is definite and capable of converting an intention into a contract. Whereas an invitation to an offer is only a circulation of an offer, it is an attempt to induce offers and precedes a definite offer. Where a party, without expressing his final willingness, proposes certain terms on which he is willing to negotiate, he does not make an offer, but invites only the other party to make an offer on those terms. This is the basic distinction between offer and invitation to offer.

The display of articles with a price in it in a self-service shop is merely an invitation to offer. It is in no sense an offer for sale, the acceptance of which constitutes a contract. In this case, Ms. Lovely by selecting the dress and approaching the shopkeeper for payment simply made an offer to buy the dress selected by her. If the shopkeeper does not accept the price, the interested buyer cannot compel him to sell.

5. Mr. Aseem is a learned advocate. His car was stolen from his house. He gave an advertisement in newspaper that he will give the reward of Rs. 10,000 who will give the information about his car. Mr. Vikram reads the advertisement and on making some efforts got the stolen car and informed Mr. Aseem. Mr. Aseem found his car but denied giving reward of Rs. 10,000 to Mr. Vikram with the words, “An advertisement in newspaper is just an invitation to make offer and not an offer. Hence, he is not liable to make the reward.” State with reasons whether under Indian Contract Act, 1872, Mr. Vikram can claim the reward of Rs. 10,000.

Sol. An invitation to offer is different from offer. Quotations, menu cards, price tags, advertisements in newspaper for sale are not offer. These are merely invitations to public to make an offer. An invitation to offer is an act precedent to making an offer. Acceptance of an invitation to an offer does not result in the contract and only an offer emerges in the process of negotiation. But there is an exception to above provisions. When advertisement in newspaper is made for reward, it is the general offer to public.

On the basis of above provisions and facts, it can be said that as advertisement made by Mr. Aseem to find lost car is an offer, he is liable to pay Rs. 10,000 to Mr. Vikram

6. Define an offer. Explain the essentials of a valid offer. How an offer is different from an invitation to offer?

Sol. Definition: The word Proposal and offer are used interchangeably and it is defined under Section 2(a) of the Indian Contract Act, 1872 as when one person signifies to another his willingness to do or to abstain from doing anything with a view to obtaining the assent of that other to such act or abstinence, he is said to make a proposal.

Essentials: The following are important essentials of an offer:

- (i) Must be capable of creating legal relation.
- (ii) Must be certain, definite and not vague.



- (iii) Must be communicated.
- (iv) Must be made with a view to obtaining the assent of the other party
- (v) May be conditional
- (vi) Offer should not contain a term the non compliance of which would amount to acceptance
- (vii) May be general or specific
- (viii) May be expressed or implied
- (ix) A statement of price is not an offer

Offer and an Invitation to an offer: In terms of Section 2(a) of the Act, an offer is the final expression of willingness by the offeror to be bound by the offer should the other party chooses to accept it. On the other hand, offers made with the intention to negotiate or offers to receive offers are known as invitation to offer. Thus, where a party without expressing his final willingness proposes certain terms on which he is willing to negotiate he does not make an offer, but only invites the other party to make an offer on those terms. Hence, the only thing that is required is the willingness of the offeree to abide by the terms of offer.

7. Father promised to pay his son a sum of rupee one lakh if the son passed C.A. examination in the first attempt. The son passed the examination in the first attempt, but father failed to pay the amount as promised. Son files a suit for recovery of the amount. State along with reasons whether son can recover the amount under the Indian Contract Act, 1872.

Sol. Problem asked in the question is based on the provisions of the Indian Contract Act, 1872 as contained in section 10. According to the provisions there should be an intention to create legal relationship between the parties. Agreements of a social nature or domestic nature do not contemplate legal relationship and as such are not contracts, which

can be enforced. This principle has been laid down in the case of *Balfour v. Balfour*. Accordingly, applying the above provisions and the case decision, in this case son cannot recover the amount of Rs. 1 lakh from father for the reasons explained above.

8. Rahul goes to super market to buy a washing machine. He selects a branded washing machine having a price tag of Rs. 15000 after a discount of Rs. 3000. Rahul reaches at cash counter for making the payment, but cashier says, "Sorry sir, the discount was upto yesterday. There is no discount from today. Hence you have to pay Rs. 18000." Rahul got angry and insists for Rs. 15000. State with reasons whether under Indian Contract Act, 1872, Rahul can enforce the cashier to sale at discounted price i.e. Rs. 15000.

Sol. An invitation to offer is different from offer. Quotations, menu cards, price tags, advertisements in newspaper for sale are not offer. These are merely invitations to public to make an offer. An invitation to offer is an act precedent to making an offer. Acceptance of an invitation to an offer does not result in the contract and only an offer emerges in the process of negotiation.

In the instant case, Rahul reaches to super market and selects a washing machine with a discounted price tag of Rs. 15000 but cashier denied to sale at discounted price by saying that discount is closed from today and request to make full payment. But Rahul insists to sale at discounted price.

On the basis of above provisions and facts, the price tag with washing machine was not offer. It is merely an invitation to offer. Hence, it is the Rahul who is making the offer not the super market. Cashier has right to reject the Rahul's offer. Therefore, Rahul cannot enforce cashier to sale at discounted price



Sampurna (CA-Foundation)

THE INDIAN CONTRACT ACT, 1872_ PART - 2 NATURE OF CONTRACT & CONSIDERATION

Q. Bank

1. All contracts are agreements, but all agreements are not contracts". Comment.

Sol. An agreement comes into existence when one party makes a proposal or offer to the other party and that other party gives his acceptance to it. A contract is an agreement enforceable by law. It means that to become a contract an agreement must give rise to a legal obligation i.e. duty enforceable by law. If an agreement is incapable of creating a duty enforceable by law, it is not a contract. There can be agreements which are not enforceable by law, such as social, moral or religious agreements. The agreement is a wider term than the contract. All agreements need not necessarily become contracts but all contracts shall always be agreements.

All agreements are not contracts: When there is an agreement between the parties and they do not intend to create a legal relationship, it is not a contract.

All contracts are agreements: For a contract there must be two things (a) an agreement and (b) enforceability by law. Thus, existence of an agreement is a pre-requisite existence of a contract. Therefore, it is true to say that all contracts are agreements.

Thus, we can say that there can be an agreement without it becoming a contract, but we can't have a contract without an agreement.

2. Explain the type of contracts in the following agreements under the Indian Contract Act, 1872:

- (1) A coolie in uniform picks up the luggage of A to be carried out of the railway station without being asked by A and A allows him to do so.
- (2) Obligation of finder of lost goods to return them to the true owner.
- (3) A contract with B (owner of the factory) for the supply of 10 tons of sugar, but before the supply is affected, the fire caught in the factory and everything was destroyed.

Sol. It is an implied contract and A must pay for the services of the coolie detailed by him.

- (i) **Implied Contracts:** Implied contracts come into existence by implication. Most often the implication is by law and or by action. Section 9 of the Act contemplates such implied contracts when it lays down that in so far as such proposal or acceptance is made otherwise than in words, the promise is said to be implied.
- (ii) Obligation of finder of lost goods to return them to the true owner cannot be said to arise out of a contract even in its remotest sense, as there is neither offer and acceptance nor consent. These are said to be quasi-contracts.

Quasi-Contract: A quasi-contract is not an actual contract but it resembles a contract. It is created by law under certain circumstances. The law creates and enforces legal rights and obligations when no real contract exists. Such obligations are known as quasi-contracts. In other words, it is a contract in which there is no intention on part of either party to make a contract but law imposes a contract upon the parties.

(iii) The above contract is a void contract.

Void Contract: Section 2 (j) states as follows: "A contract which ceases to be enforceable by law becomes void when it ceases to be enforceable". Thus, a void contract is one which cannot be enforced by a court of law.

3. State whether there is any contract in following cases:

- (1) A engages B to do certain work and remuneration to be paid as fixed by C.
- (2) A and B promise to pay for the studies of their maid's son
- (3) A takes a seat in public bus.
- (4) A, a chartered accountant promises to help his friend to file his return.

- Sol.** (a) It is a valid express contract
 (b) It is not a contract as it is a social agreement
 (c) It is an implied contract. A is bound to pay for the bus fare.
 (d) It is a social agreement without any intention to create a legal relationship.

4. Miss Shakuntala puts an application to be a teacher in the school. She was appointed by the trust of the school.

Her friend who works in the same school informs her about her appointment informally.

But later due to some internal reasons her appointment was cancelled. Can Miss Shakuntala claim for damages?

Sol. No, Miss Shakuntala cannot claim damages. As per Section 4, communication of acceptance is complete as against proposer when it is put in the course of transmission to him.

In the present case, school authorities have not put any offer letter in transmission. Her information from a third person will not form part of contract.

5. Define the term ‘Acceptance’. Discuss the legal provisions relating to communication of acceptance.

Sol. 1. 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 the 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.

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, 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. Mr. B makes a proposal to Mr. S by post to sell his house for Rs. 10 lakhs and posted the letter on 10th April 2020 and the letter reaches to Mr. S on 12th April 2020. He reads the letter on 13th April 2020.

Mr. S sends his letter of acceptance on 16th April 2020 and the letter reaches Mr. B on 20th April 2020. On 17th April Mr. S changed his mind and sends a telegram withdrawing his acceptance. Telegram reaches to Mr. B on 19th April 2020.

Examine with reference to the Indian Contract Act, 1872:

- (i) On which date, the offer made by Mr. B will complete?
 (ii) Discuss the validity of acceptance.

What would be validity of acceptance if letter of revocation and letter of acceptance reached together?

Sol. According to Section 4 of the Indian Contract Act, 1872, “the communication of offer is complete when

it comes to the knowledge of the person to whom it is made”.

When a proposal is made by post, its communication will be complete when the letter containing the proposal reaches the person to whom it is made. Further, mere receiving of the letter is not sufficient, he must receive or read the message contained in the letter.

In the given question, Mr. B makes a proposal by post to Mr. S to sell his house. The letter was posted on 10th April 2020 and the letter reaches to Mr. S on 12th April 2020 but he reads the letter on 13th April 2020. Thus, the offer made by Mr. B will complete on the day when Mr. S reads the letter, i.e. 13th April 2020.

(i) When communication of acceptance is complete: Where a proposal is accepted by a letter sent by the post, in terms of Section 4 of the Act, the communication of acceptance will be complete as against the proposer when the letter of acceptance is posted and as against the acceptor when the letter reaches the proposer.

Revocation of Acceptance: The acceptor can revoke his acceptance any time before the letter of acceptance reaches the offeror, if the revocation telegram arrives before or at the same time with the letter of acceptance, the revocation is absolute.

In the given question, when Mr. S accepts Mr. B's proposal and sends his acceptance by post on 16th April 2020, the communication of acceptance as against Mr. B is complete on 16th April 2020, when the letter is posted. As against Mr. S acceptance will be complete, when the letter reaches Mr. B i.e. 20th April 2020. Whereas, acceptor, will be bound by his acceptance only when the letter of acceptance has reached the proposer.

The telegram for revocation of acceptance reached Mr. B on 19th April 2020 i.e. before the letter of acceptance of offer (20th April 2020). Hence, the revocation is absolute. Therefore, acceptance to an offer is invalid.

(ii) It will not make any difference even if the telegram of revocation and letter of acceptance would have reached on the same day, i.e. the revocation then also would have been absolute. As per law, acceptance can be revoked anytime before the communication of acceptance is complete. Since revocation was made before the communication of acceptance was

complete and communication can be considered as complete only when the letter of acceptance reaches the proposer i.e. Mr. B

7. Explain the modes of revocation of an offer as per the Indian Contract Act, 1872.

Sol. Modes of revocation of Offer

- (i)** By notice of revocation
- (ii) By lapse of time:** The time for acceptance can lapse if the acceptance is not given within the specified time and where no time is specified, then within a reasonable time.
- (iii) By non-fulfillment of condition precedent:** Where the acceptor fails to fulfill a condition precedent to acceptance the proposal gets revoked.
- (iv) By death or insanity:** Death or insanity of the proposer would result in automatic revocation of the proposal but only if the fact of death or insanity comes to the knowledge of the acceptor.
 - (i) By counter offer
 - (ii) By the non- acceptance of the offer according to the prescribed or usual mode
 - (iii) By subsequent illegality

8. Comment on the following statements:

- (a) Acceptance must be absolute and unqualified.
- (b) Acceptance must be in the prescribed mode.

Sol. **Acceptance must be absolute and unqualified:** As per section 7 of the Indian Contract Act, 1872 acceptance is valid only when it is absolute and unqualified and is also expressed in some usual and reasonable manner unless the proposal prescribes the manner in which it must be accepted. If the proposal prescribes the manner in which it must be accepted, then it must be accepted accordingly.

Example: 'A' enquires from 'B', "Will you purchase my car for Rs. 2 lakhs?" If 'B' replies "I shall purchase your car for Rs. 2 lakhs, if you buy my motorcycle for Rs. 50000/-, here 'B' cannot be considered to have accepted the proposal. If on the other hand 'B' agrees to purchase the car from 'A' as per his proposal subject to availability of valid Registration Certificate/book for the car, then the

acceptance is in place though the offer contained no mention of R.C. book. This is because expecting a valid title for the car is not a condition. Therefore, the acceptance in this case is unconditional.

Acceptance must be in the prescribed mode: Where the mode of acceptance is prescribed in the proposal, it must be accepted in that manner. But if the proposer does not insist on the proposal being accepted in the manner prescribed after it has been accepted otherwise, i.e., not in the prescribed manner, the proposer is presumed to have consented to the acceptance.

Example: If the offeror prescribes acceptance through messenger and offeree sends acceptance by email, there is no acceptance of the offer if the offeror informs the offeree that the acceptance is not according to the mode prescribed. But if the offeror fails to do so, it will be presumed that he has accepted the acceptance and a valid contract will arise.

9. Explain the type of contracts in the following agreements under the Indian Contract Act, 1872:

- (1) X promise to sell his scooter to Y for Rs. 1 Lac. However, the consent of X has been procured by Y at a gun point.
- (2) A bought goods from B in 2015. But no payment was made till 2019.
- (3) G agrees to give tuitions to H, a pre-engineering student, from the next month and H in consideration promises to pay G Rs. 5,000 per month.

- Sol.**
- (i) In the instant case, X is an aggrieved party and the contract is voidable at his option but not at the option of Y. It means if X accepts the contract, the contract becomes a valid contract then Y has no option of rescinding the contract.
 - (ii) B cannot sue A for the payment in 2019 as it has crossed three years and barred by Limitation Act. A good debt becomes unenforceable after the period of three years as barred by Limitation Act.
 - (iii) Where, G agrees to give tuitions to H, a pre-engineering student, from the next month and H in consideration promises to pay G Rs. 5,000 per month, the contract is executory because

10. Ramaswami proposed to sell his house to Ramanathan. Ramanathan sent his acceptance by post. Next day, Ramanathan sends a telegram withdrawing his acceptance. Examine the validity of the acceptance according to the Indian Contract Act, 1872 in the light of the following:

- (1) The telegram of revocation of acceptance was received by Ramaswami before the letter of acceptance.
- (2) The telegram of revocation and letter of acceptance both reached together.

Sol. The problem is related with the communication and time of acceptance and its revocation.

As per Section 4 of the Indian Contract Act, 1872, the communication of an acceptance is complete as against the acceptor when it comes to the knowledge of the proposer.

An acceptance may be revoked at any time before the communication of the acceptance is complete as against the acceptor, but not afterwards.

Referring to the above provisions:

- (a) Yes, the revocation of acceptance by Ramanathan (the acceptor) is valid.
- (b) If Ramaswami opens the telegram first (and this would be normally so in case of a rational person) and reads it, the acceptance stands revoked. If he opens the letter first and reads it, revocation of acceptance is not possible as the contract has already been concluded.

11. A coolie in uniform picks up the luggage of R to be carried out of the railway station without being asked by R and R allows him to do so.

Examine whether the coolie is entitled to receive money from R under the Indian Contract Act, 1872

Sol. Implied Contracts: Implied contracts come into existence by implication. Most often the implication is by law and or by action. Section 9 of the Indian Contract Act, 1872 contemplates such implied contracts when it lays down that in so far as such proposal or acceptance is made otherwise than in words, the promise is said to be implied.

In the present case, it is an implied contract and R must pay for the services of the coolie.

- 12.** Mr. Pratham applied for a job as principal of a school. The school management decided to appoint him.

One member of the school management committee privately informed Mr. Pratham that he was appointed but official communication was not given from the school. Later, the management of the school decided to appoint someone else as a principal.

Mr. Pratham filed a suit against the school for cancellation of his appointment and claimed damages for loss of salary.

State with reasons, will Mr. Pratham be successful in suit filed against school under the Indian Contract Act, 1872?

- Sol.** As per the rules of acceptance, the acceptance should be communicated to offeror by offeree himself or his authorized agent. Communication of acceptance by third person cannot be concluded in valid acceptance.

In the instant case, Mr. Pratham applied for a job as principal of a school and one member of the school management committee privately informed Mr. Pratham that he was appointed. Later, the management of the school appointed someone else as a principal.

On the basis of above provisions and facts, communication of appointment of Mr. Pratham should be made by school management committee or any authorised agent. The communication by third person cannot be termed as communication of acceptance. Therefore, no valid contract was formed between Mr. Pratham and school and Mr. Pratham cannot file a suit against the school for cancellation of his appointment.

- 13.** “To form a valid contract, consideration must be adequate”. Comment.

- Sol.** The law provides that a contract should be supported by consideration. So long as consideration exists, the Courts are not concerned to its adequacy, provided it is of some value. The adequacy of the consideration is for the parties to consider at the time of making the agreement, not for the Court when it is sought to be enforced (*Bolton v. Modden*). Consideration must however, be something to which the law attaches value though it need not be equivalent in value to the promise made.

According to Explanation 2 to Section 25 of the Indian Contract Act, 1872, an agreement to which the consent of the promisor is freely given is not void merely because the consideration is inadequate but the inadequacy of the consideration may be taken into account by the Court in determining the question whether the consent of the promisor was freely given.

- 14.** Mr. Sohanlal sold 10 acres of his agricultural land to Mr. Mohanlal on 25th September 2020 for Rs. 25 Lakhs. The Property papers mentioned a condition, amongst other details, that whosoever purchases the land is free to use 9 acres as per his choice but the remaining 1 acre has to be allowed to be used by Mr. Chotelal, son of the seller for carrying out farming or other activity of his choice. On 12th October, 2020, Mr. Sohanlal died leaving behind his son and wife. On 15th October, 2020 purchaser started construction of an auditorium on the whole 10 acres of land and denied any land to the son. Now Mr. Chotelal wants to file a case against the purchaser and get a suitable redressal. Discuss the above in light of provisions of Indian Contract Act, 1872 and decide upon Mr. Chotelal’s plan of action?

- Sol.** Problem as asked in the question is based on the provisions of the Indian Contract Act, 1872 as contained in section 2(d) and on the principle ‘privity of consideration’. Consideration is one of the essential elements to make a contract valid and it can flow from the promisee or any other person. In view of the clear language used in definition of ‘consideration’ in Section 2(d), it is not necessary that consideration should be furnished by the promisee only. A promise is enforceable if there is some consideration for it and it is quite immaterial whether it moves from the promisee 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. Sohanlal has entered into a contract with Mr. Mohanlal, but Mr. Chotelal has not given any consideration to Mr. Mohanlal but the consideration did flow from Mr. Sohanlal to Mr. Mohanlal on the behalf of Mr. Chotelal and such consideration from third party is sufficient to enforce the promise of Mr. Mohanlal to allow Mr. Chotelal to use 1 acre of land. Further the deed of sale and the

promise made by Mr. Mohanlal to Mr. Chotelal to allow the use of 1 acre of land were executed simultaneously and therefore they should be regarded as one transaction and there was sufficient consideration for it.

Moreover, it is provided in the law that “in case covenant running with the land, where a person purchases land with notice that the owner of the land is bound by certain duties affecting land, the covenant affecting the land may be enforced by the successor of the seller.”

In such a case, third party to a contract can file the suit although it has not moved the consideration.

Hence, Mr. Chotelal is entitled to file a petition against Mr. Mohanlal for execution of contract.

15. The general rule is that an agreement without consideration is void. Discuss the cases where the agreement though made without consideration will be valid and enforceable as per Indian Contract Act, 1872.

Or

State the exceptions to the rule "An agreement without consideration is void".

Or

“No consideration, no contract” Comment.

Or

Are there any circumstances under which a contract, under the provisions of the Indian Contract Act, 1872, without consideration is valid? Explain.

- Sol.** The general rule is that an agreement made without consideration is void (Section 25). In every valid contract, consideration is very important. A contract may only be enforceable when consideration is there.

Exception to general Rule: -

1. **Natural Love and Affection:** Conditions to be fulfilled under section 25 (1)

- (i) It must be made out of natural love and affection between the parties.
- (ii) Parties must stand in near relationship to each other.
 - (i) It must be in writing.
 - (ii) It must also be registered under the law.

A written and registered agreement based on natural love and affection between the parties standing in near relation (e.g., husband and wife) to each other is enforceable even without consideration

Example: A husband, by a registered agreement promised to pay his earnings to his wife. Held the agreement though without consideration, was valid.

Example: A out of natural love and affection promises to give his newly wedded daughter- in-law a golden necklace worth Rs. 5,00,000. ‘A’ made the promise in writing and signed it and registered. The agreement is valid.

2. **Compensation for past voluntary services:** A promise to compensate, wholly or in part, a person who has already voluntarily done something for the promisor, is enforceable under Section 25(2). In order that a promise to pay for the past voluntary services be binding, the following essential factors must exist:

- (i) The services should have been rendered voluntarily.
- (ii) The services must have been rendered for the promisor.
- (iii) The promisor must be in existence at the time when services were rendered.
- (iv) The promisor must have intended to compensate the promise.

3. Promise to pay time barred debt: Where a promise in writing signed by the person making it or by his authorised agent, is made to pay a debt barred by limitation it is valid without consideration [Section 25(3)].

Example: A is indebted to C for Rs. 60,000 but the debt is barred by the Limitation Act. A sign a written promise now to pay Rs. 50,000 in final settlement of the debt. This is a contract without consideration, but enforceable.

4. **Agency:** According to Section 185 of the Indian Contract Act, 1872, no consideration is necessary to create an agency.
5. **Completed gift:** In case of completed gifts, the rule no consideration no contract does not apply. Explanation (1) to Section 25 states “nothing in this section shall affect the validity as between the donor and donee, of any **gift actually made.**” Thus, gifts do not require any consideration.

6. **Bailment:** No consideration is required to affect the contract of bailment.

Meaning of bailment: Section 148 of the Indian Contract Act, 1872, defines bailment as the delivery of goods from one person to another for some purpose. This delivery is made upon a contract that post accomplishment of the purpose, the goods will either be returned or disposed of, according to the directions of the person delivering them.

Example: Mr. A hand over the keys of his godown to Mr. Y as Mr. Y had deposited his goods in the same. Mr. Y gets possession of godown but not the ownership. As soon as Mr. Y lifts his goods from godown he is liable to hand over the keys back to Mr. A.

7. **Charity:** If a promisee undertakes the liability on the promise of the person to contribute to charity, there the contract shall be valid. (Kadarnath v. Gorie Mohammad)

16. Mr. Ramesh promised to pay Rs. 50,000 to his wife Mrs. Lali so that she can spend the sum on her 30th birthday. Mrs. Lali insisted her husband to make a written agreement if he really loved her. Mr. Ramesh made a written agreement and the agreement was registered under the law. Mr. Ramesh failed to pay the specified amount to his wife Mrs. Lali. Mrs. Lali wants to file a suit against Mr. Ramesh and recover the promised amount. Referring to the applicable provisions of the Contract Act, 1872, advise whether Mrs. Lali will succeed.

Sol. Parties must intend to create legal obligations: There must be an intention on the part of the parties to create legal relationship between them. Social or domestic type of agreements are not enforceable in court of law and hence they do not result into contracts.

In the given question, Mr. Ramesh promised to pay Rs. 50,000 to his wife so that she can spend the same on her birthday. However, subsequently, Mr. Ramesh failed to fulfil the promise, for which Mrs. Lali wants to file a suit against Mr. Ramesh. Here, in the given circumstance wife will not be able to recover the amount as it was a social agreement and the parties did not intend to create any legal relations.

17. Define consideration. What are the legal rules regarding consideration under the Indian Contract Act, 1872?

Or

Define consideration. State the characteristics of a valid consideration.

- Sol. (a) Consideration [Section 2(d) of the Indian Contract Act, 1872]:** When at the desire of the promisor, the promisee or any other person has done or abstained from doing, or does or abstains from doing or promises to do or abstain from doing something, such an act or abstinence or promise is called consideration for the promise.

Legal Rules Regarding Consideration

- (i) **Consideration must move at the desire of the promisor:** Consideration must be offered by the promisee or the third party at the desire or request of the promisor. This implies “return” element of consideration.

- (ii) **Consideration may move from promisee or any other person:** In India, consideration may proceed from the promisee or any other person who is not a party to the contract. In other words, there can be a stranger to a consideration but not stranger to a contract.

- (iii) **Executed and executory consideration:** A consideration which consists in the performance of an act is said to be executed. When it consists in a promise, it is said to be executory. The promise by one party may be the consideration for an act by some other party, and vice versa.

- (iv) **Consideration may be past, present or future:** It is a general principle that consideration is given and accepted in exchange for the promise. The consideration, if past, may be the motive but cannot be the real consideration of a subsequent promise. But in the event of the services being rendered in the past at the request or the desire of the promisor, the subsequent promise is regarded as an admission that the past consideration was not gratuitous.

- (v) **Consideration need not be adequate:** Consideration need not to be of any particular value. It need not be

approximately of equal value with the promise for which it is exchanged but it must be something which the law would regard as having some value.

(vi) **Performance of what one is legally bound to perform:** The performance of an act by a person who is legally bound to perform the same cannot be consideration for a contract. Hence, a promise to pay money to a witness is void, for it is without consideration. Hence such a contract is void for want of consideration. But where a person promises to do more than he is legally bound to do, such a promise provided it is not opposed to public policy, is a good consideration. It should not be vague or uncertain.

(vi) **Consideration must be real and not illusory:** Consideration must be real and must not be illusory. It must be something to which the law attaches some value. If it is legally or physically impossible it is not considered valid consideration.

(vii) **Consideration must not be unlawful, immoral, or opposed to public policy:** Only presence of consideration is not sufficient it must be lawful. Anything which is immoral or opposed to public policy also cannot be valued as valid consideration.

18. Mr. Y given loan to Mr. G of INR 30,00,000. Mr. G defaulted the loan on due date and debt became time barred.

After the time barred debt, Mr. G agreed to settle the full amount to Mr. Y. Whether acceptance of time barred debt Contract is enforceable in law?

Sol. 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.

In the given case, the loan given by Mr. Y to Mr. G has become time barred. Thereafter, Mr. G agreed to make payment of full amount to Mr. Y.

Referring to above provisions of the Indian Contract Act, 1872 contract entered between parties post time barred debt is valid so, Mr. G is bound to pay the agreed amount to Mr. Y provided the above mentioned conditions of section 25 (3) are fulfilled.

19. A stranger to a contract cannot sue, however in some cases even a stranger to contract may enforce a claim. Explain.

Or

“Only a person who is party to a contract can sue on it”.

Explain this statement and describe its exceptions, if any.

Sol. Though under the Indian Contract Act, 1872, the consideration for an agreement may proceed from a third party, the third party cannot sue on contract. Only a person who is party to a contract can sue on it. Thus, the concept of stranger to consideration is valid and is different from stranger to a contract.

The aforesaid rule, that stranger to a contract cannot sue is known as a “doctrine of privity of contract”, is however, subject to certain exceptions.

Stranger to a contract cannot sue is known as a “doctrine of privity of contract”. This rule is however, subject to certain exceptions. In other words, even a stranger to a contract may enforce a claim in the following cases:

- (1) **In the case of trust,** a beneficiary can enforce his right under the trust, though he was not a party to the contract between the settler and the trustee.
- (2) **In the case of a family settlement,** if the terms of the settlement are reduced into writing, the members of family who originally had not been parties to the settlement may enforce the agreement.
- (3) **In the case of certain marriage contracts,** or arrangements, a provision may be made for the benefit of a person. The person may enforce the agreement though he is not a party to the agreement.
- (4) **In the case of assignment of a contract,** when the benefit under a contract has been assigned, the assignee can enforce the contract.
- (5) **Acknowledgement or estoppel** – where the promisor by his conduct acknowledges himself as an agent of the third party, it would result into a binding obligation towards third party.

(6) **In the case of covenant running with the land**, the person who purchases land with notice that the owner of land is bound by certain duties affecting land, the covenant affecting the land may be enforced by the successor of the seller.

(7) **Contracts entered into through an agent:**
The principal can enforce the contracts entered by his agent where the agent has acted within the scope of his authority and in the name of the principal.

20. Mr. Balwant, an old man, by a registered deed of gift, granted certain landed property to Ms. Reema, his daughter. By the terms of the deed, it was stipulated that an annuity of Rs. 20, 000 should be paid every year to Mr. Sawant, who was the brother of Mr. Balwant. On the same day Ms. Reema made a promise to Mr. Sawant and executed in his favour an agreement to give effect to the stipulation. Ms. Reema failed to pay the stipulated sum. In an action against her by Mr. Sawant, she contended that since Mr. Sawant had not furnished any consideration, he has no right of action.

Examining the provisions of the Indian Contract Act, 1872, decide, whether the contention of Ms. Reema is valid?

Sol. In India, consideration may proceed from the promisee or any other person who is not a party to the contract. The definition of consideration as given in section 2(d) makes that proposition clear. According to the definition, when at the desire of the promisor, the promisee or any other person does something such an act is consideration. In other words, there can be a stranger to a consideration but not a stranger to a contract.

In the given problem, Mr. Balwant has entered into a contract with Ms. Reema, but Mr. Sawant has not

given any consideration to Ms. Reema but the consideration did flow from Mr. Balwant to Ms. Reema and such consideration from a third party is sufficient to enforce the promise of Ms. Reema, the daughter, to pay an annuity to Mr. Sawant. Further the deed of gift and the promise made by Ms. Reema to Mr. Sawant 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. Hence, the contention of Ms. Reema is not valid.

21. Mr. Ram Lal Birla was a big businessman of city Pune having two sons and one married daughter. He decided to gift his one house to his daughter. For this purpose, he called his lawyer at his house and made a written document for such gift. The lawyer advised him to get the transfer document properly registered. When they both were going for registration of the document, they met with an accident and both of them died. Later, his daughter found the document and claimed the house on the basis of that document. Explain, whether she can get the house as gift under the Indian Contract Act, 1872?

Sol. Section 25 of the Indian Contract Act, 1872 provides that an agreement made without consideration is valid if it is expressed in writing and registered under the law for the time being in force for the registration of documents and is made on account of natural love and affection between parties standing in a near relation to each other.

In the instant case, the transfer of the house made by Mr. Ram Lal Birla on account of natural love and affection between the parties standing in a near relation to each other is written but not registered. Hence, this transfer is not enforceable and his daughter cannot get the house as gift under the Indian Contract Act, 1872.

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Other Essential Elements of Contract

22. Examine the validity of the following contracts as per the Indian Contract Act, 1872 giving reasons: -

- (1) X aged 16 years borrowed a loan of Rs. 50,000 for his personal purposes. Few months later he had become major and could not pay back the amount borrowed, on due date. The lender wants to file a suit against X.
- (2) J contracts to take in cargo for K at a foreign port. J's government afterwards declares war against the country in which the port is situated and therefore the contract could not be fulfilled. K wants to file a suit against J.

Sol. (a) According to Section 11 of the Indian Contract Act, 1872, every person is competent to contract who is of the age of majority according to the law to which he is subject and therefore, a minor is not competent to contract and any agreement with or by a minor is void from the very beginning. A minor cannot ratify it on attaining the majority as the original agreement is void ab initio.

According to Section 68 of the Act, a claim for necessities supplied to a minor is enforceable by law. Necessaries mean those things that are essentially needed by a minor. They cannot include luxuries or costly or unnecessary articles.

In the present case, X, the borrower, was minor at the time of taking the loan, therefore, the agreement was void ab initio. Attaining majority thereafter will not validate the contract nor X can ratify it. The loan was for personal purposes and not for necessities supplied to him. Hence, the lender cannot file a suit against X for recovery of the loan as it is not enforceable by law.

(b) As per Section 56 of the Indian Contract Act, 1872 the subsequent or supervening impossibility renders the contract void. Supervening impossibility may take place owing to various circumstances as contemplated under that section, one of which is the declaration of war subsequent to the contract made. In the instant case the contract when made between J and K was valid but afterwards J's government declares war against the country in which the port is situated as a result of which the contract becomes

void. Hence, K cannot file a suit against J for performance of the contract.

23. Mr. S aged 58 years was employed in a Government Department. He was going to retire after two years. Mr. D made a proposal to Mr. S to apply for voluntary retirement from his post so that Mr. D can be appointed in his place. Mr. D offered a sum of Rs 10 Lakhs as consideration to Mr. S in order to induce him to retire.

Sol. Mr. S refused at first instance but when he evaluated the amount offered as consideration is just double of his cumulative remuneration to be received during the tenure of two years of employment, he agreed to receive the consideration and accepted the above agreement to receive money to retire from his office. Whether the above agreement is valid? Explain with reference to provision of Indian Contract Act, 1872.

Section 10 of the Indian Contract Act, 1872 provides for the legality of consideration and objects thereto. Section 23 of the said Act also states that every agreement of which the object or consideration is unlawful is void.

The given problem talks about entering into an agreement for traffic relating to public office, which is opposed to public policy. Public policy requires that there should be no money consideration for the appointment to an office in which the public is interested. Such consideration paid, being opposed to public policy, is unlawful.

In the given case, Mr. S, who was going to be retired after two years was proposed by Mr. D, to apply for voluntary retirement from his post, in order that he can be appointed in his place. In lieu of that Mr. D offered Mr. S a sum of Rs. 10 lakh as consideration. Mr. S refused initially but later accepted the said offer to receive money to retire from his office.

Here, Mr. S's promise of sale for Mr. D, an employment in the public services is the consideration for Mr. D's promise to pay Rs. 10 lakh. Therefore, in terms of the above provisions of the Indian Contract Act, the said agreement is not valid.

It is void, as the consideration being opposed to public policy, is unlawful.

24. State with reason (s) whether the following agreements are valid or void:
- A clause in a contract provided that no action should be brought upon in case of breach.
 - Where two courts have jurisdiction to try a suit, an agreement between the parties that the suit should be filed in one of those courts alone and not in the other.
 - X offers to sell his Maruti car to Y. Y believes that X has only Wagon R Car but agrees to buy it.
 - X, a physician and surgeon, employs Y as an assistant on a salary of Rs. 75,000 per month for a term of two years and Y agrees not to practice as a surgeon and physician during these two years.

Sol. The given agreement is void.

Reason: As per Section 28 of the Indian Contract Act, 1872, this clause is in restraint of legal proceedings because it restricts both the parties from enforcing their legal rights.

Note: Alternatively, as per Section 23 of the Indian Contract Act, 1872, this clause in the agreement defeats the provision of law and therefore, being unlawful, is treated as void.

The given agreement is valid.

Reason: An agreement in restraint of legal proceeding is the one by which any party thereto is restricted absolutely from enforcing his rights under a contract through a Court. A contract of this nature is void. However, in the given statement, no absolute restriction is marked on parties on filing of suit. As per the agreement suit may be filed in one of the courts having jurisdiction.

The said agreement is void.

Reason: This agreement is void as the two parties are thinking about different subject matters so that there is no real consent and the agreement may be treated as void because of mistake of fact as well as absence of consensus.

The said agreement is valid.

Reason: An agreement by which any person is restrained from exercising a lawful profession, trade or business of any kind, is to that extent void. But, as an exception, agreement of service by which an

employee binds himself, during the term of his agreement, not to compete with his employer is not in restraint of trade.

25. Distinguish between wagering agreement and contract of insurance. Or
Enumerate the differences between 'Wagering Agreements' and 'Contract of Insurance' with reference to provision of the Indian Contract Act, 1872.

Sol.

Basis of differences	Contracts of Insurance	Wagering Agreement
Meaning	It is a contract to indemnify the loss.	It is a promise to pay money or money's worth on the happening or non- happening of an uncertain event.
Consideration	The crux of insurance contract is the mutual consideration (premium and compensation amount).	There is no consideration between the two parties. There is just gambling for money.
Insurable Interest	Insured party has insurable interest in the life or property sought to be insured.	There is no property in case of wagering agreement. There is betting on other's life and properties.
Contract Indemnity of	Except life insurance, the contract of insurance indemnifies the insured person against loss.	Loser has to pay the fixed amount on the happening of uncertain event.
Enforceability	It is valid and enforceable	Its void & unenforceable agreement.
Premium	Calculation of premium is based on scientific and actuarial calculation of risks.	No such logical calculations are required in case of wagering agreement.
Public Welfare	They are beneficial to the society	They have been regarded as against the public welfare.

26. Examine with reason that the given statement is correct or incorrect "Minor is liable to pay for the necessaries supplied to him".

Sol. Minor is liable to pay for the necessaries supplied to him: This statement is incorrect. The case of necessaries supplied to a minor or to any other person whom such minor is legally bound to support is governed by section 68 of the Indian Contract Act,

1872. A claim for necessaries supplied to a minor is enforceable by law, **only against minor's estate, if he possesses**. But a minor is not liable for any price that he may promise and never for more than the value of the necessaries. There is **no personal liability of the minor, but only his property is**

27. Define Fraud. Whether "mere silence will amount to fraud" as per the Indian Contract Act, 1872?

Sol. Definition of Fraud under Section 17: 'Fraud' means and includes any of the following acts committed by a party to a contract, or with his connivance, or by his agent, with an intent to deceive another party thereto or his agent, or to induce him to enter into the contract:

the suggestion, as a fact, of that which is not true, by one who does not believe it to be true;

the active concealment of a fact by one having knowledge or belief of the fact;

a promise made without any intention of performing it;

any other act fitted to deceive;

any such act or omission as the law specially declares to be fraudulent.

Mere silence will amount to fraud: This statement is incorrect as per the Indian Contract Act, 1872. A party to the contract is under no obligation to disclose the whole truth to the other party. 'Caveat Emptor' i.e. let the purchaser beware is the rule applicable to contracts. There is no duty to speak in such cases and silence does not amount to fraud. Similarly, there is no duty to disclose facts which are within the knowledge of both the parties.

28. "Mere silence is not fraud" but there are some circumstances where the "silence is fraud". Explain the circumstances as per the provision of Indian Contract Act, 1872?

Sol. Mere silence is not fraud

Mere silence as to facts likely to affect the willingness of a person to enter into a contract is not fraud, unless the circumstances of the case are such that, regard being had to them, it is the duty of the person keeping silence to speak, or unless his silence is, in itself, equivalent to speech.

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.

Cases where silence is fraud:

(i) **Duty of person to speak:** Where the circumstances of the case are such that it is the duty of the person observing silence to speak.

Following contracts come within this category:

(a) **Fiduciary Relationship:** Here, the person in whom confidence is reposed is under a duty to act with utmost good faith and make full disclosure of all material facts concerning the agreement, known to him.

(b) **Contracts of Insurance:** In contracts of marine, fire and life insurance, there is an implied condition that full disclosure of material facts shall be made, otherwise the insurer is entitled to avoid the contract.

(c) **Contracts of marriage:** Every material fact must be disclosed by the parties to a contract of marriage.

(d) **Contracts of family settlement:** These contracts also require full disclosure of material facts within the knowledge of the parties.

(e) **Share Allotment contracts:** Persons issuing 'Prospectus' at the time of public issue of shares/debentures by a joint stock company have to disclose all material facts within their knowledge.

Where the silence itself is equivalent to speech:

For example, A says to B "If you do not deny it, I shall assume that the horse is sound." A says nothing. His silence amounts to speech.

29. Explain the term 'Coercion' and what are the effects of coercion under Indian Contract Act, 1872.

Sol. Coercion (Section 15 of the Indian Contract Act, 1872): "Coercion" is the committing, or threatening to commit, any act forbidden by the Indian Penal Code or the unlawful detaining, or threatening to

detain any property, to the prejudice of any person whatever, with the intention of causing any person to enter into an agreement.”

Effects of coercion under section 19 of Indian Contract Act, 1872. Contract induced by coercion is **voidable** at the option of the party whose consent was soobtained. As to the consequences of the rescission of voidable contract, the party rescinding a void contract should, if he has received any benefit, thereunder from the other party to the contract, restore such benefit so far as may be applicable, to the person from whom it wasreceived. A person to whom money has been paid or anything delivered under coercion must repay or return it.

30. Mr. X a businessman has been fighting a long-drawn litigation with Mr. Y an industrialist. To support his legal campaign, he enlists the services of Mr. C a Judicial officer stating that the amount of Rs.10 lakhs would be paid to him if he does not take up the brief of Mr. Y.

Sol. Mr. C agrees but, at the end of the litigation Mr. X refuses to pay to Mr. C. Decide whether Mr. C can recover the amount promised by Mr. X under the provisions of the Indian Contract Act, 1872?

The problem as asked in the question is based on Section 10 of the Indian Contract Act, 1872. This Section says that all agreements are contracts if they are made by the free consent of the parties competent to contract, for a lawful consideration and with a lawful object and are not expressly declared to be void. Further, Section 23 also states that every agreement of whichthe object is unlawful is void.

Accordingly, one of the essential elements of a valid contract in the light of the said provision isthat the agreement entered into must not be which the law declares to be either illegal or void. An illegal agreement is an agreement expressly or impliedly prohibited by law. Avoid agreement is one without any legal effects. The given instance is a **case of interference with the course of justice and results as opposed to public policy. This can also be called as an agreement in restraint of legalproceedings.** This agreement restricts one’s right to enforce his legal rights. Such an agreement has been expressly declared to be void under section 28 of the Indian Contract Act, 1872. Hence, Mr. C in the given case cannot recover the amount of Rs. 10 lakhs promised

by Mr.X because it is a void agreement and cannot be enforced by law.

31. Define Misrepresentation and Fraud. Explain the difference between Fraud and Misrepresentation as per the Indian Contract Act, 1872.

Sol. Definition of Fraud under Section 17 of the Indian Contract Act, 1872:

'Fraud' means and includes any of the following acts committed by a party to a contract, or with his connivance, or by his agent, with an intent to deceive another party thereto or hisagent, or to induce him to enter into the contract:

- the suggestion, as a fact, of that which is not true, by one who does not believe it to be true;
- the active concealment of a fact by one having knowledge or belief of the fact;
- a promise made without any intention of performing it;
- any other act fitted to deceive;
- any such act or omission as the law specially declares to be fraudulent.

As per Section 18 of the Indian Contract Act, 1872, misrepresentation means and includes-

- the positive assertion, in a manner not warranted by the information of the person making it, of that which is not true, though he believes it to be true;
- any breach of duty which, without an intent to deceive, gains an advantage to the person committing it, or anyone claiming under him; by misleading another to his prejudice or to the prejudice of anyone claiming under him;

causing, however, innocently, a party to an agreement to make a mistake as to the substance of the thing which is the subject of the agreement.

32. Distinction between fraud and misrepresentation.

Sol.

Basis of difference	Fraud	Misrepresentation
Intention	To deceive the other party by hiding the truth.	There is no such intention to deceive the other party.
Knowledge of truth	The person making the suggestion believes that the statement as untrue.	The person making the statement believes it to be true,

		although it is not true.
Rescission of the contract and claim for damages	The injured party can Repudiate the contract and claim damages.	The injured party is entitled to repudiate the contract or sue for restitution but cannot claim the damages.
Means to discover the truth	The party using the fraudulent act cannot secure or protect himself by saying that the injured party had means to discover the truth.	Party can always plead that the injured party had the means to discover the truth.

33. 'X' agreed to become an assistant for 2 years to 'Y' who was practicing Chartered Accountant at Jodhpur. It was also agreed that during the term of agreement 'X' will not practice as a Chartered Accountant on his own account within 20 kms of the office of 'Y' at Jodhpur. At the end of one year, 'X' left the assistantship of 'Y' and started practice on his own account within the said area of 20 kms.

Referring to the provisions of the Indian Contract Act, 1872, decide whether 'X' could be restrained from doing so?

- Sol. Agreement in Restraint of Trade:** Section 27 of the Indian Contract Act, 1872 deals with agreements in restraint of trade. According to the said section, every agreement by which any person is restrained from exercising a lawful profession, trade or business of any kind, is to that extent void. However, in the case of the service agreements restraint of trade is valid. In an agreement of service by which a person binds himself during the term of agreement not to take service with anyone else directly or indirectly to promote any business in direct competition with that of his employer is not in restraint of trade, so it is a valid contract. In the instant case, agreement entered by 'X' with 'Y' is reasonable, and do not amount to restraint of trade and hence enforceable.

Therefore, 'X' can be restrained by an injunction from practicing on his own account in within the said area of 20 Kms for another one year.

34. A student was induced by his teacher to sell his brand-new car to the latter at less than the purchase price to secure more marks in the examination.

Accordingly, the car was sold. However, the father of the student persuaded him to sue his teacher. State on what ground the student can sue the teacher?

- Sol.** Yes, the student can sue his teacher on the ground of **undue influence** under the provisions of Indian Contract Act, 1872. A contract brought as a result of coercion, undue influence, fraud or misrepresentation would be **voidable** at the option of the person whose consent was caused. According to section 16 of the Indian Contract Act, 1872, "A contract is said to be induced by 'undue influence' where the relations subsisting between the parties are such that one of the parties is in a position to dominate the will of the other and he uses that position to obtain an unfair advantage over the other".

A person is deemed to be in position to dominate the will of another:

Where he holds a real or apparent authority over the other; or Where he stands in a fiduciary relationship to the other; or Where he makes a contract with a person whose mental capacity is temporarily or permanently affected by reason of age, illness or mental or bodily distress for example, an old illiterate person.

A contract brought as a result of coercion, undue influence, fraud or misrepresentation would be voidable at the option of the person whose consent was caused.

35. "Though a minor is not competent to contract, nothing in the Contract Act prevents him from making the other party bound to the minor". Discuss.

- Sol.** Minor can be a beneficiary or can take benefit out of a contract: Though a minor is not competent to contract, nothing in the Contract Act prevents him from making the other party bound to the minor.

For example: A promissory note duly executed in favour of a minor is not void and can be sued upon by him, because he though incompetent to contract, may yet accept a benefit.

A minor cannot become partner in a partnership firm. However, he may with the consent of all the partners, be admitted to the benefits of partnership (Section 30 of the Indian Partnership Act, 1932).

36. P sells by auction to Q a horse which P knows to be unsound. The horse appears to be sound but P knows

about the unsoundness of the horse. Is this contract valid in the following circumstances:

- (1) If P says nothing about the unsoundness of the horse to Q.
- (2) If P says nothing about it to Q who is P's daughter who has just come of age.
- (3) If Q says to P "If you do not deny it, I shall assume that the horse is sound." P says nothing

Sol. According to section 17 of the Indian Contract Act, 1872, mere silence as to facts likely to affect the willingness of a person to enter into a contract is not fraud, unless the circumstances of the case are such that, regard being had to them, it is the duty of the person keeping silence to speak, or unless his silence is, in itself, equivalent to speech. Hence, in the instant case,

- This contract is valid since as per section 17 mere silence as to the facts likely to affect the willingness of a person to enter into a contract is not fraud. Here, it is not the duty of the seller to disclose defects.
- This contract is not valid since as per section 17 it becomes P's duty to tell Q about the unsoundness of the horse because a fiduciary relationship exists between P and his daughter Q Here, P's silence is equivalent to speech and hence amounts to fraud.
- This contract is not valid since as per section 17, P's silence is equivalent to speech and hence amounts to fraud.

37. Explain the concept of 'misrepresentation' in matters of contract.

Sol. Misrepresentation: According to Section 18 of the Indian Contract Act, 1872, misrepresentation means and includes- the positive assertion, in a manner not warranted by the information of the person making it, of that which is not true, though he believes it to be true; any breach of duty which, without an intent to deceive, gains an advantage to the person committing it, or any one claiming under him; by misleading another to his prejudice or to the prejudice of any one claiming under him; causing, however, innocently, a party to an agreement to make a mistake as to the substance of the thing which is the subject of the agreement.

38. 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.

Sol. In the instant case, 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 amount to final acceptance of the sale.

39. Discuss the essentials of Undue Influence as per the Indian Contract Act, 1872 Or

Explain the circumstances in which the person is deemed to be in a position to dominate the will of the other person under the Indian Contract Act, 1872.

Sol. The essential ingredients under this provision are:
Relation between the parties: A person can be influenced by the other when a near relation between the two exists.

Position to dominate the will: Relation between the parties exist in such a manner that one of them is in a position to dominate the will of the other. A person is deemed to be in such position in the following circumstances:

(a) **Real and apparent authority:** Where a person holds a real authority over the other as in the case of master and servant, doctor and patient and etc.

Example: A father, by reason of his authority over the son can dominate the will of the son.

(b) **Fiduciary relationship:** Where relation of trust and confidence exists between the parties to a contract. Such type of relationship exists between father and son, solicitor and client, husband and wife, creditor and debtor, etc.

- (c) Example: By reason of fiduciary relationship, a solicitor can dominate the will of his client and a trustee can dominate the will of the beneficiary.

Example: A spiritual guru induced his devotee to gift to him the whole of his property in return of a promise of salvation of the devotee. Held, the consent of the devotee was given under undue influence. Here, the relationship was fiduciary relationship between Guru and devotee and Guru was in a position to dominate the will of devotee.

- (d) **Mental distress:** An undue influence can be used against a person to get his consent on a contract where the mental capacity of the person is temporarily or permanently affected by the reason of mental or bodily distress, illness or of oldage.

Example: A doctor is deemed to be in a position to dominate the will of his patient enfeebled by protracted illness.

- (e) **Unconscionable bargains:** Where one of the parties to a contract is in a position to dominate the will of the other and the contract is apparently unconscionable i.e., unfair, it is presumed by law that consent must have been obtained by undue influence. Unconscionable bargains are witnessed mostly in money-lending transactions and in gifts.

Example: A youth of 18 years of age, spend thrift and a drunkard, borrowed Rs. 90,000 on a bond bearing compound interest at 2% per mensem (p.m.). It was held by the court that the transaction is unconscionable, the rate of interest charged being so exorbitant [Kirpa Ram vs. Sami-Ud-din Ad. Khan (1903)]

The object must be to take undue advantage:

Where the person is in a position to influence the will of the other in getting consent, must have the object to take advantage of the other.

Example: A teacher asks her daughter to get marry to one of his brilliant students. Both the girl and boy were smart, settled and intelligent. Here the teacher had a relation which can have influence on both of

them. But as no undue advantage of such influence was taken such contract of marriage is said to be made by free consent.

Burden of proof: The burden of proving the absence of the use of the dominant position to obtain the unfair advantage will lie on the party who is in a position to dominate the will of the other.

40. What is a wagering agreement? Describe the transactions which resembles with wagering transactions but are not void.

Sol. Wagering agreement (Section 30 of the Indian Contract Act, 1872): An agreement by way of a wager is void. It is an agreement involving payment of a sum of money upon the determination of an uncertain event. The essence of a wager is that each side should **stand to win or lose, depending on the way an uncertain event** takes place in reference to which the chance is taken and in the occurrence of which neither of the parties has legitimate interest.

For example, A agrees to pay Rs. 50,000 to B if it rains, and B promises to pay a like amount to A if it does not rain, the agreement will be by way of wager. But if one of the parties has control over the event, agreement is not a wager.

Transactions resembling with wagering transaction but are not void

Chit fund: Chit fund does not come within the scope of wager (Section 30). In case of a chit fund, a certain number of persons decide to contribute a fixed sum for a specified period and at the end of a month, the amount so contributed is paid to the lucky winner of the lucky draw.

Commercial transactions or share market transactions: In these transactions in which delivery of goods or shares is intended to be given or taken, do not amount to wagers.

Games of skill and Athletic Competition: Crossword puzzles, picture competitions and athletic competitions where prizes are awarded on the basis of skill and intelligence are the games of skill and hence such competition are valid. According to the Prize Competition Act, 1955 prize competition in games of skill are not wagers provided the prize money does not exceed Rs. 1,000.

A contract of insurance: A contract of insurance is a type of contingent contract and is valid under law and these contracts are different from wagering agreements.

41. X, a minor was studying in M.Com. in a college. On 1st July, 2019 he took a loan of Rs.1,00,000 from B for payment of his college fees and to purchase books and agreed to repay by 31st December, 2019. X possesses assets worth Rs. 9 lakhs. On due date, X fails to pay back the loan to B. B now wants to recover the loan from X out of his (X's) assets. Referring to the provisions of Indian Contract Act, 1872 decide whether B would succeed.

Sol. Yes, B can proceed against the assets of X. According to section 68 of Indian Contract Act, 1872, if a person, incapable of entering into a contract, or any one whom he is legally bound to support, is supplied by another person with necessaries suited to his condition in life, the person who has furnished such supplies is entitled to be reimbursed from the property of such incapable person.

Since the loan given to X is for the necessaries suited to the conditions in life of the minor, his assets can be sued to reimburse B.

42. Mr. SHYAM owned a motor car. He approached Mr. HARISH and offered to sell his motorcar for Rs. 3,00,000. Mr. SHYAM told Mr. HARISH that the motor car is running at the rate of 20 KMs per litre of petrol. Both the fuel meter and the speed meter of the car were working perfectly. Mr. HARISH agreed with the proposal of Mr. SHYAM and took delivery of the car by paying Rs. 3,00,000/- to Mr. SHYAM. After 10 days, Mr. HARISH came back with the car and stated that the claim made by Mr. SHYAM regarding fuel efficiency was not correct and therefore there was a case of misrepresentation. Referring to the provisions of the Indian Contract Act, 1872, decide and write whether Mr. HARISH can rescind the contract on the above ground.

Sol. As per the provisions of Section 19 of the Indian Contract Act, 1872, when consent to an agreement is caused by coercion, fraud or misrepresentation, the agreement is a contract voidable at the option of the party whose consent was so caused. A party to a contract, whose consent was caused by fraud or misrepresentation, may, if he thinks fit, insist that the contract shall be performed, and that he shall be put in the position in which he would have been if the representations made had been true.

Exception: If such consent was caused by misrepresentation or by silence, fraudulent within the meaning of section 17, the contract, nevertheless, is not voidable if the party whose consent was so

caused had the means of discovering the truth with ordinary diligence. In the situation given in the question, both the fuel meter and the speed meter of the car were working perfectly, Mr. HARISH had the means of discovering the truth with ordinary diligence. Therefore, the contract is not voidable. Hence, Mr. HARISH cannot rescind the contract on the above ground.

43. Chandan was suffering from some disease and was in great pain. He went to Dr. Jhunjhunwala whose consultation fee was Rs. 300. The doctor agreed to treat him but on the condition that Chandan had to sign a promissory note of Rs. 5000 payable to doctor. Chandan signed the promissory note and gave it to doctor. On recovering from the disease, Chandan refused to honour the promissory note. State with reasons, can doctor recover the amount of promissory note under the provisions of the Indian Contract Act, 1872?

Sol. Section 16 of Indian Contract Act, 1872 provides that a contract is said to be induced by "undue influence" where the relations subsisting between the parties are such that one of the parties is in a position to dominate the will of the other and uses that position to obtain an unfair advantage over the other

Further, a person is deemed to be in a position to dominate the will of another-

where he holds a real or apparent authority over the other, or where he stands in a fiduciary relation to the other; or where he makes a contract with a person whose mental capacity is temporarily or permanently affected by reason of age, illness, or mental or bodily distress. Section 19 A provides that when consent to an agreement is caused by undue influence, the agreement is a contract voidable at the option of the party whose consent was so caused. Any such contract may be set aside either absolutely or, if the party who was entitled to avoid it has received any benefit thereunder, upon such terms and conditions as to the Court may seem just. From the facts of the case, Chandan signed the promissory note under undue influence applied by doctor. Hence, Dr. Jhunjhunwala cannot recover the amount of promissory note but can claim his normal consultation fee from Chandan.

44. Point out with reason whether the following agreements are valid or void
- (i) Kamala promises Ramesh to lend Rs. 500,000 in lieu of consideration that Ramesh gets Kamala's marriage dissolved and he himself marries her.
 - (ii) Sohan agrees with Mohan to sell his black horse. Unknown to both the parties, the horse was dead at the time of agreement.
 - (iii) Ram sells the goodwill of his shop to Shyam for Rs. 4,00,000 and promises not to carry on such business forever and anywhere in India
 - (iv) In an agreement between Prakash and Girish, there is a condition that they will not institute legal proceedings against each other without consent.
 - (v) Ramamurthy, who is a citizen of India, enters into an agreement with an alien friend.

Sol. Validity of agreements

Void Agreement: As per Section 23 of the Indian Contract Act, 1872, an agreement is void if the object or consideration is against the public policy.

Void Agreement: As per Section 20 of the Indian Contract Act, 1872 the contracts caused by mistake of fact are void. There is mistake of fact as to the existence of subject-matter.

Void Agreement: As per Section 27 of the Indian Contract Act, 1872 an agreement in restraint of trade is void. However, a buyer can put such a condition on the seller of good will, not to carry on same business. However, the conditions must be reasonable regarding the duration and the place of the business.

Void Agreement: An agreement in restraint of legal proceedings is void as per Section 28 of the Indian Contract Act, 1872.

Valid Agreement: An agreement with alien friend is valid, but an agreement with alien enemy is void.

45. Mere silence does not amount to fraud". Discuss.

Sol. Mere silence is not fraud (General Rule)

A party to the contract is under no obligation to disclose the whole truth to the other party. 'Caveat Emptor' i.e. let the purchaser beware is the rule applicable to contracts. There is no duty to speak in such cases and silence does not amount to fraud. Similarly, there is no duty to disclose facts which are within the knowledge of both the parties.

Example: H sold to W some pigs which were to his knowledge suffering from fever. The pigs were sold 'with all faults and H did not disclose the fact of fever to W. Held there was no fraud. [Word vs. Hobbs. (1878)].

Example: A sells by auction to B, a horse which A knows to be unsound, A says nothing to B about the unsoundness of horse. This is not fraud by A.

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 the 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.

Silence is fraud when:

Duty of person to speak: Where the circumstances of the case are such that it is the duty of the person observing silence to speak. For example, in contracts of *uberrimae fidei* (contracts of utmost good faith). Following contracts come within this category:

Fiduciary Relationship: Here, the person in whom confidence is reposed is under a duty to act with utmost good faith and make full disclosure of all material facts concerning the agreement, known to him.

A broker was asked to buy shares for client. He sold his own shares without disclosing this fact. The client was entitled to avoid the contract or affirm it with a right to claim secret profit made by broker on the transaction since the relationship between the broker and the client was relationship of utmost good faith. (*Regier V. Campbell Staurt*)

Contracts of Insurance: In contracts of marine, fire and life insurance, there is an implied condition that full disclosure of material facts shall be made, otherwise the insurer is entitled to avoid the contract.

Contracts of marriage: Every material fact must be disclosed by the parties to a contract of marriage (*Hazi Ahmed v. Abdul Gassi*).

Contracts of family settlement: These contracts also require full disclosure of material facts within the knowledge of the parties.

Share Allotment contracts: Persons issuing ‘Prospectus’ at the time of public issue of shares/debentures by a joint stock company have to disclose all material facts within their knowledge.

Where the silence itself is equivalent to speech: For example, A says to B “If you do not deny it, I shall assume that the horse is sound.” A says nothing. His silence amounts to speech.

In case of fraudulent silence, contracts are not voidable if the party whose consent was so obtained had the means of discovering the truth with ordinary diligence (Exception to section 19).

46. Rahul, a minor, falsely representing his age, enters into an agreement with a shopkeeper for a loan amount for purchasing a laptop. He gave his expensive watch as a security and took a loan of Rs. 40,000. He was very happy to get Rs. 40,000 and quickly went to the market and purchased a laptop worth Rs. 30,000. He happily spent the rest of the amount with his friends on a pleasure trip.

Sol. As per Section 11 of Indian Contract Act, 1872, a minor is not competent to enter into any contract. Any agreement with minor is *void-ab-initio* means void from the very beginning. When a person forms an agreement with minor, such an agreement is devoid of any legal consequences for the person because minor cannot be enforced by law to perform his part of performance in an agreement.

However, if minor obtains any property by fraudulently misrepresenting his age, he can be ordered to restore the property or goods thus obtained. Although no action can be taken against the minor, but if has any property (of other party) in his possession, court can order him to return the same.

Hence, in the present case, Rahul is not liable to repay Rs. 40,000 that he has borrowed from the shopkeeper, but he can be ordered by the court to return the laptop (which was in his possession) to the shopkeeper.

47. “An agreement, the meaning of which is not certain, is void”. Discuss.

Sol. **Agreement - the meaning of which is uncertain (Section 29 of the Indian Contract Act, 1872):** An agreement, the meaning of which is not certain, is

void, but where the meaning thereof is capable of being made certain, the agreement is valid.

For example, A agrees to sell B “a hundred tons of oil”. There is nothing whatever to show what kind of oil was intended. The agreement is void for uncertainty. But the agreement would be valid if A was dealer only in coconut oil because in such a case its meaning would be capable of being made certain.

48. Ishaan, aged 16 years, was studying in an engineering college. On 1st March, 2016 he took a loan of Rs. 2 lakhs from Vishal for the payment of his college fee and agreed to pay by 30th May, 2017. Ishaan possesses assets worth Rs. 15 lakhs. On due date Ishaan fails to pay back the loan

Sol. According to Section 11 of the Indian Contract Act, 1872, every person is competent to contract who is of the age of majority according to the law to which he is subject, and who is of sound mind and is not disqualified from contracting by any law to which he is subject. A person who has completed the age of 18 years is a major and otherwise he will be treated as minor. Thus, Ishaan who is a minor is incompetent to contract and any agreement with him is void [*Mohori Bibi Vs Dharmo Das Ghose 1903*].

Section 68 of the Indian Contract Act, 1872 however, prescribes the liability of a minor for the supply of the things which are the necessities of life to him. It says that though minor is not personally liable to pay the price of necessities supplied to him or money lent for the purpose, the supplier or lender will be entitled to claim the money/price of goods or services which are necessities suited to his condition of life provided that the minor has a property. The liability of minor is only to the extent of the minor’s property. Thus, according to the above provision, Vishal will be entitled to recover the amount of loan given to Ishaan for payment of the college fees from the property of the minor.

49. Kapil went to a departmental store to purchase a steel pan. He asked the salesman about the area in departmental store where steel pans are kept. The salesman indicated him the area with instructions that with steel pans, other metal’s pans were also kept. Kapil wrongfully picked an aluminum pan in place of steel pan. The salesman watched but said nothing to Kapil. Kapil reached his house and found that pan was

not a steel pan but actually an aluminum pan. Kapil filed a suit against departmental store for fraud. Discuss, whether Kapil was eligible to file suit for fraud against departmental store under Indian Contract Act, 1872?

Sol. Section 17 of Indian Contract Act, 1872 defines 'Fraud'. According to section, "Fraud" means and includes any of the following acts committed by a party to a contract or by his agent with intent to deceive or to induce a person to enter into the contract:

- the suggestion, as a fact, of that which is not true, by one who does not believe it to be true;
- the active concealment of a fact by one having knowledge or belief of the fact;
- a promise made without any intention of performing it;
- any other act fitted to deceive;
- any such act or omission as the law specially declares to be fraudulent.

It was also explained that mere silence is not fraud. Silence amounts to fraud where (a) there is a duty to speak or (b) where silence is equivalent to speech. On the basis of provisions of Section 17 and the facts given above, it was not the duty of salesman to inform Mr. Kapil about his mistake. Hence, there was no fraud and Kapil was not eligible to file suit for fraud against departmental store under Indian Contract Act, 1872.

50. Mr. Shekhar wants to sell his car. For this purpose, he appoints Mr. Nadan, a minor as his agent. Mr. Shekhar instructs Mr. Nadan that car should not be sold at price less than Rs. 1,00,000. Mr. Nadan ignores the instruction of Mr. Shekhar and sells the car to Mr. Masoom for Rs. 80,000. Explain

Sol. According to the provisions of Section 11 of the Indian Contract Act, 1872, a minor is disqualified from contracting. A contract with minor is *void-ab-initio* but minor can act as an agent. But he will **not be liable to his principal for his acts.**

In the instant case, Mr. Shekhar appoints Mr. Nadan, a minor as his agent to sell his car. Mr. Shekhar clearly instructed to Mr. Nadan that the minimum sale price of the car should be Rs. 1,00,000 yet Mr. Nadan sold the car to Mr. Masoom for Rs. 80,000.

- Considering the facts, although the contract between Mr. Shekhar and Mr. Nadan is valid, Mr. Nadan will not be liable to his principal for his acts. Hence, Mr. Shekhar cannot recover the loss of Rs. 20,000.
- Further, Mr. Masoom purchased the car from agent of Mr. Shekhar, he got good title. Hence, Mr. Shekhar cannot recover his car from Mr. Masoom.

51. Point out with reason whether the following agreements are valid or void:

- (i) Riya promises Samarth to lend Rs. 500,000 in lieu of consideration that Samarth gets Riya's marriage dissolved and he himself marries her.
- (ii) Aryan agrees with Mathew to sell his black horse. Unknown to both the parties, the horse was dead at the time of agreement.
- (iii) Ravi sells the goodwill of his shop to Shyam for Rs. 4,00,000 and promises not to carry on such business forever and anywhere in India.
- (iv) In an agreement between Prakash and Girish, there is a condition that they will not institute legal proceedings against each other without consent.

Sol. Validity of agreements

- *Void Agreement:* As per Section 23 of the Indian Contract Act, 1872, an agreement is void if the object or consideration is against the public policy.
- *Void Agreement:* As per Section 20 of the Indian Contract Act, 1872 the contracts caused by mistake of fact are void. There is mistake of fact as to the existence of subject matter.
- *Void Agreement:* As per Section 27 of the Indian Contract Act, 1872 an agreement in restraint of trade is void. However, a buyer can put such a condition on the seller of good will, not to carry on same business. However, the conditions must be reasonable regarding the duration and the place of the business.
- *Void Agreement:* An agreement in restraint of legal proceedings is void as per Section 28 of the Indian Contract Act, 1872.

52. Rohan is running a grocery store in Delhi. He sells his grocery business, including goodwill worth Rs. 1,00,000 to Rohit for a sum of Rs. 5,00,000. After the

sale of goodwill, Rohit made an agreement with Rohan. As per this agreement, Rohan is not to open another grocery store (similar kind of business) in the whole of India for next ten years. However, Rohan opens another store in the same city two months later. What are the rights available with Rohit regarding the restriction imposed on Rohan with reference to Indian Contract Act, 1872?

Sol. Section 27 of the Indian Contract Act, 1872 provides that any agreement that restrains a person from carrying on a lawful trade, profession or business is void agreement. However, there are certain exceptions to this rule. One of the statutory exceptions includes sale of Goodwill. The restraint as to sale of goodwill would be a valid restraint provided-

- Where the restraint is to refrain from carrying on a similar business
- The restraint should be within the specified local limits

- The restraint should be not to carry on the similar business after sale of goodwill to the buyer for a price
- The restriction should be reasonable. Reasonableness of restriction will depend upon number of factors as considered by court.
- In the given case, Rohan has sold the goodwill and there is restraint for not carrying on the same business of grocery store. However the restriction imposed on Rohan **is unreasonable as he cannot carry similar business in whole of India for next 10 years.** The restriction on restraint to similar kind of trade should be reasonable to make it a valid agreement. Therefore, Rohit cannot take any legal action against Rohan as the restriction is unreasonable as per Section 27 of Indian Contract Act, 1872. Hence, the agreement made between Rohan and Rohit in restraint of trade is void agreement.

Sampurna (CA-Foundation)

PERFORMANCE OF CONTRACT

53. A, B, C and D are the four partners in a firm. They jointly promised to pay Rs. 6,00,000 to F. B and C have become insolvent. B was unable to pay any amount and C could pay only Rs. 50,000. A is compelled to pay the whole amount to F. Decide the extent to which A can recover the amount from D with reference to the provisions of the Indian Contract Act, 1872.

Sol. Joint promisors (Section 42 of the Indian Contract Act, 1872) When two or more persons have made a joint promise, then unless a contrary intention appears by the contract, all such persons must jointly fulfil the promise.

Any one of joint promisors may be compelled to perform (Section 43)

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 any one or more of such joint promisors to perform the whole of the promise.

If any one of two or more joint promisors makes default in such contribution, the remaining joint promisors must bear the loss arising from such default in **equal shares**.

In the instant case, A, B, C and D have jointly promised to pay Rs. 6,00,000 to F. B and C become insolvent. B was unable to pay any amount and C could pay only Rs. 50,000. A is compelled to pay the whole amount to F.

Hence, A is entitled to receive Rs. 50,000 from C and Rs. 2,75,000 from D, as worked out below:

From C Rs. 50,000= (C's Liability Rs. 1,50,000
Less: Amount he could not pay Rs. 1,00,000).

From D Rs. 2,75,000= (D's Liability Rs. 1,50,000 + 1/2 of liability of B (Loss) $(1,50,000 \times 1/2)$ i.e. Rs. 75,000 + 1/2 of C's liability (Loss) $(1,00,000 \times 1/2)$ i.e., Rs. 50,000) In other words, equal proportion i.e., Rs. 5,50,000 (i.e. Rs. 6,00,000 – Rs. 50,000) / 2.

54. Explain any five circumstances under which contracts need not be performed with the consent of both the parties

Sol. Under following circumstances, the contracts need not be performed with the consent of both the parties:

- (i) **Novation:** Where the parties to a contract substitute a new contract for the old, it is called novation. A contract in existence may be substituted by a new contract either between the same parties or between different parties the consideration mutually being the discharge of old contract. Novation can take place only by mutual agreement between the parties. On novation, the old contract is discharged and consequently it need not be performed. (Section 62 of the Indian Contract Act, 1872)
- (ii) **Rescission:** A contract is also discharged by rescission. When the parties to a contract agree to rescind it, the contract need not be performed. (Section 62)
- (iii) **Alteration:** Where the parties to a contract agree to alter it, the original contract is rescinded, with the result that it need not be performed. In other words, a contract is also discharged by alteration. (Section 62)
- (iv) **Remission:** Every promisee may dispense with or remit, wholly or in part, the performance of the promise made to him, or may extend the time for such performance or may accept instead of it any satisfaction which he thinks fit. In other words, a contract is discharged by remission. (Section 63)
- (v) **Rescinds voidable contract:** When a person at whose option a contract is voidable rescinds it, the other party thereto need not perform any promise therein contained in which he is the promisor. **Neglect of promise:** If any promise neglects or refuses to afford the promisor reasonable facilities for the performance of his promise, the promisor is excused by such neglect or refusal as to any non-performance caused thereby. (Section 67)



55. X, Y and Z jointly borrowed Rs. 90,000 from L. Decide each of the following in the light of the Indian Contract Act, 1872:

Sol. (i) Yes, L can compel only Y to pay Rs. 90,000/- since as per Section 43 of the Indian Contract Act, 1872, in the absence of express agreement to the contrary, the promise may compel any one or more of the joint promisors to perform the whole of the promise.

(ii) As per Section 42, when two or more persons have made a joint promise, then, unless a contrary intention appears by the contract, all such persons, during their joint lives and after the death of any of them, his representative jointly with the survivor or survivors and after the death of last survivor, the representatives of all jointly must fulfill the promise.

In the instant case, if X, Y and Z died then the legal representatives of all (i.e. X, Y and Z) shall be liable to pay the loan jointly. L cannot compel only the legal representatives of Y to pay the loan of Rs. 90,000.

(iii) According to Section 44, where two or more persons have made a joint promise, a release of one of such joint promisors by the promise does not discharge the other joint promisor or joint promisors, neither does it free the joint promisors so released from responsibility to the other joint promisor or promisors.

In this case, the release of X does not discharge Y and Z from their liability. Y and Z remain liable to pay the entire amount of Rs. 90,000 to L. And though X is not liable to pay to L, but he remains liable to pay to Y and Z i.e. he is liable to make the contribution to the other joint promisors.

56. Explain what is meant by 'Supervening Impossibility' as per the Indian Contract Act, 1872 with the help of an example. What is the effect of such impossibility?

Sol. According to Section 56 of the Indian Contract Act, 1872, the impossibility of performance may be of the two types, namely (a) initial impossibility, and (b) subsequent impossibility.

Subsequent impossibility is also known as Supervening impossibility i.e. becomes impossible after entering into contract. When performance of promise become impossible or illegal by occurrence

of an unexpected event or a **change of circumstances beyond the contemplation of parties**, the contract becomes void e.g. change in law etc. In other words, sometimes, the performance of a contract is quite possible when it is made. But subsequently, some event happens which renders the performance impossible or unlawful. **Such impossibility is called the subsequent or supervening. It is also called the post-contractual impossibility.**

Example: 'A' and 'B' contracted to marry each other. Before the time fixed for the marriage, 'A' became mad. In this case, the contract becomes void due to subsequent impossibility, and thus discharged.

Effect of impossibility: The effect of such impossibility is that it makes the contract void, and the parties are discharged from further performance of the contract.

X, Y and Z are partners in a firm. They jointly promised to pay Rs. 3,00,000 to D. Y become insolvent and his private assets are sufficient to pay 1/5 of his share of debts. X is compelled to pay the whole amount to D. Examining the provisions of the Indian Contract Act, 1872, decide the extent to which X can recover the amount from Z.

As per section 43 of the Indian Contract Act, 1872, when two or more persons make a joint promise, the promisee may, in the absence of express agreement to the contrary, compel any one or more of such joint promisors to perform the whole of the promise.

Each of two or more joint promisors may compel every other joint promisor to contribute equally with himself to the performance of the promise, unless a contrary intention appears from the contract.

If any one of two or more joint promisors makes default in such contribution, the remaining joint promisors **must bear the loss arising from such default in equal shares.**

In the instant case, X, Y and Z jointly promised to pay Rs. 3,00,000. Y become insolvent and his private assets are sufficient to pay 1/5 of his share of debts. X is compelled to pay the whole amount. X is entitled to receive Rs. 20,000 from Y's estate, and Rs. 1,40,000 from Z.

57. Mr. Rich aspired to get a self-portrait made by an artist. He went to the workshop of Mr. C an artist and asked whether he could sketch the former's portrait on oil painting canvass. Mr. C agreed to the offer and asked for Rs. 50,000 as full advance payment for the above creative work. Mr. C clarified that the painting shall be completed in 10 sittings and shall take 3 months.

On reaching to the workshop for the 6th sitting, Mr. Rich was informed that Mr. C became paralyzed and would not be able to paint for near future. Mr. C had a son Mr. K who was still pursuing his studies and had not taken up his father's profession yet?

Discuss in light of the Indian Contract Act, 1872?

- (1) Can Mr. Rich ask Mr. K to complete the artistic work in lieu of his father?
- (2) Could Mr. Rich ask Mr. K for refund of money paid in advance to his father?

Sol. A contract which involves the use of personal skill or is founded on personal consideration **comes to an end on the death of the promisor**. As regards any other contract the legal representatives of the deceased promisor are bound to perform it unless a contrary intention appears from the contract (Section 37 of the Indian Contract Act, 1872). But their liability under a contract is limited to the value of the property they inherit from the deceased.

- (1) In the instant case, since painting involves the use of personal skill and on becoming Mr. C paralyzed, Mr. Rich cannot ask Mr. K to complete the artistic work in lieu of his father Mr. C.
- (2) According to section 65 of the Indian Contract Act, 1872, when an agreement is discovered to be void or when a contract becomes void, any person who has received any advantage under such agreement or contract is bound to restore it, or to make compensation for it to the person from whom he received it.

Hence, in the instant case, the agreement between Mr. Rich and Mr. C has become void because of paralysis to Mr. C. So, Mr. Rich can ask Mr. K for refund of money paid in advance to his father, Mr. C.

58. Mr. X and Mr. Y entered into a contract on 1st August, 2018, by which. Mr. X had to supply 50 tons of sugar to Mr. Y at a certain price strictly within a

period of 10 days of the contract. Mr. Y also paid an amount of Rs. 50,000 towards advance as per the terms of the above contract. The mode of transportation available between their places is roadway only. Severe flood came on 2nd August, 2018 and the only road connecting their places was damaged and could not be repaired within fifteen days. Mr. X offered to supply sugar on 20th August, 2018 for which Mr. Y did not agree. On 1st September, 2018, Mr. X claimed compensation of Rs. 10,000 from Mr. Y for refusing to accept the supply of sugar, which was not there within the purview of the contract. On the other hand, Mr. Y claimed for refund of Rs. 50,000 which he had paid as advance in terms of the contract. Analyse the above situation in terms of the provisions of the Indian Contract Act, 1872 and decide on Y's contention.

Sol. Subsequent or Supervening impossibility (Becomes impossible after entering into contract):

When performance of promise become impossible or illegal by occurrence of an unexpected event or a change of circumstances beyond the contemplation of parties, the contract becomes void e.g. change in law etc. Also, according to section 65 of the Indian Contract Act, 1872, when an agreement is discovered to be void or when a contract becomes void, any person who has received any advantage under such agreement or contract is bound to restore it, or to make compensation for it to the person from whom he received it.

In the given question, after Mr. X and Mr. Y have entered into the contract to supply 50 tons of sugar, the event of flood occurred which made it impossible to deliver the sugar within the stipulated time. Thus, the promise in question became void. Further, Mr. X has to pay back the amount of Rs. 50,000 that he received from Mr. Y as an advance for the supply of sugar within the stipulated time. Hence, the contention of Mr. Y is correct.

59. Mr. Sonumal a wealthy individual provided a loan of Rs. 80,000 to Mr. Datumal on 26.02.2019. The borrower Mr. Datumal asked for a further loan of Rs. 1,50,000. Mr. Sonumal agreed but provided the loan in parts at different dates. He provided Rs. 1,00,000 on 28.02.2019 and remaining Rs. 50,000 on 03.03.2019. On 10.03.2019 Mr. Datumal while paying off part Rs. 75,000 to Mr. Sonumal insisted that the lender should adjusted Rs. 50,000 towards the loan taken on 03.03.2019 and balance as against the loan on 26.02.2019. Mr. Sonumal objected to this

arrangement and asked the borrower to adjust in the order of date of borrowal of funds.

Now you decide:

- (1) Whether the contention of Mr. Datumal correct or otherwise as per the provisions of the Indian Contract Act, 1872?
- (2) What would be the answer in case the borrower does not insist on such order of adjustment of repayment?
- (3) What would the mode of adjustment/appropriation of such part payment in case neither Mr. Sonumal nor Mr. Datumal insist any order of adjustment on their part?

Sol. Appropriation of Payments: In case where a debtor owes several debts to the same creditor and makes payment which is not sufficient to discharge all the debts, the payment shall be appropriated (i.e. adjusted against the debts) as per the provisions of Section 59 to 61 of the Indian Contract Act, 1872.

- (1) As per the provisions of 59 of the Act, where a debtor owing several distinct debts to one person, makes a payment to him either with **express intimation** or under circumstances implying that the payment is to be applied to the discharge of some particular debt, the payment, if accepted, must be applied accordingly.

Therefore, the contention of Mr. Datumal is correct and he can specify the manner of appropriation of repayment of debt.

- (2) As per the provisions of 60 of the Act, where the debtor has omitted to intimate and there are no other circumstances indicating to which debt the payment is to be applied, the creditor may apply it at his discretion to any lawful debt actually due and payable to him from the debtor, where its recovery is or is not barred by the law in force for the time being as to the limitation of suits. Hence in case where Mr. Datumal fails to specify the manner of appropriation of debt on part repayment, Mr. Sonumal the creditor, can appropriate the payment as per his choice.
- (3) As per the provisions of 61 of the Act, where neither party makes any appropriation, the payment shall be applied in discharge of the debts in order of time, whether they are or are not barred by the law in force for the time

being as to the limitation of suits. If the debts are of equal standing, the payments shall be applied in discharge of each proportionately.

Hence in case where neither Mr. Datumal nor Mr. Sonumal specifies the manner of appropriation of debt on part repayment, the appropriation can be made in proportion of debts.

60. Mr. S and Mr. R made contract wherein Mr. S agreed to deliver paper cup manufacture machine to Mr. R and to receive payment on delivery. On the delivery date, Mr. R didn't pay the agreed price. Decide whether Mr. S is bound to fulfil his promise at the time of delivery?

Sol. As per Section 51 of the Indian Contract Act, 1872, when a contract consists of reciprocal promises to be simultaneously performed, no promisor needs to perform his promise unless the promisee is ready and willing to perform his reciprocal promise. Such promises constitute concurrent conditions and the performance of one of the promises is conditional on the performance of the other. If one of the promises is not performed, the other too need not be performed. Referring to the above provisions, in the given case, Mr. S is not bound to deliver goods to Mr. R since payment was not made by him at the time of delivery of goods

61. 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 However, A was not aware of the payment. Now B is intending to sue A for the amount of Rs. 1,00,000. Discuss whether the contention of B is right?

Sol. 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 authorized 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.

62. Decide with reasons whether the following agreements are valid or void under the provisions of the Indian Contract Act, 1872:

- (1) Vijay agrees with Saini to sell his black horse for Rs. 3,00,000. Unknown to both the Parties, the horse was dead at the time of the agreement.
- (2) Sarvesh sells the goodwill of his shop to Vikas for Rs. 10,00,000 and promises not to carry on such business forever and anywhere in India.
- (3) Mr. X agrees to write a book with a publisher. After few days, X dies in an accident.

Sol. (1) As per Section 20 of the Indian Contract Act, 1872, an agreement under by mistake of fact are void. In this case, there is mistake of fact as to the existence of the subject- matter, i.e., with respect to the selling of horse which was dead at the time of the agreement. It is unknown to both the parties. Therefore, **it is a void agreement.**

- (2) As per Section 27 of the Indian Contract Act, 1872, an agreement in restraint of trade is void. However, a buyer can put such a condition on the seller of goodwill, not to carry on same business, provided that the conditions must be reasonable regarding the duration and place of the business. Since in the given case, **restraint to carry on business was forever and anywhere in India, so the agreement in question is void.**

- (3) As per section 2(j) of the Contract Act, “A contract which ceases to be enforceable by law becomes void when it ceases to be enforceable”. In the present case, Mr. X agrees to write a book with a publisher. After few days, X dies in an accident. Here **the contract becomes void** due to the impossibility of performance of the contract.

63. “The basic rule is that the promisor must perform exactly what he has promised to perform.” Explain stating the obligation of parties to contracts.

Sol. Obligations of parties to contracts (Section 37 of the Indian Contract Act, 1872)

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 Rs. 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 Rs. 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 representatives 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.** Thus, from above it can be drawn that performance may be actual or offer to perform.

64. What will be rights with the promisor in following cases? Explain with reasons:

- (1) Mr. X promised to bring back Mr. Y to life again.
- (2) An agreed to sell 50 kgs of apple to B. The loaded truck left for delivery on 15th March but due to riots in between reached B on 19th March.

- (3) An artist promised to paint on the fixed date for a fixed amount of remuneration but met with an accident and lost his both hands.
- (4) Abhishek entered into contract of import of toys from China. But due to disturbance in the relation of both the countries, the imports from China were banned.

- Sol.**
- (1) Abhishek entered into contract of import of toys from China. But due to disturbance in the relation of both the countries, the imports from China were banned.
 - (2) The contract is **void because of its initial impossibility** of performance.
 - (3) **Time is essence of this contract.** As by the time apples reached B, they were already rotten. The **contract is discharged due to destruction** of subject matter of contract.
 - (i) Such contract is of personal nature and hence cannot be performed due to occurrence of an event resulting in impossibility of performance of contract.
 - (ii) Such contract is discharged without performance because of subsequent illegality nature of the contract.

- 65.** A enters into a contract with B that he (A) sells his house for Rs. 10,00,000 to B. Further they both signed an agreement that if B uses the house for gambling purposes, then B shall pay A Rs. 50,000 for it. B agreed to this, however after a year of sale, B started gambling business in that house. Can A claim Rs. 50,000 from B? Discuss with reference to the provisions of Indian Contract Act, 1872.

Sol. According to Section 24 of the Indian Contract Act, 1872, in an agreement, where some part of the object is legal and the other part is illegal, the question arises about the validity and enforceability of such agreements. Where the legal and illegal part can be severed and divided, and separated, lawful part of object is enforceable, and the unlawful part of the object is void.

In the given case, A sells the house to B, is a valid transaction as the sale of house and consideration paid for the same i.e. Rs.10,00,000 is valid and enforceable. However, the agreement to pay Rs. 50,000 for gambling done in the house is illegal and thus void.

Hence, in the instant case, sale of house agreement is valid agreement and gambling agreement is illegal and not enforceable by law.

- 66.** Mr. Singhanian entered into a contract with Mr. Sonu to sing in his hotel for six weeks on every Saturday and Sunday. Mr. Singhanian promised to pay Rs. 20,000 for every performance. Mr. Sonu performed for two weeks but on third week his health condition was very bad, so he did not come to sing. Mr. Singhanian terminated the contract. State in the light of provisions of the Indian Contract Act, 1872:-

Sol. According to Section 40 of the Indian Contract Act, 1872, if it appears from the nature of the case that it was the intention of the parties to any contract that any promise contained in it should be performed by the promisor himself, such promise must be performed by the promisor. Section 41 provides that when a promisee accepts performance of the promise from a third person, he cannot afterwards enforce it against the promisor.

Therefore, in the instant case,

- (1) As Mr. Sonu could not perform as per the contract, Mr. Singhanian can repudiate the contract.
- (2) In the second situation, as Mr. Singhanian allowed Mr. Sonu to perform in the fourth week without saying anything, by conduct, Mr. Singhanian had given his assent to continue the contract. Mr. Singhanian cannot terminate the contract however he can claim damages from Mr. Sonu.
- (3) In case Mr. Singhanian allows Mr. Mika to perform in the third week without saying anything, by conduct, Mr. Singhanian had given his assent for performance by third party. Now Mr. Singhanian cannot terminate the contract nor can claim any damages from Mr. Sonu.

- 67.** Ajay, Vijay and Sanjay are partners of software business and jointly promises to pay Rs. 6,00,000 to Kartik. Over a period of time Vijay became insolvent, but his assets are sufficient to pay one-fourth of his debts. Sanjay is compelled to pay the whole. Decide whether Sanjay is required to pay whole amount himself to Kartik in discharging joint promise under the Indian Contract Act, 1872.

Sol. As per section 43 of the Indian Contract Act, 1872, when two or more persons make a joint promise, the promisee may, in the absence of express agreement to the contrary, compel any one or more of such joint promisors to perform the whole of the promise.

Each of two or more joint promisors may compel every other joint promisor to contribute equally with himself to the performance of the promise, unless a contrary intention appears from the contract.

If any one of two or more joint promisors makes default in such contribution, the remaining joint promisors must bear the loss arising from such default in equal shares.

Therefore, in the instant case, Sanjay is entitled to receive Rs. 50,000 from Vijay's assets and Rs. 2,75,000 from Ajay.

68. X, Y and Z jointly borrowed Rs. 50,000 from A. The whole amount was repaid to A by Y. Decide in the light of the Indian Contract Act, 1872 whether:

- (1) Y can recover the contribution from X and Z,
- (2) Legal representatives of X are liable in case of death of X,
- (3) Y can recover the contribution from the assets, in case Z becomes insolvent.

Sol. Section 42 of the Indian Contract Act, 1872 requires that when two or more persons have made a joint promise, then, unless a contrary intention appears from the contract, all such persons jointly must fulfill the promise. In the event of the death of any of them, his representative jointly with the survivors and in case of the death of all promisors, the representatives of all jointly must fulfill the promise.

Section 43 allows the promisee to seek performance from any of the joint promisors. The liability of the joint promisors has thus been made not only joint but "joint and several". Section 43 provides that in the absence of express agreement to the contrary, the promisee may compel any one or more of the joint promisors to perform the whole of the promise.

Section 43 deals with the contribution among joint promisors. The promisors, may compel every joint promisor to contribute equally to the performance of the promise (unless a contrary intention appears from the contract). If any one of the joint promisors makes default in such contribution the remaining joint

promisors must bear the loss arising from such default in equal shares.

As per the provisions of above sections,

- (1) Y can recover the contribution from X and Z because X, Y and Z are joint promisors.
- (2) Legal representative of X are liable to pay the contribution to Y. However, a legal representative is liable only to the extent of property of the deceased received by him.
- (3) Y also can recover the contribution from Z's assets.

69. State the grounds upon which a contract may be discharged under the provisions of the Indian Contract Act, 1872.

Sol. Discharge of a Contract:

- (i) A contract may be discharged in any one of the following ways:

Discharge by performance: It takes place when the parties to the contract fulfil their obligations arising under the contract within the time and in the manner prescribed. Discharge by performance may be

- (1) Actual performance; or
- (2) Attempted performance.

Actual performance is said to have taken place, when each of the parties has done what he had agreed to do under the agreement. When the promisor offers to perform his obligation, but the promisee refuses to accept the performance, it amounts to **attempted performance** or tender.

Example: A contracts to sell his car to B on the agreed price. As soon as the car is delivered to B and B pays the agreed price for it, the contract comes to an end by performance.

Example: A contracted to supply certain quantity of timber to B. B made the supply of timber at appointed time and place but A refused to accept the delivery. This is called as attempted performance

- (ii) **Discharge by mutual agreement:** Section 62 of the Indian Contract Act provides if the parties to a contract agree to substitute a new contract for it, or to rescind or remit or alter it, the original contract need not be performed. The principles of Novation, Rescission, Alteration and Remission are already discussed.

Example : A owes B Rs. 1,00,000. A enters into an agreement with B and mortgage his (A's), estates for Rs. 50,000 in place of the debt of Rs. 1,00,000. This is a new contract and extinguishes the old.

Example : A owes B Rs. 5,00,000. A pays to B Rs. 3,00,000 who accepts it in full satisfaction of the debt. The whole is discharged.

(iii) **Discharge by impossibility of performance:** The impossibility may exist from the very start. In that case, it would be impossibility ab initio/Initial impossibility. Alternatively, it may supervene. Supervening impossibility / Post Contractual impossibility may take place owing to:

- an unforeseen change in law;
- the destruction of the subject-matter essential to that performance;
- the non-existence or non-occurrence of particular state of things, which was naturally contemplated for performing the contract, as a result of some personal incapacity like dangerous malady;
- the declaration of a war (Section 56).

Example: A agrees with B to discover a treasure by magic. The agreement is void due to initial impossibility.

Example: A and B contract to marry each other. Before the time fixed for the marriage, A goes mad. The contract becomes void.

Example: A contracts to act at a theatre for six months in consideration of a sum paid in advance by B. On several occasions A is too ill to act. The contract to act on those occasions becomes void.

Example: X agrees to sell his horse to Y for Rs. 5,000 but the horse died in an accident. Here, it become impossible to perform the contract due to destruction of the subject. Thus, a valid contract changes into void contract because of impossibility of performance

(i) **Discharge by lapse of time:** A contract should be performed within a specified period as prescribed by the Limitation Act, 1963. If it is not performed and if no action is taken by the promisee within the specified period of limitation, he is deprived of remedy at law.

Example : If a creditor does not file a suit against the buyer for recovery of the price within three years, the debt becomes time-barred and hence irrecoverable.

(ii) **Discharge by operation of law:** A contract may be discharged by operation of law which includes by death of the promisor, by insolvency etc.

(iii) **Discharge by breach of contract:** Breach of contract may be actual breach of contract or anticipatory breach of contract. If one party defaults in performing his part of the contract on the due date, he is said to have committed breach thereof. When on the other hand, a person repudiates a contract before the stipulated time for its performance has arrived, he is deemed to have committed anticipatory breach. If one of the parties to a contract breaks the promise the party injured thereby, has not only a right of action for damages but he is also discharged from performing his part of the contract.

Example: A contracted with B to supply 100 kgs of rice on 1st June. But A failed to deliver the same on said date. This is actual breach of contract. If time is not essential essence of contract B can give him another date for supply of goods and he will not be liable to claim for any damages if prior notice for the same is not given to A while giving another date.

(iv) **Promisee may waive or remit performance of promise:** Every promisee may dispense with or remit, wholly or in part, the performance of the promise made to him, or may extend the time for such performance or may accept instead of it any satisfaction which he thinks fit. In other words, a contract may be discharged by remission. (Section 63)

Example : A owes B Rs. 5,00,000. C pays to B Rs. 1,00,000 and B accepts them, in satisfaction of his claim on A. This payment is a discharge of the whole claim.

(v) **Effects of neglect of promisee to afford promisor reasonable facilities for performance:** If any promisee neglects or refuses to afford the promisor reasonable facilities for the performance of his promise,

the promisor is excused by such neglect or refusal as to any non-performance caused thereby. (Section 67)

- (vi) **Merger of rights:** Sometimes, the inferior rights and the superior rights coincide and meet in one and the same person. In such cases, the inferior rights merge into the superior rights. On merger, the inferior rights vanish and are not required to be enforced.

A took a land on lease from B. Subsequently, A purchases that very land. Now, A becomes the owner of the land and the ownership rights being superior to rights of a lessee, the earlier contract of lease stands terminated.

Example: A took a land on lease from B. Subsequently, A purchases that very land. Now, A becomes the owner of the land and the ownership rights being superior to rights of a lessee, the earlier contract of lease stands terminated.

70. Mr. Murari owes payment of 3 bills to Mr. Girdhari as on 31st March, 2020. (i) Rs. 12,120 which was due in May 2016. (ii) Rs. 5,650 which was due in August 2018 (iii) Rs. 9,680 which was due in May 2019. Mr. Murari made payment on 1st April 2020 as below without any notice of how to appropriate them:

- (1) A cheque of Rs. 9,680
- (2) A cheque of Rs. 15,000

- Sol.** Advice under the provisions of the Indian Contract Act, 1872.

If the performance consists of payment of money and there are several debts to be paid, the payment shall be appropriated as per provisions of Sections 59, 60 and 61 of the Indian Contract Act, 1872.

- (1) The debtor has, at the time of payment, the right of appropriating the payment.
- (2) In default of debtor, the creditor has option of election and
- (3) in default of either the law will allow appropriation of debts in order of time.

In the present case, Mr. Murari had made two payments by way of two cheques. One cheque was exactly the amount of the bill drawn. It would be understood even though not specifically appropriated by Mr. Murari that it will be against the bill of exact amount. Hence cheque of Rs. 9,680 will be

appropriated against the bill of Rs. 9,680 which was due in May 2019.

Cheque of Rs. 15000 can be appropriated against any lawful debt which is due even though the same is time-barred.

Hence, Mr. Girdhari can appropriate the same against the debt of Rs. 12,120 which was due in 2016 and balance against Rs. 5650 which was due in August 2018.

71. Enumerate the persons by whom a contract may be performed under the provisions of the Indian Contract Act, 1872.

Sol. As per section 40 of the Indian Contract Act, 1872, the promise under a contract may be performed, as the circumstances may permit, by the promisor himself, or by his agent or his legal representative.

- i. **Promisor himself:** If there is something in the contract to show that it was the intention of the parties that the promise should be performed by the promisor himself, such promise must be performed by the promisor. This means contracts which involve the exercise of personal skill or diligence, or which are founded on personal confidence between the parties must be performed by the promisor himself.
- ii. **Agent:** Where personal consideration is not the foundation of a contract, the promisor or his representative may employ a competent person to perform it.
- iii. **Legal Representatives:** A contract which involves the use of personal skill or is founded on personal consideration comes to an end on the death of the promisor. As regards any other contract the legal representatives of the deceased promisor are bound to perform it unless a contrary intention appears from the contract. But their liability under a contract is limited to the value of the property they inherit from the deceased.
- iv. **Third persons:** 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 authorized nor ratified the act of the third party.



- v. **Joint promisors:** When two or more persons have made a joint promise, then unless a contrary intention appears by the contract, all such persons must jointly fulfill the promise. If any of them dies, his legal representatives must, jointly with the surviving promisors, fulfill the promise. If all of them die, the legal representatives of all of them must fulfill the promise jointly

72. Mr. JHUTH entered into an agreement with Mr. SUCH to purchase his (Mr. SUCH's) motor car for Rs. 5,00,000/- within a period of three months. A security amount of Rs. 20,000/- was also paid by Mr. JHUTH to Mr. SUCH in terms of the agreement. After completion of three months of entering into the agreement, Mr. SUCH tried to contract Mr. JHUTH to purchase the car in terms of the agreement. Even after lapse of another three-month period, Mr. JHUTH neither responded to Mr. SUCH, nor to his phone calls. After lapse of another period of six months. Mr. JHUTH contracted Mr. SUCH and denied to purchase the motor car. He also demanded back the security amount of Rs. 20,000/- from Mr. SUCH. Referring to the provisions of the Indian Contract Act, 1872, state whether Mr. SUCH is required to refund the security amount to Mr. JHUTH.

Also examine the validity of the claim made by Mr. JHUTH, if the motor car would have destroyed by an accident within the three month's agreement period.

- Sol.** In terms of the provisions of Section 65 of the Indian Contract Act, 1872, when an agreement is discovered to be void or when a contract becomes void, any person who has received any advantage under such agreement or contract is bound to restore it, or to make compensation for it to the person from whom he received it.

Referring to the above provision, we can analyse the situation as under :-

The contract is not a void contract. Mr. SUCH is not responsible for Mr. JHUTH's negligence. Therefore, Mr. SUCH can rescind the contract and retain the security amount since the security is not a benefit received under the contract, it is a security that the purchaser would fulfill his contract and is ancillary to the contract for the sale of the Motor Car.

Regarding the second situation given in the question, the agreement becomes void due to the destruction of the Motor car, which is the subject matter of the agreement here. Therefore, the security amount received by Mr. SUCH is required to be refunded back to Mr. JHUTH.

Sampurna (CA-Foundation)

BREACH OF CONTRACT & ITS REMEDIES

73. “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.

Sol. 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. Dela Tour:**

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.”

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

- 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
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.

74. “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.

Sol. 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 calculation 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.

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 Chunni Lal 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.

75. ‘X’ entered into a contract with ‘Y’ to supply him 1,000 water bottles @ Rs. 5.00 per water bottle, to be delivered at a specified time. Thereafter, ‘X’ contracts with ‘Z’ for the purchase of 1,000 water bottles @ Rs. 4.50 per water bottle, and at the same

time told 'Z' that he did so for the purpose of performing his contract entered into with 'Y'. 'Z' failed to perform his contract in due course and market price of each water bottle on that day was Rs. 5.25 per water bottle. Consequently, 'X' could not procure any water bottle and 'Y' rescinded the contract. Calculate the amount of damages which 'X' could claim from 'Z' in the circumstances? What would be your answer if 'Z' had not informed about the 'Y's contract? Explain with reference to the provisions of the Indian Contract Act, 1872.

Sol. Breach of Contract-Damages: Section 73 of the Indian Contract Act, 1872 lays down that when a contract has been broken, the party who suffers by such 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.

The leading case on this point is "Hadley v. Baxendale" in which it was decided by the Court that the special circumstances under which the contract was actually made were communicated by the plaintiff to the defendant, and thus known to both the parties to the contract, the damages resulting from the breach of such contract which they would reasonably contemplate, would be the amount of injury which would ordinarily follow from the breach of contract under these special circumstances so known and communicated.

The problem asked in this question is based on the provisions of Section 73 of the Indian Contract Act, 1872. In the instant case 'X' had intimated to 'Z' that he was purchasing water bottles from him for the purpose of performing his contract with 'Y'. Thus, 'Z' had the knowledge of the special circumstances. Therefore, 'X' is entitled to claim from 'Z' Rs. 500/- at the rate of 0.50 paise i.e. 1000 water bottles x 0.50 paise (difference between the procuring price of water bottles and contracted selling price to 'Y') being the amount of profit 'X' would have made by the performance of his contract with 'Y'.

If 'X' had not informed 'Z' of 'Y's contract, then the number of damages would have been the difference between the contract price and the market price on the day of default. In other words, the number of

damages would be Rs. 750/- (i.e. 1000 water bottles x 0.75 paise).

76. M Ltd., contract with Shanti Traders to make and deliver certain machinery to them by 30.6.2017 for Rs. 11.50 lakhs. Due to labour strike, M Ltd. could not manufacture and deliver the machinery to Shanti Traders. Later, Shanti Traders procured the machinery from another manufacturer for Rs. 12.75 lakhs. Due to this Shanti Traders was also prevented from performing a contract which it had made with Zenith Traders at the time of their contract with M Ltd. and were compelled to pay compensation for breach of contract. Advise Shanti Traders the amount of compensation which it can claim from M Ltd., referring to the legal provisions of the Indian Contract Act, 1872

Sol. Section 73 of the Indian Contract Act, 1872 provides for consequences of breach of contract. According to it, when a contract has been broken, the party who suffers by such 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 given for any remote and indirect loss or damage sustained by reason of the breach. It is further provided in the explanation to the section that in estimating the loss or damage from a breach of contract, the means which existed of remedying the inconvenience caused by the non-performance of the contract must be taken into account.

Applying the above principle of law to the given case, M Ltd. is obliged to compensate for the loss of Rs. 1.25 lakh (i.e. Rs. 12.75 minus Rs. 11.50 = Rs. 1.25 lakh) which had naturally arisen due to default in performing the contract by the specified date.

Regarding the amount of compensation which Shanti Traders were compelled to make to Zenith Traders, it depends upon the fact whether M Ltd., knew about the contract of Shanti Traders for supply of the contracted machinery to Zenith Traders on the specified date. If so, M Ltd. is also obliged to reimburse the compensation which Shanti Traders had to pay to Zenith Traders for breach of contract. Other wise M Ltd. is not liable

77. A & B entered into a contract to supply unique item, alternate of which is not available in the market. A refused to supply the agreed unique item to B. What directions could be given by the court for breach of such contract.

Sol. Where there is a breach of contract for supply of a unique item, mere monetary damages may not be an adequate remedy for the other party. In such a case, the court may give order for specific performance and direct the party in breach to carry out his promise according to the terms of contract. Here, in this case, the court may direct A to supply the item to B because the refusal to supply the agreed unique item cannot be compensated through money.

78. Seema was running a boutique in New Delhi. She has to deliver some cloth to her friend Kiran who was putting up an exhibition at Mumbai. Seema delivered the sewing machine and some cloth to a railway company to be delivered at a place where the exhibition was to be held. Seema expected to earn an exceptional profit from the sales made at this exhibition however she did not bring this fact to the notice of the railway's authorities. The goods were delivered at the place after the conclusion of the exhibition. On account of such breach of contract by railways authorities, can Seema recover the loss of profits under the Indian Contract Act, 1872?

Sol. As per Section 73 to 75 of Indian Contract Act, 1872, Damage means a sum of money claimed or awarded in compensation for a loss or an injury. Whenever a party commits a breach, the aggrieved party can claim the compensation for the loss so suffered by him. General damages are those which arise naturally in the usual course of things from the breach itself. (Hadley Vs Baxendale). Therefore, when breach is committed by a party, the defendant shall be held liable for all such losses that naturally arise in the usual course of business. Such damages are called ordinary damages. However, special damages are those which arise in unusual circumstances affecting the aggrieved party and such damages are recoverable only when the special circumstances were brought to the knowledge of the defendant. If no special notice is given, then the aggrieved party can only claim the ordinary damages.

In the given case, Seema was to earn an exceptional profit out of the sales made at the exhibition, however she never informed about it to the railway authorities. Since the goods were delivered after the conclusion of the exhibition, therefore Seema can recover only the losses arising in the ordinary course of business. Since no notice about special circumstances was given to railways authorities, she could not recover the loss of profits.

79. What is the law relating to determination of compensation, on breach of contract, contained in section 73 of the Indian Contract Act, 1872?

Sol. Compensation on Breach of Contract: Section 73 of the Indian Contract Act, 1872 provides that when a contract has been broken, the party who suffers by such 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 given for any remote and indirect loss or damage sustained by reason of the breach**. The explanation to the section further provides that in estimating the loss or damage from a breach of contract, the means which existed of remedying the inconvenience caused by the non-performance of the contract must be taken into account.

80. Mr. X was a Disk Jockey at a five star hotel bar. As per the contract, he is supposed to perform every weekend (i.e. twice a week). Mr. X will be paid Rs. 1500 per day. However, after a month, Mr. X willfully absents himself from the performance.

(i) Does the hotel have the right to end the contract?

(ii) If the hotel sends out a mail to X that they are interested to continue the contract and X accepts, can the hotel rescind the contract after a month on this ground subsequently?

(iii) In which of the cases – (termination of contract or continuance of contract) can the hotel claim damages that it has suffered as a result of this breach?

Sol. By analyzing Section 39 of the Indian Contract Act 1872, it is understood that when a party to a contract has refused to perform or disabled himself from performing his promise entirely, the following two rights accrue to the aggrieved party (promisee)

- i. To terminate the contract
- ii. To indicate by words or by conduct that he is Interested in its continuance.

In either of the two cases, the promisee would be able to claim damages that he suffers.

In the given case,

1. Yes, the hotel has the right to end the contract with Mr. X, the DJ.
2. The hotel has the right to continue the contract with X. But once this right is exercised, they cannot subsequently rescind the contract on this ground subsequently.
3. In both the cases, the hotel (promisee) is entitled to claim damages that has been suffered as a result of breach.

81. Mr. Murti was travelling to Manali with his wife by bus of Himalya Travels Pvt. Ltd. Due to some technical default in the bus, the driver has to stop the bus in a mid way in cold night. Driver advised the passenger to get the shelter in nearest hotel which was at a distance of only one kilometre from that place. The wife of Mr. Murti caught cold and fell ill due to

being asked to get down and she had to walk in cold night to reach hotel. Mr. Murti filed the suit against Himalya Travels Pvt. Ltd. for damages for the personal inconvenience, hotel charges and medical treatment for his wife. Explain, whether Mr. Murti would get compensation for which he filed the suit?

Sol. Section 73 of Indian Contract Act, 1872 provides that when a contract has been broken, the party who suffers by such 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. But such compensation is not to be given for any remote and indirect loss or damage sustained by reason of the breach.

In the instant case, Mr. Murti filed the suit against Himalya Travels Pvt. Ltd. for damages for the personal inconvenience, hotel charges and medical treatment for his wife.

On the basis of above provisions and facts of the case, it can be said that Mr. Murti can claim damages for the personal inconvenience and hotel charges but **not for medical treatment for his wife because it is a remote or indirect loss.**

Sampurna (CA-Foundation)

CONTINGENT AND QUASI CONTRACT

82. Explain the-term ‘Quasi Contracts’ and state their characteristics.

Or

What is meant by 'Quasi-Contract'? State any three salient features of a quasi-contract as per the Indian Contract Act, 1872.

Sol. (a) Meaning of ‘Quasi Contract’: Under certain special circumstances obligation resembling those created by a contract is 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 Quasi-contract:

- I. It does not arise from any agreement of the parties concerned but it is imposed by law.
- II. The right under it is always a right to money and generally though not always to a liquidated sum of money.
- III. It is a right which is available not against all the world, but against a particular person or persons only, so that in this respect it resembles a contractual right.
- IV. It is a duty and not promise is the basis of such contract.

A suit for its breach may be filed in the same way as in case of a complete contract.

83. X, a minor was studying in M.Com. in a college. On 1st July, 2019 he took a loan of `1,00,000 from B for payment of his college fees and to purchase books and agreed to repay by 31st December, 2019. X possesses assets worth ` 9 lakhs. On due date, X fails to pay back the loan to B. B now wants to recover the loan from X out of his (X's) assets. Referring to the provisions of Indian Contract Act, 1872 decide whether B would succeed.

Sol. Yes, B can proceed against the assets of X. According to section 68 of Indian Contract Act, 1872, if a person, incapable of entering into a contract, or any one whom he is legally bound to support, is supplied by

another person with necessaries suited to his condition in life, the person who has furnished such supplies is entitled to be reimbursed from the property of such incapable person.

Since the loan given to X is for the necessaries suited to the conditions in life of the minor, his assets can be sued to reimburse B.

84. P left his carriage on D's premises. Landlord of D seized the carriage against the rent due from D. P paid the rent and got his carriage released. Can P recover the amount from D?

Sol. Yes, P can recover the amount from D. Section 69 states a person who is interested in the payment of money which another person is bound by law to pay, and who therefore pays it, is entitled to get it reimbursed by the other.

In the present case, D was lawfully bound to pay rent. P was interested in making the payment to D's landlord as his carriage was seized by him. Hence being an interested party P made the payment and can recover the same from D.

85. Explain the term Contingent Contract with reference to the Indian Contract Act, 1872 with the help of an example. Also discuss the rules relating to enforcement of a contingent contract.

Or

Explain the meaning of ‘Contingent Contracts’ and state the rules relating to such contracts.

Sol. (a) Definition of ‘Contingent Contract’ (Section 31 of the Indian Contract Act, 1872): A contract to do or not to do something, if some event, collateral to such contract, does or does not happen.

Example: A contracts to pay B Rs. 1,00,000 if B's house is burnt. This is a contingent contract.

Rules Relating to Enforcement: The rules relating to enforcement of a contingent contract are laid down in sections 32, 33, 34, 35 and 36 of the Act.

(a) **Enforcement of contracts contingent on an event happening:** Where a contract identifies happening of a future contingent event, the contract cannot be enforced until and unless the event ‘happens’. If the

happening of the event becomes impossible, then the contingent contract is void.

- (b) **Enforcement of contracts contingent on an event not happening:** Where a contingent contract is made contingent on non-happening of an event, it can be enforced only when its happening becomes impossible.
- (c) A contract would cease to be enforceable if it is contingent upon the conduct of a living person when that living person does something to make the 'event' or 'conduct' as impossible of happening.
- (d) **Contingent on happening of specified event within the fixed time:** Section 35 says that Contingent contracts to do or not to do anything, if a specified uncertain event happens within a fixed time, becomes void if, at the expiration of time fixed, such event has not happened, or if, before the time fixed, such event becomes impossible.
- (e) **Contingent on specified event not happening within fixed time:** Section 35 also says that - "Contingent contracts to do or not to do anything, if a specified uncertain event does not happen within a fixed time, may be enforced by law when the time fixed has expired, and such event has not happened or before the time fixed has expired, if it becomes certain that such event will not happen".

Contingent on an impossible event (Section 36): Contingent agreements to do or not to do anything, if an impossible event happens are void, whether the impossibility of the event is known or not to the parties to the agreement at the time when it is made.

86. What is Contingent Contract? Discuss the essentials of Contingent Contract as per the Indian Contract Act, 1872.

Sol. (a) According to section 31 of the Indian Contract Act, 1872, contingent contract means a contract to do or not to do something, if some event, collateral to such contract, does or does not happen.

Example: Contracts of Insurance, indemnity and guarantee.

Essentials of a contingent contract

- (i) **The performance of a contingent contract would depend upon the happening or non-happening of some event or condition.** The condition may be precedent or subsequent.
- (ii) **The event referred to, is collateral to the contract.** The event is not part of the contract.

The event should be neither performance promised nor a consideration for a promise.

- (iii) The **contingent** event should not be a mere 'will' of the promisor. The event should be contingent in addition to being the will of the promisor.
- (iv) The event must be **uncertain**. Where the event is certain or bound to happen, the contract is due to be performed, then it is a not contingent contract.

87. X found a wallet in a restaurant. He enquired of all the customers present there but the true owner could not be found. He handed over the same to the manager of the restaurant to keep till the true owner is found. After a week he went back to the restaurant to enquire about the wallet. The manager refused to return it back to X, saying that it did not belong to him.

In the light of the Indian Contract Act, 1872, can X recover it from the Manager?

Sol. Responsibility of finder of goods (Section 71 of the Indian Contract Act, 1872): A person who finds goods belonging to another and takes them into his custody is subject to same responsibility as if he were a bailee.

Thus, a finder of lost goods has:

- (i) to take proper care of the property as man of ordinary prudence would take
- (ii) no right to appropriate the goods and
- (iii) to restore the goods if the owner is found.

In the light of the above provisions, the manager must return the wallet to X, since X is entitled to retain the wallet found against everybody except the true owner.

88. Explain the meaning of 'Quasi-Contracts'. State the circumstances which are identified as quasi contracts by the Indian Contract Act, 1872.

Sol. Quasi-Contracts: Even in the absence of a contract, certain social relationships give rise to certain specific obligations to be performed by certain persons. These are known as "quasi- contracts" as they create some obligations as in the case of regular contracts. Quasi-contracts are based on the principles of equity, justice and good conscience.

The salient features of quasi-contracts are:

- (i) such a right is always a right to money and generally, though not always, to aliquidated sum of money;
- (ii) does not arise from any agreement between the parties concerned but the obligation is imposed by law and;
- (iii) the rights available are not against all the world but against a particular person or persons only, so in this respect it resembles to a contractual right.

Circumstances Identified as Quasi-Contracts:

- (1) **Claim for necessities supplied to persons incapable of contracting:** Any person supplying necessities of life to persons who are incapable of contracting is entitled to claim the price from the other person's property. Similarly, where money is paid to such persons for purchase of necessities, reimbursement can be claimed.
- (2) **Payment by an interested person:** A person who has paid a sum of money which another person is obliged to pay, is entitled to be reimbursed by that other person provided that the payment has been made by **him to protect his own interest.**
- (3) **Obligation of person enjoying benefits of non-gratuitous act:** Where a person lawfully does anything for another person, or delivers anything to him not intending to do so gratuitously and such other person enjoys the benefit thereof, the latter is bound to pay compensation to the former in respect of, or to restore, the thing so done or delivered.
- (4) **Responsibility of finder of goods:** A person who finds goods belonging to another person and takes them into his custody is subject to same responsibility as if he were a bailee.

- (5) **Liability for money paid or thing delivered by mistake or by coercion:** A person to whom money has been paid or anything delivered by mistake or under coercion, must repay or return it.

In all the above cases contractual liability arises without any agreement between the parties.

- 89.** PQR, a hospital in Delhi, recruits Dr. A, on contract basis for a period of 3 months. The hospital management promises to pay Dr. A, a lumpsum amount of Rs. 1,00,000 if Dr. A test positive for novel corona virus (Covid 19) during the contract period of 3 months.

Identify the type of contract and highlight the rule of enforcement. Also, what will happen if Dr. A does not contract Covid 19.

- Sol.** Section 31 of the Indian Contract Act, 1872 provides that "A contract to do or not to do something, if some event, collateral to such contract, does or does not happen" is a Contingent Contract. Section 35 says that Contingent contracts to do or not to do anything, if a specified uncertain event happens within a fixed time, becomes void if, at the expiration of time fixed, such event has not happened, or if, before the time fixed, such event becomes impossible. In the instant case, the **contract between PQR hospital & Dr. A is a Contingent Contract** because the promisor, PQR hospital need to perform his obligation of paying Dr. A, the lumpsum amount of Rs. 1,00,000, only if he contracts with Covid 19 within a span of 3 months.

In Case, if Dr. A does not contract Covid 19, then the contract stands void automatically

Sampurna (CA-Foundation)

THE SALES OF GOODS ACT, 1930 FORMATION OF THE CONTRACT OF SALE

Q. Bank

1. Distinguish between 'Sale' and 'Hire Purchase' under the Sale of Goods Act, 1930.

Sol.

Basis of Difference	Sale	Hire-Purchase
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 instalment.
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 instalment.
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 instalments.
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 instalment, the owner has right to take back the goods.
Transfer of title	The buyer can pass a good title to a bona fide purchaser from him.	The hirer cannot pass any title event a bona fide purchaser.
Resale	The buyer in sale can resell the goods.	The hire purchaser cannot resell unless he has paid all the instalments.

2. What is meant by delivery of goods under the Sale of Goods Act, 1930? State various modes of delivery.

Or

Explain the term "Delivery and its form" under the Sale of Goods Act, 1930.

Sol. (a) Delivery of goods [section 2(2) of the Sale of Goods Act, 1930]: Delivery means voluntary transfer of possession from one person to another. 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.

Modes of delivery: Following are the modes of delivery for transfer of possession:

Actual delivery: When the goods are physically delivered to the buyer.

Constructive delivery: When it is affected 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.

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.

3. Differentiate between Ascertained and Unascertained Goods with example.

Sol. Ascertained Goods are those goods which are identified in accordance with the agreement **after the contract of sale is made**. This term is not defined in the Act but has been judicially interpreted. 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. In this case, the contract is for the sale of ascertained goods, as the cotton bales to be sold are identified and agreed after the formation of the contract. It may be noted that before the ascertainment of the goods, the contract was for the sale of unascertained goods **Unascertained goods:** The goods which are not specifically identified or ascertained at the time of making of the contract are known as 'unascertained goods'. They are indicated or defined only by description or sample.

Example :- X has ten horses. He promises to sell one of them but does not specify which horse he will sell. It is a contract of sale of unascertained goods

4. State briefly the essential element of a contract of sale under the Sale of Goods Act, 1930.

Sol. Essentials of Contract of Sale

The following elements must co-exist so as to constitute a contract of sale of goods under the Sale of Goods Act, 1930.

- (i) There must be at least two parties
- (ii) The subject matter of the contract must necessarily be goods
- (iii) A price in money (not in kind) should be paid or promised.
- (iv) A transfer of property in goods from seller to the buyer must take place.
- (v) A contract of sale may be absolute or conditional [section 4(2)].
- (vi) All other essential elements of a valid contract must be present in the contract of sale.

5. Classify the following transactions according to the types of goods they are:

- (i) A wholesaler of cotton has 100 bales in his godown. He agrees to sell 50 bales and these bales were selected and set aside.

- (ii) A agrees to sell to B one packet of sugar out of the lot of one hundred packets lying in his shop.

- (iii) T agrees to sell to S all the apples which will be produced in his garden this year.

Sol. (i) A wholesaler of cotton has 100 bales in his godown. So, the goods are existing goods. He agrees to sell 50 bales and these bales were selected and set aside. On selection, the goods become ascertained. In this case, the contract is for the sale of ascertained goods, as the cotton bales to be sold are identified and agreed after the formation of the contract.

- (ii) If A agrees to sell to B one packet of sugar out of the lot of one hundred packets lying in his shop, it is a sale of existing but unascertained goods because it is not known which packet is to be delivered.

- (iii) T agrees to sell to S all the apples which will be produced in his garden this year. It is contract of sale of future goods, amounting to 'an agreement to sell.'

6. Archika went to a jewellery shop and asked the shopkeeper to show the gold bangles with white polish. The shopkeeper informed that he has gold bangles with lots of designs but not in white polish rather if Archika select gold bangles in his shop, he will arrange white polish on those gold bangles without any extra cost. Archika select a set of designer bangles and pay for that. The shopkeeper requested Archika to come after two days for delivery of those bangles so that white polish can be done on those bangles. When Archika comes after two days to take delivery of bangles, she noticed that due to white polishing, the design of bangles has been disturbed. Now, she wants to avoid the contract and asked the shopkeeper to give her money back but shopkeeper has denied for the same.

- (i) State with reasons whether Archika can recover the amount under the Sale of Goods Act, 1930.

- (ii) What would be your answer if shopkeeper says that he can repair those bangles but he will charge extra cost for same?

Sol. As per Section 4(3) of the Sale of Goods Act, 1930, where under a contract of sale, the property in the goods is transferred from the seller to the buyer, the contract is called a sale, but where the transfer of the property in the goods is to take place at a future time or subject to some condition thereafter to be fulfilled, the contract is called an agreement to sell and as per Section 4(4), an agreement to sell becomes a sale when the time elapses or the conditions are fulfilled subject to which the property in the goods is to be transferred.

(i) On the basis of above provisions and facts given in the question, it can be said that there is an agreement to sell between Archika and shopkeeper and not a sale. Even the payment was made by Archika, the property in goods can be transferred only after the fulfilment of conditions fixed between buyer and seller. As the white polish was done but original design is disturbed due to polishing, bangles are not in original position. **Hence, Archika has right to avoid the agreement to sell and can recover the price paid.**

(ii) On the other hand, if shopkeeper offers to bring the bangles in original position by repairing, he cannot charge extra cost from Archika. Even he has to bear some expenses for repair; he cannot charge it from Archika.

7. X contracted to sell his car to Y. They did not discuss the price of the car at all. X later refused to sell his car to Y on the ground that the agreement was void being uncertain about price. Can Y demand the car under the Sale of Goods Act, 1930?

Sol. Payment of the price by the buyer is an important ingredient of a contract of sale. **If the parties totally ignore the question of price while making the contract**, it would not become an uncertain and invalid agreement. It will rather be a valid contract and the buyer shall pay a **reasonable price**. (Section 9 of the Sale of Goods Act, 1930)

In the given case, X and Y have entered into a contract for sale of car but they did not fix the price of the car. X refused to sell the car to Y on this ground. Y can legally demand the car from X and X can recover a reasonable price of the car from Y.

8. Explain the term goods and other related terms under the Sale of Goods Act, 1930.

Sol. "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) of the Sale of Goods Act, 1930] '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 Sale of Goods Act.

9. A agrees to buy a new TV from a shopkeeper for Rs. 30,000 payable partly in cash of Rs. 20,000 and partly in exchange of old TV set. Is it a valid Contract of Sale of Goods? Give reasons for your answer.

Sol. It is necessary under the Sale of Goods Act, 1930 that the goods should be exchanged for money. If the goods are exchanged for goods, it will not be called a sale. It will be considered as barter. However, a contract for transfer of movable property for a definite price payable partly in goods and partly in cash is held to be a contract of Sale of Goods.

In the given case, the new TV set is agreed to be sold for Rs. 30,000 and the price is payable partly in exchange of old TV set and partly in cash of Rs. 20,000. So, in this case, it is a valid contract of sale under the Sale of Goods Act, 1930.

10. A agrees to sell to B 100 bags of sugar arriving on a ship from Australia to India within next two months. Unknown to the parties, the ship has already sunk. Does B have any right against A under the Sale of Goods Act, 1930?

Sol. In this case, B, the buyer has no right against A the seller. Section 8 of the Sale of Goods Act, 1930 provides that where there is an agreement to sell specific goods and the goods without any fault of either party perish, damaged or lost, the agreement is thereby avoided. This provision is based on the ground of supervening impossibility of performance which makes a contract void.



So, all the following conditions required to treat it as a void contract are fulfilled in the above case:

- (i) There is an agreement to sell between A and B
- (ii) It is related to specific goods
- (iii) The goods are lost because of the sinking of ship before the property or risk passes to the buyer.
- (iv) The loss of goods is not due to the fault of either party.

Sampurna (CA-Foundation)

CONDITION & WARRANTIES

Q. Bank

11. A breach of condition can be treated as a breach of warranty". Explain this statement as per relevant provisions of the Sale of Goods Act, 1930.

Sol. Section 13 of the Sale of Goods Act, 1930 specifies cases where a breach of condition be treated as a breach of warranty. As a result of which the buyer loses his right to rescind the contract and can claim damages only.

In the following cases, a contract is not avoided even on account of a breach of a condition:

- (i) Where the buyer altogether waives the performance of the condition. A party may for his own benefit, waive a stipulation. It should be a voluntary waiver by buyer.
- (ii) Where the buyer elects to treat the breach of the conditions, as one of a warranty. That is to say, he may claim only damages instead of repudiating the contract. Here, the buyer has not waived the condition but decided to treat it as a warranty.
- (iii) Where the contract is non-severable and the buyer has accepted either the whole goods or any part thereof. Acceptance means acceptance as envisaged in Section 72 of the Indian Contract Act, 1872.
- (iv) Where the fulfilment of any condition or warranty is excused by law by reason of impossibility or otherwise.

12. TK ordered timber of 1 inch thickness for being made into drums. The seller agreed to supply the required timber of 1 inch. However, the timber supplied by the seller varies in thickness from 1 inch to 1.4 inches. The timber is commercially fit for the purpose for which it was ordered. TK rejects the timber. Explain with relevant provisions of the Sale of Goods Act, 1930 whether TK can reject the timber.

Sol. Condition as to quality or fitness [Section 16(1) of the Sale of Goods Act, 1930].

The condition as to the reasonable fitness of goods for a particular purpose may be implied if the buyer had made known to the seller the purpose of his purchase and relied upon the skill and judgment of

the seller to select the best goods and the seller has ordinarily been dealing in those goods. There is implied condition on the part of the seller that the goods supplied shall be reasonably fit for the purpose for which the buyer wants them, provided the following conditions are fulfilled: The buyer should have made known to the seller the particular purpose for which goods are required. The buyer should rely on the skill and judgement of the seller.

The goods must be of a description dealt in by the seller, whether he be a manufacturer or not.

In the instant case, as the timber supplied by the seller is commercially fit for the purposes for which it was ordered, it means the implied condition on the part of the seller is fulfilled. Hence, TK cannot reject the timber. Alternate Answer:-

According to Section 15 of the Sale of Goods Act, 1930 where there is a contract for the sale of goods by description, there is an implied condition that the goods shall correspond with the description. The buyer is not bound to accept and pay for the goods which are not in accordance with the description of goods. Thus, it has to be determined whether the buyer has undertaken to purchase the goods by their description, i.e., whether the description was essential for identifying the goods where the buyer had agreed to purchase. If that is required and the goods tendered do not correspond with the description, it would be breach of condition entitling the buyer to reject the goods. In the instant case, as the timber supplied by seller varies in thickness from 1 inch to 1.4 inches, it does not correspond with the description ordered by TK i.e. of 1 inch, TK may reject the timber.

13. What are the differences between a 'Condition' and 'Warranty' in a contract of sale?

Or

Difference between conditions and warranties.

Sol. The following are important differences between conditions and warranties:

Point of difference	Condition	Warranty

s		
Meaning	A condition is a stipulation essential to the main purpose of the contract.	A warranty is a stipulation collateral to the main purpose of the contract.
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.
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.

14. Mr. T was a retail trader of fans of various kinds. Mr. M came to his shop and asked for an exhaust fan for kitchen. Mr. T showed him different brands and Mr. M approved of a particular brand and paid for it. Fan was delivered at Mr. M's house; at the time of opening the packet he found that it was a table fan. He informed Mr. T about the delivery of the wrong fan. Mr. T refused to exchange the same, saying that the contract was complete after the delivery of the fan and payment of price.

(i) Discuss whether Mr. T is right in refusing to exchange as per provisions of Sale of Goods Act, 1930?

(ii) What is the remedy available to Mr. M?

Sol. (i) According to Section 15 of the Sale of Goods Act, 1930, where the goods are sold by sample as well as by description, the implied condition is that the goods supplied shall correspond to both with the sample and the description. In case, the goods do not correspond with the sample or with description or vice versa or both, the buyer can repudiate the contract. Further, as per Section 16(1) of the Sales of Goods Act, 1930, when the buyer makes known to the seller the particular purpose for which the goods are required and he relies on the judgment or skill of the seller, it is the duty of the seller to supply such goods as are reasonably fit for that purpose.

In the given case, Mr. M had revealed Mr. T that he wanted the exhaust fan for the kitchen. Since the table fan delivered by Mr. T was unfit for the purpose for which Mr. M wanted the fan, therefore, T cannot refuse to exchange the fan.

(ii) When one party does not fulfill his obligation according to the agreed terms, the other party may treat the contract as repudiated or can insist for performance as per the original contract. Accordingly, the remedy available to Mr. M is that he can either rescind the contract or claim refund of the price paid by him or he may require Mr. T to replace it with the fan he wanted.

15. Classify the following transactions according to the types of goods they are: Mr. Das, a general store owner went to purchase 200 kg of Basmati Rice of specific length from a whole seller. He saw the samples of rice and agreed to buy the one for which the price was quoted as Rs. 150 per kg. While examining the sample Mr. Das failed to notice that the rice contained a mix of long and short grain of rice.

The whole seller supplied the required quantity exactly the same as shown in the sample. However, when Mr. Das sold the rice to one of his regular customers, she complained that the rice contained two different qualities of rice and returned the rice. With reference to the provisions of the Sales of Goods Act, 1930, discuss the options open to Mr. Das for grievance redressal. What would be your answer in case Mr. Das specified his exact requirement as to length of rice?

Sol. As per the provisions of Sub-Section (2) of Section 17 of the Sale of Goods Act, 1930, in a contract of sale by sample, there is an implied condition that:

(a) the bulk shall correspond with the sample in quality;

(b) the buyer shall have a reasonable opportunity of comparing the bulk with the sample.

In the instant case, Mr. Das on examination of the sample on which he agreed to buy, failed to notice that it contained a mix of long and short grain of rice. In the light of the provisions of Sub-Clause (b) of Sub-Section (2) of Section 17 of the Act, Mr. Das will not be successful as he examined the sample of Basmati rice (which exactly corresponded to the entire lot) without noticing the fact that even though

the sample was that of Basmati Rice but it contained a mix of long and short grains. It **could have been discovered by Mr. Das, by an ordinary examination of the goods** that it contained a mix of long and short grains. This reflects lack of due diligence on part of Mr. Das.

Therefore, Mr. Das, the buyer does not have any option available to him for grievance redressal.

In case Mr. Das specified his exact requirement as to length of rice, then there is an implied condition that the goods shall correspond with the description. If it is not so, then in such case, seller will be held liable.

16. M/s Woodworth & Associates, a firm dealing with the wholesale and retail buying and selling of various kinds of wooden logs, customized as per the requirement of the customers. They dealt with Rose wood, Mango wood, Teak wood, Burma wood etc. Mr. Das, a customer came to the shop and asked for wooden logs measuring 4 inches broad and 8 feet long as required by the carpenter. Mr. Das specifically mentioned that he required the wood which would be best suited for the purpose of making wooden doors and window frames. The Shop owner agreed and arranged the wooden pieces cut into as per the buyers requirements. The carpenter visited Mr. Das's house next day, and he found that the seller has supplied Mango Tree wood which would most unsuitable for the purpose. The carpenter asked Mr. Das to return the wooden logs as it would not meet his requirements. The Shop owner refused to return the wooden logs on the plea that logs were cut to specific requirements of Mr. Das and hence could not be resold.

- (i) Explain the duty of the buyer as well as the seller according to the doctrine of "Caveat Emptor".
- (ii) Whether Mr. Das would be able to get the money back or the right kind of wood as required serving his purpose?

Sol. Duty of the buyer according to the doctrine of "Caveat Emptor": In case of sale of goods, the doctrine 'Caveat Emptor' means '**let the buyer beware**'. When sellers display their goods in the open market, it is for the buyers to make a proper selection or choice of the goods. If the goods turn out to be defective, he cannot hold the seller liable. The seller is in no way responsible for the bad selection of

the buyer. The seller is not bound to disclose the defects in the goods which he is selling.

Duty of the seller according to the doctrine of "Caveat Emptor": The following exceptions to the Caveat Emptor are the duties of the seller:

- (1) Fitness as to quality or use
- (2) Goods purchased under patent or brand name
- (3) Goods sold by description
- (4) Goods of Merchantable Quality
- (5) Sale by sample
- (6) Goods by sample as well as description
- (7) Trade usage
- (8) Seller actively conceals a defect or is guilty of fraud

As Mr. Das has specifically mentioned that he required the wood which would be best suited for the purpose of making wooden doors and window frames but the seller supplied Mango tree wood which is **most unsuitable for the purpose**. Mr. Das is entitled to get the money back or the right kind of wood as required serving his purpose. It is the duty of the seller to supply such goods as are reasonably fit for the purpose mentioned by buyer. [Section 16(1) of the Sale of Goods Act, 1930]

17. What is the Doctrine of "Caveat Emptor"? What are the exceptions to the Doctrine of "Caveat Emptor"?

Or

Explain the term "Caveat-Emptor" under the Sale of Goods Act, 1930? What are the exceptions to this rule?

Sol. Caveat Emptor

In case of sale of goods, the doctrine 'Caveat Emptor' means '**let the buyer beware**'. When sellers display their goods in the open market, **it is for the buyers to make a proper selection or choice of the goods. If the goods turn out to be defective, he cannot hold the seller liable**. The seller is in no way responsible for the bad selection of the buyer. The seller is not bound to disclose the defects in the goods which he is selling.

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"**

Exceptions: Following are the exceptions to the doctrine of Caveat Emptor:

Fitness as to quality or use: Where the buyer makes known to the seller the particular purpose for which the goods are required, so as to show that he relies on the seller's skill or judgment and the goods are of a description which is in the course of seller's business to supply, it is the duty of the seller to supply such goods as are reasonably fit for that purpose [Section 16 (1) of the Sales of Goods Act, 1930].

Goods purchased under patent or brand name: In case where the goods are purchased under its patent name or brand name, there is no implied condition that the goods shall be fit for any particular purpose [Section 16(1)].

Goods sold by description: Where the goods are sold by description there is an implied condition that the goods shall correspond with the description [Section 15]. If it is not so then seller is responsible.

Goods of Merchantable Quality: Where the goods are bought by description from a seller who deals in goods of that description there is an implied condition that the goods shall be of merchantable quality. The rule of Caveat Emptor is not applicable. But where the buyer has examined the goods this rule shall apply if the defects were such which ought to have not been revealed by ordinary examination [Section 16(2)].

Sale by sample: Where the goods are bought by sample, this rule of Caveat Emptor does not apply if the bulk does not correspond with the sample [Section 17].

Goods by sample as well as description: Where the goods are bought by sample as well as description, the rule of Caveat Emptor is not applicable in case the goods do not correspond with both the sample and description or either of the condition [Section 15].

Trade Usage: An implied warranty or condition as to quality or fitness for a particular purpose may be annexed by the usage of trade and if the seller deviates from that, this rule of Caveat Emptor is not applicable [Section 16(3)].

Seller actively conceals a defect or is guilty of fraud: Where the seller sells the goods by making some misrepresentation or fraud and the buyer relies on it or 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. In such a case

the buyer has a right to avoid the contract and claim damages.

18. Mrs. Geeta went to the local rice and wheat wholesale shop and asked for 100 kgs of Basmati rice. The Shopkeeper quoted the price of the same as Rs. 125 per kg to which she agreed. Mrs. Geeta insisted that she would like to see the sample of what will be provided to her by the shopkeeper before she agreed upon such purchase. The shopkeeper showed her a bowl of rice as sample. The sample exactly corresponded to the entire lot. The buyer examined the sample casually without noticing the fact that even though the sample was that of Basmati Rice but it contained a mix of long and short grains. The cook on opening the bags complained that the dish if prepared with the rice would not taste the same as the quality of rice was not as per requirement of the dish. Now Mrs. Geeta wants to file a suit of fraud against the seller alleging him of selling mix of good and cheap quality rice. Will she be successful?

Explain the basic law on sale by sample under Sale of Goods Act 1930?

Decide the fate of the case and options open to the buyer for grievance redressal as per the provisions of Sale of Goods Act 1930?

What would be your answer in case Mrs. Geeta specified her exact requirement as to length of rice?

- Sol.** As per the provisions of Sub-Section (2) of Section 17 of the Sale of Goods Act, 1930, in a contract of sale by sample, there is an implied condition that:

- (a) the bulk shall correspond with the sample in quality;
- (b) the buyer shall have a reasonable opportunity of comparing the bulk with the sample.

In the instant case, in the light of the provisions of Sub-Clause (b) of Sub-Section (b) of Section 17 of the Act, Mrs. Geeta will not be successful as she casually examined the sample of rice (which exactly corresponded to the entire lot) without noticing the fact that even though the sample was that of Basmati Rice but it contained a mix of long and short grains.

Sale by Sample: (Section 17 of the Sale of Goods Act, 1930): As per the provisions of Sub-Section (1) of section 17 of the Sale of Goods Act, 1930, a contract of sale is a contract for sale by sample where there is a term in the contract, express or implied, to that effect.

As per the provisions of Sub-Section (2) of section 17 of the Sale of Goods Act, 1930, in a contract of sale by sample, there is an implied condition that:

- (a) that the bulk shall correspond with the sample in quality;
- (b) that the buyer shall have a reasonable opportunity of comparing the bulk with the sample.
- (c) that the goods shall be free from any defect, rendering them unmerchantable, which would not be apparent on reasonable examination of the sample.

In the instant case, the buyer does not have any option available to him for grievance redressal.

In case Mrs. Geeta specified her exact requirement as to length of rice, then there is an implied condition that the goods shall correspond with the description. If it is not so, the seller will be held liable.

19. Explain the “condition as to Merchantability” and “condition as to wholesomeness” under the Sale of Goods Act, 1930.

Sol. Condition as to Merchantability [Section 16(2) of the Sale of Goods Act, 1930]: 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. Provided that, if the buyer has examined the goods, there shall be no implied condition as regards defects which such examination ought to have revealed.

The expression “merchantable quality”, though not defined, nevertheless connotes goods of such a quality and in such a condition a man of ordinary prudence would accept them as goods of that description. It does not imply any legal right or legal title to sell.

Example: If a person orders motor horns from a manufacturer of horns, and the horns supplied are scratched and damaged owing to bad packing, he is entitled to reject them as unmerchantable.

Condition as to wholesomeness: In the case of eatables and provisions, in addition to the implied condition as to merchantability, there is another implied condition that the goods shall be wholesome.

Example: A supplied F with milk. The milk contained typhoid germs. F’s wife consumed the milk

and was infected and died. Held, there was a breach of condition as to fitness and A was liable to pay damages.

20. For the purpose of making uniform for the employees, Mr. Yadav bought dark blue coloured cloth from Vivek, but did not disclose to the seller the purpose of said purchase. When uniforms were prepared and used by the employees, the cloth was found unfit. However, there was evidence that the cloth was fit for caps, boots and carriage lining. Advise Mr. Yadav whether he is entitled to have any remedy under the sale of Goods Act, 1930?

Sol. Fitness of Cloth: As per the provision of Section 16(1) of the Sale of Goods Act, 1930, an implied condition in a contract of sale that an article is fit for a particular purpose only arises when the purpose for which the goods are supplied is known to the seller, the buyer relied on the seller’s skills or judgement and seller deals in the goods in his usual course of business.

In this case, the cloth supplied is capable of being applied to a variety of purposes, the buyer should have told the seller the specific purpose for which he required the goods.

But he did not do so. Therefore, the implied condition as to the fitness for the purpose does not apply. Hence, the buyer will not succeed in getting any remedy from the seller under the Sale of Goods Act, 1930.

21. What is an Implied Warranty and state the various types of Implied Warranties.

Sol. Implied Warranties: It is a warranty which the law implies into the contract of sale. In other words, it is the stipulation which has not been included in the contract of sale in express words. But the law presumes that the parties have incorporated it into their contract. It will be interesting to know that implied warranties are read into every contract of sale unless they are expressly excluded by the express agreement of the parties.

These may also be excluded by the course of dealings between the parties or by usage of trade (Section 62).

Implied Warrants:

- (1) **Warranty as to undisturbed possession [Section 14(b)]:** An implied warranty that the buyer shall have and enjoy quiet possession of

the goods. That is to say, if the buyer having got possession of the goods, is later on disturbed in his possession, he is entitled to sue the seller for the breach of the warranty.

(2) **Warranty as to non-existence of encumbrances [Section 14(c)]:** An implied warranty that the goods shall be free from any charge or encumbrance in favour of any third party not declared or known to the buyer before or at the time the contract is entered into.

(3) **Warranty as to quality or fitness by usage of trade [Section 16(3)]:** An implied warranty as to quality or fitness for a particular purpose may be annexed or attached by the usage of trade.

(4) **Disclosure of dangerous nature of goods:** Where the goods are dangerous in nature and the buyer is ignorant of the danger, the seller must warn the buyer of the probable danger. If there is a breach of warranty, the seller may be liable in damages.

22. Mr. Amit was shopping in a self-service Super market. He picked up a bottle of cold drink from a shelf.

While he was examining the bottle, it exploded in his hand and injured him.

He files a suit for damages against the owner of the market on the ground of breach of condition.

Decide under the Sale of Goods Act, 1930, whether Mr. Amit would succeed in his claim?

Sol. The problem as given in the is based on Section 16(2) of the Sale of Goods Act, 1930, which states that 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. Though the term 'merchantable quality' is not defined in the Act, it means that in the present case, the bottle must be properly sealed. In other words, if the goods are purchased for self-use, they should be reasonably fit for the purpose for which it is being used. In the instant case, on an examination of the bottle of cold drink, it exploded and injured the buyer. Applying the provision of Section 16(2), Mr. Amit would succeed in claim for damages from the owner of the shop.

23. Mrs. G bought a tweed coat from P. When she used the coat, she got rashes on her skin as her skin was abnormally sensitive.

But she did not make this fact known to the seller i.e. P. Mrs. G filled a case against the seller to recover damages. Can she recover damages under the Sale of Goods Act, 1930?

Sol. According to Section 16(1) of Sales of Goods Act, 1930, normally in a contract of sale there is no implied condition or warranty as to quality or fitness for any particular purpose of goods supplied. The general rule is that of "Caveat Emptor" that is "let the buyer beware". But where the buyer expressly or impliedly makes known to the seller the particular purpose for which the goods are required and also relies on the seller's skill and judgement and that this is the business of the seller to sell such goods in the ordinary course of his business, the buyer can make the seller responsible. In the given case, Mrs. G purchased the tweed coat without informing the seller i.e. P about the sensitive nature of her skin. Therefore, she cannot make the seller responsible on the ground that the tweed coat was not suitable for her skin. Mrs. G cannot treat it as a breach of implied condition as to fitness and quality and has no right to recover damages from the seller.

24. Mr. T was a retailer trader of fans of various kinds. Mr. M came to his shop and asked for an exhaust fan for kitchen.

Mr. T showed him different brands and Mr. M approved of a particular brand and paid for it.

Fan was delivered at Mr. M's house; at the time of opening the packet he found that it was a table fan.

He informed Mr. T about the delivery of the wrong fan.

Mr. T refused to exchange the same, saying that the contract was complete after the delivery of the fan and payment of price.

Discuss whether Mr. T is right in refusing to exchange as per provisions of the Sale of Goods Act, 1930?

What is the remedy available to Mr. M?

Sol. According to Section 15 of the Sale of Goods Act, 1930, where the goods are sold by sample as well as by description, the implied condition is that the goods supplied shall correspond to both with the sample and the description. In case, the goods do not correspond

with the sample or with description or vice versa or both, the buyer can repudiate the contract. Further, as per Section 16(1) of the Sales of Goods Act, 1930, when the buyer makes known to the seller the particular purpose for which the goods are required and he relies on the judgment or skill of the seller, it is the duty of the seller to supply such goods as are reasonably fit for that purpose.

- (1) In the given case, Mr. M had revealed Mr. T that he wanted the exhaust fan for the kitchen. Since the table fan delivered by Mr. T was unfit for the purpose for which Mr. M wanted the fan, therefore, T cannot refuse to exchange the fan.
- (2) When one party does not fulfill his obligation according to the agreed terms, the other party may treat the contract as repudiated or can insist for performance as per the original contract. Accordingly, the remedy available to Mr. M is that he can either
 - (a) rescind the contract or
 - (b) claim refund of the price paid by
 - (c) him or he may require Mr. T to replace it with the fan he wanted

25. AB Cloth House, a firm dealing with the wholesale and retail buying and selling of various kinds of clothes, customized as per the requirement of the customers. They dealt with Silk, Organdie, cotton, khadi, chiffon and many other different varieties of cloth. Mrs. Reema, a customer came to the shop and asked for specific type of cloth suitable for making a saree for her daughter's wedding. She specifically mentioned that she required cotton silk cloth which is best suited for the purpose. The Shop owner agreed and arranged the cloth pieces cut into as per the buyers' requirements. When Reema went to the tailor for getting the saree stitched, she found that seller has supplied her cotton organdie material, cloth was not suitable for the said purpose. It has heavily starched and not suitable for making the saree that Reema desired for. The Tailor asked Reema to return the cotton organdie cloth as it would not meet his requirements. The Shop owner refused to return the cloth on the plea that it was cut to specific requirements of Mrs. Reema and hence could not be resold. With reference to the doctrine of "Caveat Emptor" explain the duty of the buyer as well as the seller. Also explain whether Mrs. Reema would be

able to get the money back or the right kind of cloth as per the requirement?

Sol. Duty of the buyer according to the doctrine of "Caveat Emptor": In case of sale of goods, the doctrine 'Caveat Emptor' means 'let the buyer beware'. When sellers display their goods in the open market, it is for the buyers to make a proper selection or choice of the goods. If the goods turn out to be defective, he cannot hold the seller liable. The seller is in no way responsible for the bad selection of the buyer. The seller is not bound to disclose the defects in the goods which he is selling.

Duty of the seller according to the doctrine of "Caveat Emptor": The following exceptions to the Caveat Emptor are the duties of the seller:

- (1) Fitness as to quality or use
- (2) Goods purchased under patent or brand name
- (3) Goods sold by description
- (4) Goods of Merchantable Quality
- (5) Sale by sample
- (6) Goods by sample as well as description
- (7) Trade usage
- (8) Seller actively conceals a defect or is guilty of fraud

Based on the above provision and facts given in the, it can be concluded that Mrs. Reema is entitled to get the money back or the right kind of cloth as required serving her purpose. It is the duty of the seller to supply such goods as are reasonably fit for the purpose mentioned by buyer. [Section 16 (1) of the Sale of Goods Act, 1930].

26. Certain goods were sold by sample by A to B, who in turn sold the same goods by sample to C and C by sample sold the goods to D. The goods were not according to the sample. Therefore, D who found the deviation of the goods from the sample rejected the goods and gave a notice to C. C sued B and B sued A. Advise B and C under the Sale of Goods Act, 1930.

Sol. In the instant case, D who noticed the deviation of goods from the sample can reject the goods and treat it as a breach of implied condition as to sample which provides that when the goods are sold by sample the goods must correspond to the sample in quality and the buyer should be given reasonable time and opportunity of comparing the bulk with the sample. Whereas **C can recover only damages from B and**

B can recover damages from A. For C and B it will not be treated as a breach of implied condition as to sample as they have accepted and sold the goods according to Section 13(2) of the Sales of Goods Act, 1930.

27. 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 unfit for touring purposes. What remedy Ram is having now under the Sale of Goods Act, 1930?

Or

X consults Y, a motor-car dealer for a car suitable for touring purposes to promote the sale of his product. Y suggests 'Santro' and X accordingly buys it from Y. The car turns out to be unfit for touring purposes. What remedy X is having now under the Sale of Goods Act, 1930?

- Sol. 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)]

"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)]

Whether a stipulation in a contract of sale is a condition or a warranty depends in each case on the construction of the contract. A stipulation may be a condition, though called a warranty in the contract. [Sub-section (4)]

In the instant case, the term that the 'car should be suitable for touring purposes' is a condition of the contract. It is so vital that its non-fulfilment defeats the very purpose for which Ram purchases the car. **Ram is therefore entitled to reject the car and have refund of the price.**

28. "There is no implied warranty or condition as to quality or fitness for any particular purpose of goods supplied under a contract of sale." Discuss the significance and State exceptions, if any.

Sol. The statement given in the is the fundamental principle of law of sale of goods, sometime expressed by the maxim 'Caveat Emptor' meaning thereby 'Let the buyer be aware'. In other words, it is no part of the seller's duty in a contract of sale of goods to give the buyer an article suitable for a particular purpose, or of particular quality, unless the quality or fitness is made an express term of the contract. The person who buys goods must keep his eyes open, his mind active and should be cautious while buying the goods. If he makes a bad choice, he must suffer the consequences of lack of skill and judgement in the absence of any misrepresentation or guarantee by the seller.

There are, however, certain exceptions to the rule which are stated as under:

- (1) **Fitness as to quality or use:** Where the buyer makes known to the seller the particular purpose for which the goods are required, so as to show that he relies on the seller's skill or judgment and the goods are of a description which is in the course of seller's business to supply, it is the duty of the seller to supply such goods as are reasonably fit for that purpose [Section 16 (1)].
- (2) **Goods purchased under patent or brand name:** In case where the goods are purchased under its patent name or brand name, there is no implied condition that the goods shall be fit for any particular purpose [Section 16(1)].
- (3) **Goods sold by description:** Where the goods are sold by description there is an implied condition that the goods shall correspond with the description [Section 15]. If it is not so, then seller is responsible.
- (4) **Goods of Merchantable Quality:** Where the goods are bought by description from a seller who deals in goods of that description there is an implied condition that the goods shall be of merchantable quality. The rule of Caveat Emptor is not applicable. But where the buyer has examined the goods, this rule shall apply if the defects were such which ought to have not been revealed by ordinary examination [Section 16(2)].
- (5) **Sale by sample:** Where the goods are bought by sample, this rule of Caveat Emptor does not apply if the bulk does not correspond with the sample [Section 17].

- (6) **Goods by sample as well as description:** Where the goods are bought by sample as well as description, the rule of Caveat Emptor is not applicable in case the goods do not correspond with both the sample and description or either of the condition [Section 15].
- (7) **Trade Usage:** An implied warranty or condition as to quality or fitness for a particular purpose may be **annexed by the usage of trade** and if the seller deviates from that, this rule of Caveat Emptor is not applicable [Section 16(3)].
- (8) **Seller actively conceals a defect or is guilty of fraud:** Where the seller sells the goods by making some **misrepresentation or fraud** and the buyer relies on it or 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. In such a case the buyer has a right to avoid the contract and **claim damages**.

29. What are the implied conditions in a contract of 'Sale by sample' under the Sale of Goods Act, 1930? State also the implied warranties operatives under the said Act.

Sol. The-following are implied conditions in a contract of sale by sample in accordance with Section 17 of the Sale of Goods Act, 1930;

- (a) that the bulk shall correspond with the sample in quality;
- (b) that the buyer shall have a reasonable opportunity of comparing the bulk with the sample.
- (c) that the goods shall be free from any defect, rendering them unmerchantable, which would not be apparent on a reasonable examination of the sample [Section 17(2)].

Implied Warrants:

Warranty as to undisturbed possession [Section 14(b)]: An implied warranty that the buyer shall have and enjoy quiet possession of the goods. That is to say, if the buyer having got possession of the goods, is later on disturbed in his possession, he is entitled to sue the seller for the breach of the warranty.

Warranty as to non-existence of encumbrances [Section 14(c)]: An implied warranty that the goods

shall be free from any charge or encumbrance in favour of any third party not declared or known to the buyer before or at the time the contract is entered into.

Warranty as to quality or fitness by usage of trade [Section 16(3)]: An implied warranty as to quality or fitness for a particular purpose may be annexed or attached by the usage of trade.

Disclosure of dangerous nature of goods: Where the goods are dangerous in nature and the buyer is ignorant of the danger, the seller must warn the buyer of the probable danger. If there is a breach of warranty, the seller may be liable in damages.

30. Prashant reaches a sweet shop and ask for 1 Kg of 'Burfi' if the sweets are fresh. Seller replies 'Sir, my all sweets are fresh and of good quality.' Prashant agrees to buy on the condition that first he tastes one piece of 'Burfi' to check the quality. Seller gives him one piece to taste. Prashant, on finding the quality is good, ask the seller to pack. On reaching the house, Prashant finds that 'Burfi' is stale not fresh while the piece tasted was fresh. Now, Prashant wants to avoid the contract and return the 'Burfi' to seller.

State with reason whether Prashant can avoid the contract under the Sale of Goods Act, 1930? Will your answer be different if Prashant does not taste the sweet?

Sol. By virtue of provisions of Section 17 of the Sale of Goods Act, 1930, in the case of a contract for sale by sample there is an implied condition that the bulk shall correspond with the sample in quality and the buyer shall have a reasonable opportunity of comparing the bulk with the sample. According to Section 15, where there is a contract for the sale of goods by description, there is an implied condition that the goods shall correspond with the description. If the goods do not correspond with implied condition, the buyer can avoid the contract and reject the goods purchased.

In the instant case, the sale of sweet is sale by sample and the quality of bulk does not correspond with quality of sample. Hence, Prashant can return the sweet and avoid the contract.

In the other case, the sale of sweet is the case of sale by description and the quality of goods does not correspond with description made by seller. Hence, answer will be same. Prashant can return the sweet and avoid the contract.

31. Mr. P was running a shop selling good quality washing machines. Mr. Q came to his shop and asked for washing machine which is suitable for washing woollen clothes. Mr. P showed him a particular machine which Mr. Q liked and paid for it. Later on, when the machine was delivered at Mr. Q's house, it was found that it was wrong machine and also unfit for washing woollen clothes. He immediately informed Mr. P about the delivery of wrong machine. Mr. P refused to exchange the same, saying that the contract was complete after the delivery of washing machine and payment of price. With reference to the provisions of Sale of Goods Act, 1930, discuss whether Mr. P is right in refusing to exchange the washing machine?

Sol. According to Section 15 of the Sale of Goods Act, 1930, whenever the goods are sold as per sample as well as by description, the implied condition is that the goods must correspond to both sample as well as description. In case the goods do not correspond to sample or description, the buyer has the right to repudiate the contract.

Further under Sale of Goods Act, 1930 when the buyer makes known to the seller the particular purpose for which the goods are required and he relies on his judgment and skill of the seller, it is the duty of the seller to supply such goods which are fit for that purpose.

In the given case, Mr. Q has informed to Mr. P that he wanted the washing machine for washing woollen clothes. However, the machine which was delivered by Mr. P was unfit for the purpose for which Mr. Q wanted the machine.

Based on the above provision and facts of case, we understand that there is breach of implied condition as to sample as well as description, therefore Mr. Q can either

- (a) repudiate the contract or
- (b) claim the refund of the price paid by him or
- (c) he may require Mr. P to replace the washing machine with desired one.

32. A person purchased bread from a baker's shop. The piece of bread contained a stone in it which broke buyer's tooth while eating. What are the rights available to the buyer against the seller under the Sale of Goods Act, 1930?

Sol. This is a case related to implied condition as to wholesomeness which provides that the eatables and provisions must be wholesome that is they must be fit for human consumption. In this case, the piece of bread contained a stone which broke buyer's tooth while eating, thereby considered unfit for consumption. Hence, the buyer can treat it as breach of implied **condition as to wholesomeness** and can also claim damages from the seller

Sampurna (CA-Foundation)

Transfer of ownership & delivery of goods

Q. Bank

33. "Risk Prima Facie passes with property." Elaborate in the context of the Sales of Goods Act, 1930.

Sol. Risk prima facie passes with property (Section 26 of the Sales of Goods Act, 1930)

According to Section 26, 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.

It is provided that, where delivery has been delayed because of the fault of either buyer or seller, the goods are at the risk of the party in fault as regards any loss which might not have occurred but for such fault.

Provided also that nothing in this section shall affect the duties or liabilities of either seller or buyer as bailee of the goods of the other party

34. What is appropriation of goods under the Sale of Goods Act, 1930? State the essentials regarding appropriation of unascertained goods.

Or

State the various essential elements involved in the sale of unascertained goods and its appropriation as per the Sale of Goods Act, 1930.

Sol. Appropriation of goods: Appropriation of goods involves selection of goods with the intention of using them in performance of the contract and with the mutual consent of the seller and the buyer. The essentials regarding appropriation of unascertained goods are:

There is a contract for the sale of unascertained or future goods.

The goods should conform to the description and quality stated in the contract.

The goods must be in a deliverable state.

The goods must be unconditionally (as distinguished from an intention to appropriate) appropriated to the contract either by delivery to the buyer or his agent or the carrier.

The appropriation must be made by:

- (a) the seller with the assent of the buyer; or
- (b) the buyer with the assent of the seller.
- (c) The assent may be express or implied.
- (d) The assent may be given either before or after appropriation.

35. "A non-owner can convey better title to the bonafide purchaser of goods for value." Discuss the cases when a person other than the owner can transfer title in goods as per the provisions of the Sales of Goods Act, 1930?

Or

Explain the circumstances in detail in which non-owner can convey better title to Bona fide purchaser of goods for value as per the Sale of Goods Act, 1930.

Or

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

Sol. In the following cases, a non-owner can convey better title to the bona fide purchaser of goods for value.

(1) **Sale by a Mercantile Agent:** A sale made by a mercantile agent of the goods for 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 Section 27**).

Mercantile Agent means an agent having in the customary course of business as such agent authority either to sell goods, or to consign goods for the purposes of sale, or to buy goods, or to raise money on the security of goods [Section 2(9)].

- (2) **Sale by one of the joint owners (Section 28):** If one of several joint owners of goods has the sole possession of them by permission of the co-owners, the property in the goods is transferred to any person who buys them from such joint owner in good faith and has not at the time of the contract of sale notice that the seller has no authority to sell.
- (3) **Sale by a person in possession under voidable contract:** A buyer would acquire a good title to the goods sold to him by a 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**).
- (4) **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 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. A pledge or other disposition of the goods or documents of title by the seller in possession are equally valid [**Section 30(1)**].
- (5) **Sale by buyer obtaining possession before the property in the goods has vested in him:** Where a buyer with the consent of the 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, he would get a good title to them [**Section 30(2)**]. However, a person in possession of goods under a 'hire-purchase' agreement which gives him only an option to buy is not covered within the section unless it amounts to a sale.

- (6) **Effect of Estoppel:** Where the owner is estopped by the conduct from denying the seller's authority to sell, the transferee will get a good title as against the true owner. But before a good title by estoppel can be made, it must be shown that the true owner had actively suffered or held out the other person in question as the true owner or as a person authorized to sell the goods.
- (7) **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)**].
- (8) Sale under the provisions of other Acts:
 - (a) Sale by an Official Receiver or Liquidator of the Company will give the purchaser a valid title.
 - (b) Purchase of goods from a finder of goods will get a valid title under circumstances [Section 169 of the Indian Contract Act, 1872]
 - (c) A sale by pawnee can convey a good title to the buyer [Section 176 of the Indian Contract Act, 1872]

36. Mr. G sold some goods to Mr. H for certain price by issue of an invoice, but payment in respect of the same was not received on that day. The goods were packed and lying in the godown of Mr. G. The goods were inspected by H's agent and were found to be in order. Later on, the dues of the goods were settled in cash. Just after receiving cash, Mr. G asked Mr. H that goods should be taken away from his godown to enable him to store other goods purchased by him. After one day, since Mr. H did not take delivery of the goods, Mr. G kept the goods out of the godown in an open space. Due to rain, some goods were damaged. Referring to the provisions of the Sale of Goods Act, 1930, analyse the above situation and decide who will be held responsible for the above damage. Will your answer be different, if the dues were not settled in cash and are still pending?

Sol. According to section 44 of the Sales of Goods Act, 1932, 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. The property in the goods or beneficial right in the goods passes to the buyer at appoint of time depending upon ascertainment, appropriation and delivery of goods. Risk of loss of goods *prima facie* follows the passing of property in goods. Goods remain at the seller's risk unless the property there in is transferred to the buyer, but after transfer of property therein to the buyer the goods are at the buyer's risk whether delivery has been made or not.

In the given case, since Mr. G has already intimated Mr. H, that he wanted to store some other goods and thus Mr. H should take the delivery of goods kept in the godown of Mr. G, the loss of goods damaged should be borne by Mr. H.

If the price of the goods would not have settled in cash and some amount would have been pending then Mr. G will be treated as an unpaid seller and he can enforce the following rights against the goods as well as against the buyer personally:

- (a) Where under a contract of sale the property in the goods has passed to the buyer and the buyer wrongfully neglects or refuses to pay for the goods according to the terms of the contract, the seller may sue him for the price of the goods. [Section 55(1) of the Sales of Goods Act, 1930]
- (b) Where under a contract of sale the price is payable on a day certain irrespective of delivery and the buyer wrongfully neglects or refuses to pay such price, the seller may sue him for the price although the property in the goods has not passed and the goods have not been appropriated to the contract. [Section 55(2) of the Sales of Goods Act, 1930].

37. Ms. R owns a Two-Wheeler which she handed over to her friend Ms. K on sale or return basis. Even after a week, Ms. K neither returned the vehicle nor made payment for it.

She instead pledged the vehicle to Mr. A to obtain a loan. Ms. R now wants to claim the Two-Wheeler from Mr. A. Will she succeed?

Examine with reference to the provisions of the Sale of Goods Act, 1930, what recourse is available to Ms. R?

Would your answer be different if it had been expressly provided that the vehicle would remain the property of Ms. R until the price has been paid?

Sol. As per the provisions of Section 24 of the Sale of Goods Act, 1930, when goods are delivered to the buyer on approval or "on sale or return" or other similar terms, the property therein passes to the buyer-

- (a) when the buyer signifies his approval or acceptance to the seller or does any other act adopting the transaction;
- (b) if he does not signify his approval or acceptance to the seller but retains the goods without giving notice of rejection, then, if a time has been fixed for the return of the goods, on the expiration of such time, and, if no time has been fixed, on the expiration of a reasonable time; or
- (c) he does something to the good which is equivalent to accepting the goods e.g. he pledges or sells the goods.

Referring to the above provisions, we can analyse the situation given in the question: -

- (i) In the instant case, Ms. K, who had taken delivery of the two-wheeler on Sale or Return basis pledged the two-wheeler to Mr. A, has attracted the third condition that she has done something to the good which is equivalent to accepting the goods e.g. She pledges or sells the goods. Therefore, the property therein (Two-wheeler) passes to Mr. A. Now in this situation, Ms. R cannot claim back her two-wheeler from Mr. A, but she can claim the price of the two-wheeler from Ms. K only.
- (ii) It may be noted that where the goods have been delivered by a person on "sale or return" on the terms that the goods were to remain the property of the seller till they are paid for, the property therein does not pass to the buyer until the terms are complied with, i.e., price is paid for.

Hence, in this case, it is held that at the time of pledge, the ownership was not transferred to Ms. K. Thus, the pledge was not valid and Ms. R could recover the two-wheeler from Mr. A.

- 38.** Describe the consequences of “destruction of goods” under the Sale of Goods Act, 1930, where the goods have been destroyed after the agreement to sell but before the sale is affected.

Sol. Destruction of Goods-Consequences: 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.

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 part 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 and 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.

- 39.** J the owner of a Fiat car wants to sell his car. For this purpose, he hands over the car to P, a mercantile agent for sale at a price not less than Rs. 50,000. The agent sells the car for Rs. 40,000 to A, who buys the car in good faith and without notice of any fraud. P misappropriated the money also. J sues A to recover the Car. Decide given reasons whether J would succeed.

Sol. The problem in this case is based on the provisions of the Sale of Goods Act, 1930 contained in the proviso to Section 27. The proviso provides that a mercantile agent is one who in the customary course of his

business, has, as such agent, authority either 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 [Section 2(9)]. The buyer of goods from a mercantile agent, who has no authority from the principal to sell, gets a good title to the goods if the following conditions are satisfied:

1. The agent should be in possession of the goods or documents of title to the goods with the consent of the owner.
2. The agent should sell the goods while acting in the ordinary course of business of a mercantile agent.
3. The buyer should act in good faith.
4. The buyer should not have at the time of the contract of sale notice that the agent has no authority to sell.

In the instant case, P, the agent, was in the possession of the car with J’s consent for the purpose of sale. A, the buyer, therefore obtained a good title to the car. Hence, J in this case, cannot recover the car from A.

- 40.** What are the rules related to Acceptance of Delivery of Goods?

Sol. Rules related to acceptance of delivery: 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; or
- (c) retains the goods after the lapse of a reasonable time, without intimating to the seller that he has rejected them (Section 42).

Ordinarily, a seller cannot compel the buyer to return the rejected goods; but the seller is entitled to a notice of the rejection.

Where the seller is ready and willing to deliver the goods and requests the buyer to take delivery, and the buyer does not take delivery within a reasonable time, he is liable to the seller for any loss occasioned by the neglect or refusal to take delivery, and also reasonable charge for the care and custody of the goods (Sections 43 and 44).

- 41.** Mr. S agreed to purchase 100 bales of cotton from V, out of his large stock and sent his men to take delivery of the goods.

They could pack only 60 bales. Later on, there was an accidental fire and the entire stock was destroyed including 60 bales that were already packed. Referring to the provisions of the Sale of Goods Act, 1930 explain as to who will bear the loss and to what extent?

- Sol.** Section 26 of the Sale of Goods Act, 1930 provides that 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 buyer's risk.

whether delivery has been made or not. Further Section 18 read with Section 23 of the Act provide that in a contract for the sale of unascertained goods, no property in the goods is transferred to the buyer, unless and until the goods are ascertained and where there is contract for the sale of unascertained or future goods by description, and goods of that description and in a deliverable state are unconditionally appropriated to the contract, either by the seller with the assent of the buyer or by the buyer with the assent of the seller, the property in the goods thereupon passes to the buyer. Such assent may be express or implied.

Applying the aforesaid law to the facts of the case in hand, it is clear that Mr. S has the right to select the good out of the bulk and he has sent his men for same purpose.

Hence the problem can be answered based on the following two assumptions and the answer will vary accordingly.

- (i) Where the bales have been selected with the consent of the buyer's representatives:

In this case the 60 bales has been transferred to the buyer and goods have been appropriated to the contract. Thus, loss arising due to fire in case of 60 bales would be borne by Mr. S. As regards 40 bales, the loss would be borne by Mr. V, since the goods have not been identified and appropriated.

- (ii) Where the bales have not been selected with the consent of buyer's representatives:

In this case, the goods has not been transferred at all and hence the loss of 100 bales would be borne by Mr. V completely.

- 42.** A went to B's shop and selected some jewellery. He falsely represented himself to be a man of credit and thereby persuaded B to take the payment by cheque. He further requested him to hand over the particular type of ring immediately. On the due date, when the seller, B presented the cheque for payment, the cheque was found to be dishonoured. Before B could avoid the contract on the ground of fraud by A, he had sold the ring to C. C had taken the ring in good faith and without any notice of the fact that the goods with A were under a voidable contract. Discuss if such a sale made by non-owner is valid or not as per the provisions of Sale of Goods Act, 1930?

- Sol.** Section 27 of Sale of Goods Act, 1930 states that no man can sell the goods and give a good title unless he is the owner of the goods. However, there are certain exceptions to this rule of transfer of title of goods.

One of the exceptions is sale by person in possession under a voidable contract (Section 29 of Sale of Goods Act, 1930)

If a person has possession of goods under a voidable contract.

The contract has not been rescinded or avoided so far

The person having possession sells it to a buyer

The buyer acts in good faith

The buyer has no knowledge that the seller has no right to sell.

Then, such a sale by a person who has possession of goods under a voidable contract shall amount to a valid sale and the buyer gets the better title.

Based on the provisions, Mr. A is in possession of the ring under a voidable contract as per provisions of Indian Contract Act, 1872. Also, B has not rescinded or avoided the contract, Mr. A is in possession of the ring and he sells it new buyer Mr. C who acts in good faith and has no knowledge that A is not the real owner. Since all the conditions of Section 29 of Sale of Goods Act, 1930 are fulfilled, therefore sale of ring made by Mr. A to Mr. C is a valid sale.

- 43.** Referring to the provisions of the Sale of Goods Act, 1930, state the circumstances under which when goods are delivered to the buyer "on approval" or "on

sale or return” or other similar terms, the property therein passes to the buyer. Ms. Preeti owned a motor car which she handed over to Mr. Joshi on sale or return basis. After a week, Mr. Joshi pledged the motor car to Mr. Ganesh. Ms. Preeti now claims back the motor car from Mr. Ganesh. Will she succeed? Referring to the provisions of the Sale of Goods Act, 1930, decide and examine what recourse is available to Ms. Preeti.

Sol. As per the provisions of Section 24 of the Sale of Goods Act, 1930, when goods are delivered to the buyer on approval or “on sale or return” or other similar terms, the property therein passes to the buyer-

(a) when the buyer signifies his approval or acceptance to the seller or does any other act adopting the transaction;

(b) if he does not signify his approval or acceptance to the seller but retains the goods without giving notice of rejection, then, if a time has been fixed for the return of the goods, on the expiration of such time, and, if no time has been fixed, on the expiration of a reasonable time; or

(c) he does something to the good which is equivalent to accepting the goods e.g. he pledges or sells the goods. Referring to the above provisions, we can analyse the situation given in the question.

Since, Mr. Joshi, who had taken delivery of the Motor car on Sale or Return basis and pledged the motor car to Mr. Ganesh, has attracted the third condition that he has done something to the good which is equivalent to accepting the goods e.g. he pledges or sells the goods. Therefore, the property therein (Motor car) passes to Mr. Joshi. Now in this situation, Ms. Preeti cannot claim back her Motor Car from Mr. Ganesh, but she can claim the price of the motor car from Mr. Joshi only.

44. Akansh purchased a Television set from Jethalal, the owner of Gada Electronics on the condition that first three days he will check its quality and if satisfied he will pay for that otherwise he will return the Television set. On the second day, the Television set was spoiled due to an earthquake. Jethalal demands the price of Television set from Akansh. Whether Akansh is liable to pay the price under the Sale of Goods Act, 1930? If not, who will ultimately bear the loss?

Sol. As per the provisions of Section 24 of the Sale of Goods Act, 1930, when goods are delivered to the buyer on approval or “on sale or return” or other similar terms, the property therein passes to the buyer-

when the buyer signifies his approval or acceptance to the seller or does any other act adopting the transaction;

if he does not signify his approval or acceptance to the seller but retains the goods without giving notice of rejection, then, if a time has been fixed for the return of the goods, on the expiration of such time, and, if no time has been fixed, on the expiration of a reasonable time; or

he does something to the good which is equivalent to accepting the goods e.g. he pledges or sells the goods.

Further, as per Section 8, where there is an agreement to sell specific goods, and subsequently the goods without any fault on the part of the seller or buyer perish or become so damaged as no longer to answer to their description in the agreement before the risk passes to the buyer, the agreement is thereby avoided.

According to above provisions and fact, the property is not passes to Akansh i.e. buyer as no condition of Section 24 is satisfied. Hence, risk has not passed to buyer and the agreement is thereby avoided. Akansh is not liable to pay the price. The loss finally should be borne by Seller, Mr. Jethalal.

45. Sohan is a trader in selling of wheat. Binod comes to his shop and ask Sohan to show him some good quality wheat. Binod is satisfied with the quality of wheat. Sohan agrees to sell 100 bags of wheat to Binod on 10th June 2021. The delivery of wheat and the payment was to be made in next three months i.e. by 10 th September 2021 by Binod. Before the goods are delivered to Binod, Sohan gets another customer Vikram in his shop who is ready to pay higher price for the wheat. Sohan sells the goods of Binod (which were already lying in his possession even after sale) to Vikram. Vikram has no knowledge that Sohan is not the owner of goods. With reference to Sale of Goods Act,1930, discuss if such a sale made by Sohan to Vikram is a valid sale?

Sol. The given question deals with the rule related to transfer of title of goods. Section 27 of the Sale of Goods Act ,1930 specify the general rule " No man

can sell the goods and give a good title unless he is the owner of the goods". The latin maxim " NEMO DET QUOD NON HABET". However, there are certain exceptions to this rule. One of the exceptions is given in Section 30 (1) of Sale of Goods Act, 1930 wherein the sale by seller in possession of goods even after sale is made, is held to be valid. If the following conditions are satisfied, then it amounts to a valid sale although the seller is no more the owner of goods after sale.

- (i) A seller has possession of goods after sale
- (ii) with the consent of the other party (i.e., buyer)
- (iii) the seller sells goods (already sold) to a new buyer
- (iv) the new buyer acts in good faith
- (v) The new buyer has no knowledge that the seller has no authority to sell.

In the given question, the seller Sohan has agreed to sell the goods to Binod, but delivery of the goods is still pending. Hence Sohan is in possession of the goods and this is with the consent of buyer i.e. Binod. Now Sohan sell those goods to Vikram, the new buyer. Vikram is buying the goods in good faith and also has no knowledge that Sohan is no longer the owner of goods.

Since all the above conditions given under Section 30 (1) of Sale of Goods Act, 1930 are satisfied, therefore the sale made by Sohan to Vikram is a valid sale even if Sohan is no longer the owner of goods.

- 46.** Avyukt purchased 100 Kgs of wheat from Bhaskar at Rs. 30 per kg. Bhaskar says that wheat is in his warehouse in the custody of Kishore, the warehouse keeper. Kishore confirmed Avyukt that he can take the delivery of wheat from him and till then he is holding wheat on Avyukt's behalf. Before Avyukt picks the goods from warehouse, the whole wheat in the warehouse has flowed in flood. Now Avyukt wants his price on the contention that no delivery has been done by seller. Whether Avyukt is right with his views under the Sale of Goods Act, 1930.

Sol. As per the provisions of the Sale of Goods Act, 1930 there are three modes of delivery, i) Actual delivery, ii) Constructive delivery and iii) Symbolic delivery. When delivery is affected without any change in the custody or actual possession of the things, it is called

constructive delivery or delivery by acknowledgement. Constructive delivery takes place when a person in possession of goods belonging to seller acknowledges to the buyer that he is holding the goods on buyer's behalf.

In the instant case, Kishore acknowledges Avyukt that he is holding wheat on Avyukt's behalf. Before picking the wheat from warehouse by Avyukt, whole wheat was flowed in flood.

On the basis of above provisions and facts, it is clear that possession of the wheat has been transferred through constructive delivery. Hence, Avyukt is not right. He cannot claim the price back.

- 47.** A, B and C were joint owner of a truck and the possession of the said truck was with B. X purchased the truck from B without knowing that A and C were also owners of the truck. Decide in the light of provisions of Sales of Goods Act 1930, whether the sale between B and X is valid or not?

Sol. In the above case, A, B and C were the joint owners of the truck and the possession of the truck was with B. Now B sold the said truck to X. X without knowing this fact purchased the truck from B.

The sale between B and X is perfectly valid because Section 28 of the Sales of Goods Act provides that in case one of the several joint owners has the possession of the goods by the permission of the co-owners and if the buyer buys them in good faith without the knowledge of the fact that seller has no authority to sell, it will give rise to a valid contract of sale.

- 48.** X agreed to purchase 300 tons of wheat from Y out of a larger stock. X sent his men with the sacks and 150 tons of wheat were put into the sacks. Then there was a sudden fire and the entire stock was gutted. Who will bear the loss and why?

Sol. According to Section 21 of the Sales of Goods Act, 1930, if the goods are not in a deliverable state and the contract is for the sale of specific goods, the property does not pass to the buyer unless: -

- (i) The seller has done his act of putting the goods in a deliverable state and
- (ii) The buyer has knowledge of it.

Sometimes the seller is required to do certain acts so as to put the goods in deliverable state like packing, filling in containers etc. No property in goods passes unless such act is done and buyer knows about it.

In the given case, X has agreed to purchase 300 tons of wheat from Y out of a larger stock. X sent his men (agent) to put the wheat in the sacks. Out of 300 tones only 150 tons were put into the sacks. There was a sudden fire and the entire stock was gutted. In this case, according to the provisions of law, 150 tons sale has taken place. So, buyer X will be responsible to bear the loss. The loss of rest of the wheat will be that of the seller Y. The wheat which was put in the sacks fulfils both the conditions that are: -

- (1) The wheat is put in a deliverable state in the sacks.
- (2) The buyer is presumed to have knowledge of it because the men who put the wheat in the sacks are that of the buyer.

49. The buyer took delivery of 20 tables from the seller on sale or return basis without examining them. Subsequently, he sold 5 tables to his customers. The customer lodged a complaint of some defect in the tables. The buyer sought to return tables to the seller. Was the buyer entitled to return the tables to the seller under the provisions of the Sale of Goods Act, 1930?

Sol. According to Section 24 of the Sales of Goods Act, 1930, in case of delivery of goods on approval basis, the property in goods passes from seller to the buyer: When the person to whom the goods are given either accepts them or does an act which implies adopting the transaction. When the person to whom the goods are given retains the goods without giving his approval or giving notice of rejection beyond the time fixed for the return of goods and in case no time is fixed after the lapse of reasonable time. In the given

case, seller has delivered 20 tables to the buyer on sale or return basis. Buyer received the tables without examining them. Out of these 20 tables, he sold 5 tables to his customer. It implies that he has accepted 5 tables out of 20. When the buyer received the complaint of some defect in the tables, he wanted to return all the tables to the seller. According to the provisions of law he is entitled to return only 15 tables to the seller and not those 5 tables which he has already sold to his customer. These tables are already accepted by him so the buyer becomes liable under the doctrine of "Caveat Emptor".

50. A delivered a horse to B on sale and return basis. The agreement provided that B should try the horse for 8 days and return, if he did not like the horse. On the third day the horse died without the fault of B. A files a suit against B for the recovery of price. Can he recover the price?

Sol. A delivered the horse to B on sale or return basis. It was decided between them that B will try the horse for 8 days and in case he does not like it, he will return the horse to the owner A. But on the third day the horse died without any fault of B. The time given by the seller A to the buyer B has not expired yet. Therefore, the ownership of the horse still belongs to the seller A. B will be considered as the owner of the horse only when B does not return the horse to A within stipulated time of 8 days.

The suit filed by A for the recovery of price from B is invalid and he cannot recover the price from B. [Section 24]

Sampurna (CA-Foundation)

UNPAID SELLER

Q. Bank

51. AB sold 500 bags of wheat to CD. Each bag contains 50 Kilograms of wheat. AB sent 450 bags by road transport and CD himself took remaining 50 bags. Before CD receives delivery of 450 bags sent by road transport, he becomes bankrupt. AB being still unpaid, stops the bags in transit. The official receiver, on CD's insolvency claims the bags. Decide the case with reference to the provisions of the Sale of Goods Act, 1930.

Sol. Right of stoppage in transit (Section 50 of the Sale of Goods Act, 1930):

Subject to the provisions of this Act, when the buyer of goods becomes insolvent, the unpaid seller who has parted with the possession of the goods has the right of stopping them in transit, that is to say, he may resume possession of the goods as long as they are in the course of transit and may retain them until paid or tendered price of the goods

When the unpaid seller has parted with the goods to a carrier and the buyer has become insolvent, he can exercise this right of asking the carrier to return the goods back, or not to deliver the goods to the buyer. In the instant case, CD, the buyer becomes insolvent, and 450 bags are in transit. AB, the seller, can stop the goods in transit by giving a notice of it to CD. The official receiver, on CD's insolvency cannot claim the bags.

52. 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.

Sol. 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.

53. What are the rules which regulate the Sale by Auction under the Sale of Goods Act, 1930?

Or

Referring to the provisions of the Sale of Goods Act, 1930, state the rules provided to regulate the "Sale by Auction."

Sol. Legal Rules of Auction sale: Section 64 of the Sale of Goods Act, 1930 provides following rules to regulate the sale by auction:

- (g) **Where goods are sold in lots:** Where goods are put up for sale in lots, each lot is *prima facie* deemed to be subject of a separate contract of sale.
- (h) **Completion of the contract of sale:** The sale is complete when the auctioneer announces its completion by the fall of hammer or in any other customary manner and until such announcement is made, any bidder may retract from his bid.
- (i) **Right to bid may be reserved:** Right to bid may be reserved expressly by or on behalf of the seller and where such a right is **expressly reserved**, but not otherwise, the seller or any one person on his behalf may bid at the auction.
- (j) **Where the sale is not notified by the seller:** Where the sale is not notified to be subject to a right to bid on behalf of the seller, it shall not be lawful for the seller to bid himself or to employ any person to bid at such sale, or for the auctioneer knowingly to take any bid from the seller or any such person; and any sale contravening this rule may be treated as fraudulent by the buyer.

- (k) **Reserved price:** The sale may be notified to be subject to a reserve or upset price; and
- (l) **Pretended bidding:** If the seller makes use of pretended bidding to raise the price, the sale is **voidable** at the option of the buyer

54. Discuss the rights of an unpaid seller against the buyer under the Sales of Goods Act, 1930.

Sol. (1) **Suit for price (Section 55)**

- (a) Where under a contract of sale, the property in the goods has passed to the buyer and the buyer wrongfully neglects or refuses to pay for the goods according to the terms of the contract, the seller may sue him for the price of the goods. [Section 55(1)]
- (b) Where under a contract of sale, the price is payable on a certain day irrespective of delivery and the buyer wrongfully neglects or refuses to pay such price, the seller may sue him for the price although the property in the goods has not passed and the goods have not been appropriated to the contract. [Section 55(2)].
- (2) **Suit for damages for non-acceptance (Section 56):** Where the buyer wrongfully neglects or refuses to accept and pay for the goods, the seller may sue him for damages for non-acceptance. As regards measure of damages, Section 73 of the Indian Contract Act, 1872 applies in this case.
- (3) **Repudiation of contract before due date (Section 60):** Where the buyer repudiates the contract before the date of delivery, the seller may treat the contract as rescinded and sue damages for the breach. This is known as the '**rule of anticipatory breach of contract**'.
- (4) **Suit for interest [Section 61]:** Where there is specific agreement between the seller and the buyer as to interest on the price of the goods from the date on which payment becomes due, the seller may recover interest from the buyer. If, however, there is no specific agreement to this effect, the seller may charge interest on the price when it becomes due from such day as he may notify to the buyer. In the absence of a contract to the contrary, the Court may award interest to the seller in a suit by him at such rate as it thinks fit on the amount of the price from

the date of the tender of the goods or from the date on which the price was payable.

55. Mr. D sold some goods to Mr. E for Rs. 5,00,000 on 15 days credit. Mr. D delivered the goods. On due date Mr. E refused to pay for it. State the position and rights of Mr. D as per the Sale of Goods Act, 1930.

Sol. (a) **Position of Mr. D:** Mr. D sold some goods to Mr. E for Rs. 5,00,000 on 15 days credit. Mr. D delivered the goods. On due date Mr. E refused to pay for it. So, Mr. D is an unpaid seller as according to section 45(1) of the Sale of Goods Act, 1930 the seller of goods is deemed to be an 'Unpaid Seller' when the whole of the price has not been paid or tendered and the seller had an immediate right of action for the price.

Rights of Mr. D: As the goods have parted away from Mr. D, therefore, Mr. D cannot exercise the right against the goods, he can only exercise his rights against the buyer i.e. Mr. E which are as under:

(i) **Suit for price (Section 55)**

In the mentioned contract of sale, the price is payable after 15 days and Mr. E refuses to pay such price, Mr. D may sue Mr. E for the price.

(ii) **Suit for damages for non-acceptance (Section 56):** Mr. D may sue Mr. E for damages for non-acceptance if Mr. E wrongfully neglects or refuses to accept and pay for the goods. As regards measure of damages, Section 73 of the Indian Contract Act, 1872 applies.

(iii) **Suit for interest [Section 61]:** If there is no specific agreement between the Mr. D and Mr. E as to interest on the price of the goods from the date on which payment becomes due, Mr. D may charge interest on the price when it becomes due from such day as he may notify to Mr. E.

56. Explain the rights of unpaid seller against the goods.

Sol. (a) **Rights of an unpaid seller against the goods:** As per the provisions of Section 46 of the Sale of Goods Act, 1930, notwithstanding that the property in the goods may have passed to the buyer, the unpaid seller of goods, as such, has by implication of law-

(a) a lien on the goods for the price while he is in possession of them;

- (b) in case of the insolvency of the buyer, a right of stopping the goods in transit after he has parted with the possession of them;
- (c) a right of re-sale as limited by this Act. [Sub-section (1)]

Where the property in goods has not passed to the buyer, the unpaid seller has, in addition to his other remedies, a right of withholding delivery similar to and co-extensive with his rights of lien and stoppage in transit where the property has passed to the buyer. [Sub-section (2)]

These rights can be exercised by the unpaid seller in the following circumstances:

- (i) **Right of lien (Section 47):** According to sub-section (1), the unpaid seller of goods who is in possession of them is entitled to retain possession of them until payment or tender of the price in the following cases, namely:-
 - (a) where the goods have been sold without any stipulation as to credit;
 - (b) where the goods have been sold on credit, but the term of credit has expired;
 - (c) where the buyer becomes insolvent.
- (ii) **Right of stoppage in transit (Section 50):** When the buyer of goods becomes insolvent, the unpaid seller who has parted with the possession of the goods has the right of stopping them in transit, that is to say, he may resume possession of the goods as long as they are in the course of transit, and may retain them until paid or tendered price of the goods.
- (iii) **Right to re-sell the goods (Section 54):** The unpaid seller can exercise the right to re-sell the goods under the following conditions:
 1. Where the goods are of a perishable nature
 2. Where he gives notice to the buyer of his intention to re-sell the goods
 3. Where an unpaid seller who has exercised his right of lien or stoppage in transit resells the goods
 4. A re-sale by the seller where a right of re-sale is expressly reserved in a contract of sale
 5. Where the property in goods has not passed to the buyer

57. Describe the term “unpaid seller” under the Sale of Goods Act, 1930? When can an unpaid seller exercise the right of stoppage of goods in transit?

Sol. Unpaid Seller : According to Section 45 of the Sale of Goods Act, 1930, the seller of goods is deemed to be an ‘Unpaid Seller’ when-

- (a) the whole of the price has not been paid or tendered.
- (b) a bill of exchange or other negotiable instrument has been received as conditional payment, and it has been dishonoured.

Right of stoppage of goods in transit

When the unpaid seller has parted with the goods to a carrier and the buyer has become insolvent, he can exercise this right by asking the carrier to return the goods back, or not to deliver the goods to the buyer. However, the right of stoppage in transit is exercised only when the following conditions are fulfilled:

- (a) The seller must be unpaid.
- (b) The seller must have parted with the possession of goods.
- (c) The goods must be in the course of transit.
- (d) The buyer must have become insolvent.
- (e) The right is subject to provisions of the Act.

58. What are the rights of buyer against the seller, if the seller commits a breach of contract under the Sale of Goods Act, 1930?

Sol. If the seller commits a breach of contract, the buyer gets the following rights against the seller: -

1. **Damages for non-delivery [Section 57]:** Where the seller wrongfully neglects or refuses to deliver the goods to the buyer, the buyer may sue the seller for damages for non-delivery.
2. **Suit for specific performance (Section 58):** Where the seller commits a breach of the contract of sale, the buyer can appeal to the court for specific performance. The court can order for specific performance only when the goods are ascertained or specific.
3. **Suit for breach of warranty (Section 59):** Where there is breach of warranty on the part of the seller, or where the buyer elects to treat breach of condition as breach of warranty, the buyer is not entitled to reject the goods only on the basis of such breach of warranty. But he may –
 - (i) set up against the seller the breach of warranty in diminution or extinction of the price; or

- (ii) sue the seller for damages for breach of warranty.

4. **Repudiation of contract before due date (Section 60):** Where either party to a contract of sale repudiates the contract before the date of delivery, the other may either treat the contract as subsisting and wait till the date of delivery, or he may treat the contract as rescinded and sue for damages for the breach.

5. **Suit for interest:**

- (1) Nothing in this Act shall affect the right of the seller or the buyer to recover interest or special damages, in any case where by law interest or special damages may be recoverable, or to recover the money paid where the consideration for the payment of it has failed.
- (2) In the absence of a contract to the contrary, the court may award interest at such rate as it thinks fit on the amount of the price to the buyer in a suit by him for the refund of the price in a case of a breach of the contract on the part of the seller from the date on which the payment was made.

59. Explain the provisions of law relating to unpaid seller's 'right of lien' and distinguish it from the "right of stoppage the goods in transit".

Sol. Right of lien of an unpaid seller

The legal provisions regarding the right of lien of an unpaid seller has been stated from Sections 47 to 49 of the Sale of Goods Act, 1930 which may be enumerated as follows:

- (i) According to Section 47, the unpaid seller of the goods who is in possession of them is entitled to retain possession of them until payment or tender of the price in the following cases namely:
- (a) where the goods have been sold without any stipulation as to credit.
- (b) where the goods have been sold on credit, but the term of credit has expired; or
- (c) where the buyer becomes insolvent.

The seller may exercise his right of lien not withstanding that he is in possession of the goods as agent or bailee for the buyer.

- (ii) Section 48 states that where an unpaid seller has made part delivery of the goods, he may exercise his right of lien on the remainder,

unless such part delivery has been made under such circumstances as to show an agreement to waive the lien.

- (iii) According to Section 49 the unpaid seller loses his lien on goods:
- (a) 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.
- (b) when the buyer or his agent lawfully obtains possession of the goods;
- (c) by waiver thereof.

The unpaid seller of the goods, having a lien thereon, does not lose his lien by reason only that he has obtained a decree to the price of the goods.

Right of lien and Right to stoppage the goods in transit; distinction:

- (i) The essence of a right of lien is to retain possession whereas the right of stoppage in transit is right to regain possession.
- (ii) Seller should be in possession of goods under lien while in stoppage in transit (i) Seller should have parted with the possession (ii) possession should be with a carrier and (iii) Buyer has not acquired the possession.
- (iii) Right of lien can be exercised even when the buyer is not insolvent, but it is not the case with right of stoppage in transit.
- (iv) Right of stoppage in transit begins when the right of lien ends. Thus, the end of the right of lien is the starting point of the right of stoppage the goods in transit.

60. Suraj sold his car to Sohan for Rs. 75,000. After inspection and satisfaction, Sohan paid Rs. 25,000 and took possession of the car and promised to pay the remaining amount within a month. Later on Sohan refuses to give the remaining amount on the ground that the car was not in a good condition. Advise Suraj as to what remedy is available to him against Sohan.

Sol. As per the section 55 of the Sale of Goods Act, 1930 an unpaid seller has a right to institute a suit for price against the buyer personally. The said Section lays down that :-

- (i) Where under a contract of sale the property in the goods has passed to buyer and the buyer wrongfully neglects or refuses to pay for the

goods, the seller may sue him for the price of the goods [Section 55(1)].

- (ii) Where under a contract of sale the price is payable on a certain day irrespective of delivery and the buyer wrongfully neglects or refuses to pay such price, the seller may sue him for the price. It makes no difference even if the property in the goods has not passed and the goods have not been appropriated to the contract [Section 55(2)].

This problem is based on above provisions. Hence, Suraj will succeed against Sohan for recovery of the remaining amount. Apart from this Suraj is also entitled to:-

- (1) Interest on the remaining amount
- (2) Interest during the pendency of the suit.
- (3) Costs of the proceedings.

- 61.** Rachit arranges an auction to sale an antic wall clock. Megha, being one of the bidders, gives highest bid. For announcing the completion of sale, the auctioneer fall the hammer on table but suddenly hammer brakes and damages the watch. Megha wants to avoid the contract. Can she do so under the provisions of the Sale of Goods Act, 1930?

Sol. By virtue of provisions of Section 64 of the Sale of Goods Act, 1930, in case of auction sale, the sale is complete when the auctioneer announces its completion by the fall of the hammer or in some other customary manner.

In the instant case, Megha gives the highest bid in the auction for the sale of antic wall clock arranged by Rachit. While announcing the completion of sale by fall of hammer on the table, hammer brakes and damages the clock.

On the basis of above provisions, **it can be concluded that the sale by auction cannot be completed until hammer comes in its normal position after falling on table.** Hence, in the given problem, sale is not completed. Megha will not be liable for loss and can avoid the contract.

- 62.** 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?

Sol. 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 loss 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;

Yes, he can exercise his right of lien even after he has obtained a decree for the price of goods from the court.

- 63.** A agrees to sell certain goods to B on a certain date on 10 days credit. The period of 10 days expired and goods were still in the possession of A. B has also not paid the price of the goods. B becomes insolvent. A refuses to deliver the goods to exercise his right of lien on the goods. Can he do so under the Sale of Goods Act, 1930?

Sol. Lien is the right of a person to retain possession of the goods belonging to another until claim of the person in possession is satisfied. The unpaid seller has also right of lien over the goods for the price of the goods sold.

Section 47(1) of the Sales of Goods Act, 1930 provides that the unpaid seller who is in the possession of the goods is entitled to exercise right of lien in the following cases:-

1. Where the goods have been sold without any stipulation as to credit
2. Where the goods have been sold on credit but the term of credit has expired

3. Where the buyer has become insolvent even though the period of credit has not yet expired. In the given case, A has agreed to sell certain goods to B on a credit of 10 days. The period of 10 days has expired. B has neither paid the price of goods nor taken the possession of the goods. That means the goods are still physically in the possession of A, the seller. In the mean time B, the buyer has become insolvent. In this case, A is entitled to exercise the right of lien on the goods because the buyer has become insolvent and the term of credit has expired without any payment of price by the buyer.

64. A, who is an agent of a buyer, had obtained the goods from the Railway Authorities and loaded the goods on his truck. In the meantime, the Railway Authorities received a notice from B, the seller for stopping the goods in transit as the buyer has become insolvent. Referring to the provisions of Sale of Goods Act, 1930, decide whether the Railway Authorities can stop the goods in transit as instructed by the seller?

Sol. The right of stoppage of goods in transit means the right of stopping the goods after the seller has parted with the goods. Thereafter the seller regains the possession of the goods.

This right can be exercised by an unpaid seller when he has lost his right of lien over the goods because the goods are delivered to a carrier for the purpose of taking the goods to the buyer. This right is available to the unpaid seller only when the buyer has become insolvent. The conditions necessary for exercising this right are: -

1. The buyer has not paid the total price to the seller
2. The seller has delivered the goods to a carrier thereby losing his right of lien
3. The buyer has become insolvent
4. The goods have not reached the buyer, they are in the course of transit. (Section 50, 51 and 52)

In the given case A, who is an agent of the buyer, had obtained the goods from the railway authorities and loaded the goods on his truck. After this the railway authorities received a notice from the seller B to stop the goods as the buyer had become insolvent.

According to the Sales of Goods Act, 1930, the railway authorities cannot stop the goods because the goods are not in transit. A who has loaded the goods on his truck is the agent of the buyer. That means railway authorities have given the possession of the goods to the buyer. The transit comes to an end when the buyer or his agent takes the possession of the goods.

65. J sold a machine to K. K gave a cheque for the payment. The cheque was dishonoured. But J handed over a delivery order to K. K sold the goods to R on the basis of the delivery order. J wanted to exercise his right of lien on the goods. Can he do so under the provisions of the Sale of Goods Act, 1930?

Sol. The right of lien and stoppage in transit are meant to protect the seller. These will not be affected even when the buyer has made a transaction of his own goods which were with the seller under lien. But under two exceptional cases these rights of the seller are affected: -

1. When the buyer has made the transaction with the consent of the seller
2. When the buyer has made the transaction on the basis of documents of title such as bill of lading, railway receipt or a delivery order etc.

In the given case, J has sold the machine to K and K gave a cheque for the payment. But the cheque was dishonoured that means J, the seller is an unpaid seller. So, he is entitled to exercise the right of lien, but according to section 53(1) his right of lien is defeated because he has given the document of title to the buyer and the buyer has made a transaction of sale on the basis of this document. So, R who has purchased the machine from K can demand the delivery of the machine

Sampurna (CA-Foundation)

THE INDIAN PARTNERSHIP ACT, 1932 GENERAL NATURE OF PARTNERSHIP

Q. Bank

1. Mr. XU and Mr. YU are partners in a partnership firm. Mr. XU introduced MU (an employee) as his partner to ZU. MU remained silent. ZU, a trader believing MU as partner supplied 50 Laptops to the firm on credit. After expiry of credit period, ZU did not get amount of Laptop sold to the partnership firm. ZU filed a suit against XU and MU for the recovery of price. Does MU is liable for such purpose?

Sol. As per Section 28 of Indian Partnership Act, 1932, Partnership by holding out is also known as partnership by estoppel. Where a man holds himself out as a partner, or allows others to do it, he is then stopped from denying the character he has assumed and upon the faith of which creditors may be presumed to have acted. A person may himself, by his words or conduct have induced others to believe that he is a partner or he may have allowed others to represent him as a partner. The result in both the cases is identical.

In the given case, **MU (the Manager) is also liable for the price** because he becomes a partner by holding out as per Section 28 of Indian Partnership Act, 1932.

2. Ms. Lucy while drafting partnership deed taken care of few important points. What are those points? She wants to know the list of information which must be part of partnership deed drafted by her. Also, give list of information to be included in partnership deed?

Sol. Ms. Lucy while drafting partnership deed must take care of following important points:

- No particular formalities are required for an agreement of partnership.
- Partnership deed may be in writing or formed verbally. The document in writing containing the various terms and conditions as to the relationship of the partners to each other is called the 'partnership deed'.
- Partnership deed should be drafted with care and be stamped according to the provisions of the Stamp Act, 1899.

- If partnership comprises immovable property, the instrument of partnership must be in writing, stamped and registered under the Registration Act.

List of information included in Partnership Deed while drafting Partnership Deed by Ms. Lucy:

1. Name of the partnership firm.
2. Names of all the partners.
3. Nature and place of the business of the firm.
4. Date of commencement of partnership.
5. Duration of the partnership firm.
6. Capital contribution of each partner.
7. Profit Sharing ratio of the partners.
8. Admission and Retirement of a partner.
9. Rates of interest on Capital, Drawings and loans.
10. Provisions for settlement of accounts in the case of dissolution of the firm.
11. Provisions for Salaries or commissions, payable to the partners, if any.
12. Provisions for expulsion of a partner in case of gross breach of duty or fraud.

Note: Ms. Lucy may add or delete any provision according to the needs of the partnership firm.

3. Define partnership and name the essential elements for the existence of a partnership as per the Indian Partnership Act, 1932. Explain any two such elements in detail.

Sol. Definition of Partnership: 'Partnership' is the relation between persons who have agreed to share the profits of a business carried on by all or any of them acting for all. (Section 4 of the Indian Partnership Act, 1932)

The definition of the partnership contains the following five elements which must co-exist before a partnership can come into existence:



1. Association of two or more persons
2. Agreement
3. Business
4. Agreement to share Profits
5. Business carried on by all or any of them acting for all

ELEMENTS OF PARTNERSHIP

The definition of the partnership contains the following five elements which must co-exist before a partnership can come into existence:

1. **Association of two or more persons:** Partnership is an association of 2 or more persons. Again, only persons recognized by law can enter into an agreement of partnership. Therefore, a firm, since it is not a person recognized in the eyes of law cannot be a partner. Again, a minor cannot be a partner in a firm, but with the consent of all the partners, may be admitted to the benefits of partnership. The Partnership Act is silent about the maximum number of partners but Section 464 of the Companies Act, 2013 read with the relevant Rules has now put a limit of 50 partners in any association / partnership firm.
2. **Agreement:** It may be observed that partnership must be the result of an agreement between two or more persons. There must be an agreement entered into by all the persons concerned. This element relates to voluntary contractual nature of partnership. Thus, the nature of the partnership is voluntary and contractual. An agreement from which relationship of Partnership arises may be express. It may also be implied from the act done by partners and from a consistent course of conduct being followed, showing mutual understanding between them. It may be oral or in writing.
3. **Business:** In this context, we will consider two propositions. First, there must exist a business. For the purpose, the term 'business' includes every trade, occupation and profession. The existence of business is essential. Secondly, the motive of the business is the "acquisition of gains" which leads to the formation of partnership. Therefore, there can be no partnership where there is no intention to carry on the business and to share the profit thereof.
4. **Agreement to share profits:** The sharing of profits is an essential feature of partnership. There can be no partnership where only one of the

partners is entitled to the whole of the profits of the business. Partners must agree to share the profits in any manner they choose. But an agreement to share losses is not an essential element. It is open to one or more partners to agree to share all the losses. However, in the event of losses, unless agreed otherwise, these must be borne in the profit-sharing ratio.

5. **Business carried on by all or any of them acting for all:** The business must be carried on by all the partners or by anyone or more of the partners acting for all. **This is the cardinal principle of the partnership Law.** In other words, there should be a binding contract of mutual agency between the partners. An act of one partner in the course of the business of the firm is in fact an act of all partners. Each partner carrying on the business is the principal as well as the agent for all the other partners. He is an agent in so far as he can bind the other partners by his acts and he is a principal to the extent that he is bound by the act of other partners. It may be noted that **the true test of partnership is mutual agency rather than sharing of profits.** If the element of mutual agency is absent, then there will be no partnership.

4. State whether the following are partnerships:
 - (1) A and B jointly own a car which they used personally on Sundays and holidays and let it on hire as taxi on other days and equally divide the earnings.
 - (2) Two firms each having 12 partners combine by an agreement into one firm.
 - (3) A and B, co-owners, agree to conduct the business in common for profit.
 - (4) Some individuals form an association to which each individual contributes Rs. 500 annually. The objective of the association is to produce clothes and distribute the clothes free to the war widows.
 - (5) A and B, co-owners share between themselves the rent derived from a piece of land. A and B buy commodity X and agree to sell the commodity with sharing the profits equally.
- Sol.** (i) No, this is not a case of partnership because the sharing of profits or of gross returns accruing from property holding joint or common interest in the property would not by itself make such person's partners.

Alternatively, this part can also be answered as below:

Yes, this is a case of partnership, as the car is used personally only on Sundays and holidays and used for most of the days as a Taxi. Hence, it is inferred that the main purpose of owning the car is to let it for business purpose. Also, there is an agreement for equally dividing the earnings.

- (ii) Yes, this is a case of partnership because there is an agreement between two firms to combine into one firm.
- (iii) Yes, this is a case of partnership because A & B, co-owners, have agreed to conduct a business in common for profit.
- (iv) No, this is not a case of partnership as no charitable association can be floated in partnership. No, this is not a case of partnership as they are co-owners and not the partners. Further, there exist no business.
- (v) Yes, this is a case of partnership as there exist the element of doing business and sharing of profit equally.

5. "Sharing in the profits is not conclusive evidence in the creation of partnership". Comment.

Sol. Sharing of profit is an essential element to constitute a partnership. But it is only a prima facie evidence and not conclusive evidence, in that regard. The sharing of profits or of gross returns accruing from property by persons holding joint or common interest in the property would not by itself make such person's partners. Although the right to participate in profits is a strong test of partnership, and there may be cases where, upon a simple participation in profits, there is a partnership, yet whether the relation does or does not exist must depend upon the whole contract between the parties.

Where there is an express agreement between partners to share the profit of a business and the business is being carried on by all or any of them acting for all, there will be no difficulty in the light of provisions of Section 4, in determining the existence or otherwise of partnership.

But the task becomes difficult when either there is no specific agreement or the agreement is such as does not specifically speak of partnership. In such a case for testing the existence or otherwise of partnership relation, Section 6 has to be referred.

According to Section 6, regard must be had to the real relation between the parties as shown by all relevant facts taken together. The rule is easily stated and is clear but its application is difficult. Cumulative effect of all relevant facts such as written or verbal agreement, real intention and conduct of the parties, other surrounding circumstances, are to be considered while deciding the relationship between the parties and ascertaining the existence of partnership.

Hence, the statement is true / correct that mere sharing in the profits is not conclusive evidence

6. What do you mean by "Particular Partnership" under the Indian Partnership Act, 1932?

Sol. Particular partnership: A partnership may be organized for the prosecution of a single adventure as well as for the conduct of a continuous business. Where a person becomes a partner with another person in any particular adventure or undertaking, the partnership is called 'particular partnership'.

A partnership, constituted for a single adventure or undertaking is, subject to any agreement, dissolved by the completion of the adventure or undertaking.

7. Who is a nominal partner under the Indian Partnership Act, 1932? What are his liabilities?

Sol. Nominal Partner: A person who lends his name to the firm, without having any real interest in it, is called a nominal partner. **Liabilities:** He is not entitled to share the profits of the firm. Neither he invests in the firm nor takes part in the conduct of the business. He is, however liable to third parties for all acts of the firm.

8. Business carried on by all or any of them acting for all." Discuss the statement under the Indian Partnership Act, 1932.

Sol. Business carried on by all or any of them acting for all: The business must be carried on by all the partners or by anyone or more of the partners acting for all. In other words, there should be a binding contract of mutual agency between the partners.

An act of one partner in the course of the business of the firm is in fact an act of all partners. Each partner carrying on the business is the principal as well as the agent for all the other partners. He is an agent in so far as he can bind the other partners by his acts and he is a principal to the extent that he is bound by the act of other partners.

It may be noted that the true test of partnership is mutual agency. If the element of mutual agency is absent, then there will be no partnership.

In KD Kamath & Co., the Supreme Court has held that the two essential conditions to be satisfied are that:

- (1) there should be an agreement to share the profits as well as the losses of business; and
- (2) the business must be carried on by all or any of them acting for all, within the meaning of the definition of 'partnership' under section 4.

The fact that the exclusive power and control, by agreement of the parties, is vested in one partner or the further circumstance that only one partner can operate the bank accounts or borrow on behalf of the firm are not destructive of the theory of partnership provided the two essential conditions, mentioned earlier, are satisfied.

9. What is the conclusive evidence of partnership? State the circumstances when partnership is not considered between two or more parties.

Sol. Conclusive evidence of partnership: Existence of Mutual Agency which is the cardinal principle of partnership law is very much helpful in reaching a conclusion with respect to determination of existence of partnership. Each partner carrying on the business is the principal as well as an agent of other partners. So, the act of one partner done on behalf of firm, binds all the partners. If the element of mutual agency relationship exists between the parties constituting a group formed with a view to earn profits by running a business, a partnership may be deemed to exist.

Circumstances when partnership is not considered between two or more parties: Various judicial pronouncements have laid to the following factors leading to no partnership between the parties:

- (i) Parties have not retained any record of terms and conditions of partnership.
- (ii) Partnership business has maintained no accounts of its own, which would be open to inspection by both parties
- (iii) No account of the partnership was opened with any bank
- (iv) No written intimation was conveyed to the Deputy Director of Procurement with respect to the newly created partnership.

10. "Whether a group of persons is or is not a firm, or whether a person is or not a partner in a firm." Explain the mode of determining existence of partnership as per the Indian Partnership Act, 1932?

Sol. Mode of determining existence of partnership (Section 6 of the Indian Partnership Act, 1932): In determining whether a group of persons is or is not a firm, or whether a person is or not a partner in a firm, regard shall be had to the real relation between the parties, as shown by all relevant facts taken together. For determining the existence of partnership, it must be proved.

- (1) There was an **agreement** between all the persons concerned
- (2) The agreement was to **share the profits** of a business and
- (3) the business was **carried on by all or any of them** acting for all.

Agreement: Partnership is created by agreement and not by status (Section 5). 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 are not partners in such business.

Sharing of Profit: Sharing of profit is an essential element to constitute a partnership. But, it is only a *prima facie* evidence and not conclusive evidence, in that regard. The sharing of profits or of gross returns accruing from property by persons holding joint or common interest in the property would not by itself make such persons partners. Although the right to participate in profits is a strong test of partnership, and there may be cases where, upon a simple participation in profits, there is a partnership, yet whether the relation does or does not exist must depend upon the whole contract between the parties.

Agency: Existence of Mutual Agency which is the cardinal principle of partnership law, is very much helpful in reaching a conclusion in this regard. Each partner carrying on the business is the principal as well as an agent of other partners. So, the act of one partner done on behalf of firm, binds all the partners. If the elements of mutual agency relationship exist between the parties constituting a group formed with a view to earn profits by running a business, a partnership may be deemed to exist

11. What do you mean by Goodwill as per the provisions of Indian Partnership Act, 1932?

Sol. Goodwill: The term "Goodwill" has not been defined under the Indian Partnership Act, 1932. Section 14 of the Act lays down that goodwill of a business is to be regarded as a property of the firm.

Goodwill may be defined as the value of the reputation of a business house in respect of profits expected in future over and above the normal level of profits earned by undertaking belonging to the same class of business.

12. State the differences between Partnership and Hindu Undivided Family.

Sol.

Basis of difference	Partnership	Joint Hindu family
Mode of creation	Partnership is created necessarily by an agreement.	The right in the joint family is created by status means its creation by birth in the family.
Death of a member	Death of a partner ordinarily leads to the dissolution of partnership.	The death of a member in the Hindu undivided family does not give rise to dissolution of the family business.
Management	All the partners are equally entitled to take part in the partnership business.	The right of management of joint family business generally vests in the Karta, the governing male member or female member of the family. ¹
Authority to bind	Every partner can, by his act, bind the firm.	The Karta or the manager, has the authority to contract for the family business and the other members in the family.
Liability	In a partnership, the liability of a partner is unlimited.	In a Hindu undivided family, only the liability of the Karta is unlimited, and the other coparcener are liable only to the extent of their share in the profits of the family business.
Calling for accounts on closure	A partner can bring a suit against the firm	On the separation of the joint family, a member is not entitled to ask for account of the family business
	for accounts, provided he also seeks the dissolution of the firm.	
Governing Law	A partnership is governed by the Indian Partnership Act, 1932.	A Joint Hindu Family business is governed by the Hindu Law.
Minor's capacity	In a partnership, a minor cannot become a partner, though he can be admitted to the benefits of partnership, only with the consent of all the partners.	In Hindu undivided family business, a minor becomes a member of the ancestral business by the incidence of birth. He does not have to wait for attaining majority.
Continuity	A firm subject to a contract between the partners gets dissolved by death or insolvency of a partner.	A Joint Hindu family has the continuity till it is divided. The status of Joint Hindu family is not thereby

		affected by the death of a member.
Number of Members	In case of Partnership number of members should not exceed 50.	Members of HUF who carry on a business may be unlimited in number.
Share in the business	In a partnership, each partner has a defined share by virtue of an agreement between the partners.	In a HUF, no coparceners has a definite share. His interest is a fluctuating one. It is capable of being enlarged by deaths in the family diminished by births in the family.

13. Explain the following kinds of partnership under the Indian Partnership Act, 1932:

- (1) Partnership at will
- (2) Particular partnership

Sol. Partnership at will: According to Section 7 of the Indian Partnership Act, 1932, partnership at will is a partnership when:

- (1) no fixed period has been agreed upon for the duration of the partnership; and
- (2) there is no provision made as to the determination of the partnership.

These two conditions must be satisfied before a partnership can be regarded as a partnership at will. But, where there is an agreement between the partners either for the duration of the partnership or for the determination of the partnership, the partnership is not partnership at will.

Where a partnership entered into for a fixed term is continued after the expiry of such term, it is to be treated as having become a partnership at will.

A partnership at will may be dissolved by any partner by giving notice in writing to all the other partners of his intention to dissolve the same.

Particular partnership: A partnership may be organized for the prosecution of a single adventure as well as for the conduct of a continuous business. Where a person becomes a partner with another person in any particular adventure or undertaking the partnership is called 'particular partnership'. A partnership, constituted for a single adventure or undertaking is, subject to any agreement, dissolved by the completion of the adventure or undertaking.

14. X and Y are partners in a partnership firm. X introduced A, a manager, as his partner to Z. A remained silent. Z, a trader believing A as partner supplied 100 T.V. sets to the firm on credit. After expiry of credit period, Z did not get amount of T.V. sets sold to the partnership firm. Z filed a suit against X and A for the recovery of price. Advise Z whether

he can recover the amount from X and A under the Indian Partnership Act, 1932.

Sol. In the given case, along with X, the Manager (A) is also liable for the price because he becomes a partner by holding out (Section 28, Indian Partnership Act, 1932).

Partner by holding out (Section 28): Partnership by holding out is also known as partnership by estoppel. Where a man holds himself out as a partner, or allows others to do it, he is then stopped from denying the character he has assumed and upon the faith of which creditors may be presumed to have acted.

It is only the person to whom the representation has been made and who has acted thereon that has right to enforce liability arising out of 'holding out'.

You must also note that for the purpose of fixing liability on a person who has, by representation, led another to act, it is not necessary to show that he was actuated by a fraudulent intention.

The rule given in Section 28 is also applicable to a former partner who has retired from the firm without giving proper public notice of his retirement. In such cases, a person who, even subsequent to the retirement, give credit to the firm on the belief that he was a partner, will be entitled to hold him liable.

15. Explain the provisions of the Indian Partnership Act, 1932 relating to the creation of Partnership by holding out.

Sol. Partnership by holding out is also known as partnership by estoppel. Where a man holds himself out as a partner, or allows others to do it, he is then stopped from denying the character he has assumed and upon the faith of which creditors may be presumed to have acted.

A person may himself, by his words or conduct have induced others to believe that he is a partner or he may have allowed others to represent him as a partner. The result in both the cases is identical.

Example: X and Y are partners in a partnership firm. X introduced A, a manager, as his partner to Z. A remained silent. Z, a trader believing A as partner supplied 100 T.V sets to the firm on credit. After expiry of credit period, Z did not get amount of T.V sets sold to the partnership firm. Z filed a suit against X and A for the recovery of price. Here, in the given case, A, the Manager is also liable for the price because he becomes a partner by holding out (Section 28, Indian Partnership Act, 1932).

It is only the person to whom the representation has been made and who has acted thereon that has right to enforce liability arising out of 'holding out'.

Sampurna (CA-Foundation)

RELATIONS OF PARTNERS

Q. Bank

16. State the modes by which a partner may transfer his interest in the firm in favour of another person under the Indian Partnership Act, 1932. What are the rights of such a transferee?

Sol. Section 29 of the Indian Partnership Act, 1932 provides that a share in a partnership is transferable like any other property, but as the partnership relationship is based on mutual confidence, the assignee of a partner's interest by sale, mortgage or otherwise cannot enjoy the same rights and privileges as the original partner.

The rights of such a transferee are as follows:

- (1) During the continuance of partnership, such transferee is not entitled
 - (a) to interfere with the conduct of the business,
 - (b) to require accounts, or
 - (c) to inspect books of the firm.

He is only entitled to receive the share of the profits of the transferring partner and he is bound to accept the profits as agreed to by the partners, i.e., he cannot challenge the accounts.

- (2) On the dissolution of the firm or on the retirement of the transferring partner, the transferee will be entitled, against the remaining partners:
 - (a) to receive the share of the assets of the firm to which the transferring partner was entitled, and
 - (b) for the purpose of ascertaining the share, he is entitled to an account as from the date of the dissolution.

By virtue of Section 31, no person can be introduced as a partner in a firm without the consent of all the partners. A partner cannot by transferring his own interest, make anybody else a partner in his place, unless the other partners agree to accept that person as a partner. At the same time, a partner is not debarred from transferring his interest. A partner's interest in the partnership can be regarded as an existing interest and tangible property which can be assigned.

17. Whether a minor may be admitted in the business of a partnership firm? Explain the rights of a minor in the partnership firm.

Sol. A minor cannot be bound by a contract because a minor's contract is void and not merely voidable. Therefore, a minor cannot become a partner in a firm because partnership is founded on a contract. Though a minor cannot be a partner in a firm, he can nonetheless be admitted to the benefits of partnership under Section 30 of the Indian Partnership Act, 1932. In other words, he can be validly given a share in the partnership profits. When this has been done and it can be done with the consent of all the partners then the rights and liabilities of such a partner will be governed under Section 30 as follows:

Rights:

- (i) A minor partner has a right to his agreed share of the profits and of the firm.
- (ii) He can have access to, inspect and copy the accounts of the firm.
- (iii) He can sue the partners for accounts or for payment of his share but only when severing his connection with the firm, and not otherwise.

On attaining majority, he may within 6 months elect to become a partner or not to become a partner. If he elects to become a partner, then he is entitled to the share to which he was entitled as a minor. If he does not, then his share is not liable for any acts of the firm after the date of the public notice served to that effect.

18. M/s XYZ & Associates, a partnership firm with X, Y, Z as senior partners were engaged in the business of carpet manufacturing and exporting to foreign countries. On 25th August, 2018, they inducted Mr. G, an expert in the field of carpet manufacturing as their partner. On 10th January 2020, Mr. G was blamed for unauthorized activities and thus expelled from the partnership by united approval of rest of the partners. Examine whether action by the partners was justified or not? What should have the factors to be kept in mind prior expelling a partner from the firm by other partners according to the provisions of the Indian Partnership Act, 1932?

Sol. Expulsion of a Partner (Section 33 of the Indian Partnership Act, 1932):

- A partner may not be expelled from a firm by a majority of partners except in exercise, in good faith, of powers conferred by contract between the partners.
- The test of good faith as required under Section 33(1) includes three things:
- The expulsion must be in the interest of the partnership.
- The partner to be expelled is served with a notice.
- He is given an opportunity of being heard.
- If a partner is otherwise expelled, the expulsion is null and void.
- Action by the partners of M/s XYZ & Associates, a partnership firm to expel Mr. G from the partnership was justified as he was expelled by united approval of the partners exercised in good faith to protect the interest of the partnership against the unauthorized activities charged against Mr. G. A proper notice and opportunity of being heard has to be given to Mr. G.
- The following are the factors to be kept in mind prior expelling a partner from the firm by other partners:
- the power of expulsion must have existed in a contract between the partners;

the power has been exercised by a majority of the partners; and it has been exercised in good faith.

19. A, B and C are partners in a firm. As per terms of the partnership deed, A is entitled to 20 percent of the partnership property and profits. A retires from the firm and dies after 15 days. B and C continue business of the firm without settling accounts. Explain the rights of A's legal representatives against the firm under the Indian Partnership Act, 1932?

Sol. Section 37 of the Indian Partnership Act, 1932 provides that where a partner dies or otherwise ceases to be a partner and there is no final settlement of account between the legal representatives of the deceased partner or the firms with the property of the firm, then, in the absence of a contract to the contrary, the legal representatives of the deceased partner or the retired partner are entitled to claim either.

Such shares of the profits earned after the death or retirement of the partner which is attributable to the use of his share in the property of the firm; or Interest at the rate of 6 per cent annum on the amount of his share in the property.

Based on the aforesaid provisions of Section 37 of the Indian Partnership Act, 1932 in the given problem, A's Legal representatives shall be entitled, at their option to:

the 20% shares of profits (as per the partnership deed); or

interest at the rate of 6 per cent per annum on the amount of A's share in the property.

20. Master X was introduced to the benefits of partnership of M/s ABC & Co. with the consent of all partners. After attaining majority, more than six months elapsed and he failed to give a public notice as to whether he elected to become or not to become a partner in the firm. Later on, Mr. L, a supplier of material to M/s ABC & Co., filed a suit against M/s ABC & Co. for recovery of the debt due.

In the light of the Indian Partnership Act, 1932, explain:

- (1) To what extent X will be liable if he failed to give public notice after attaining majority?
- (2) Can Mr. L recover his debt from X?

Sol. As per the provisions of Section 30(5) of the Indian Partnership Act, 1932, at any time within six months of his attaining majority, or of his obtaining knowledge that he had been admitted to the benefits of partnership, whichever date is later, such person may give public notice that he has elected to become or that he has elected not to become a partner in the firm, and such notice shall determine his position as regards the firm.

However, if he fails to give such notice, he shall become a partner in the firm on the expiry of the said six months.

If the minor becomes a partner by his failure to give the public notice within specified time, his rights and liabilities as given in Section 30(7) are as follows:

He becomes personally liable to third parties for all acts of the firm done since he was admitted to the benefits of partnership.

His share in the property and the profits of the firm remains the same to which he was entitled as a minor.

In the instant case, since, X has failed to give a public notice, he shall become a partner in the M/s ABC & Co. and becomes personally liable to Mr. L, a third party.

In the light of the provisions of Section 30(7) read with Section 30(5) of the Indian Partnership Act, 1932, since X has failed to give public notice that he has not elected to not to become a partner within six months, he will be deemed to be a partner after the period of the above six months and therefore, Mr. L can recover his debt from him also in the same way as he can recover from any other partner.

21. Mr. A (transferor) transfer his share in a partnership firm to Mr. B (transferee). Mr. B is not entitled for few rights and privileges as Mr. A (transferor) is entitled therefor. Discuss in brief the points for which Mr. B is not entitled during continuance of partnership?

Sol. As per Section 29 of Indian Partnership Act, 1932, a transfer by a partner of his interest in the firm, either absolute or by mortgage, or by the creation by him of a charge on such interest, does not entitle the transferee, during the continuance of the firm, to interfere in the conduct of business, or to require accounts, or to inspect the books of the firm, but entitles the transferee only to receive the share of profits of the transferring partner, and the transferee shall accept the account of profits agreed to by the partners.

In the given case during the continuance of partnership, such transferee Mr. B is not entitled:

- to interfere with the conduct of the business.
- to require accounts.
- to inspect books of the firm.

However, Mr. B is only entitled to receive the share of the profits of the transferring partner and he is bound to accept the profits as agreed to by the partners, i.e. he cannot challenge the accounts.

22. M, N and P were partners in a firm. The firm ordered JR Limited to supply the furniture. P dies, and M and N continues the business in the firm's name. The firm did not give any notice about P's death to the public or the persons dealing with the firm. The furniture was delivered to the firm after P's death, fact about his death was known to them at the time of delivery. Afterwards the firm became insolvent and failed to pay the price of furniture to JR Limited.

Explain with reasons:

- (1) Whether P's private estate is liable for the price of furniture purchased by the firm?
- (2) Whether does it make any difference if JR Limited supplied the furniture to the firm believing that all the three partners are alive?

Sol. According to Section 35 of the Indian Partnership Act, 1932, where under a contract between the partners the firm is not dissolved by the death of a partner, the estate of a deceased partner is not liable for any act of the firm done after his death.

Further, in order that the estate of the deceased partner may be absolved from liability for the future obligations of the firm, it is not necessary to give any notice either to the public or the persons having dealings with the firm.

In the given question, JR Limited has supplied furniture to the partnership firm, after P's death. The firm did not give notice about P's death to public or people dealing with the firm. Afterwards, the firm became insolvent and could not pay JR Limited.

In the light of the facts of the case and provisions of law:

Since the delivery of furniture was made after P's death, his estate would not be liable for the debt of the firm. A suit for goods sold and delivered would not lie against the representatives of the deceased partner. This is because there was no debt due in respect of the goods in P's lifetime.

It will not make any difference even if JR Limited supplied furniture to the firm believing that all the three partners are alive, as it is not necessary to give any notice either to the public or the persons having dealings with the firm, so the estate of the deceased partner may be absolved from liability for the future obligations of the firm.

23. Discuss the liability of a partner for the act of the firm and liability of firm for act of a partner to third parties as per Indian Partnership Act, 1932.

Sol. Liability of a partner for acts of the firm (Section 25 of the Indian Partnership Act, 1932): Every partner is liable, jointly with all the other partners and also severally, for all acts of the firm done while he is a partner. The partners are jointly and severally responsible to third parties for all acts which come under the scope of their express or implied authority. This is because that all the acts done within the scope of authority are the acts done towards the business of the firm.

The expression 'act of firm' connotes any act or omission by all the partners or by any partner or agent

of the firm, which gives rise to a right enforceable by or against the firm. Again in order to bring a case under Section 25, it is necessary that the act of the firm, in respect of which liability is brought to be enforced against a party, must have been done while he was a partner.

Liability of the firm for wrongful acts of a partner and for misapplication by partners (Sections 26 & 27 of the Indian Partnership Act, 1932): Where, -

by the wrongful act or omission of a partner in the ordinary course of the business of a firm, or with the authority of his partners, loss or injury is caused to any third party, or any penalty is incurred, the firm is liable therefor to the same extent as the partner.

A partner acting within his apparent authority receives money or property from a third party and misapplies it, or a firm in the course of its business receives money or property from a third party, and the money or property is misapplied by any of the partners while it is in the custody of the firm, the firm is liable to make good the loss.

24. Define Implied Authority. In the absence of any usage or custom of trade to the contrary, the implied authority of a partner does not empower him to do certain acts. State the acts which are beyond the implied authority of a partner under the provisions of the Indian Partnership Act, 1932?

Sol. According to Section 19 of the Indian Partnership Act, 1932, subject to the provisions of Section 22, the act of a partner which is done to carry on, in the usual way, business of the kind carried on by the firm, binds the firm. The authority of a partner to bind the firm conferred by this section is called his “implied authority”.

In the absence of any usage or custom of trade to the contrary, the implied authority of a partner does not empower him to-

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

25. Mr. M is one of the four partners in M/s XY Enterprises. He owes a sum of Rs. 6 crore to his friend Mr. Z which he is unable to pay on due time. So, he wants to sell his share in the firm to Mr. Z for settling the amount. In the light of the provisions of the Indian Partnership Act, 1932, discuss each of the following:

- (1) Can Mr. M validly transfer his interest in the firm by way of sale?
- (2) What would be the rights of the transferee (Mr. Z) in case Mr. M wants to retire from the firm after a period of 6 months from the date of transfer?

Sol. A transfer by a partner of his interest in the firm, either absolute or by mortgage, or by the creation by him of a charge on such interest, does not entitle the transferee, during the continuance of the firm, to interfere in the conduct of business, or to require accounts, or to inspect the books of the firm, but entitles the transferee only to receive the share of profits of the transferring partner, and the transferee shall accept the account of profits agreed to by the partners.

If the firm is dissolved or if the transferring partner ceases to be a partner, the transferee is entitled as against the remaining partners to receive the share of the assets of the firm to which the transferring partner is entitled, and, for the purpose of ascertaining that share, to an account as from the date of the dissolution.

In the light of facts of the question and provision of law:

Yes, Mr. M can validly transfer his interest in the firm by way of sale.

On the retirement of the transferring partner (Mr. M), the transferee (Mr. Z) will be entitled, against the remaining partners:

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.

So, in this case on Mr. M’s retirement, Mr. Z would be entitled to receive the value of Mr. M’s share to the extent of Rs. 6 crore in the firm’s assets.

26. Mr. A (transferor) transfer his share in a partnership firm to Mr. B (transferee). Mr. B is not entitled for few rights and privileges as Mr. A (transferor) is entitled therefor. Discuss in brief the points for which

Mr. B is not entitled during continuance of partnership?

Sol. As per Section 29 of Indian Partnership Act, 1932, a transfer by a partner of his interest in the firm, either absolute or by mortgage, or by the creation by him of a charge on such interest, does not entitle the transferee, during the continuance of the firm, to interfere in the conduct of business, or to require accounts, or to inspect the books of the firm, but entitles the transferee only to receive the share of profits of the transferring partner, and the transferee shall accept the account of profits agreed to by the partners.

In the given case during the continuance of partnership, such transferee Mr. B is not entitled:

- to interfere with the conduct of the business.
- to require accounts.
- to inspect books of the firm.

However, Mr. B is only entitled to receive the share of the profits of the transferring partner and he is bound to accept the profits as agreed to by the partners, i.e. he cannot challenge the accounts.

27. Sohan, Rohan and Jay were partners in a firm. The firm is dealer in office furniture. They have regular dealings with M/s AB and Co. for the supply of furniture for their business. On 30th June 2018, one of the partners, Mr. Jay died in a road accident. The firm has ordered M/s AB and Co. to supply the furniture for their business on 25 May 2018, when Jay was also alive. Now Sohan and Rohan continue the business in the firm's name after Jay's death. The firm did not give any notice about Jay's death to the public or the persons dealing with the firm. M/s AB and Co. delivered the furniture to the firm on 25 July 2018. The fact about Jay's death was known to them at the time of delivery of goods. Afterwards the firm became insolvent and failed to pay the price of furniture to M/s AB and Co. Now M/s AB and Co. has filed a case against the firm for recovery of the price of furniture. With reference to the provisions of Indian Partnership Act, 1932, explain whether Jay's private estate is also liable for the price of furniture purchased by the firm?

Sol. According to Section 35 of the Indian Partnership Act, 1932, where under a contract between the partners the firm is not dissolved by the death of a

partner, the estate of a deceased partner is not liable for any act of the firm done after his death.

Further, in order that the estate of the deceased partner may be absolved from liability for the future obligations of the firm, it is not necessary to give any notice either to the public or the persons having dealings with the firm.

In the light of the facts of the case and provisions of law, since the delivery of furniture was made after Jay's death, his estate would not be liable for the debt of the firm. A suit for goods sold and delivered would not lie against the representatives of the deceased partner.

This is because there was no debt due in respect of the goods in Jay's lifetime. He was already dead when the delivery of goods was made to the firm and also it is not necessary to give any notice either to the public or the persons having dealings with the firm on a death of a partner (Section 35). So, the estate of the deceased partner may be absolved from liability for the future obligations of the firm.

28. X, Y and Z are partners in a Partnership Firm. They were carrying their business successfully for the past several years. Spouses of X and Y fought in ladies club on their personal issue and X's wife was hurt badly. X got angry on the incident and he convinced Z to expel Y from their partnership firm. Y was expelled from partnership without any notice from X and Z. Considering the provisions of the Indian Partnership Act, 1932, state whether they can expel a partner from the firm. What are the criteria for test of good faith in such circumstances?

Sol. A partner may not be expelled from a firm by a majority of partners except in exercise, in good faith, of powers conferred by contract between the partners. It is, thus, essential that:

- the power of expulsion must have existed in a contract between the partners;
- the power has been exercised by a majority of the partners; and
- it has been exercised in good faith.

If all these conditions are not present, the expulsion is not deemed to be in bonafide interest of the business of the firm

- The test of good faith as required under Section 33(1) includes three things:
- The expulsion must be in the interest of the partnership.
- The partner to be expelled is served with a notice.

He is given an opportunity of being heard.

If a partner is otherwise expelled, the expulsion is null and void.

Thus, according to the test of good faith as required under Section 33(1), expulsion of Partner Y is not valid.

29. What is the provision related to the effect of notice to an acting partner of the firm as per the Indian Partnership Act, 1932?

Sol. Effect of notice to an acting partner of the firm

According to Section 24 of the Indian Partnership Act, 1932, notice to a partner who habitually acts in the business of the firm of any matter relating to the affairs of the firm operates as notice to the firm, except in the case of a fraud on the firm committed by or with the consent of that partner.

Thus, the notice to one is equivalent to the notice to the rest of the partners of the firm, just as a notice to an agent is notice to his principal. This notice must be actual and not constructive. It must further relate to the firm's business. Only then it would constitute a notice to the firm.

30. Discuss the provisions regarding personal profits earned by a partner under the Indian Partnership Act, 1932?

Sol. Personal Profit earned by Partners (Section 16 of the Indian Partnership Act, 1932)

According to section 16, subject to contract between the partners:

If a partner derives any profit for himself from any transaction of the firm, or from the use of the property or business connection of the firm or the firm name, he shall account for that profit and pay it to the firm; If a partner carries on any business of the same nature and competing with that of the firm, he shall account for and pay to the firm all profits made by him in that business.

31. "Though a minor cannot be a partner in a firm, he can nonetheless be admitted to the benefits of partnership." Referring to the provisions of the Indian Partnership Act, 1932, state the rights which can be enjoyed by a minor partner.

Sol. Rights which can be enjoyed by a minor partner:

A minor partner has a right to his agreed share of the profits and of the firm.

He can have access to, inspect and copy the accounts of the firm.

He can sue the partners for accounts or for payment of his share but only when severing his connection with the firm, and not otherwise.

On attaining majority, he may within 6 months elect to become a partner or not to become a partner. If he elects to become a partner, then he is entitled to the share to which he was entitled as a minor. If he does not, then his share is not liable for any acts of the firm after the date of the public notice served to that effect.

32. State the liabilities of a minor partner both:

- (1) Before attaining majority and
- (2) After attaining majority

Sol. Liabilities of a minor partner before attaining majority:

The liability of the minor is confined only to the extent of his share in the profits and the property of the firm.

Minor has no personal liability for the debts of the firm incurred during his minority.

Minor cannot be declared insolvent, but if the firm is declared insolvent his share in the firm vests in the Official Receiver/ Assignee.

Liabilities of a minor partner after attaining majority:

Within 6 months of his attaining majority or on his obtaining knowledge that he had been admitted to the benefits of partnership, whichever date is later, the minor partner has to decide whether he shall remain a partner or leave the firm.

Where he has elected not to become partner he may give public notice that he has elected not to become partner and such notice shall determine his position as regards the firm. If he fails to give such notice, he shall become a partner in the firm on the expiry of the said six months

33. State the legal position of a minor partner after attaining majority:

- (1) When he opts to become a partner of the same firm.
- (2) When he decides not to become a partner.

Sol. When he becomes partner: If the minor becomes a partner on his own willingness or by his failure to give the public notice within specified time, his rights and liabilities as given in Section 30(7) of the Indian Partnership Act, 1932, are as follows:

He becomes personally liable to third parties for all acts of the firm done since he was admitted to the benefits of partnership.

His share in the property and the profits of the firm remains the same to which he was entitled as a minor

When he elects not to become a partner:

His rights and liabilities continue to be those of a minor up to the date of giving public notice.

His share shall not be liable for any acts of the firm done after the date of the notice.

He shall be entitled to sue the partners for his share of the property and profits. It may be noted that such minor shall give notice to the Registrar that he has or has not become a partner.

- 34.** Mr. M, Mr. N and Mr. P were partners in a firm, which was dealing in refrigerators. On 1st October, 2018, Mr. P retired from partnership, but failed to give public notice of his retirement. After his retirement, Mr. M, Mr. N and Mr. P visited a trade fair and enquired about some refrigerators with latest techniques. Mr. X, who was exhibiting his refrigerators with the new techniques was impressed with the interactions of Mr. P and requested for the visiting card of the firm. The visiting card also included the name of Mr. P as a partner even though he had already retired. Mr. X supplied some refrigerators to the firm and could not recover his dues from the firm. Now, Mr. X wants to recover the dues not only from the firm, but also from Mr. P.

Analyse the above case in terms of the provisions of the Indian Partnership Act, 1932 and decide whether Mr. P is liable in this situation.

- Sol.** A retiring partner continues to be liable to third party for acts of the firm after his retirement until public notice of his retirement has been given either by himself or by any other partner. But the retired partner will not be liable to any third party if the latter deals with the firm without knowing that the former was partner.

Also, if the partnership is at will, the partner by giving notice in writing to all the other partners of his intention to retire will be deemed to be relieved as a partner without giving a public notice to this effect.

Also, as per section 28 of the Indian Partnership Act, 1932, where a man holds himself out as a partner, or allows others to do it, he is then stopped from denying the character he has assumed and upon the faith of which creditors may be presumed to have acted.

In the light of the provisions of the Act and facts of the case, Mr. P is also liable to Mr. X.

- 35.** When the continuing guarantee can be revoked under the Indian Partnership Act, 1932?

- Sol.** Revocation of continuing guarantee (Section 38 of the Indian Partnership Act, 1932)

According to section 38, a continuing guarantee given to a firm or to third party in respect of the transaction of a firm is, in the absence of an agreement to the contrary, revoked as to future transactions from the date of any change in the constitution of the firm. Such change may occur by the death, or retirement of a partner, or by introduction of a new partner.

- 36.** Comment on 'the right to expel partner must be exercised in good faith' under the Indian Partnership Act, 1932.

- Sol.** A partner may not be expelled from a firm by a majority of partners except in exercise, in good faith, of powers conferred by contract between the partners. It is, thus, essential that:

the power of expulsion must have existed in a contract between the partners;

the power has been exercised by a majority of the partners; and

it has been exercised in good faith.

If all these conditions are not present, the expulsion is not deemed to be in *bona fide* interest of the business of the firm.

- 37.** P, Q, R and S are the partners in M/S PQRS & Co., a partnership firm which deals in trading of Washing Machines of various brands. Due to the conflict of views between partners, P & Q decided to leave the partnership firm and started competitive business on 31st July, 2019, in the name of M/S PQ & Co. Meanwhile, R & S have continued using the property in the name of M/S PQRS & Co. in which P & Q also has a share.

Based on the above facts, explain in detail the rights of outgoing partners as per the Indian Partnership Act, 1932 and comment on the following:

- (1) Rights of P & Q to start a competitive business.
- (2) Rights of P & Q regarding their share in property of M/S PQRS & Co.

- Sol.** Rights of outgoing partner to carry on competing business (Section 36 of the Indian Partnership Act, 1932)

An outgoing partner may carry on business competing with that of the firm and he may advertise such business, but subject to contract to the contrary, he may not,-

- use the firm name,
- represent himself as carrying on the business of the firm or
- solicit the custom of persons who were dealing with the firm before he ceased to be a partner.

Although this provision has imposed some restrictions on an outgoing partner, it effectively permits him to carry on a business competing with that of the firm. However, the partner may agree with his partners that on his ceasing to be so, he will not carry on a business similar to that of the firm within a specified period or within specified local limits. Such an agreement will not be in restraint of trade if the restraint is reasonable [Section 36 (2)].

From the above, we can infer that P & Q can start competitive business in the name of M/S PQ & Co after following above conditions in the absence of any agreement.

Right of outgoing partner in certain cases to share subsequent profits (Section 37 of the Indian Partnership Act, 1932)

According to Section 37, where any member of a firm has died or otherwise ceased to be partner, and the surviving or continuing partners carry on the business of the firm with the property of the firm without any final settlement of accounts as between them and the outgoing partner or his estate, then, in the absence of a contract to the contrary, the outgoing partner or his estate is entitled at the option of himself or his representatives to such share of the profits made since he ceased to be a partner as may be attributable to the use of his share of the property of the firm or to interest at the rate of six per cent per annum on the amount of his share in the property of the firm.

In the instant case, P & Q can share in property of M/s PQRS & Co. keeping in view of the above provisions.

- 38.** Explain in detail the circumstances which lead to liability of firm for misapplication by partners as per provisions of the Indian Partnership Act, 1932.

Sol. Where-

a partner acting within his apparent authority receives money or property from a third party and misapplies it, or

a firm in the course of its business receives money or property from a third party, and the money or property is misapplied by any of the partners while it is in the custody of the firm, the firm is liable to make good the loss.

It may be observed that the workings of the two clauses of Section 27 is designed to bring out clearly an important point of distinction between the two categories of cases of misapplication of money by partners.

Clause (a) covers the case where a partner acts within his authority and due to his authority as partner, he receives money or property belonging to a third party and misapplies that money or property. For this provision to be attracted, it is not necessary that the money should have actually come into the custody of the firm.

On the other hand, the provision of clause (b) would be attracted when such money or property has come into the custody of the firm and it is misapplied by any of the partners.

The firm would be liable in both the cases

- 39.** What do you mean by “implied authority” of the partners in a firm? Point out the extent of partner’s implied authority in case of emergency, referring to the provisions of the Indian Partnership Act, 1932.

Sol. Implied Authority of Partner as Agent of the Firm (Section 19): Subject to the provisions of section 22, the act of a partner which is done to carry on, in the usual way, business of the kind carried on by the firm, binds the firm.

The authority of a partner to bind the firm conferred by this section is called his “implied authority”.

In the absence of any usage or custom of trade to the contrary, the implied authority of a partner does not empower him to-

Submit a dispute relating to the business of the firm to arbitration;

open a banking account on behalf of the firm in his own name;

compromise or relinquish any claim or portion of a claim by the firm;

withdraw a suit or proceedings filed on behalf of the firm;

admit any liability in a suit or proceedings against the firm;

acquire immovable property on behalf of the firm;

transfer immovable property belonging to the firm; and

enter into partnership on behalf of the firm.

Mode Of Doing Act To Bind Firm (Section 22): In order to bind a firm, an act or instrument done or executed by a partner or other person on behalf of the firm shall be done or executed in the firm name, or in

any other manner expressing or implying an intention to bind the firm.

40. “Partner indeed virtually embraces the character of both a principal and an agent”. Describe the said statement keeping in view of the provisions of the Indian Partnership Act, 1932.

Sol. “**Partner indeed virtually embraces the character of both a principal and an agent**”: Subject to the provisions of section 18 of the Indian Partnership Act, 1932, a partner is the agent of the firm for the purposes of the business of the firm.

A partnership is the relationship between the partners who have agreed to share the profits of the business carried on by all or any of them acting for all (Section 4). This definition suggests that any of the partners can be the agent of the others.

Section 18 clarifies this position by providing that, subject to the provisions of the Act, a partner is the agent of the firm for the purpose of the business of the firm. **The partner indeed virtually embraces the character of both a principal and an agent.** So far as he acts for himself and in his own interest in the common concern of the partnership, he may properly be deemed as a principal and so far as he acts for his partners, he may properly be deemed as an agent.

The principal distinction between him and a mere agent is that he has a community of interest with other partners in the whole property and business and liabilities of partnership, whereas an agent as such has no interest in either.

The rule that a partner is the agent of the firm for the purpose of the business of the firm cannot be applied to all transactions and dealings between the partners themselves. It is applicable only to the act done by partners for the purpose of the business of the firm.

41. Moni and Tony were partners in the firm M/s MOTO & Company. They admitted Sony as partner in the firm and he is actively engaged in day-to-day activities of the firm. There is a tradition in the firm that all active partners will get a monthly remuneration of Rs. 20,000 but no express agreement was there. After admission of Sony in the firm, Moni and Tony were continuing getting salary from the firm but no salary was given to Sony from the firm. Sony claimed his remuneration but denied by existing partners by saying that there was no express agreement for that. Whether under the Indian Partnership Act, 1932, Sony can claim remuneration from the firm?

Sol. By virtue of provisions of Section 13(a) of the Indian Partnership Act, 1932 a partner is not entitled to

receive remuneration for taking part in the conduct of the business. But this rule can always be varied by an express agreement, or by a course of dealings, in which event the partner will be entitled to remuneration. Thus, a partner can claim remuneration even in the absence of a contract, when such remuneration is payable under the continued usage of the firm. In other words, where it is customary to pay remuneration to a partner for conducting the business of the firm, he can claim it even in the absence of a contract for the payment of the same.

In the given problem, existing partners are getting regularly a monthly remuneration from firm customarily being working partners of the firm. As Sony also admitted as working partner of the firm, he is entitled to get remuneration like other partners.

42. Ram & Co., a firm consists of three partners A, B and C having one third share each in the firm. According to A and B, the activities of C are not in the interest of the partnership and thus want to expel C from the firm. Advise A and B whether they can do so quoting the relevant provisions of the Indian Partnership Act, 1932.

Sol. It is not possible for the majority of partners to expel a partner from the firm without satisfying the conditions as laid down in Section 33 of the Indian Partnership Act, 1932. The essential conditions before expulsion can be done are:

the power of expulsion must have existed in a contract between the partners;

the power has been exercised by a majority of the partners; and

It has been exercised in good faith.

The test of good faith includes:

- that the expulsion must be in the interest of the partnership;
- that the partner to be expelled is served with a notice; and
- that the partner has been given an opportunity of being heard.

Thus, in the given case A and B the majority partners can expel the partner only if the above conditions are satisfied and procedure as stated above has been followed.

43. State the legal consequences of the following as per the provisions of the Indian Partnership Act, 1932:

- (1) Retirement of a partner
- (2) Insolvency of a partner

Sol. RETIREMENT OF A PARTNER (SECTION 32):

A partner may retire:

with the consent of all the other partners;
in accordance with an express agreement by the partners; or

where the partnership is at will, by giving notice in writing to all the other partners of his intention to retire.

A retiring partner may be discharged from any liability to any third party for acts of the firm done before his retirement by an agreement made by him with such third party and the partners of the reconstituted firm, and such agreement may be implied by a course of dealing between the third party and the reconstituted firm after he had knowledge of the retirement.

Notwithstanding the retirement of a partner from a firm, he and the partners continue to be liable as partners to third parties for any act done by any of them which would have been an act of the firm if done before the retirement, until public notice is given of the retirement:

Provided that a retired partner is not liable to any third party who deals with the firm without knowing that he was a partner.

Notices under sub-section (3) may be given by the retired partner or by any partner of the reconstituted firm.

Insolvency of a partner (Section 34)

The insolvent partner cannot be continued as a partner.

He will be ceased to be a partner from the very date on which the order of adjudication is made.

The estate of the insolvent partner is not liable for the acts of the firm done after the date of order of adjudication.

The firm is also not liable for any act of the insolvent partner after the date of the order of adjudication, Ordinarily but not invariably, the insolvency of a partner results in dissolution of a firm; but the partners are competent to agree among themselves that the adjudication of a partner as an insolvent will not give rise to dissolution of the firm

44. A, B and C are partners of a partnership firm carrying on the business of construction of apartments. B who himself was a wholesale dealer of iron bars was entrusted with the work of selection of iron bars after examining its quality. As a wholesaler, B is well aware of the market conditions. Current market price of iron bar for construction is Rs. 350 per Kilogram.

B already had 1000 Kg of iron bars in stock which he had purchased before price hike in the market for Rs. 200 per Kg. He supplied iron bars to the firm without the firm realizing the purchase cost. Is B liable to pay the firm the extra money he made, or he doesn't have to inform the firm as it is his own business and he has not taken any amount more than the current prevailing market price of Rs. 350? Assume there is no contract between the partners regarding the above.

- Sol.** According to section 16 of the Indian Partnership Act, 1932, subject to contract between partners if a partner derives any profit for himself from any transaction of the firm, or from the use of the property or business connection of the firm or the firm name, he shall account for that profit and pay it to the firm; if a partner carries on any business of the same nature as and competing with that of the firm, he shall account for and pay to the firm all profits made by him in that business.

In the given scenario, Mr. B had sold iron bar to the firm at the current prevailing market rate of Rs. 350 per Kg though he had stock with him which he bought for Rs. 200 per Kg. Hence, he made an extra profit of Rs. 150 per Kg. This is arising purely out of transactions with the firm. Hence, Mr. B is accountable to the firm for the extra profit earned thereby

45. Mr. A (transferor) transfers his share in a partnership firm to Mr. B (transferee). Mr. B felt that the book of accounts was displaying only a small amount as profit in spite of a huge turnover. He wanted to inspect the book of accounts of the firm arguing that it is his entitlement as a transferee. However, the other partners were of the opinion that Mr. B cannot challenge the books of accounts. As an advisor, help them solve the issue applying the necessary provisions from the Indian Partnership Act, 1932.

- Sol.** As per Section 29 of the Indian Partnership Act, 1932, during the continuance of the business, a transferee is not entitled
- To interfere with the conduct of the business
 - To require the accounts
 - To inspect the books of the firm He is only entitled to his share of profit.

Keeping the above points, in the given case, since the partnership business is in continuance, **Mr. B is bound to accept the profits as agreed to by the partners. He cannot challenge the accounts.** He is

only entitled to receive the share of profits of Mr. A (transferring partner).

46. A, B and C are partners in a firm called ABC Firm. A, with the intention of deceiving D, a supplier of office stationery, buys certain stationery on behalf of the ABC Firm. The stationery is of use in the ordinary course of the firm's business. A does not give the stationery to the firm, instead brings it to his own use. The supplier D, who is unaware of the private use of stationery by A, claims the price from the firm. The firm refuses to pay for the price, on the ground that the stationery was never received by it (firm). Referring to the provisions of the Indian Partnership Act, 1932 decide:

Whether the Firm's contention shall be tenable?

What would be your answer if a part of the stationery so purchased by A was delivered to the firm by him, and the rest of the stationery was used by him for private use, about which neither the firm nor the supplier D was aware?

Sol. The problem in the question is based on the 'Implied Authority' of a partner provided in Section 19 of the Indian Partnership Act, 1932. The section provides that subject to the provisions of Section 22 of the Act, the act of a partner, which is done to carry on, in the usual way, business of the kind carried on by the firm, binds the firm. The authority of a partner to bind the firm conferred by this section is called his 'Implied Authority' [Sub-Section (1) of section 19]. Furthermore, every partner is in contemplation of law the general and accredited agent of the partnership and may consequently bind all the other partners by his acts in all matters which are within the scope and object of the partnership. Hence, if the partnership is of a general commercial nature, he may buy goods on account of the partnership.

Considering the above provisions and explanation, the questions as asked in the problem may be answered as under:

The firm's contention is not tenable, for the reason that the partner, in the usual course of the business on behalf of the firm has an implied authority to bind the firm. The firm is, therefore, liable for the price of the goods.

In the second case also, the answer would be the same as above, i.e. the implied authority of the partner binds the firm.

In both the cases, however, the firm ABC can take action against A, the partner but it has to pay the price of stationery to the supplier D.

47. A, B, and C are partners of a partnership firm ABC & Co. The firm is a dealer in office furniture. A was in charge of purchase and sale, B was in charge of maintenance of accounts of the firm and C was in charge of handling all legal matters. Recently through an agreement among them, it was decided that A will be in charge of maintenance of accounts and B will be in charge of purchase and sale. Being ignorant about such agreement, M, a supplier supplied some furniture to A, who ultimately sold them to a third party. Referring to the provisions of the Partnership Act, 1932, advise whether M can recover money from the firm.

What will be your advice in case M was having knowledge about the agreement?

Sol. According to Section 20 of the Indian Partnership Act, 1932, the partners in a firm may, by contract between the partners, extend or restrict implied authority of any partners.

Notwithstanding any such restriction, any act done by a partner on behalf of the firm which falls within his implied authority binds the firm, unless the person with whom he is dealing knows of the restriction or does not know or believe that partner to be a partner. The implied authority of a partner may be extended or restricted by contract between the partners. Under the following conditions, the restrictions imposed on the implied authority of a partner by agreement shall be effective against a third party:

The third party knows above the restrictions, and
The third party does not know that he is dealing with a partner in a firm.

Now, referring to the case given in the question, M supplied furniture to A, who ultimately sold them to a third party and M was also ignorant about the agreement entered into by the partners about the change in their role. M also is not aware that he is dealing with a partner in a firm. Therefore, M on the basis of knowledge of implied authority of A, can recover money from the firm.

But in the second situation, if M was having knowledge about the agreement, he cannot recover money from the firm.

- 48.** X, Y and Z are partners in a Partnership Firm. They were carrying their business successfully for the past several years. Due to expansion of business, they planned to hire another partner Mr A. Now the firm has 4 partners X, Y, Z and A. The business was continuing at normal pace. In one of formal business meeting, it was observed that Mr. Y misbehaved with Mrs. A (wife of Mr. A). Mr. Y was badly drunk and also spoke rudely with Mrs. A. Mrs. A felt very embarrassed and told her husband Mr. A about the entire incident. Mr. A got angry on the incident and started arguing and fighting with Mr. Y in the meeting place itself. Next day, in the office Mr. A convinced X and Z that they should expel Y from their partnership firm. Y was expelled from partnership without any notice from X, A and Z.

Considering the provisions of the Indian Partnership Act, 1932, state whether they can expel a partner from the firm. What are the criteria for test of good faith in such circumstances?

- Sol.** According to Section 33 of Indian Partnership Act, 1932, a partner may not be expelled from a firm by a majority of partners except in exercise, in good faith, of powers conferred by contract between the partners. It is, thus, essential that:

the power of expulsion must have existed in a contract between the partners;

the power has been exercised by a majority of the partners; and

it has been exercised in good faith.

If all these conditions are not present, the expulsion is not deemed to be in bonafide interest of the business of the firm.

The test of good faith as required under Section 33(1) includes three things:

The expulsion must be in the interest of the partnership.

The partner to be expelled is served with a notice.

He is given an opportunity of being heard.

If a partner is otherwise expelled, the expulsion is null and void.

According to the test of good faith as required under Section 33(1), expulsion of Partner Y is not valid as he was not served any notice and also he was not given an opportunity of being heard. Also the matter of fight between A and Y was on personal reasons, hence not satisfying the test of good faith in the interest of partnership. Since

- 49.** Mahesh, Suresh and Dinesh are partners in a trading firm. Mahesh, without the knowledge or consent of Suresh and Dinesh borrows himself Rs. 50,000 from Ramesh, a customer of the firm, in the name of the firm. Mahesh, then buys some goods for his personal use with that borrowed money. Can Mr. Ramesh hold Mr. Suresh & Mr. Dinesh liable for the loan? Explain the relevant provisions of the Indian Partnership Act, 1932.

- Sol.** Implied authority of a partner

Yes, as per sections 19 and 22 of the Indian Partnership Act, 1932 unless otherwise provided in the partnership deed, every partner has an implied authority to bind every other partner for acts done in the name of the firm, provided the same falls within the ordinary course of business and is done in a usual manner. Mahesh has a right to borrow the money of Rs. 50,000/- from Ramesh on behalf of his firm in the usual manner. Since, Ramesh has no knowledge that the amount was borrowed by Mahesh without the consent of the other two partners, Mr. Suresh and Mr. Dinesh, he can hold both of them (Suresh and Dinesh) liable for the re-payment of the loan.

- 50.** In the absence of any usage or custom of trade to the contrary, the implied authority of a partner does not empower him to do certain acts. State the acts which are beyond the implied authority of a partner under the provisions of the Indian Partnership Act, 1932?

- Sol.** Implied authority of partner as agent of the firm (Section 19):

Subject to the provisions of section 22, the act of a partner which is done to carry on, in the usual way, business of the kind carried on by the firm, binds the firm. The authority of a partner to bind the firm conferred by this section is called his “implied authority”

In the absence of any usage or custom of 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 proceedings 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 partnership on behalf of the firm.

Sampurna (CA-Foundation)

Registration and Dissolution of a Firm

Q. Bank

51. What is the procedure of registration of a partnership firm under the Indian Partnership Act, 1932?

Sol. (SECTION 58): (1) The registration of a firm may be affected at any time by sending by post or delivering to the Registrar of the area in which any place of business of the firm is situated or proposed to be situated, a statement in the prescribed form and accompanied by the prescribed fee, stating-

- The firm's name
- The place or principal place of business of the firm,
- The names of any other places where the firm carries on business,
- the date when each partner joined the firm,
- the names in full and permanent addresses of the partners, and
- the duration of the firm.

The statement shall be signed by all the partners, or by their agents specially authorised in this behalf. Each person signing the statement shall also verify it in the manner prescribed.

A firm name shall not contain any of the following words, namely:-

Note: 'Crown', 'Emperor', 'Empress', 'Empire', 'Imperial', 'King', 'Queen', 'Royal', or words expressing or implying the sanction, approval or patronage of Government **except when the State Government signifies its consent** to the use of such words as part of the firm-name by order in writing.

52. When does dissolution of a partnership firm take place under the provisions of the Indian Partnership Act, 1932? Explain.

Sol. Dissolution of Firm: The Dissolution of Firm means the discontinuation of the jural relation existing between all the partners of the Firm. But when only one of the partners retires or becomes incapacitated from acting as a partner due to death, insolvency or insanity, the partnership, i.e., the relationship between such a partner and other is dissolved, but the rest may decide to continue. In such cases, there is in practice, no dissolution of the firm. The particular partner goes out, but the remaining partners carry on

the business of the Firm. In the case of dissolution of the firm, on the other hand, the whole firm is dissolved. The partnership terminates as between each and every partner of the firm.

Dissolution of a Firm may take place (Section 39 - 44) as a result of any agreement between all the partners (i.e., dissolution by agreement);

by the adjudication of all the partners, or of all the partners but one, as insolvent (i.e., compulsory dissolution);

by the business of the Firm becoming unlawful (i.e., compulsory dissolution);

subject to agreement between the parties, on the happening of certain contingencies, such as:

effluence of time; (ii) completion of the venture for which it was entered into; (iii) death of a partner; (iv) insolvency of a partner.

by a partner giving notice of his intention to dissolve the firm, in case of partnership at will and the firm being dissolved as from the date mentioned in the notice, or if no date is mentioned, as from the date of the communication of the notice; and

by intervention of court in case of: (i) a partner becoming the unsound mind; (ii) permanent incapacity of a partner to perform his duties as such; (iii) Misconduct of a partner affecting the business; (iv) willful or persistent breach of agreement by a partner; (v) transfer or sale of the whole interest of a partner; (vi) improbability of the business being carried on save at a loss;

the court being satisfied on other equitable grounds that the firm should be dissolved.

53. "Indian Partnership Act does not make the registration of firms compulsory nor does it impose any penalty for non-registration." In light of the given statement, discuss the consequences of non-registration of the partnership firms In India?

Or

"Indian Partnership Act does not make the registration of firms compulsory nor does it impose any penalty for non-registration." Explain. Discuss

the various disabilities or disadvantages that a non-registered partnership firm can face in brief?

Sol. Under the English Law, the registration of firms is compulsory. Therefore, there is a penalty for non-registration of firms. But the Indian Partnership Act does not make the registration of firms compulsory nor does it impose any penalty for non-registration. However, **under Section 69**, non-registration of partnership gives rise to a number of disabilities which we shall presently discuss. Although registration of firms is not compulsory, yet the consequences or disabilities of non-registration have a persuasive pressure for their registration. These disabilities briefly are as follows:

No suit in a civil court by firm or other co-partners against third party: The firm or any other person on its behalf cannot bring an action against the third party for breach of contract entered into by the firm, unless the firm is registered and the persons suing are or have been shown in the register of firms as partners in the firm. In other words, a registered firm can only file a suit against a third party and the persons suing have been in the register of firms as partners in the firm.

No relief to partners for set-off of claim: If an action is brought against the firm by a third party, then neither the firm nor the partner can claim any set-off, if the suit be valued for more than Rs. 100 or pursue other proceedings to enforce the rights arising from any contract.

Aggrieved partner cannot bring legal action against other partner or the firm: A partner of an unregistered firm (or any other person on his behalf) is precluded from bringing legal action against the firm or any person alleged to be or to have been a partner in the firm. But such a person may sue for dissolution of the firm or for accounts and realization of his share in the firm's property where the firm is dissolved.

Third party can sue the firm: In case of an unregistered firm, an action can be brought against the firm by a third party.

54. Subject to agreement by partners, state the rules that should be observed by the partners in settling the accounts of the firm after dissolution under the provisions of the Indian Partnership Act, 1932.

Sol. Mode of Settlement of partnership accounts: As per Section 48 of the Indian Partnership Act, 1932, in

settling the accounts of a firm after dissolution, the following rules shall, subject to agreement by the partners, be observed:-

Losses, including deficiencies of capital, shall be paid first out of profits, next out of capital, and, lastly, if necessary, by the partners individually in the proportions in which they were entitled to share profits;

The assets of the firm, including any sums contributed by the partners to make up deficiencies of capital, must be applied in the following manner and order:

in paying the debts of the firm to third parties;

in paying to each partner rateably what is due to him from capital;

in paying to each partner rateably what is due to him on account of capital; and the residue, if any, shall be divided among the partners in the proportions in which they were entitled to share profits.

55. Distinguish between dissolution of firm and dissolution of partnership.

Or

"Dissolution of a firm is different from dissolution of Partnership". Discuss

Sol.

S. No.	Basis of Difference	Dissolution of Firm	Dissolution of Partnership
1.	Continuation of business	It involves discontinuation of business in partnership.	It does not affect continuation of business. It involves only reconstitution of the firm.
2.	Winding up	It involves winding up of the firm and requires realization of assets and settlement of liabilities.	It involves only reconstitution and requires only revaluation of assets and liabilities of the firm.
3.	Order of court	A firm may be dissolved by the order of the court.	Dissolution of partnership is not ordered by the court.



4.	Scope	It necessarily involves dissolution of partnership.	It may or may not involve dissolution of firm.
5.	Final closure of books	It involves final closure of books of the firm.	It does not involve final closure of the books of the firm.

56. Mr. A, Mr. B and Mr. C were partners in a partnership firm M/s ABC & Co., which is engaged in the business of trading of branded furniture. The name of the partners was clearly written along with the firm name in front of the head office of the firm as well as on letter-head of the firm. On 1st October, 2018, Mr. C passed away. His name was neither removed from the list of partners as stated in front of the head office nor from the letter-heads of the firm. As per the terms of partnership, the firm continued its operations with Mr. A and Mr. B as partners. The accounts of the firm were settled and the amount due to the legal heirs of Mr. C was also determined on 10th October, 2018. But the same was not paid to the legal heirs of Mr. C. On 16th October, 2018, Mr. X, a supplier supplied furniture worth Rs. 20,00,000 to M/s ABC & Co. M/s ABC & Co. could not repay the amount due to heavy losses. Mr. X wants to recover the amount not only from M/s ABC & Co., but also from the legal heirs of Mr. C. Analyse the above situation in terms of the provisions of the Indian Partnership Act, 1932 and decide whether the legal heirs of Mr. C can also be held liable for the dues towards Mr. X.

Sol. Generally, the effect of the death of a partner is the dissolution of the partnership, but the rule in regard to the dissolution of the partnership, by death of partner, is subject to a contract between the parties and the partners are competent to agree that the death of one will not have the effect of dissolving the partnership as regards the surviving partners unless the firm consists of only two partners. In order that the estate of the deceased partner may be absolved from liability for the future obligations of the firm, it is not necessary to give any notice either to the public or the persons having dealings with the firm. In the light of the provisions of the Act and the facts of the question, Mr. X (creditor) can have only a

personal decree against the surviving partners (Mr. A and Mr. B) and a decree against the partnership assets in the hands of those partners. A suit for goods sold and delivered would not lie against the representatives of the deceased partner. Hence, the legal heirs of Mr. C cannot be held liable for the dues towards Mr. X.

57. Ram, Mohan and Gopal were partners in a firm. During the course of partnership, the firm ordered Sunrise Ltd. to supply a machine to the firm. Before the machine was delivered, Ram expired. The machine, however, was later delivered to the firm. Thereafter, the remaining partners became insolvent and the firm failed to pay the price of machine to Sunrise Ltd.

Explain with reasons:

- (1) Whether Ram's private estate is liable for the price of the machine purchased by the firm?
- (2) Against whom can the creditor obtain a decree for the recovery of the price?

Sol. Partnership Liability: The problem in question is based on the provisions of the Indian Partnership Act, 1932 contained in Section 35. The Section provides that where under a contract between the partners the firm is not dissolved by the death of a partner, the estate of a deceased partner is not liable for any act of the firm done after his death. Therefore, considering the above provisions, the problem may be answered as follows:

Ram's estate in this case will not be liable for the price of the Machinery purchased. This is because there was not debt due in respect of the goods in Ram's life time.

The creditors in this case can have only a personal decree against the surviving partners and decree against the partnership assets in the hands of those partners. However, since the surviving partners are already insolvent, no suit for recovery of the debt would lie against them. A suit for goods sold and delivered would not lie against the representative of the deceased partner

58. State the grounds on which Court may dissolve a partnership firm in case any partner files a suit for the same.

Or

What are the various grounds under the Indian Partnership Act, 1932, on which the Court may, at the suit of the partner, dissolve a firm?

Sol. Dissolution by the Court (Section 44 of the Indian Partnership Act, 1932)

Court may, at the suit of the partner, dissolve a firm on any of the following ground:

Insanity/unsound mind: Where a partner (not a sleeping partner) has become of unsound mind, the court may dissolve the firm on a suit of the other partners or by the next friend of the insane partner. Temporary sickness is no ground for dissolution of firm.

Permanent incapacity: When a partner, other than the partner suing, has become in any way permanently incapable of performing his duties as partner, then the court may dissolve the firm. Such permanent incapacity may result from physical disability or illness etc.

Misconduct: Where a partner, other than the partner suing, is guilty of conduct which is likely to affect prejudicially the carrying on of business, the court may order for dissolution of the firm, by giving regard to the nature of business. **It is not necessary that misconduct must relate to the conduct of the business.**

The important point is the adverse effect of misconduct on the business. In each case nature of business will decide whether an act is misconduct or not.

Persistent breach of agreement: Where a partner other than the partner suing, willfully or persistently commits breach of agreements relating to the management of the affairs of the firm or the conduct of its business, or otherwise so conduct himself in matters relating to the business that it is not reasonably practicable for other partners to carry on the business in partnership with him, then the court may dissolve the firm at the instance of any of the partners. Following comes in to category of breach of contract:

- Embezzlement,
- Keeping erroneous accounts
- Holding more cash than allowed
- Refusal to show accounts despite repeated request etc.

Example If one of the partners keeps erroneous accounts and omits to enter receipts or if there is

continued quarrels between the partners or there is such a state of things that destroys the mutual confidence of partners, the court may order for dissolution of the firm.

Transfer of interest: Where a partner other than the partner suing, has transferred the whole of his interest in the firm to a third party or has allowed his share to be charged or sold by the court, in the recovery of arrears of land revenue due by the partner, the court may dissolve the firm at the instance of any other partner.

Continuous/Perpetual losses: Where the business of the firm cannot be carried on except at a loss in future also, the court may order for its dissolution.

Just and equitable grounds: Where the court considers any other ground to be just and equitable for the dissolution of the firm, it may dissolve a firm. The following are the cases for the just and equitable grounds-

Deadlock in the management.

Where the partners are not in talking terms between them.

Loss of substratum.

Gambling by a partner on a stock exchange.

59. Referring to the Provisions of the Indian Partnership Act, 1932, answer the following:

- (1) What are the consequences of Non-Registration of Partnership firm?
- (2) What are the rights which won't be affected by Non-Registration of Partnership firm?

Sol. Consequences of Non-registration of partnership firm:

Under Section 69 of the Indian Partnership Act, 1932 non-registration of partnership gives rise to a number of disabilities. Though registration of firms is not compulsory, yet the consequences or disabilities of non-registration have a persuasive pressure for their registration. Following are the consequences:

No suit in a civil court by firm or other co-partners against third party: The firm or any other person on its behalf cannot bring an action against the third party for breach of contract entered into by the firm.

No relief to partners for set-off of claim: If an action is brought against the firm by a third party, then neither the firm nor the partner can claim any set-off, if the suit be valued for more than Rs. 100 or

pursue other proceedings to enforce the rights arising from any contract.

Aggrieved partner cannot bring legal action against other partner or the firm: A partner of an unregistered firm (or any other person on his behalf) is precluded from bringing legal action against the firm or any person alleged to be or to have been a partner in the firm.

Third-party can sue the firm: In case of an unregistered firm, an action can be brought against the firm by a third party.

Non-registration of a firm does not, however, affect the following rights:

The right of third parties to sue the firm or any partner.

The right of partners to sue for the dissolution of the firm or for the settlement of the accounts of a dissolved firm, or for realization of the property of a dissolved firm.

The power of an Official Assignee, Receiver of Court to release the property of the insolvent partner and to bring an action.

The right to sue or claim a set-off if the value of suit does not exceed Rs. 100 in value.

- 60.** A & Co. is registered as a partnership firm in 2015 with A, B and C partners. In 2016, A dies. In 2017, B and C sue X in the name and on behalf of A & Co., without fresh registration. Decide whether the suit is maintainable. Whether your answer would be same if in 2017 B and C had taken a new partner D and then filed a suit against X without fresh registration?

Sol. As regards the question whether in the case of a registered firm (whose business was carried on after its dissolution by death of one of the partners), a suit can be filed by the remaining partners in respect of any subsequent dealings or transactions without notifying to the Registrar of Firms, the changes in the constitution of the firm, it was decided that the remaining partners should sue in respect of such subsequent dealings or transactions even though the firm was not registered again after such dissolution and no notice of the partner was given to the Registrar.

The test applied in these cases was whether the plaintiff satisfied the only two requirements of Section 69 (2) of the Act namely,

the suit must be instituted by or on behalf of the firm which had been registered;

the person suing had been shown as partner in the register of firms. In view of this position of law, the suit is in the case by B and C against X in the name and on behalf of A & Co. is maintainable.

Now, in 2017, B and C had taken a new partner, D, and then filed a suit against X without fresh registration. Where a new partner is introduced, the fact is to be notified to Registrar who shall make a record of the notice in the entry relating to the firm in the Register of firms. Therefore, the firm cannot sue as D's (new partner's) name has not been entered in the register of firms. It was pointed out that in the second requirement, the phrase "person suing" means persons in the sense of individuals whose names appear in the register as partners and who must be all partners in the firm at the date of the suit.

- 61.** P, X, Y and Z are partners in a registered firm A & Co. X died and P retired. Y and Z filed a suit against W in the name and on behalf of firm without notifying to the Registrar of firms about the changes in the constitution of the firm. Is the suit maintainable?

Sol. As regards the question whether in the case of a registered firm (whose business was carried on after its dissolution by death of one of the partners), a suit can be filed by the remaining partners in respect of any subsequent dealings or transactions without notifying to the Registrar of Firms, the changes in the constitution of the firm, it was decided that the remaining partners should sue in respect of such subsequent dealings or transactions even though the firm was not registered again after such dissolution and no notice of the partner was given to the Registrar.

The test applied in these cases was whether the plaintiff satisfied the only two requirements of Section 69 (2) of the Act namely,

the suit must be instituted by or on behalf of the firm which had been registered;

the person suing had been shown as partner in the register of firms. In view of this position of law, the suit is in the case is maintainable.

62. M/s XYZ & Company is a partnership firm. The firm is an unregistered firm. The firm has purchased some iron rods from another partnership firm M/s LMN & Company which is also an unregistered firm. M/s XYZ & Company could not pay the price within the time as decided. M/s LMN & Company has filed the suit against M/s XYZ & Company for recovery of price. State under the provisions of the Indian Partnership Act, 1932;

- (1) Whether M/s LMN & Company can file the suit against M/s XYZ & Company?
- (2) What would be your answer, in case M/s XYZ & Company is a registered firm while M/s LMN & Company is an unregistered firm?
- (3) What would be your answer, in case M/s XYZ & Company is an unregistered firm while M/s LMN & Company is a registered firm?

Sol. According to provisions of Section 69 of the Indian Partnership Act, 1932 an unregistered firm cannot file a suit against a third party to enforce any right arising from contract, e.g., for the recovery of the price of goods supplied. But this section does not prohibit a third party to file suit against the unregistered firm or its partners.

On the basis of above, M/s LMN & Company cannot file the suit against M/s XYZ & Company as M/s LMN & Company is an unregistered firm.

In case M/s XYZ & Company is a registered firm while M/s LMN & Company is an unregistered firm, the answer would remain same as in point a) above.

In case M/s LMN & Company is a registered firm, it can file the suit against M/s XYZ & Company.

63. MN partnership firm has two different lines of manufacturing business. One line of business is the manufacturing of Ajinomoto, a popular seasoning & taste enhancer for food. Another line of business is the manufacture of paper plates & cups. One fine day, a law is passed by the Government banning Ajinomoto' use in food and to stop its manufacturing making it an unlawful business because it is injurious to health. Should the firm compulsorily dissolve under the Indian Partnership Act, 1932? How will its other line of business (paper plates & cups) be affected?

Sol. According to Section 41 of the Indian Partnership Act, 1932, a firm is compulsorily dissolved; by the adjudication of all the partners or of all the partners but one as insolvent, or by the happening of any event which makes it unlawful for the business of the firm to be carried on or for the partners to carry it on in partnership.

However, where more than one separate adventure or undertaking is carried on by the firm, the illegality of one or more shall not of itself cause the dissolution of the firm in respect of its lawful adventures and undertakings.

Here, MN has to compulsorily dissolve due to happening of law which bans the usage of ajino moto. Else the business of the firm shall be treated as unlawful.

However, the illegality of ajino moto business will in no way affect the legality or dissolution of the other line of business (paper plates & cups). MN can continue with paper plates and cup manufacture.



Sampurna (CA-Foundation)

COMPANIES ACT, 2013

Q. Bank

1. AK Private Limited has borrowed Rs. 36 crores from BK Finance Limited. However, as per memorandum of AK Private Limited the maximum borrowing power of the company is Rs. 30 crores. Examine, whether AK Private Limited is liable to pay this debt? State the remedy, if any available to BK Finance Limited.

Sol. This case is governed by the 'Doctrine of Ultra Vires'. According to this doctrine, any act done or a contract made by the company which travels beyond the powers of the company conferred upon it by its Memorandum of Association is wholly void and inoperative in law and is therefore not binding on the company. This is because, the Memorandum of Association of the company is, in fact, its charter; it defines its constitution and the scope of the powers of the company. Hence, a company cannot depart from the provisions contained in the memorandum however imperative may be the necessity for the departure. Hence, any agreement ultra vires the company shall be null and void.

Whether AK Private Limited is liable to pay the debt?
As per the facts given, AK Private Limited borrowed Rs. 36 crores from BK Finance Limited which is beyond its borrowing power of Rs. 30 crores.

Hence, contract for borrowing of Rs. 36 crores, being ultra vires the memorandum of association and thereby ultra vires the company, is void. AK Private Limited is not, therefore, liable to pay the debt.

Remedy available to BK Finance Limited:

In light of the legal position explained above, BK Finance Limited cannot enforce the said transaction and thus has no remedy against the company for recovery of the money lent. BK Finance limited may take action against the directors of AK Private Limited as it is the personal liability of its directors to restore the borrowed funds. Besides, BK Finance Limited may take recourse to the remedy by means of 'Injunction', if feasible.

2. What do you mean by the term Capital? Describe its classification in the domain of Company Law

Sol. (a) Meaning of capital: The term capital has variety of meanings. But in relation to a company limited by shares, the term 'capital'

means 'share capital'. Share capital means capital of the company expressed in terms of rupees divided into shares of fixed amount.

- (ii) **Classification of capital:** In the domain of Company Law, the term capital can be classified as follows:

- Nominal or authorised or registered capital:
- This expression means such capital as is authorised by memorandum of a company to be the maximum amount of share capital of the company.
- **Issued capital:** It means such capital as the company issues from time to time for subscription.
- **Subscribed capital:** As such part of the capital which is for the time being subscribed by the members of a company.
- **Called up capital:** As such part of the capital which has been called for payment. It is the total amount called up on the shares issued.
- **Paid-up capital:** It is the total amount paid or credited as paid up on shares issued. It is equal to called up capital less calls in arrears.

3. BC Private Limited and its subsidiary KL Private Limited are holding 90,000 and 70,000 shares respectively in PQ Private Limited. The paid-up share capital of PQ Private Limited is Rs. 30 Lakhs (3 Lakhs equity shares of Rs. 10 each fully paid). Analyse with reference to provisions of the Companies Act, 2013 whether PQ Private Limited is a subsidiary of BC Private Limited. What would be your answer if KL Private Limited is holding 1,60,000 shares in PQ Private Limited and no shares are held by BC Private Limited in PQ Private Limited?

Sol. 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—
controls the composition of the Board of Directors; or

exercises or controls more than one-half of the total voting power either at its own or together with one or more of its subsidiary companies:

For the purposes of this section —

- 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;
- “layer” in relation to a holding company means its subsidiary or subsidiaries.

In the instant case, BC Private Limited together with its subsidiary KL Private Limited is holding 1,60,000 shares (90,000+70,000 respectively) which is more than one half in nominal value of the Equity Share Capital of PQ Private Limited. Hence, PQ Private Limited is subsidiary of BC Private Limited.

In the second case, the answer will remain the same. KL Private Limited is a holding 1,60,000 shares i.e., more than one half in nominal value of the Equity Share Capital of PQ Private Limited (i.e., holding more than one half of voting power). Hence, KL Private Limited is holding company of PQ Private Company and BC Private Limited is a holding company of KL Private Limited.

Hence, by virtue of Chain relationship, BC Private Limited becomes the holding company of PQ Private Limited.

4. ABC Limited was registered as a public company. There were 245 members in the company. Their details are as follows:

Directors and their relatives	190
Employees	15
Ex-employees	
(shares were allotted when they were employees)	20
Others	20

(Including 10 joint holders holding shares jointly in the name of father and son) The Board of directors of the company propose to convert it into a private company. Advice whether reduction in the number of members is necessary for conversion.

- Sol.** In the given case, ABC Limited was having 245 members in the company. The Board of Directors of said company proposes to convert it into private company. In lines with Section 2 (68) of the Companies Act, 2013, a private company by its Articles, limits the number of its members to 200.

Provided 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.

It is further provided that, following persons shall not be included in the number of members-

- Persons who are in the employment of the company; and
- Persons, 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.

As per the facts, ABC Limited has members constituting of Directors & their relatives, employees, Ex- employees and others including 10 joint holders. In line with the requirement for being a private company, following shall be restricted to be as members i.e., Directors & their relatives & joint holders holding shares jointly constituting 200 members (190+10).

Accordingly, ABC Limited when converted to private company shall not be required to reduce the number of members as the number of members as per requirement of a private company, is fulfilled that is of maximum 200 members.

5. Explain Doctrine of 'Indoor Management' under the Companies Act, 2013. Also state the circumstances where the outsider cannot claim relief on the ground of 'Indoor Management'

Sol. Doctrine of Indoor Management (The Companies Act, 2013): According to the “doctrine of indoor management” the outsiders, dealing with the company though are supposed to have satisfied themselves regarding the competence of the company to enter into the proposed contracts are also entitled to assume that as far as the internal compliance to procedures and regulations by the company is concerned, everything has been done properly. They are bound to examine the registered documents of the company and ensure that the proposed dealing is not inconsistent therewith, but they are not bound to do more. They are fully entitled to presume regularity and compliance by the company with the internal procedures as required by the Memorandum and the Articles. This doctrine is a limitation of the doctrine

of “constructive notice” and popularly known as the rule laid down in the celebrated case of *Royal British Bank v. Turquand*. Thus, the doctrine of indoor management aims to protect outsiders against the company.

The above-mentioned doctrine of Indoor Management or Turquand Rule has limitations of its own. That is to say, it is inapplicable to the following cases, namely:

- **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.
- **Suspicion of Irregularity:** The doctrine in no way, rewards those who behave negligently. Where the person dealing with the company is put upon an inquiry, for example, where the transaction is unusual or not in the ordinary course of business, it is the duty of the outsider to make the necessary enquiry.
- **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.

6. Naveen incorporated a “One Person Company” making his sister Navita as the nominee. Navita is leaving India permanently due to her marriage abroad. Due to this fact, she is withdrawing her consent of nomination in the said One Person Company. Taking into considerations the provisions of the Companies Act, 2013 answer the questions given below.

- (a) If Navita is leaving India permanently, is it mandatory for her to withdraw her nomination in the said One Person Company?
- (b) If Navita maintained the status of Resident of India after her marriage, then can she continue her nomination in the said One Person Company?

Sol. (a) Yes, it is mandatory for Navita to withdraw her nomination in the said OPC as she is leaving India permanently as only a natural person who is an Indian citizen and resident in India shall be a nominee in OPC.

- (b) Yes, Navita can continue her nomination in the said OPC, if she maintained the status of

Resident of India after her marriage by staying in India for a period of not less than 120 days during the immediately preceding financial year.

7. SK Infrastructure Limited has a paid-up share capital divided into 6,00,000 equity shares of INR 100 each. 2,00,000 equity shares of the company are held by Central Government and 1,20,000 equity shares are held by Government of Maharashtra. Explain with reference to relevant provisions of the Companies Act, 2013, whether SK Infrastructure Limited can be treated as Government Company.

Sol. Government Company [Section 2(45) of the Companies Act, 2013]: Government Company means 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 Governments, or
- 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. In the instant case, paid up share capital of SK Infrastructure Limited is 6,00,000 equity shares of Rs. 100 each. 200,000 equity shares are held by Central government and 1,20,000 equity shares are held by Government of Maharashtra. The holding of equity shares by both government is 3,20,000 which is more than 51% of total paid up equity shares. Hence, SK Infrastructure Limited is a Government company.

8. Y incorporated a "One Person Company (OPC)" making his sister Z as nominee. Z is leaving India permanently due to her marriage abroad. Due to this fact, she is withdrawing her consent of nomination in the said OPC. Taking into considerations the provisions of the Companies Act, 2013 answer the questions given below:

Is it mandatory for Z to withdraw her nomination in the said OPC, if she is leaving India permanently?

Can Z continue her nomination in the said OPC, if she maintained the status of Resident of India after her marriage?

Sol. Yes, it is mandatory for Z to withdraw her nomination in the said OPC as she is leaving India permanently as only a natural person who is an Indian

citizen and residing in India for not less than 120 days shall be a nominee in OPC.

Yes, Z can continue her nomination in the said OPC, if she maintained the status of Resident of India after her marriage by staying in India for a period of not less than 120 days during the immediately preceding financial year.

9. Explain the classification of the companies on the basis of control as per the Companies Act, 2013.

Sol. In line with the Companies Act, 2013, following are the classification of the Companies on the basis of control:

Holding and subsidiary companies: ‘Holding and subsidiary’ companies are relative terms.

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)]

For the purposes of this clause, the expression “company” includes any body corporate.

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—

controls the composition of the Board of Directors; or exercises or controls more than one-half of the total voting power 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.

For the purposes of this section —

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; 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; the expression “company” includes anybody corporate;

“layer” in relation to a holding company means its subsidiary or subsidiaries

Associate company [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.

Explanation. — For the purpose of this clause — the expression “significant influence” means control of at least twenty per cent of total voting power, or control of or participation in business decisions under an agreement;

the expression “joint venture” means a joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the arrangement.

The term “Total Share Capital”, means the aggregate of the —

Paid-up equity share capital; and Convertible preference share capital.

10. What is the main difference between a Guarantee Company and a Company having Share Capital?

Sol. Difference between Guarantee Company [Section 2(21) of the Companies Act, 2013] and a Company having share capital [Section 2(22)]. In case of guarantee company, the members may be called upon to discharge their liability only after commencement of the winding up and only subject to certain conditions; whereas in the case of company having share capital, members may be called upon to discharge their liability at any time, either during the company’s life-time or during its winding up. It is clear from the definition of the guarantee company that it does not raise its initial working funds from its members. Therefore, such a company may be useful only where no working funds are needed or where these funds can be held from other sources like endowment, fees, charges, donations, etc. In *Narendra Kumar Agarwal vs. Saroj Maloo*, the Supreme Court has laid down that the right of a guarantee company to refuse to accept the transfer by a member of his interest in the company is on a different footing than that of a company limited by shares. The membership of a guarantee company may carry privileges much different from those of ordinary shareholders.

11. Ravi Private Limited has borrowed Rs. 5 crores from Mudra Finance Ltd. This debt is ultra vires to the company. Examine, whether the company is liable to pay this debt? State the remedy if any available to Mudra Finance Ltd.?

Sol. As per the facts given, Ravi Private Limited borrowed Rs. 5 crore from Mudra Finance Ltd. This debt is ultra vires to the company, which signifies that Ravi Private Limited has borrowed the amount beyond the expressed limit prescribed in its memorandum. This act of the company can be said to be **null and void**.

In consequence, any act done or a contract made by the company which travels beyond the powers not only of the directors but also of the company is wholly void and inoperative in law and is therefore not binding on the company. So is being the act void in nature, there being no existence of the contract between the Ravi Private Ltd. and Mudra Finance Ltd. Therefore, **the company Ravi Private Ltd. is liable to pay this debt amount upto the limit prescribed in the memorandum.**

Remedy available to the Mudra Finance Ltd.:

The impact of the doctrine of ultra vires is that a company can neither be sued on an ultra vires transaction, nor can it sue on it. Since the memorandum is a “public document”, it is open to public inspection. Therefore, a company which deals with the other, is deemed to know about the powers of the company.

So, Mudra Finance Ltd. can claim for the amount within the expressed limit prescribed in its memorandum.

12. Define OPC (One Person Company) and state the rules regarding its membership. Can it be converted into a non-profit company under Section 8 or a private company?

Sol. One Person Company (OPC) [Section 2(62) of the Companies Act, 2013]: The Act defines one person company (OPC) as a company which has only one person as a member. Rules regarding its membership:

- Only one person as member.
- 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.

- Any such change in the name of the person shall not be deemed to be an alteration of the memorandum.
- 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 120 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.
- OPC cannot be incorporated or converted into a company under section 8 of the Act. Though it may be converted to private or public companies

13. Sound Syndicate Ltd., a public company, its articles of association empower the managing agents to borrow both short- and long-term loans on behalf of the company, Mr. Liddle, the director of the company, approached Easy Finance Ltd., a non banking finance company for a loan of Rs. 25,00,000 in name of the company. The Lender agreed and provided the above said loan. Later on, Sound Syndicate Ltd. refused to repay the money borrowed on the pretext that no resolution authorizing such loan have been actually passed by the company and the lender should have enquired about the same prior providing such loan hence company not liable to pay such loan. Analyse the above situation in terms of the provisions of Doctrine of Indoor Management under the Companies Act, 2013 and examine whether the contention of Sound Syndicate Ltd. is correct or not?

Sol. Doctrine of Indoor Management According to this doctrine, persons dealing with the company need not inquire whether internal proceedings relating to the contract are followed correctly, once they are satisfied that the transaction is in accordance with the memorandum and articles of association. Stakeholders need not enquire whether the necessary meeting was convened and held properly or whether necessary resolution was passed properly. They are entitled to take it for granted that the company had gone through all these proceedings in a regular manner. The doctrine helps protect external members from the company and states that the people are entitled to presume that internal proceedings are as

per documents submitted with the Registrar of Companies.

Thus, What happens internal to a company is not a matter of public knowledge. An outsider can only presume the intentions of a company, but do not know the information he/she is not privy to.

If not for the doctrine, the company could escape creditors by denying the authority of officials to act on its behalf. In the given question, Easy Finance Ltd. being external to the company, need not enquire whether the necessary resolution was passed properly. Even if the company claim that no resolution authorizing the loan was passed, the company is bound to pay the loan to Easy Finance Ltd.

- 14.** What do you mean by "Companies with charitable purpose" (section 8) under the Companies Act, 2013? Mention the conditions of the issue and revocation of the licence of such company by the government.

Sol. Formation of companies with charitable purpose etc. (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.

Such company intends to apply its profit in promoting its objects and prohibiting the payment of any dividend to its members.

Examples of section 8 companies are FICCI, ASSOCHAM, National Sports Club of India, CII etc.

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.

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 sections subject to which a licence is issued or

where the affairs of the company are conducted fraudulently, or violative of the objects of the company or prejudicial to public interest, and on revocation the Registrar shall put 'Limited' or 'Private Limited' against the company's name in the register. 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.

- 15.** A company registered under section 8 of the Companies Act, 2013, earned huge profit during the financial year ended on 31st March, 2018 due to some favorable policies declared by the Government of India and implemented by the company. Considering the development, some members of the company wanted the company to distribute dividends to the members of the company. They approached you to advise them about the maximum amount of dividend that can be declared by the company as per the provisions of the Companies Act, 2013. Examine the relevant provisions of the Companies Act, 2013 and advise the members accordingly.

Sol. A company that is registered under section 8 of the Companies Act, 2013, is prohibited from the payment of any dividend to its members.

The company in question is a section 8 company and hence it cannot declare dividend. Thus, the contention of members is incorrect.

16. There are cases where company law disregards the principle of corporate personality or the principle that the company is a legal entity distinct from its shareholders or members. Elucidate

OR

Some of the creditors of Pharmaceutical Appliances Ltd. have complained that the company was formed by the promoters only to defraud the creditors and circumvent the compliance of legal provisions of the Companies Act, 2013. In this context they seek your advice as to the meaning of corporate veil and when the promoters can be made personally liable for the debts of the company.

Sol. Corporate Veil refers to a legal concept whereby the company is identified separately from the members of the company. However, this veil can be lifted which 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. Where the Courts ignore the company, and concern themselves directly with the members or managers, the corporate veil may be said to have been lifted. Only in appropriate circumstances, the Courts are willing to lift the corporate veil and that too, when questions of control are involved rather than merely a question of ownership.

Lifting of 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:

- **Trading with enemy:** If the public interest is likely to be in jeopardy, the Court may be willing to crack the corporate shell
- Where corporate entity is used to evade or circumvent tax, the corporate veil may be lifted
- Where companies form other companies as their subsidiaries to act as their agent
- Company is formed to circumvent welfare of employees

Where the device of incorporation is adopted for some illegal or improper purpose: Where the device of incorporation is adopted for some illegal or improper purpose, e.g., to defeat or circumvent law, to defraud creditors or to avoid legal obligations.

17. Mr. Anil formed a One Person Company (OPC) on 16th April, 2018 for manufacturing electric cars. The turnover of the OPC for the financial year ended 31st March, 2019 was about Rs. 2.25 Crores. His friend Sunil wanted to invest in his OPC, so they decided to convert it voluntarily into a private limited company. Can Anil do so?

Sol. As per the provisions of Sub-Rule (7) of Rule 3 of the Companies (Incorporation) Rules, 2014, an OPC cannot convert voluntarily into any kind of company except section 8 company. Mr. Anil can convert the OPC into a private limited company along with Sunil.

18. "The Memorandum of Association is a charter of a company". Discuss. Also explain in brief the contents of Memorandum of Association.

Sol. The Memorandum of Association of company is in fact its charter; it defines its constitution and the scope of the powers of the company with which it has been established under the Act. It is the very foundation on which the whole edifice of the company is built.

Object of registering a memorandum of association:

It contains the object for which the company is formed and therefore identifies the possible scope of its operations beyond which its actions cannot go.

It enables shareholders, creditors and all those who deal with company to know what its powers are and what activities it can engage in.

A memorandum is a public document under Section 399 of the Companies Act, 2013. Consequently, every person entering into a contract with the company is presumed to have the knowledge of the conditions contained therein.

The shareholders must know the purposes for which his money can be used by the company and what risks he is taking in making the investment.

A company cannot depart from the provisions contained in the memorandum however imperative may be the necessity for the departure. It cannot enter into a contract or engage in any trade or business, which is beyond the power conferred on it by the memorandum. If it does so, it would be *ultra vires* the company and void.

Contents of the memorandum: The memorandum of a company shall state—

the name of the company (Name Clause) 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 State in which the registered office of the company (Registered Office clause) is to be situated; the objects for which the company is proposed to be incorporated and any matter considered necessary in furtherance thereof (Object clause);

the liability of members of the company (Liability clause), whether limited or unlimited

the amount of authorized capital (Capital Clause) 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.

the desire of the subscribers to be formed into a company. The Memorandum shall conclude with the association clause. Every subscriber to the Memorandum shall take at least one share, and shall write against his name, the number of shares taken by him.

19. A, an assessee, had large income in the form of dividend and interest. In order to reduce his tax liability, he formed four private limited company and transferred his investments to them in exchange of their shares. The income earned by the companies was taken back by him as pretended loan. Can A be regarded as separate from the private limited company he formed?

Sol. (a) The House of Lords in *Salomon Vs Salomon & Co. Ltd.* laid down that a company is a person distinct and separate from its members, and therefore, has an independent separate legal existence from its members who have constituted the company. But under certain circumstances the separate entity of the company may be ignored by the courts. When that happens, the courts ignore the corporate entity of the company and look behind the corporate façade and hold the persons in control of the management of its affairs liable for the acts of the company. Where a company is incorporated and formed by certain persons only for the purpose of evading taxes, the courts have discretion to disregard the corporate entity and tax the income in the hands of the appropriate assessee.

- (b) In *Dinshaw Maneckjee Petit* case it was held that the company was not a genuine company at all but merely the assessee himself disguised that the legal entity of a limited company. The assessee earned huge income by way of dividends and interest. So, he opened some companies and purchased their shares in exchange of his income by way of dividend

and interest. This income was transferred back to assessee by way of loan. The court decided that the private companies were a sham and the corporate veil was lifted to decide the real owner of the income.

- (c) In the instant case, the four private limited companies were formed by A, the assessee, purely and simply as a means of avoiding tax and the companies were nothing more than the façade of the assessee himself. Therefore, the whole idea of Mr. A was simply to split his income into four parts with a view to evade tax. No other business was done by the company.
- (d) Hence, A cannot be regarded as separate from the private limited companies he formed.

20. ABC Limited has allotted equity shares with voting rights to XYZ Limited worth Rs. 15 Crores and issued Non-Convertible Debentures worth Rs. 40 Crores during the Financial Year 2019-20. After that total Paid-up Equity Share Capital of the company is Rs. 100 Crores and Non-Convertible Debentures stands at Rs. 120 Crores.

Define the Meaning of Associate Company and comment on whether ABC Limited and XYZ Limited would be called Associate Company as per the provisions of the Companies Act, 2013?

- Sol.** As per Section 2(6) of the Companies Act, 2013, an Associate Company 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 control of business decisions under an agreement.

The term “Total Share Capital”, means the aggregate of the –

- Paid-up equity share capital; and
- Convertible preference share capital.

In the given case, as ABC Ltd. has allotted equity shares with voting rights to XYZ Limited of Rs. 15 crore, which is less than requisite control of 20% of total share capital (i.e. 100 crore) to have a significant influence of XYZ Ltd. Since the said requirement is not complied, therefore ABC Ltd. and XYZ Ltd. are not associate companies as per the Companies Act, 2013. Holding/allotment of non-convertible debentures has no relevance for ascertaining significant influence.

21. What are the significant points of Section 8 Company which are not applicable for other companies? Briefly explain with reference to provisions of the Companies Act, 2013

Sol. Section 8 Company- Significant points

- ◆ Formed for the promotion of commerce, art, science, religion, charity, protection of the environment, sports, etc.
- ◆ Requirement of minimum share capital does not apply.
- ◆ Uses its profits for the promotion of the objective for which formed.
- ◆ Does not declare dividend to members.
- ◆ Operates under a special licence from the Central Government.
- ◆ Need not use the word Ltd./ Pvt. Ltd. in its name and adopt a more suitable name such as club, chambers of commerce etc.
- ◆ Licence revoked if conditions contravened.
- ◆ On revocation, the Central Government may direct it to
 - Converts its status and change its name
 - Wind – up
 - Amalgamate with another company having similar object.
- ◆ Can call its general meeting by giving a clear 14 days notice instead of 21 days.
- ◆ Requirement of minimum number of directors, independent directors etc. does not apply.
- ◆ Need not constitute Nomination and Remuneration Committee and Shareholders Relationship Committee.
- ◆ A partnership firm can be a member of Section 8 company.

22. Mike Limited company incorporated in India having Liaison office at Singapore. Explain in detail meaning of Foreign Company and analysis., on whether Mike Limited would be called as Foreign Company as it established a Liaison office at Singapore as per the provisions of the Companies Act, 2013?

Sol. Foreign Company [Section 2(42) of the Companies Act, 2013]: It means any company or body corporate incorporated outside India which—

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

Since Mike Limited is a company incorporated in India, hence, it cannot be called as a foreign company. Even though, Liaison was officially established at Singapore, it would not be called as a foreign company as per the provisions of the Companies Act, 2013.

23. Explain the concept of "Dormant Company" as envisaged in the Companies Act, 2013.

Sol. Dormant Company (Section 455 of the Companies Act, 2013)

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 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 during the last two financial years, or has not filed financial statements and annual returns during the last two financial years.

“Significant accounting transaction” means any transaction other than –

- (a) payment of fees by a company to the Registrar;
- (b) payments made by it to fulfil the requirements of this Act or any other law;
- (c) allotment of shares to fulfil the requirements of this Act; and
- (d) payments for maintenance of its office and records.

24. The Articles of Association of XYZ Ltd. provides that Board of Directors has authority to issue bonds provided such issue is authorized by the shareholders by a necessary resolution in the general meeting of the company. The company was in dire need of funds and therefore, it issued the bonds to Mr. X without passing any such resolution in general meeting. Can Mr. X recover the money from the company? Decide referring the relevant provisions of the Companies Act, 2013.

Sol. According to the Doctrine of Indoor Management, if an act is authorised by the articles or memorandum, an outsider is entitled to assume that all the detailed formalities for doing that act have been observed. As per the case of *the Royal British Bank vs. Turquand* [1856] 6E & B 327, the directors of R.B.B. Ltd. gave a bond to T. The articles empowered the directors to issue such bonds under the authority of a proper resolution. In fact, no such resolution was passed. Notwithstanding that, it was held that T could sue on the bonds on the ground that he was entitled to assume that the resolution had been duly passed. This is the doctrine of indoor management, popularly known as Turquand Rule. Since, the given question is based on the above facts, accordingly here in this case Mr. X can recover the money from the company considering that all required formalities for the passing of the resolution have been duly complied

25. When a company is registered, it is clothed with a legal personality. Explain.

Sol. When a company is registered, it is clothed with a legal personality. It comes to have almost the same rights and powers as a human being. Its existence is distinct and separate from that of its members. A company can own property, have bank account, raise loans, incur liabilities and enter into contracts.

(a) It is at law, a person different altogether from the subscribers to the memorandum of association. Its personality is distinct and separate from the personality of those who compose it.

(b) Even members can contract with company, acquire right against it or incur liability to it. For the debts of the company, only its creditors can sue it and not its members.

A company is capable of owning, enjoying and disposing of property in its own name. Although the capital and assets are contributed by the shareholders, the company becomes the owner of its capital and assets. The shareholders are not the private or joint owners of the company's property.

26. Flora Fauna Limited was registered as a public company. There are 230 members in the company as noted below:

Directors and their relatives	190
Employees	15
Ex-Employees (Shares were allotted when they	10

were employees)	
5 couples holding shares jointly in the name of husband and wife (5*2)	10
Others	5

The Board of Directors of the company propose to convert it into a private company. Also advise whether reduction in the number of members is necessary.

Sol. According to section 2(68) of the Companies Act, 2013, "Private company" means a company having a minimum paid-up share capital as may be prescribed, and which by its articles, except in case of One Person Company, limits the number of its members to two hundred.

However, 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.

It is further provided that –

- (a) persons who are in the employment of the company; and
- (b) persons 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. In the instant case, Flora Fauna Limited may be converted into a private company only if the total members of the company are limited to 200.

Total Number of members

Directors and their relatives	190
5 Couples (5*1)	5
Others	5
Total	200

Therefore, there is no need for reduction in the number of members since existing number of members are 200 which does not exceed maximum limit of 200

27. Can a non-profit organization be registered as a company under the Companies Act, 2013? If so, what procedure does it have to adopt?

Sol. Yes, a non-profit organization be registered as a company under the Companies Act, 2013 by following the provisions of section 8 of the Companies Act, 2013. 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. Such company intends to apply its profit in promoting its objects and prohibiting the payment of any dividend to its members. The Central Government has the power to issue license for registering a section 8 company.

- 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.

28. Examine the following whether they are correct or incorrect along with reasons:

- (1) A company being an artificial person cannot own property and cannot sue or be sued.
- (2) A private limited company must have a minimum of two members, while a public limited company must have at least seven members.

Sol. (a) **Incorrect:** A company is an artificial person as it is created by a process other than natural birth. It is legal or judicial as it is created by law. It is a person since it is clothed with all the rights of an individual. Further, **the** company being a separate legal entity can own property, have banking account, raise loans, incur liabilities and enter into contracts. Even members can contract with company, acquire right against it or incur liability to it. It can sue and be sued in its own name. It can do everything which any natural person can do except be sent to jail, take an oath, marry or practice a learned profession. Hence, it is a legal person in its own sense.

(b) **Correct:** Section 3 of the Companies Act, 2013 deals with the basic requirement with respect to the constitution of the **company**. In the case of a public company, any 7 or more persons can form a company for any lawful purpose by subscribing their names to memorandum and complying with the

requirements of this Act in respect of registration. In exactly the same way, 2 or more persons can form a private company

29. Briefly explain the doctrine of "ultravires" under the Companies Act, 2013. What are the consequences of ultravires acts of the company?

Sol. Doctrine of ultra vires: The meaning of the term *ultra vires* is simply "beyond (their) powers". The legal phrase "*ultra vires*" is applicable only to acts done in excess of the legal powers of the doers. This presupposes that the powers in their nature are limited.

It is a fundamental rule of Company Law that the objects of a company as stated in its memorandum can be departed from only to the extent permitted by the Act, thus far and no further. In consequence, any act done or a contract made by the company which travels beyond the powers not only of the directors but also of the company is wholly void and inoperative in law and is therefore not binding on the company. On this account, a company can be restrained from employing its fund for purposes other than those sanctioned by the memorandum. Likewise, it can be restrained from carrying on a trade different from the one it is authorised to carry on.

The impact of the doctrine of *ultra vires* is that a company can neither be sued on an *ultra vires* transaction, nor can it sue on it. Since the memorandum is a "public document", it is open to public inspection. Therefore, when one deals with a company one is deemed to know about the powers of the company. If in spite of this you enter into a transaction which is *ultra vires* the company, you cannot enforce it against the company.

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.

30. ABC Limited has allotted equity shares with voting rights to XYZ Limited worth Rs. 15 Crores and issued Non-Convertible Debentures worth Rs. 40 Crores during the Financial Year 2019-20. After that total Paid-up Equity Share Capital of the company is Rs. 100 Crores and Non-Convertible Debentures stands at Rs. 120 Crores. Define the Meaning of Associate Company and comment on whether ABC Limited and XYZ Limited would be called Associate

Company as per the provisions of the Companies Act, 2013?

Sol. As per Section 2(6) of the Companies Act, 2013, an Associate Company 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 control of business decisions under an agreement.

The term “Total Share Capital”, means the aggregate of the –

Paid-up equity share capital; and Convertible preference share capital.

In the given case, as ABC Ltd. has allotted equity shares with voting rights to XYZ Limited of Rs. 15 cr, which is less than requisite control of 20% of total share capital (i.e 100 cr) to have a significant influence of XYZ Ltd. Since the said requirement is not complied, therefore ABC Ltd. and XYZ Ltd. are not associate companies as per the Companies Act, 2013. Holding / allotment of non-convertible debentures has no relevance for ascertaining significant influence.

31. SK Infrastructure Limited has a paid-up share capital divided into 6,00,000 equity shares of Rs. 100 each. 2,00,000 equity shares of the company are held by Central Government and 1,20,000 equity shares are held by Government of Maharashtra. Explain with reference to relevant provisions of the Companies Act, 2013, whether SK Infrastructure Limited can be treated as Government Company.

Sol. Government Company [Section 2(45) of the Companies Act, 2013]: Government Company means 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 Governments, or 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.

In the instant case, paid up share capital of SK Infrastructure Limited is 6,00,000 equity shares of Rs. 100 each. 200,000 equity shares are held by Central government and 1,20,000 equity shares are held by Government of Maharashtra. The holding of equity shares by both government is 3,20,000 which is more than 51% of total paid up equity shares.

Hence, SK Infrastructure Limited is a Government company.

32. Jagannath Oils Limited is a public company and having 220 members. Of which 25 members were employee in the company during the period 1st April 2006 to 28th June 2016. They were allotted shares in Jagannath Oils Limited first time on 1st July 2007 which were sold by them on 1st August 2016. After some time, on 1st December 2016, each of those 25 members acquired shares in Jagannath Oils Limited which they are holding till date. Now company wants to convert itself into a private company. State with reasons:

(1) Whether Jagannath Oils Limited is required to reduce the number of members.

(2) Would your answer be different if above 25 members were the employee in Jagannath Oils Limited for the period from 1st April 2006 to 28th June 2017?

Sol. According to Section 2(68) of Companies Act, 2013, “Private company” means a company having a minimum paid-up share capital as may be prescribed, and which by its articles, —

restricts the right to transfer its shares;

except in case of One Person Company, limits the number of its members to two hundred:

Provided 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:

Provided further that— persons who are in the employment of the company; and persons 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 prohibits any invitation to the public to subscribe for any securities of the company;

Following the provisions of Section 2(68), 25 members were employees of the company but not during present membership which was started from 1st December 2016 i.e., after the date on which these 25 members were ceased to be employee in Jagannath Oils Limited. Hence, they will be considered as members for the purpose of the limit of 200 members. The company is required to reduce the

number of members before converting it into a private company.

On the other hand, if those 25 members were ceased to be employee on 28th June 2017, they were employee at the time of getting present membership. Hence, they will **not be counted as members** for the purpose of the limit of 200 members and the total number of members for the purpose of this subsection will be 195. Therefore, Jagannath Oils Limited is not required to reduce the number of members before converting it into a private company.

33. A, B and C has decided to set up a new club with name of ABC club having objects to promote welfare of Christian society. They planned to do charitable work or social activity for promoting the artwork of economically weaker section of Christian society. The company obtained the status of section 8 company and started operating from 1st April, 2017 onwards.

However, on 30th September 2019, it was observed that ABC club was violating the objects of its objective clause due to which it was granted the status of section 8 Company under the Companies Act 2013.

Discuss what powers can be exercised by the central government against ABC club, in such a case?

- Sol.** 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, education, sports etc. Such company intends to apply its profit in promoting its objects. Section 8 companies are registered by the Registrar only when a license is issued by the Central Government to them. Since ABC Club was a Section 8 company and it was observed on 30th September, 2019 that it had started violating the objects of its objective clause. Hence in such a situation the following powers can be exercised by the Central Government: 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 sections subject to which a licence is issued or where the affairs of the company are conducted fraudulently, or violative of the objects of the company or prejudicial to public interest, and on revocation the Registrar shall put 'Limited' or 'Private Limited' against the company's name in the register. 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. 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 the company be wound up under this Act or amalgamated with another company registered under this section. However, no such order shall be made unless the company is given a reasonable opportunity of being heard.

Where a licence is revoked and where the Central Government is satisfied that it is essential in the public interest that the company registered under this section should be amalgamated with another company registered under this section and having similar objects, then, notwithstanding anything to the contrary contained in this Act, the Central Government may, by order, provide for such amalgamation to form a single company with such constitution, properties, powers, rights, interest, authorities and privileges and with such liabilities, duties and obligations as may be specified in the order.

34. An employee Mr. Karan signed a contract with his employer company ABC Limited that he will not solicit the customers after leaving the employment from the company. But after Mr. Karan left ABC Limited, he started up his own company PQR Limited and he started soliciting the customers of ABC Limited for his own business purposes. ABC Limited filed a case against Mr. Karan for breach of the employment contract and for soliciting their customers for own business. Mr. Karan contended that there is corporate veil between him, and his company and he should not be personally held liable for this.

In this context, the company ABC Limited seek your advice as to the meaning of corporate veil and when the veil can be lifted to make the owners liable for the acts done by a company?

- Sol. Corporate Veil:** Corporate Veil refers to a legal concept whereby the company is identified separately from the members of the company. The term Corporate Veil refers to the concept that members of a company are shielded from liability connected to the company's actions. If the company incurs any debts or contravenes any laws, the corporate veil concept implies that members should not be liable for those errors. In other words, they enjoy corporate insulation.

Thus, the shareholders are protected from the acts of the company.

However, under certain exceptional circumstances the courts lift or pierce the corporate veil by ignoring the separate entity of the company and the promoters and other persons who have managed and controlled the affairs of the company. Thus, when the corporate veil is lifted by the courts, the promoters and persons exercising control over the affairs of the company are held personally liable for the acts and debts of the company.

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:

To determine the character of the company i.e. to find out whether co-enemy or friend.

To protect revenue/tax

To avoid a legal obligation

Formation of subsidiaries to act as agents Company formed for fraud/improper conduct or to defeat law

35. ABC Pvt. Ltd., is a Private Company having five members only. All the members of the company were going by car to Mumbai in relation to some business. An accident took place and all of them died. Answer with reasons, under the Companies Act, 2013 whether existence of the company has also come to the end?

Sol. Death of all members of a Private Limited Company, Under the Companies Act, 2013: The most distinguishing feature of a company is its being a separate entity from the shareholders and promoters who form it. This lends stability and perpetuity to the company form of business organization. In short, a company is brought into existence by a process of law and can be terminated or wound up or brought to an end only by a process of law. Its life is not impacted by the death, insolvency or retirement of any or all shareholder(s) or director(s). The provision for transferability or transmission of the shares helps to preserve the perpetual existence of a company by allowing the constitution and identity of shareholders to change. In the present case, ABC Pvt. Ltd. does not cease to exist even by the death of all its shareholders. The legal process will be for the successors of the deceased shareholders to get the shares registered in their names by way of the process which is called "transmission of shares". The company will cease to exist only when it is wound up by a due process of law.

36. Explain clearly the doctrine of 'Indoor Management' as applicable in cases of companies registered under the Companies Act, 1956. Explain the circumstances in which an outsider dealing with the company cannot claim any relief on the ground of 'Indoor Management'.

OR

The persons (not being members) dealing with the company are always protected by the doctrine of indoor management. Explain. Also, explain when doctrine of Constructive Notice will apply.

- Sol. Doctrine of Indoor Management:** The Doctrine of Indoor Management is the exception to the doctrine of constructive notice. The aforesaid doctrine of constructive notice does **in no sense mean that outsiders are deemed to have notice of the internal affairs of the company**. For instance, if an act is authorised by the articles or memorandum, an outsider is entitled to assume that all the detailed formalities for doing that act have been observed. This can be explained with the help of a landmark case ***The Royal British Bank vs. Turquand***. This is the doctrine of indoor management popularly known as ***Turquand Rule***.

FACTS of the Royal British Bank vs. Turquand Mr. Turquand was the official manager (liquidator) of the insolvent Cameron's Coalbrook Steam, Coal and Swansea and Loughor Railway Company. It was incorporated under the Joint Stock Companies Act, 1844. The company had given a bond for £ 2,000 to the Royal British Bank, which secured the company's drawings on its current account. The bond was under the company's seal, signed by two directors and the secretary. When the company was sued, it alleged that under its registered deed of settlement (the articles of association), directors only had power to borrow up to an amount authorized by a company resolution. A resolution had been passed but not specifying how much the directors could borrow. **Held, it was decided** that the bond was valid, so the Royal British Bank could enforce the terms. He said the bank was deemed to be aware that the directors could borrow only up to the amount resolutions allowed. Articles of association were registered with Companies House, so there was constructive notice. But the bank could not be deemed to know which ordinary resolutions passed, because these were not registrable. The bond was valid because there was no requirement to look into the company's internal workings. This is the

indoor management rule, that the company's indoor affairs are the company's problem. you will notice that the aforementioned rule of Indoor Management is important to persons dealing with a company through its directors or other persons. They are entitled to assume that the acts of the directors or other officers of the company are validly performed, if they are within the scope of their apparent authority. So long as an act is valid under the articles, if done in a particular manner, an outsider dealing with the company is entitled to assume that it has been done in the manner required.

37. What are the exceptions to the Doctrine of Indoor Management?

Sol. Actual or constructive knowledge of irregularity: The rule of Indoor management does not protect any person when the person dealing with the company has notice, whether actual or constructive, of the irregularity.

In *Howard vs. Patent Ivory Manufacturing Co.* where the directors could not defend the issue of debentures to themselves because they should have known that the extent to which they were lending money to the company required the assent of the general meeting which they had not obtained.

Likewise, in *Morris v Kansseen*, a director could not defend an allotment of shares to him as he participated in the meeting, which made the allotment. His appointment as a director also fell through because none of the directors appointed him was validly in office.

Suspicion of Irregularity: The doctrine in no way, rewards those who behave negligently.

Where the person dealing with the company is put upon an inquiry, for example, where the transaction is unusual or not in the ordinary course of business, it is the duty of the outsider to make the necessary enquiry.

The protection of the "Turquand Rule" is also not available where the circumstances surrounding the contract are suspicious and therefore invite inquiry. Suspicion should arise, for example, from the fact that an officer is purporting to act in matter, which is apparently outside the scope of his authority. Where, for example, as in the case of *Anand Bihari Lal vs. Dinshaw & Co.* the plaintiff accepted a transfer of a

company's property from its accountant, the transfer was held void. The plaintiff could not have supposed, in absence of a power of attorney that the accountant had authority to effect transfer of the company's property.

Similarly, in the case of *Haughton & Co. v. Nothard, Lowe & Wills Ltd.* where a person holding directorship in two companies agreed to apply the money of one company in payment of the debt to other, the court said that it was something so unusual "that the plaintiff were put upon inquiry to ascertain whether the persons making the contract had any authority in fact to make it." Any other rule would "place limited companies without any sufficient reasons for so doing, at the mercy of any servant or agent who should purport to contract on their behalf."

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. Forgery may in circumstances exclude the 'Turquand Rule'. The only clear illustration is found in the *Ruben v Great Fingall Consolidated*. In this case the plaintiff was the transferee of a share certificate issued under the seal of the defendant's company. The company's secretary, who had affixed the seal of the company and forged the signature of the two directors, issued the certificate. The plaintiff contended that whether the signature were genuine or forged was apart of the internal management, and therefore, the company should be estopped from denying genuineness of the document. But it was held, that the rule has never been extended to cover such a complete forgery.

38. Narendra Motors Limited is a government company. Shah Auto Private Limited is a private company having share capital of ten crores in the form of ten lacs shares of Rs. 100 each. Narendra Motors Limited is holding five lacs five thousand shares in Shah Auto Private Limited. Shah Auto Private Limited claimed the status of Government Company. Advise as legal advisor, whether Shah Auto Private Limited is government company under the provisions of Companies Act, 2013?

Sol. According to the provisions of Section 2(45) of Companies Act, 2013, Government Company means

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 Governments, or 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. According to Section 2(87), “subsidiary company” in relation to any other company (that is to say the holding company), means a company in which the holding exercises or controls more than one-half of the total voting power either at its own or together with one or more of its subsidiary companies. By virtue of provisions of Section 2(87) of Companies Act, 2013, Shah Auto Private Limited is a subsidiary company of Narendra Motors Limited because Narendra Motors Limited is holding more than one-half of the total voting power in Shah Auto Private Limited. Further as per Section 2(45), a subsidiary company of Government Company is also termed as Government Company. Hence, Shah Auto Private Limited being subsidiary of Narendra Motors Limited will also be considered as Government Company.

39. Mr. A is an Indian citizen and his stay in India during immediately preceding financial year is for 115 days. He appoints Mr. B as his nominee who is a foreign citizen but has stayed in India for 130 days during immediately preceding financial year.

- (1) Is Mr. A eligible to be incorporated as a One Person Company (OPC). If yes, can he give the name of Mr. B in the memorandum of Association as his nominee to become the member after Mr. A’s incapacity to become a member.
- (2) If Mr. A has contravened any of the provisions of the Act, what are the consequences?

Sol. As per the provisions of the Companies Act, 2013, only a natural person who is an Indian citizen and resident in India (person who stayed in India for a period of not less than 120 days during immediately preceding financial year) –

Shall be eligible to incorporate an OPC

Shall be a nominee for the sole member.

In the given case, though Mr. A is an Indian citizen, his stay in India during the immediately preceding previous year is only 115 days which is below the requirement of 120 days. Hence Mr. A is not eligible to incorporate an OPC. Also, even though Mr. B’s name is mentioned in the memorandum of Association as nominee and his stay in India during the immediately preceding financial year is more than 120 days, he is a foreign citizen and not an Indian citizen. Hence B’s name cannot be given as nominee in the memorandum. Since Mr. A is not eligible to incorporate a One Person Company (OPC), he will be contravening the provisions, if he incorporates one. He shall be punishable with fine which may extend to **ten thousand rupees** and with a further fine which may extend to **One thousand rupees every day** after the first during which such contravention occurs.

40. What is meant by a Guarantee Company? State the similarities and dissimilarities between a Guarantee Company and a Company having Share Capital.

OR

Explain the meaning of Guarantee Company? State the similarities and dissimilarities between a ‘Guarantee Company’ and ‘Company Limited by Shares

Sol. **Meaning of Guarantee Company:** Section 2(21) of the Companies Act, 2013 defines a Company Limited by Guarantee as a company having the liability of its members limited by the memorandum to such amount as the members may respectively undertake to contribute to the assets of the company in the event of its being wound up. Thus, the liability of the members of a guarantee company is limited to a stipulated amount in terms of individual guarantees given by members and mentioned in the memorandum. The members cannot be called upon to contribute more than such stipulated amount for which each member has given a guarantee in the memorandum of association.

Similarities and dis-similarities between the Guarantee Company and the Company limited by shares:

The common features between a “guarantee company” and the “company limited share” are legal entity and limited liability. In case of a company limited by shares, the liability of its members is limited to the amount remaining unpaid on the shares held by them. Both these types of

companies have to state this fact in their memorandum that the members' liability is limited.

However, the dissimilarities between a 'guarantee company' and 'company limited by shares' is that in the former case the members will be called upon to discharge their liability only after commencement of the winding up of the company and only to the extent of amounts guaranteed by them respectively; whereas in the case of a company limited by shares, the members may be called upon to discharge their liability at any time, either during the life of the company or during the course of its winding up.

41. Examine with reasons whether the following statement is correct or incorrect:

Sol. Incorrect: The common seal is a seal used by a corporation as the symbol of its incorporation. The Companies (Amendment) Act, 2015 has made the common seal optional by omitting the words "and a common seal" from Section 9 so as to provide an alternative mode of authorization for companies who opt not to have a common seal. 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.

42. Mr. X had purchased some goods from M/s ABC Limited on credit. A credit period of one month was allowed to Mr. X. Before the due date Mr. X went to the company and wanted to repay the amount due from him. He found only Mr. Z there, who was the factory supervisor of the company. Mr. Z told Mr. X that the accountant and the cashier were on leave, he is in-charge of receiving money and he may pay the amount to him. Mr. Z issued a money receipt under his signature. After two months M/s ABC Limited issued a notice to Mr. X for non-payment of the dues within the stipulated period. Mr. X informed the company that he had already cleared the dues and he is no more responsible for the same. He also contended that Mr. Z is an employee of the company whom he had made the payment and being an outsider, he trusted the words of Mr. Z as duty distribution is a job of the internal management of the company.

Analyse the situation and decide whether Mr. X is free from his liability.

Sol. Doctrine of Indoor Management: The Doctrine of Indoor Management is the exception to the doctrine of constructive notice. The doctrine of constructive notice does not mean that outsiders are deemed to have notice of the internal affairs of the company. For instance, if an act is authorised by the articles or memorandum, an outsider is entitled to assume that all the detailed formalities for doing that act have been observed. The doctrine of Indoor Management is important to persons dealing with a company through its directors or other persons. They are entitled to assume that the acts of the directors or other officers of the company are validly performed, if they are within the scope of their apparent authority. So long as an act is valid under the articles, if done in a particular manner, an outsider dealing with the company is entitled to assume that it has been done in the manner required. In the given question, Mr. X has made payment to Mr. Z and he (Mr. Z) gave to receipt of the same to Mr. X. Thus, it will be rightful on part of Mr. X to assume that Mr. Z was also authorised to receive money on behalf of the company. Hence, Mr. X will be free from liability for payment of goods purchased from M/s ABC Limited, as he has paid amount due to an employee of the company.

43. Alfa school started imparting education on 1.4.2010, with the sole objective of providing education to children of weaker society either free of cost or at a very nominal fee depending upon the financial condition of their parents. However, on 30th March 2018, it came to the knowledge of the Central Government that the said school was operating by violating the objects of its objective clause due to which it was granted the status of a section 8 company under the Companies Act, 2013. Describe what powers can be exercised by the Central Government against the Alfa School, in such a case?

Sol. 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, education, sports etc. Such company intends to apply its profit in promoting its objects. Section 8 companies are registered by the Registrar only when a license is issued by the Central Government to

them. Since, Alfa School was a Section 8 company and it had started violating the objects of its objective clause, hence in such a situation the following powers can be exercised by the Central Government:

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 subject to which a licence is issued or where the affairs of the company are conducted fraudulently, or violative of the objects of the company or prejudicial to public interest, and on revocation the Registrar shall put 'Limited' or 'Private Limited' against the company's name in the register. 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. 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 the company be wound up under this Act or amalgamated with another company registered under this section. However, no such order shall be made unless the company is given a reasonable opportunity of being heard. Where a licence is revoked and where the Central Government is satisfied that it is essential in the public interest that the company registered under this section should be amalgamated with another company registered under this section and having similar objects, then, notwithstanding anything to the contrary contained in this Act, the Central Government may, by order, provide for such amalgamation to form a single company with such constitution, properties, powers, rights, interest, authorities and privileges and with such liabilities, duties and obligations as may be specified in the order.

44. Rohan incorporated a "One Person Company". The memorandum of OPC indicates the name of his brother Vinod as the nominee of OPC. However, Vinod is starting his new business in abroad and needs to leave India permanently. Due to this fact, Vinod is withdrawing his consent of nomination in the said One Person Company. Taking into considerations the provisions of the Companies Act, 2013 answer the questions given below: -

I. If is it mandatory for Vinod to withdraw his nomination in the said OPC. Can Rohan make his 17-year-old son as a nominee in such a case?

- Sol.** Yes, it is mandatory for Vinod to withdraw his nomination in the said OPC as he is leaving India permanently as only a natural person who is an Indian citizen and resident in India or otherwise and has stayed in India for a period of not less than 120 days during the immediately preceding financial year shall be a nominee in OPC. Since Vinod will not satisfy this condition, so he needs to withdraw his nomination. No, Rohan cannot make his 17 year old son as a nominee of his OPC as no minor shall become member or nominee of the OPC or can hold beneficial interest.

45. ABC Limited was into sale and purchase of iron rods. This was the main object of the company mentioned in the Memorandum of Association. The company entered into a contract with Mr. John for some finance related work. Later on, the company repudiated the contract as being ultra vires

With reference to the same, briefly explain the doctrine of "ultra vires" under the Companies Act, 2013. What are the consequences of ultra vires acts of the company?

- Sol.** **Doctrine of ultra vires:** The meaning of the term ultra vires is simply "beyond (their) powers". The legal phrase "ultra vires" is applicable only to acts done in excess of the legal powers of the doers. This presupposes that the powers in their nature are limited. It is a fundamental rule of Company Law that the objects of a company as stated in its memorandum can be departed from only to the extent permitted by the Act, thus far and no further. In consequence, any act done or a contract made by the company which travels beyond the powers not only of the directors but also of the company is wholly void and inoperative in law and is therefore not binding on the company. On this account, a company can be restrained from employing its fund for purposes other than those sanctioned by the memorandum. Likewise, it can be restrained from carrying on a trade different from the one it is authorised to carry on.

The impact of the doctrine of ultra vires is that a company can neither be sued on an ultra vires transaction, nor can it sue on it. Since the

memorandum is a “public document”, it is open to public inspection. Therefore, when one deals with a company one is deemed to know about the powers of the company. If in spite of this you enter into a transaction which is ultra vires the company, you cannot enforce it against the company.

An act which is ultra vires the company being void, cannot be ratified even by the unanimous consent of all the shareholders of the company.

Hence in the given case, ABC Limited cannot enter into a contract outside the purview of its object clause of memorandum of association as it becomes ultra vires and thus null and void

- exercises or controls more than one-half of the total voting power either at its own or together with one or more of its subsidiary companies:

For the purposes of this section —

- 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;
- the expression “company” includes anybody corporate;

It is to be noted that Preference share capital will also be considered **if** preference shareholders have same voting rights as equity shareholders. Since question is silent we will assume that preference share does not carry voting rights

In the instant case, Ram Private Limited is having paid-up capital of Rs.10 Crores in the form of 7,00,000 Equity Shares of Rs.100 each and 3,00,000 Preference Shares of Rs.100 each. Lakhan Private Limited is holding 3,00,000 Equity Shares and 3,00,000 Preference Shares in Ram Private Limited.

On the basis of provisions of Section 2(87) and facts of the given problem, Lakhan Private Limited is holding 3,00,000 Equity Shares of total equity paid up share capital of Ram Private Limited. Therefore, as Lakhan Private Limited does not exercise or controls more than one-half of the total voting power in Ram Private Limited, Ram Private Limited is not subsidiary of Lakhan Private Limited.

46. PQR Private Ltd. is a company registered under the Companies Act, 2013 with a Paid-Up Share Capital of Rs. 40 lakh and turnover of Rs. 2.5 crores. Explain the meaning of the "Small Company" and examine whether the PQR Private Ltd. can avail the status of small company in accordance with the provisions of the Companies Act, 2013.

Sol. Small Company –significant points

- A private company
- Paid up capital – not more than Rs. 2 crores and
- Turnover – not more than Rs. 20 crores.
- Should not be – Section 8 company

– Holding or a Subsidiary company OR a company or body corporate governed by special act Thus, PQR Private Limited is a small company, since it is passing both the criteria

47. The paid-up capital of Ram Private Limited is Rs. 10 Crores in the form of 7,00,000 Equity Shares of Rs. 100 each and 3,00,000 Preference Shares of Rs. 100 each. Lakhan Private Limited is holding 3,00,000 Equity Shares and 3,00,000 Preference Shares in Ram Private Limited. State with reason, Whether Ram Private Limited is subsidiary of Lakhan Private Limited?

Sol. According to Section 2(87) of Companies Act, 2013 “subsidiary company” in relation to any other company (that is to say the holding company), means a company in which the holding company—

- controls the composition of the Board of Directors; or

48. The Object Clause of Memorandum of Association of ABC Pvt. Ltd. authorised the company to carry on the business of trading in Fruits and Vegetables. The Directors of the company in recently concluded Board Meeting decided and accordingly, the company ordered for fish for the purpose of trading. FSH Limited supplied fish to ABC Pvt. Ltd. worth Rs. 36 Lakhs. The members of the company convened an extraordinary general meeting and negated the proposal of the Board of Directors on the ground of ultra vires acts. FSH Limited being aggrieved of the said decision of ABC Pvt Ltd. seeks your advice. Advise them.

Sol. Doctrine of ultra vires: The meaning of the term ultra vires is simply “beyond (their) powers”. The legal phrase “ultra vires” is applicable only to acts

done in excess of the legal powers of the doers. This presupposes that the powers in their nature are limited. It is a fundamental rule of Company Law that the objects of a company as stated in its memorandum can be departed from only to the extent permitted by the Act, thus far and no further. In consequence, any act done or a contract made by the company which travels beyond the powers not only of the directors but also of the company is wholly void and inoperative in law and is therefore not binding on the company.

On this account, a company can be restrained from employing its fund for purposes other than those sanctioned by the memorandum. Likewise, it can be restrained from carrying on a trade different from the one it is authorized to carry on. The impact of the doctrine of ultra vires is that a company can neither be sued on an ultra vires transaction, nor can it sue on it. Since the memorandum is a “public document”, it is open to public inspection. Therefore, when one deals with a company one is deemed to know about the powers of the company. If in spite of this you enter into a transaction which is ultra vires the company, you cannot enforce it against the company.

Therefore, the resolution passed by the Board of Director ABC Pvt. Limited for an ultra vires transaction is invalid. As a result of this, the transaction entered into the supply of fish with FSH Limited is not legal and is void.

49. What is the meaning of “Certificate of Incorporation” under the provisions of the Companies Act, 2013? What are the effects of registration of a company?

Sol. Under section 7(2) the Registrar shall on the basis of documents and information filed for the formation of a company, shall register all the documents and information and issue a certificate that the company is incorporated in the prescribed form to the effect that the proposed company is incorporated under this Act. The company becomes a legal entity from the date mentioned in the certificate of incorporation and continues to be so till it is wound up.

Effects of registration of a company

Section 9 of the Companies Act, 2013 provides that, from the date of incorporation mentioned in the certificate of incorporation, such of the subscribers

to the Memorandum and all other persons, as may from time to time become members of the company, shall be a body corporate by the name contained in the memorandum, capable forthwith of exercising all the functions of an incorporated company under this Act and having perpetual succession with power to acquire, hold and dispose of property, both movable and immovable, tangible and intangible, to contract and to sue and be sued by the said name. Accordingly, when a company is registered and a certificate of incorporation is issued by the Registrar, three important consequences follow:

the company becomes a distinct legal entity. Its life commences from the date mentioned in the

certificate of incorporation capable of entering into contracts in its own name, acquiring, holding and disposing of property of any nature whatsoever and capable of suing and being sued in its own name.

it acquires a life of perpetual existence by the doctrine of succession. The members may come and go, but it goes on forever, unless it is wound up.

Its property is not the property of the shareholders. The shareholders have a right to share in the profits of the company as and when declared either as dividend or as bonus shares. Like wise any liability of the company is not the liability of the individual shareholders

50. FAREB Limited was incorporated by acquisition of FAREB & Co., a partnership firm, which was earlier involved in many illegal activities. The promoters furnished some false information and also suppressed some material facts at the time of incorporation of the company. Some members of the public (not being directors or promoters of the company) approached the National Company Law Tribunal (NCLT) against the incorporation status of FAREB Limited. NCLT is about to pass the order by directing that the liability of the members of the company shall be unlimited.

Given the above, advice on whether the above order will be legal and mention the precaution to be taken by NCLT before passing order in respect of the above as per the provisions of the Companies Act, 2013.

Sol. (i) As per section 7(7) of the Companies Act, 2013, 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, direct that liability of the members shall be unlimited.

Hence, the order of NCLT will be legal.

Precautions: Before making any order, —

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



Sampurna (CA-Foundation)

The Limited Liability Partnership Act, 2008

Q. Bank

1. State the rules regarding registered office of a Limited Liability Partnership (LLP) and change therein as per provisions of the Limited Liability Partnership Act, 2008.

Sol. Registered office of LLP and change therein (Section 13):

- (1) Every LLP shall have a registered office to which all communications and notices may be addressed and where they shall be received.
- (2) A document may be served on a LLP or a partner or designated partner thereof by sending it by post under a certificate of posting or by registered post or by any other manner, as may be prescribed, at the registered office and any other address specifically declared by the LLP for the purpose in such form and manner as may be prescribed.
- (3) A LLP may change the place of its registered office and file the notice of such change with the Registrar in such form and manner and subject to such conditions as may be prescribed and any such change shall take effect only upon such filing.
- (4) If any default is made in complying with the requirements of this section, the limited liability partnership and its every partner shall be liable to a penalty of five hundred rupees for each day during which the default continues, subject to a maximum of fifty thousand rupees for the limited liability partnership and its every partner

2. State the circumstances under which a LLP and its partners may face unlimited liability under the Limited Liability Partnership Act, 2008.

Sol. Unlimited liability in case of fraud (Section 30):

- (1) In case of fraud:
 - In the event of an act carried out by a LLP, or any of its partners,
 - with intent to defraud creditors of the LLP

or any other person, or for any fraudulent purpose,

- the liability of the LLP and partners who acted with intent to defraud creditors or for any fraudulent purpose
- shall be unlimited for all or any of the debts or other liabilities of the LLP.

However, in case any such act is carried out by a partner, the LLP is liable to the same extent as the partner unless it is established by the LLP that such act was without the knowledge or the authority of the LLP.

- (2) Where any business is carried on with such intent or for such purpose as mentioned in sub-section (1), every person who was knowingly a party to the carrying on of the business in the manner aforesaid shall be punishable with
 - imprisonment for a term which may extend to 5 years and
 - with fine which shall not be less than Rs. 50,000 but which may extend to Rs. 5 Lakhs.
- (3) Where a LLP or any partner or designated partner or employee of such LLP has conducted the affairs of the LLP **in a fraudulent manner**, then without prejudice to any criminal proceedings which may arise under any law for the time being in force, the LLP and any such partner or designated partner or employee shall be **liable to pay compensation** to any person who has suffered any loss or damage by reason of such conduct.

However, such **LLP shall not be liable** if any such partner or designated partner or employee has **acted fraudulently without knowledge of the LLP**

3. Limited Liability Partnership (LLP) gives the benefits of limited liability of a company on one hand and the flexibility of a partnership on the other. Discuss.

Or

LLP gives the benefits of limited liability of a company and the flexibility of a partnership

Or

"LLP is an alternative corporate business form that gives the benefits of limited liability of a company and the flexibility of a partnership". Explain.

- Sol. Limited Liability:** Every partner of a LLP is, for the purpose of the business of LLP, the agent of the LLP, but not of other partners (Section 26 of the LLP Act, 2008). The liability of the partners will be limited to their agreed contribution in the LLP, while the LLP itself will be liable for the full extent of its assets.

Flexibility of a partnership: The LLP allows its members the flexibility of organizing their internal structure as a partnership based on a mutually arrived agreement. The LLP form enables entrepreneurs, professionals and enterprises providing services of any kind or engaged in scientific and technical disciplines, to form commercially efficient vehicles suited to their requirements. Owing to flexibility in its structure and operation, the LLP is a suitable vehicle for small enterprises and for investment by venture capital.

4. What are the essential elements to form a LLP in India as per the LLP Act, 2008?

Sol. 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. At least 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.

5. Explain the the steps involved therein under the LLP Act, 2008.

Sol. Steps to incorporate LLP:

1. Name reservation:
 - The first step to incorporate Limited Liability Partnership (LLP) is reservation of name of LLP.
 - Applicant has to file e-Form 1, for ascertaining availability and reservation of the name of a LLP business.
2. Incorporate LLP:
 - After reserving a name, user has to file e-Form 2 for incorporating a new Limited Liability Partnership (LLP).
 - e-Form 2 contains the details of LLP proposed to be incorporated, partners'/ designated partners' details and consent of the partners/designated partners to act as partners/designated partners
3. LLP Agreement
 - 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-Form 3 within 30 days of incorporation of LLP.

6. Discuss the conditions under which LLP will be liable and not liable for the acts of the partner.

Sol. Conditions under which LLP will be liable [Section 27(2) of the LLP Act, 2008]

The LLP is liable if a partner of a LLP is liable to any person as a result of a wrongful actor omission

on his part in the course of the business of the LLP or with its authority.

Conditions under which LLP will not be liable [Section 27(1) of the LLP Act, 2008]

A LLP is not bound by anything done by a partner in dealing with a person if—

- (a) the partner in fact has no authority to act for the LLP in doing a particular act; and
- (b) the person knows that he has no authority or does not know or believe him to be a partner of the LLP.

7. State the circumstances under which LLP may be wound up by the Tribunal under the Limited Liability Partnership Act, 2008.

Or

Explain the circumstances in which LLP may be wound up by Tribunal under the LLP Act, 2008.

Sol. Circumstances in which LLP may be wound up by Tribunal (Section 64): A LLP may be wound up by the Tribunal:

1. if the LLP decides that LLP be wound up by the Tribunal;
2. if, for a period of more than six months, the number of partners of the LLP is reduced below two;
3. if the LLP is unable to pay its debts;
4. if the LLP has acted against the interests of the sovereignty and integrity of India, the security of the State or public order;
5. if the LLP has made a default in filing with the Registrar the Statement of Account and Solvency or annual return for any five **consecutive** financial years; or

if the Tribunal is of the opinion that it is just and equitable that the LLP be wound up.

8. What do you mean by Limited Liability Partnership (LLP)? What are the advantages for forming a LLP for doing business?

1. **Sol. LLP:** A LLP is a new form of legal business entity with limited liability. It is an alternative corporate business vehicle that not only gives the benefits of limited liability at low compliance cost but allows its partners the flexibility of organising their internal structure

as a traditional partnership. 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.

LLP is an alternative corporate business form that gives the benefits of limited liability of a company and the flexibility of a partnership.

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.

Advantages of LLP form:

- (a) LLP is organized and operates on the basis of an agreement.
- (b) It provides flexibility without imposing detailed legal and procedural requirements
- (c) It enables professional/technical expertise and initiative to combine with financial risk-taking capacity in an innovative and efficient manner.
- (d) It is easy to form
- (e) In LLP form, all partners enjoy limited liability
- (f) Flexible capital structure is there in this form
- (g) It is easy to dissolve

9. List the differences between the Limited Liability Partnership and the Limited Liability Company.

Sol.

	Basis	LLP	Limited Liability Company
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 contract 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	Name of the public company to contain the word “limited”

		partnership” or “LLP” as suffix.	and Pvt. Co. to contain the word “Private limited” as suffix.
5	No. 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. Members can be organizations, trusts, another business form or individuals.
6	Liability of Members / partners	Liability of a partners is limited to the extent of agreed contribution in case of intention is 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 by the shareholders.
8	Minimum number of directors/ designated partners	Minimum 2 designated partners.	Pvt. Co. – 2 directors Public co. – 3 directors

liability of the partners will be limited.

LLP is an alternative corporate business form that gives the benefits of limited liability of a company and the flexibility of a partnership.

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.

Characteristic/Salient Features of LLP

1. **LLP is a body corporate:** Section 2(1)(d) of the LLP Act, 2008 provides that a LLP is a body corporate formed and incorporated under this Act and is a legal entity separate from that of its partners and shall have perpetual succession. Therefore, any change in the partners of a LLP shall not affect the existence, rights or liabilities of the LLP.

Section 3 of LLP Act provides that a LLP is a body corporate formed and incorporated under this Act and is a legal entity separate from that of its partners.

2. **Perpetual Succession:** The LLP can continue its existence irrespective of changes in partners. Death, insanity, retirement or insolvency of partners has no impact on the existence of LLP. It is capable of entering into contracts and holding property in its own name.
3. **Separate Legal Entity:** The LLP as a separate legal entity, is liable to the full extent of its assets but liability of the partners is limited to their agreed contribution in the LLP. In other words, creditors of LLP shall be the creditors of LLP alone.
4. **Mutual Agency:** No partner is liable on account of the independent or un-authorized actions of other partners, thus individual partners are shielded from joint liability created by another partner’s wrongful business decisions or misconduct. In other words, all partners will be the agents of the LLP alone. No one partner can bind the other partner by his acts.
5. **LLP Agreement:** Mutual rights and duties of the partners within a LLP are governed by an agreement between the partners. The LLP Act, 2008 provides flexibility to partner to devise the agreement as per their choice. In the absence of

10. What is the meaning of the Limited Liability Partnership? State the various characteristics of it?

1. Sol. Meaning of Limited Liability Partnership (LLP):

A LLP is a new form of legal business entity with limited liability. It is an alternative corporate business vehicle that not only gives the benefits of limited liability at low compliance cost but allows its partners the flexibility of organising their internal structure as a traditional partnership. The LLP is a separate legal entity and, while the LLP itself will be liable for the full extent of its assets, the

any such agreement, the mutual rights and duties shall be governed by the provisions of the LLP Act, 2008.

6. **Artificial Legal Person:** A LLP is an artificial legal person because it is created by a legal process and is clothed with all rights of an individual. It can do everything which any natural person can do, except of course that, it cannot be sent to jail, cannot take an oath, cannot marry or get divorce nor can it practice a learned profession like CA or Medicine. A LLP is invisible, intangible, immortal (it can be dissolved by law alone) but not fictitious because it really exists.
7. **Common Seal:** A LLP being an artificial person can act through its partners and designated partners. LLP may have a common seal, if it decides to have one [Section 14(c)]. Thus, 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:** Every partner of a LLP is, for the purpose of the business of LLP, the agent of the LLP, but not of other partners (Section 26). The liability of the partners will be limited to their agreed contribution in the LLP. Such contribution may be of tangible or intangible nature or both.

Example: The professionals like Engineering consultants, Legal Advisors and Accounting

Professionals are afraid of entering into business due to unlimited liability. Hence the LLP partnership Act provides an avenue for these professionals to Limited Liability Partnership firms which restricts their liability to the agreed amount. This has encouraged Professionals to form LLP.

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:** The essential requirement for forming LLP is carrying on a **lawful business with a view to earn profit**. Thus, LLP cannot be formed for charitable or non-economic purpose.
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 agreements 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:** Every form or application of document required to be filed or delivered under the act and rules made thereunder, shall be filed in computer readable electronic form on its website www.mca.gov.in and authenticated by a partner or designated partner of LLP by the use of electronic or digital signature.
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 as **place of business within India**”. Foreign LLP can become a partner in an Indian LLP

11. What is the procedure for changing the name of Limited Liability Partnership (LLP) under the LLP Act, 2008?

- (1) **Sol.** Notwithstanding anything contained in sections 15 and 16, if through inadvertence or otherwise, a limited liability partnership, on its first registration or on its registration by a new body corporate, its registered name; ">name, is registered by a name which is identical with or too nearly resembles to—
 - (a) that of any other limited liability partnership or a company; or

- (b) a registered trade mark of a proprietor under the Trade Marks Act, 1999, as is likely to be mistaken for it, then on an application of such limited liability partnership or proprietor referred to in clauses (a) and (b) respectively or a company, the Central Government may direct that such limited liability partnership to change its name or new name within a period of three months from the date of issue of such direction:

Provided that an application of the proprietor of the registered trademarks shall be maintainable within a period of three years from the date of incorporation or registration or change of name of the limited liability partnership under this Act.

- (2) Where a limited liability partnership changes its name or obtains a new name under sub-section (1), it shall within a period of fifteen days from the date of such change, give notice of the change to Registrar along with the order of the Central Government, who shall carry out necessary changes in the certificate of incorporation and within thirty days of such change in the certificate of incorporation, such limited liability partnership shall change its name in the limited liability partnership agreement.
- (3) If the limited liability partnership is in default in complying with any direction given under sub-section (1), the Central Government shall allot a new name to the limited liability partnership in such manner as may be prescribed and the Registrar shall enter the new name in the register of limited liability partnerships in place of the old name and issue a fresh certificate of incorporation with new name, which the limited liability partnership shall use thereafter:

Provided that nothing contained in this sub-section shall prevent a limited liability partnership from subsequently changing its name in accordance with the provisions of section 16.

- (1) **Sol.** Every limited liability partnership shall have at least two designated partners who are individuals and at least one of them shall be a resident in India:

Provided that in case of a limited liability partnership in which all the partners are bodies corporate or in which one or more partners are individuals and bodies corporate, at least two individuals who are partners of such limited liability partnership or nominees of such bodies corporate shall act as designated partners.

Explanation. For the purposes of this section, the term resident in India means a person who has stayed in India for a period of not less than one hundred and **twenty days during the financial year**.

- (2) Subject to the provisions of sub-section (1),
- (i) if the incorporation document
 - (a) specifies who are to be designated partners, such persons shall be designated partners on incorporation; or states that each of the partners from time to time of limited liability partnership is to be designated partner, every partner shall be a designated partner;
 - (ii) any partner may become a designated partner by and in accordance with the limited liability partnership agreement and a partner may cease to be a designated partner in accordance with limited liability partnership agreement.
- (3) An individual shall not become a designated partner in any limited liability partnership unless he has given his prior consent to act as such to the limited liability partnership in such form and manner as may be prescribed.
- (4) Every limited liability partnership shall file with the Registrar the particulars of every individual who has given his consent to act as designated partner in such form and manner as may be prescribed within thirty days of his appointment.
- (5) An individual eligible to be a designated partner shall satisfy such conditions and requirements as may be prescribed.

12. What do you mean by Designated Partner? Whether it is mandatory to appoint Designated partner in a LLP?

Every designated partner of a limited liability partnership shall obtain a Designated Partners Identification Number (DPIN) from the Central Government and the provisions of **sections 153 to 159 (both inclusive) of the Companies Act, 2013** shall apply *mutatis mutandis* for the said purpose

13. Differentiate between a LLP and a partnership firm?
Sol.

	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 third parties.
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 forever.	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	Liability of each partner is unlimited. It can

		extent to agreed contribution except in case of willful fraud.	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 at least one of them shall be resident in India.	There is no provision for such partners under the 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 of documents	LLP is required to file: Annual statement of accounts Statement of solvency 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.

14. Who are the individuals which shall not be capable of becoming a partner of a Limited Liability Partnership?

Sol. Partners (Section 5 of Limited Liability Partnership Act, 2008): Any individual or body corporate may be a partner in a LLP.

However, an individual shall not be capable of becoming a partner of a LLP, if—

- (a) he has been found to be of unsound mind by a Court of competent jurisdiction and the finding is in force;
- (b) he is an undischarged insolvent; or
- (c) he has applied to be adjudicated as an insolvent and his application is pending.

15. What are the effects of registration of LLP?

Sol. On registration of a LLP , by its name, it shall be capable of :- (Section 14):

- (1) Suing and being sued
- (2) Acquiring, owning, holding and developing or property, whether movable or immovable, tangible or intangible
- (3) Having a common seal, if it decided to have one Doing and suffering such other acts and things as bodies corporate may lawfully do and suffer

16. Examine the concept of LLP.

Sol. Meaning – A LLP is a new form of legal business entity with limited liability. It is an alternative corporate business vehicle that gives the benefits of limited liability but allows its

partners the flexibility of organising their internal structure as a traditional partnership. 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.

Concept of “limited liability partnership” :-

- The LLP can continue its existence irrespective of changes in partners. It is capable of entering into contracts and holding property in its own name.
- The LLP is a separate legal entity, is liable to the full extent of its assets but liability of the partners is limited to their agreed contribution in the LLP.
- Further, no partner is liable on account of the independent or un-authorized actions of other partners, thus individual partners are shielded from joint liability created by another partner’s wrongful business decisions or misconduct.
- Mutual rights and duties of the partners within a LLP are governed by an agreement between the partners or between the partners and the LLP as the case may be. The LLP, however, is not relieved of the liability for its other obligations as a separate entity.
- LLP is an alternative corporate business form that gives the benefits of limited liability of a company and the flexibility of a partnership.

