

CA Foundation Contract law **UNIT – 7**

INDEMNITY AND GUARANTEE

Q.1. Nov 22 Marks 4

Manish, a minor, lost his parents in COVID-19 pandemic. Due to poor financial background Manish was facing difficulties in maintaining his livelihood. He approached Mr. Sohel (a grocery shopkeeper) to supply him grocery items and to wait for some period for receiving his dues. Mr. Sohel did not agree with the proposal; but when Mr. Ganesh, a local person, who is a major, agreed to provide guarantee that he would pay the dues in case Manish fails to pay the amount, Mr. Sohel supplied the required groceries to Manish. After few months when Manish failed to clear his dues, Mr. Sohel approached Mr. Ganesh and asked him to clear the dues of Manish. Mr. Ganesh refused to pay the amount on two grounds; firstly, that there was no consideration in the contract of guarantee and secondly that Manish is a minor and therefore on both the grounds the contract of guarantee is not valid.

*Referring to the relevant provisions of the Indian Contract Act, 1872, decide, whether the contention of Mr. Ganesh, (the surety) is tenable? Will your answer differ in case both Manish (the principal debtor) and Mr. Ganesh (the surety) are minors? **(4 Marks)***

(i) Whether the contention of Mr. Ganesh (the Surety) is Tenable?

In the light of the given facts in the question, the guarantee was given by Mr. Ganesh (the surety) to Mr. Sohel that he would pay the dues in case Mr. Manish (the Principal Debtor) fails to pay the amount. However, later on it was contended by Mr. Ganesh that there was no consideration in the contract of guarantee and also that Manish is a minor and therefore the contract of guarantee is not valid.

As per the provisions of Section 127 of the Indian Contract Act, 1872, anything done, or promise made, for the benefit of the principal debtor, may be a sufficient consideration to the surety for giving the guarantee.

In the given case, Mr. Ganesh has provided guarantee to Mr. Sohel for the benefit of Mr. Manish which will be treated as sufficient consideration even though there is absence of direct consideration. In other words, a guarantee without consideration is void, but there is no need for a direct consideration between the surety and the creditor.

Regarding the contention that Manish is a minor and therefore, the contract of guarantee will be invalid is not tenable due to the fact that Mr. Ganesh (surety) and Mr. Sohel (the creditor) are not minors. In other words, the capability of the principal debtor (being a minor) does not affect the validity of the agreement of the guarantee.

In view of the above, it can be concluded that the contention of Mr. Ganesh is not tenable.

(ii) In case both Manish (the principal debtor) and Mr. Ganesh (the surety) are minors:

The answer will differ in case both Manish (the principal debtor) and Mr. Ganesh (the surety) are minors. In such a situation, the agreement will be treated as void from inception as the minors cannot give guarantee even with a claim for necessities.

Q.2. Dec 2021 Marks 4

Alpha Motor Ltd. agreed to sell a bike to Ashok under hire-purchase agreement on guarantee of Abhishek. The Terms were: hire-purchase price ₹ 96,000 payable in 24 monthly instalments of ₹ 8,000 each. Ownership to be transferred on the payment of last instalment. State whether Abhishek is discharged in each of the following alternative case under the provisions of the Indian Contract Act, 1872:

(i) Ashok paid 12 instalments but failed to pay next two instalments. Alpha Motor Ltd. sued Abhishek for the payment of arrears and Abhishek paid these two instalments i.e. 13th and 14th. Abhishek then gave a notice to Alpha Motor Ltd. to revoke his guarantee for the remaining months.

(ii) If after 15th months, Abhishek died due to COVID-19.

(4 Marks)

According to section 130 of the Indian Contract Act, 1872, the continuing guarantee may at any time be revoked by the surety as to future transactions by notice to the creditors. Once the guarantee is revoked, the surety is not liable for any future transaction however he is liable for all the transactions that happened before the notice was given.

A specific guarantee can be revoked only if liability to principal debtor has not accrued.

(i) In the given question Ashok paid 12 instalments (out of total 24 monthly instalments), but failed to pay next two instalments. Abhishek (guarantor) paid the 13th and 14th instalments but then he revoked guarantee for the remaining months. Thus, Abhishek is not liable for instalments that was made after the notice, but he is liable for instalments made before the notice (which he had paid i.e. 13th and 14th instalments).

(ii) According to section 131 of the Indian Contract Act, 1872, in the absence of any contract to the contrary, the death of surety operates as a revocation of a continuing guarantee as to the future transactions taking place after the death of surety. However, the surety's estate remains liable for the past transactions which have already taken place before the death of the surety.

In the given question, Abhishek (guarantor) died after 15th month. This will operate as a revocation of a continuing guarantee as to the future transactions taking place after the death of surety (i.e. Abhishek). However, the Abhishek's estate remains liable for the past transactions (i.e. 15th month and before) which have already taken place before the death of the surety.

Q.3. Dec 2021 Marks 4

Shyam, at the request of Govind, sells goods which were, in the possession of Govind. However, Govind had no right to dispose of such goods. Shyam did not know this and handed over the proceed of the sale to Govind. Afterwards, Manohar, who was the true owner of the goods, sued Shyam and recovered the value of the goods. In the light of the provisions of the Indian Contract Act, 1872, answer the following questions:

(i) *Is Govind liable to indemnify Shyam for his payment to Manohar?*

(ii) *What will be the liability of Govind if the goods is a prohibited drug? (4 Marks)*

According to section 178 of the Indian Contract Act, 1872, where a mercantile agent is, with the consent of the owner, in possession of goods or the documents of title to goods, any pledge made by him, when acting in the ordinary course of business of a mercantile agent, shall be as valid as if he were expressly authorised by the owner of the goods to make the same; provided that the pawnee acts in good faith and has not at the time of the pledge notice that the Pawnor has no authority to pledge.

It is also to be noted that:

1. The possession of goods must be with the consent of the owner. If possession has been obtained dishonestly or by a trick, a valid pledge cannot be effected.
 2. The pledgee should have no notice of the pledger's defect of title. If the pledgee knows that the pledger has a defective title, the pledge will not be valid.
- (i) In the given question, Shyam had no notice of the Govind's defect of title. He acted in ordinary course of business of a mercantile agent considering Govind as owner of the good and genuinely handed over the proceed of the sale to him. Therefore, said transaction is invalid.

Thus, Govind shall be liable to indemnify Shyam for his payment to Manohar.

- (ii) Govind shall not be liable to indemnify Shyam as selling of prohibited drugs is a prohibited act and against the public policy.

Q.4. Dec 2021 Marks 4

Due to urgent need of money amounting to ₹ 3,00,000, Pawan approached Raman and asked him for the money. Raman lent the money on the guarantee of Suraj, Tarun and Usha. Pawan makes default in payment and Suraj pays full amount to Raman. Suraj, afterwards, claimed contribution from Tarun and Usha refused to contribute on the basis that there is no contract between Suraj and him. Examine referring to the provisions of the Indian Contract Act, 1872, whether Tarun can escape from his liability. (4 Marks)

Equality of burden is the basis of Co-suretyship. This is contained in section 146 of the Indian Contract Act, 1872, which states that "when two or more persons are co-sureties for the same debt, or duty, either jointly, or severally and whether under the same or different contracts and whether with or without the knowledge of each other, the co-sureties in the absence of any contract to the contrary, are liable, as between themselves, to pay each an equal share of the whole debt, or of that part of it which remains unpaid by the principal debtor".

Accordingly, on the default of Pawan in payment, Tarun cannot escape from his liability. All the three sureties Suraj, Tarun and Usha are liable to pay equally, in absence of any contract between them.

Q.5. July 2021 Marks 4

Paul (minor) purchased a smart phone on credit from a mobile dealer on the surety given by Mr. Jack, (a major). Paul did not pay for the mobile. The mobile dealer demanded the payment from Mr. Jack because the contract entered with Paul (minor) is void. Mr. Jack argued that he is not liable to pay the amount since Paul (Principal Debtor) is not liable. Whether the argument is correct under the Indian Contract Act, 1872?

What will be your answer if Jack and Paul both are minor?

(4 Marks)

In the case of a contract of guarantee, where a minor is a principal debtor, the contract is still valid.

In the given question, the contract is a valid contract and Jack (major) shall be liable to pay the amount even if Paul (Principal debtor) is not liable (as Paul is minor).

If both Jack and Paul are minors then the agreement of guarantee is void because the surety as well as the principal debtor are incompetent to contract.

Q.6. Jan 2021 Marks 4

Satya has given his residential property on rent amounting to ₹ 25,000 per month to Tushar. Amit became the surety for payment of rent by Tushar. Subsequently, without Amit's consent, Tushar agreed to pay higher rent to Satya. After a few months of this, Tushar defaulted in paying the rent.

(i) Explain the meaning of contract of guarantee according to the provisions of the Indian Contract Act, 1872.

(ii) State the position of Amit in this regard.

(4 Marks)

- (i) **Contract of guarantee:** As per the provisions of section 126 of the Indian Contract Act, 1872, a contract of guarantee is a contract to perform the promise made or discharge the liability, of a third person in case of his default.

Three parties are involved in a contract of guarantee:

Surety- person who gives the guarantee,

Principal debtor- person in respect of whose default the guarantee is given,

Creditor- person to whom the guarantee is given

- (ii) According to the provisions of section 133 of the Indian Contract Act, 1872, where there is any variance in the terms of contract between the principal debtor and creditor without surety's consent, it would discharge the surety in respect of all transactions taking place subsequent to such variance.

In the instant case, Satya (Creditor) cannot sue Amit (Surety), because Amit is discharged from liability when, without his consent, Tushar (Principal debtor) has changed the terms of his contract with Satya (creditor). It is immaterial whether the variation is beneficial to the surety or does not materially affect the position of the surety.

Q.7. Nov 2020 Marks 2

Mr. CB was invited to guarantee an employee Mr. BD who was previously dismissed for dishonesty by the same employer. This fact was not told to Mr. CB. Later on, the employee embezzled funds. Whether CB is liable for the financial loss as surety under the provisions of the Indian Contract Act, 1872?

As per section 143 of the Indian Contract Act, 1872, any guarantee which the creditor has obtained by means of keeping silence as to material circumstances, is invalid. In the given instance, Mr. CB was invited to give guarantee of an employee Mr. BD to the same employer who previously dismissed Mr. BD for dishonesty. This fact was not told to Mr. CB. Here, keeping silence as to previous dismissal of Mr. BD for dishonesty is a material fact and if Mr. BD later embezzled the funds of the employer, Mr. CB will not be held liable for the financial loss as surety since such a contract of guarantee entered is invalid in terms of the above provisions.

Q.8. Nov 2020 Marks 2

Mr. X agreed to give a loan to Mr. Y on the security of four properties. Mr. A gave guarantee against the loan. Actually Mr. X gave a loan of smaller amount on the security of three properties. Whether Mr. A is liable as surety in case Mr. Y failed to repay the loan? (2 + 2 = 4 Marks)

- (ii) As per the provisions of section 133 of the Indian Contract Act, 1872, any variance, made without the surety's consent, in the terms of the contract between the principal [debtor] and the creditor, discharges the surety as to transactions subsequent to the variance.

In the given instance, the actual transaction was not in terms of the guarantee given by Mr. A. The loan amount as well as the securities were reduced without the knowledge of the surety.

So, accordingly, Mr. A is not liable as a surety in case Y failed to repay the loan.

Q.9. Nov 2019 Marks 4

'C' advances to 'B', ₹ 2,00,000 on the guarantee of 'A'. 'C' has also taken a further security for the same borrowing by mortgage of B's furniture worth ₹ 2,00,000 without knowledge of 'A'. C cancels the mortgage. After 6 months 'B' becomes insolvent and 'C' 'sues 'A' his guarantee. Decide the liability of 'A' if the market value of furniture is worth ₹80,000, under the Indian Contract Act, 1872. (4 Marks)

Surety's right to benefit of creditor's securities: According to section 141 of the Indian Contract Act, 1872, a surety is entitled to the benefit of every security which the creditor has against the principal debtor at the time when the contract of suretyship is entered into, whether the surety knows of the existence of such security or not; and, if the creditor loses, or, without the consent of the surety, parts with such security, the surety is discharged to the extent of the value of the security.

In the instant case, C advances to B, ₹ 2,00,000 rupees on the guarantee of A. C has also taken a further security for ₹ 2,00,000 by mortgage of B's furniture without knowledge of A. C cancels the mortgage. B becomes insolvent, and C sues A on his guarantee. A is discharged from liability to the amount of the value of the furniture i.e. ₹ 80,000 and will remain liable for balance ₹ 1,20,000.

Q.10. May 2019 Marks 4

Aarathi is the wife of Naresh. She purchased some sarees on credit from M/s Rainbow Silks, Jaipur.

M/s Rainbow Silks, Jaipur demanded the amount from Naresh. Naresh refused. M/s Rainbow Silks, Jaipur filed a suit against Naresh for the said amount. Decide in the light of provisions of the Indian Contract Act, 1872, whether M/s Rainbow Silks, Jaipur would succeed?
(4 Marks)

The situation asked in the question is based on the provisions related with the modes of creation of agency relationship under the Indian Contract Act, 1872. Agency may be created by a legal presumption; in a case of cohabitation by a married woman (i.e. wife is considered as an implied agent of her husband). If wife lives with her husband, there is a legal presumption that a wife has authority to pledge her husband's credit for necessaries. But the legal presumption can be rebutted in the following cases:

- (i) Where the goods purchased on credit are not necessaries.
- (ii) Where the wife is given sufficient money for purchasing necessaries.
- (iii) Where the wife is forbidden from purchasing anything on credit or contracting debts.
- (iv) Where the trader has been expressly warned not to give credit to his wife.

If the wife lives apart for no fault on her part, wife has authority to pledge her husband's credit for necessaries. This legal presumption can be rebutted only in cases (iii) and (iv) above.

Applying the above conditions in the given case M/s Rainbow Silks will succeed. It can recover the said amount from Naresh if sarees purchased by Aarathi are necessaries for her.

Q.11. May 2019 Marks 4

Manoj guarantees for Ranjan, a retail textile merchant, for an amount of Rs. 1,00,000, for which Sharma, the supplier may from time to time supply goods on credit basis to Ranjan during the next 3 months. After 1 month, Manoj revokes the guarantee, when Sharma had supplied goods on credit for Rs. 40,000. Referring to the provisions of the Indian Contract Act, 1872, decide whether Manoj is discharged from all the liabilities to Sharma for any subsequent credit supply. What would be your answer in case Ranjan makes default in paying back Sharma for the goods already supplied on credit i.e. Rs. 40,000 ?

- As per section 130 of the Indian Contract Act, 1872 a specific guarantee cannot be revoked by the surety if the liability has already accrued.
- The surety, may at any time, revoke a continuing guarantee as to future transactions, by notice to the creditor, but the surety remains liable for transactions already entered into.
- As per the above provisions:
 - (i) Yes, Manoj is discharged from all subsequent credit supply because it is a case of continuing guarantee.
 - (ii) Manoj is liable for payment of Rs. 40,000 to Sharma because the transaction has already completed. Sharma had supplied goods amount of Rs. 40,000 on credit.

Q.12. Nov 2018 Marks 4

Mr. Chetan was appointed as Site Manager of ABC Constructions Company on a two years contract at a monthly salary of ₹ 50,000. Mr. Pawan gave a surety in respect of Mr. Chetan's conduct. After six months the company was not in position to pay ₹ 50,000 to Mr. Chetan because of financial constraints. Chetan agreed for a lower salary of ₹ 30,000 from the company. This was not communicated to Mr. Pawan. Three months afterwards it was discovered that Chetan had been doing fraud since the time of his appointment. What is the liability of Mr. Pawan during the whole duration of Chetan's Appointment.

As per the provisions of Section 133 of the Indian Contract Act, 1872, if the creditor makes any variance (i.e. change in terms) without the consent of the surety, then surety is discharged as to the transactions subsequent to the change.

In the instant case, Mr. Pawan is liable as a surety for the loss suffered by ABC Constructions company due to misappropriation of cash by Mr. Chetan during the first six months but not for misappropriations committed after the reduction in salary.

Hence, Mr. Pawan, will be liable as a surety for the act of Mr. Chetan before the change in the terms of the contract i.e., during the first six months. Variation in the terms of the contract (as to the reduction of salary) without consent of Mr. Pawan, will discharge Mr. Pawan from all the liabilities towards the act of the Mr. Chetan after such variation.

Q.13. Nov 2017 Marks 4

A gives to C a continuing guarantee to the extent of ₹ 5,000 for the vegetables to be supplied by C to B from time to time on credit. Afterwards, B became embarrassed, and without the knowledge of A, B, and C contract that C shall continue to supply B with vegetables for ready money. and that the payments shall be applied to the then-existing debts between B and C. Examining the provision of the Indian Contract Act, 1872, decide whether A is liable on his guarantee given to C. (Nov 2008,5 marks)

OR

'A' gives to 'M' a continuing guarantee to the extent of ₹ 8,000 for the fruits to be supplied by 'M' to 'S' from time to time on credit. After wards, 'S' became embarrassed and without the knowledge of 'A', 'M', and 'S' contract that 'M' shall continue to supply 'S' with fruits for ready money and that payments shall be applied to the then existing debts between 'S' and 'M'. Examining the provision of the Indian Contract Act, 1872, decide whether 'A' is liable on his guarantee given to 'M'. (Nov 2017, 4 marks)

According to Sec. 133, where there is any variance ;n the terms of contract between the principal debtor and creditor without surety's consent it would discharge the surety in respect of all transactions taking place subsequent to such variance. On the other hand, Sec. 135 provides that, if the creditor makes a settlement with the principal debtor, the surety is discharged If the consent of surety is not obtained,

Present Case: –

Hence, in the first instance, since S and M have varied the terms of the contract, without A's consent, it has discharged A from all the transactions taking place after such variation under Sec. 133.

In the second instance, S and M have made a settlement that the further supply of vegetables will be for cash, and the payment shall be applied to the existing debts without the consent of A.

Hence, A is discharged in respect of all the transactions taking place after the variation in the terms of contract. However, A will remain liabte on his guarantee given to M for the existing debts i.e. if S is unable to settle off the debts existing before the variation, the liability of A will arise.

Q.14. Nov 2017 Marks 5

'Ramesh' and 'Suresh' were engaged in business having same nature. 'Ramesh' stands surety for 'Suresh' for any amount which 'Kamlesh' may lend to 'Suresh' from time to time during the next 6 months subject to a maximum of ₹ 85,000. 3 months later, 'Ramesh' revokes the guarantee, when 'Kamlesh' had lent to 'Suresh' ₹ 35,000. Decide whether 'Ramesh' is discharged from all the liabilities to 'Kamlesh' for any subsequent loan under the provisions of the Indian Contract Act, 1872. Would your answer differ in case 'Suresh' makes a default in paying back to 'Kamlesh' the money already borrowed i.e. ₹ 35,000?

(5 Marks)

Revocation of continuing guarantee: The problem asked in the question is based on section 130 of the Indian Contract Act, 1872 relating to the revocation of a continuing guarantee as to future transactions which can be done mainly in the following two ways:

1. **By Notice:** A continuing guarantee may at any time be revoked by the surety as to future transactions, by giving notice to the creditor.
2. **By death of surety:** The death of the surety operates, in the absence of any contract to the contrary, as a revocation of a continuing guarantee, so far as regards future transactions. (Section 131)

So far as the transactions before revocation are concerned, the liability of the surety for previous transactions (i.e. before revocation) remains.

Thus, applying the above provisions in the given case,

- 'Ramesh' is discharged from all the liabilities to 'Kamlesh' for any subsequent loan.
- Answer in the second case would differ i.e. 'Ramesh' is liable to 'Kamlesh' for ₹ 35,000 on default of 'Suresh' since the loan was taken before the notice of revocation was given to 'Kamlesh'.

Q.15. Nov 2015 Marks 5

A' stands surety for 'B for any amount which 'C' may lend to B from time to time during the next three months subject to a maximum of ₹ 50,000. One month later A revokes the guarantee, when C had lent to B ₹ 5,000. Referring to the provisions of the Indian Contract Act. 1872 decide whether 'A' is discharged from all the liabilities to 'C' for any subsequent loan. What would be your answer in case 'B' makes a default in paying back to 'C' the money already borrowed i.e. ₹ 5,000? (Nov 2002,6 marks)
OR

Ravi becomes guarantor for Ashok for the amount Which may be given to him by Nalin within six months. The maximum limit of the said amount is 1 lakh. After two months Ravi withdraws his guarantee. Upto the aime of revocation of guarantee, Nalin had given to Ashok ₹ 20,000. Referring to the provisions of the Indian Contract Act. 1872 decide:

- (i) Whether Ravi is discharged from his liabilities to Nalin for any subsequent loan.
- (ii) Whether Ravi is liable if Ashok fails to pay the amount of ₹ 20,000 to Nalin? (May 2006, 5 marks)

'Amit' stands surety for 'Etkram' for any amount which 'Chander' may lend to 'Bikram' from time to time during the next three months subject to a maximum amount of ₹ 1,00,000 (one lakh only). One month later 'Amit' revokes the surety, when Chander' had already lent to 'Bikram' ₹ 10,000 (ten thousand). Referring to the provisions of the Indian Contract Act, 1872. Decide:

- (i) Whether 'Amit' is discharged from all the liabilities to 'Chander' for any subsequent loan given to 'Bikram'?
- (ii) What would be your answer in case 'Bikram' makes a default in paying back to 'Chander' the already borrowed amount of ₹ 10,000? (Nov 2015, 5 marks)

OR

'Ramesh' and 'Suresh' are engaged in business having same nature. 'Ramesh' stands surety for Suresh' for any amount which 'Kamlesh may lend to Suresh' from time to time during the next 6 months subject to a maximum of ₹ 85,000. 3 months later, 'Ramesh' revokes the guarantee, when 'Kamlesh' had lent to 'Suresh' ₹ 35,000. Decide whether Ramesh' is discharged from all the liabilities to 'Kamlesh' for any subsequent loan under the provisions of the Indian Contract Act, 1872. Would your answer differ in case 'Suresh' makes a default in paying back to 'Kamlesh' the money already borrowed i.e. ₹ 35,000? (Nov 2017, 5 marks)

The problem as asked in the question depends on the provisions of the Indian Contract Act, 1872 as contains in Section 130. The section relates to the revocation of a continuing guarantee as to future transactions which can be done in any of the two ways:

1. By notice: By notice to the creditor, the continuing guarantee can be revoked at any time by the surety as to future transactions.

2. By death of surety: In regard to the future transaction the death of the surety operates. in the absence of any contract to the contrary, as a revocation.

The liability of the surety remains same for the previous transactions. Thus by using the above rule in the question. A is discharged from all the liabilities to C for any subsequent loan. In second case the answer will change that is A will be liable to C for ₹ 5,000 on default of B because the loan was taken before the notice of revocation was given to C.

Q.16. NOV 2023 MARKS 4

Mr. R extended a loan to Mr. D with X, Y, and Z as sureties. Each surety executed a bond with varying penalty amounts- X with a penalty of ₹ 10,000, Y with ₹ 20,000 and Z with ₹ 40,000, in the event of Mr. D's failure to repay the borrowed money to Mr. R. Examine the liabilities of the sureties in accordance with the provisions of the Indian Contract Act, 1872, when Mr. D defaults to the tune of ₹ 42,000. Additionally, assess the situation, if there is no contractual arrangement among the sureties. (4 Marks)

As per section 146 of the Indian Contract Act, 1872, when two or more persons are co-sureties for the same debt, or duty, either jointly, or severally and whether under the same or different contracts and whether with or without the knowledge of each other, the co-sureties in the absence of any contract to the contrary, are liable, as between themselves, to pay each an equal share of the whole debt, or of that part of it which remains unpaid by the principal debtor.

Section 147 provides, the principal of equal contribution is, however, subject to the maximum limit fixed by a surety to his liability. Co-sureties who are bound in different sums are liable to pay equally as far as the limits of their respective obligations permit.

In the given question, Mr. D makes a default of ₹ 42,000, and X, Y and Z as sureties have executed the bond with varying penalty amounts. Hence, X is liable to pay ₹ 10,000, and Y and Z ₹ 16,000 each.

In the given case, if there was no contractual arrangement among the sureties, they would be liable for equal contribution. Hence, X, Y and Z are liable to pay ₹ 14,000 each.

Q.17. May 2023 Marks 4

'S' guarantees 'V' for the transactions to be done between 'V' & 'B' during the month of March, 2022. 'V' supplied goods of ₹ 30,000 on 01.03.2022 and of ₹ 20,000 on 03.03.2022 to 'B'. On 05.03.2022, 'S' died in a road accident. On 10.03.2022, being ignorant of the death of 'S', 'V' further supplied goods of ₹ 40,000. On default in payment by 'B' on due date, 'V' sued on legal heirs of 'S' for recovery of ₹ 90,000. Describe, whether legal heirs of 'S' are liable to pay ₹ 90,000 under the provisions of Indian Contract Act, 1872.

What would be your answer, if the estate of 'S' is worth of ₹ 45,000 only? (4 Marks)

Revocation of continuing guarantee by surety's death (Section 131 of the Indian Contract Act, 1872): In the absence of any contract to the contrary, the death of surety operates as a revocation of a continuing guarantee as to the future transactions taking place after the death of surety. However, the surety's estate remains liable for the past transactions which have already taken place before the death of the surety.

Accordingly, in the given instance, legal heirs of S are not liable to pay ₹ 90,000 but for ₹ 50,000 as death of surety operates as a revocation of a continuing guarantee as to the future transactions, i.e., ₹ 40,000 in this case, taking place after the death of surety.

Further, surety's estate remains liable for the transactions taken place before the death of the surety. Legal heirs of surety will be obliged to perform the contract on behalf of surety to the extent of share inherited. V shall be entitled to recover ₹ 45,000 only from the estate of S.

Q.18. What are the rights of the indemnity-holder when sued?

Rights of Indemnity- holder when sued (Section 125): The promisee in a contract of indemnity, acting within the scope of his authority, is entitled to recover from the promisor— (a) all damages which he may be compelled to pay in any suit (b) all costs which he may have been compelled to pay in bringing/ defending the suit and (c) all sums which he may have paid under the terms of any compromise of suit. It may be understood that the rights contemplated under section 125 are not exhaustive. The indemnity holder/ indemnified has other rights besides those mentioned above. If he has incurred a liability and that liability is absolute, he is entitled to call upon his indemnifier to save him from the liability and to pay it off.

Q.19. Define contract of indemnity and contract of guarantee and state the conditions when guarantee is considered invalid?

Section 124 of the Indian Contract Act, 1872 states that "A contract by which one party promises to save the other from loss caused to him by the conduct of the promisor himself, or the conduct of any person", is called a "contract of indemnity". Section 126 of the Indian Contract Act, 1872 states that "A contract to perform the promise made or

discharge liability incurred by a third person in case of his default” is called a “contract of guarantee”. The conditions under which the guarantee is invalid or void is provided in section 142, 143 and 144 of the Indian Contract Act. These include: (i) Guarantee obtained by means of misrepresentation. (ii) Guarantee obtained by means of keeping silence as to material circumstances. (iii) When contract of guarantee is entered into on the condition that the creditor shall not act upon it until another person has joined in it as co-surety and that other party fails to join as such.

Q.20. Mr. X, is employed as a cashier on a monthly salary of ` 12,000 by ABC bank for a period of three years. Y gave surety for X’s good conduct. After nine months, the financial position of the bank deteriorates. Then X agrees to accept a lower salary of ` 10,500/- per month from Bank. Two months later, it was found that X has misappropriated cash since the time of his appointment. What is the liability of Y?

According to section 133 of the Indian Contract Act, 1872, where there is any variance in the terms of contract between the principal debtor and creditor without surety’s consent, it would discharge the surety in respect of all transactions taking place subsequent to such variance. In the instant case, the creditor has made variance (i.e. change in terms) without the consent of surety. Thus, surety is discharged as to the transactions subsequent to the change. Hence, Y is liable as a surety for the loss suffered by the bank due to misappropriation of cash by X during the first nine months but not for misappropriations committed after the reduction in salary.

Q.21. A contracts with B for a fixed price to construct a house for B within a stipulated time. B would supply the necessary material to be used in the construction. C guarantees A’s performance of the contract. B does not supply the material as per the agreement. Is C discharged from his liability.

According to Section 134 of the Indian Contract Act, 1872, the surety is discharged by any contract between the creditor and the principal debtor by which the principal debtor is discharged or by any act or omission for the creditor the legal consequence of which is the discharge of the principal debtor. In the given case, B omits to supply the necessary construction material. Hence, C is discharged from his liability.

Q.22. Mr. D was in urgent need of money amounting to ` 5,00,000. He asked Mr. K for the money. Mr. K lent the money on the sureties of A, B and N without any contract between them in case of default in repayment of money by D to K. D makes default in payment. B refused to contribute, examine whether B can escape liability?

Co-sureties liable to contribute equally (Section 146 of the Indian Contract act, 1872): Equality of burden is the basis of Co-suretyship. This is contained in section 146 which states that “when two or more persons are co-sureties for the same debt, or duty, either jointly, or severally and whether under the same or different contracts and whether with

or without the knowledge of each other, the co-sureties in the absence of any contract to the contrary, are liable, as between themselves, to pay each an equal share of the whole debt, or of that part of it which remains unpaid by the principal debtor". Accordingly, on the default of D in payment, B cannot escape from his liability. All the three sureties A, B and N are liable to pay equally, in absence of any contract between them.

Q.23. Mr. Chetan was appointed as Site Manager of ABC Constructions Company on a two years' contract at a monthly salary of ` 50,000. Mr. Pawan gave a surety in respect of Mr. Chetan's conduct. After six months the company was not in position to pay ` 50,000 to Mr. Chetan because of financial constraints. Chetan agreed for a lower salary of ` 30,000 from the company. This was not communicated to Mr. Pawan. Three months afterwards it was discovered that Chetan had been doing fraud since the time of his appointment. What is the liability of Mr. Pawan during the whole duration of Chetan's appointment.

As per the provisions of Section 133 of the Indian Contract Act, 1872, if the creditor makes any variance (i.e. change in terms) without the consent of the surety, then surety is discharged as to the transactions subsequent to the change. In the instant case, Mr. Pawan is liable as a surety for the loss suffered by ABC Constructions company due to misappropriation of cash by Mr. Chetan during the first six months but not for misappropriations committed after the reduction in salary. Hence, Mr. Pawan, will be liable as a surety for the act of Mr. Chetan before the change in the terms of the contract i.e., during the first six months. Variation in the terms of the contract (as to the reduction of salary) without consent of Mr. Pawan, will discharge Mr. Pawan from all the liabilities towards the act of the Mr. Chetan after such variation.

Q.24. A agrees to sell goods to B on the guarantee of C for the payment of the price of goods in default of B. Is the agreement of guarantee valid in each of the following alternate cases: Case 1. If A is a Minor Case 2: If B is a Minor Case 3: If C is a minor.

Case 1: The agreement of guarantee is void because the creditor is incompetent to contract.

Case 2: The agreement of guarantee is valid because the capability of the principal debtor does not affect the validity of the agreement of the guarantee.

Case 3: The agreement of guarantee is void because the surety is incompetent to contract.

Q.25. S asks R to beat T and promises to indemnify R against the consequences. R beats T and is fined ` 50,000. Can R claim ` 50,000 from S.

R cannot claim ` 50,000 from S because the object of the agreement was unlawful. A contract of indemnity to be valid must fulfil all the essentials of a valid contract.

Q.26. Manoj guarantees for Ranjan, a retail textile merchant, for an amount of ₹ 1,00,000, for which Sharma, the supplier may from time to time supply goods on credit basis to Ranjan during the next 3 months. After 1 month, Manoj revokes the guarantee, when Sharma had supplied goods on credit for ₹ 40,000. Referring to the provisions of the Indian Contract Act, 1872, decide whether Manoj is discharged from all the liabilities to Sharma for any subsequent credit supply. What would be your answer in case Ranjan makes default in paying back Sharma for the goods already supplied on credit i.e. ₹ 40,000?

Discharge of Surety by Revocation: As per section 130 of the Indian Contract Act, 1872, a continuing guarantee may, at any time, be revoked by the surety, as to future transactions, by notice to the creditor, but the surety remains liable for transactions already entered into. As per the above provisions, liability of Manoj is discharged with relation to all subsequent credit supplies made by Sharma after revocation of guarantee, because it is a case of continuing guarantee. However, liability of Manoj for previous transactions (before revocation) i.e. for ₹ 40,000 remains. He is liable for payment of ₹ 40,000 to Sharma because the transaction was already entered into before revocation of guarantee.

Q.27. 'C' advances to 'B', ₹ 2,00,000 on the guarantee of 'A'. 'C' has also taken a further security for the same borrowing by mortgage of B's furniture worth ₹ 2,00,000 without knowledge of 'A'. 'C' cancels the mortgage. After 6 months 'B' becomes insolvent and 'C' sues 'A' his guarantee. Decide the liability of 'A' if the market value of furniture is worth ₹ 80,000, under the Indian Contract Act, 1872.

Surety's right to benefit of creditor's securities: According to section 141 of the Indian Contract Act, 1872, a surety is entitled to the benefit of every security which the creditor has against the principal debtor at the time when the contract of suretyship is entered into, whether the surety knows of the existence of such security or not; and, if the creditor loses, or, without the consent of the surety, parts with such security, the surety is discharged to the extent of the value of the security. In the instant case, C advances to B, ₹ 2,00,000 rupees on the guarantee of A. C has also taken a further security for ₹ 2,00,000 by mortgage of B's furniture without knowledge of A. C cancels the mortgage. B becomes insolvent, and C sues A on his guarantee. A is discharged from liability to the amount of the value of the furniture i.e. ₹ 80,000 and will remain liable for balance ₹ 1,20,000.