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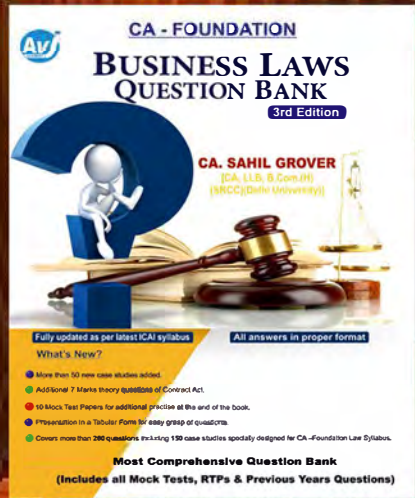


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# INDIAN REGULATORY FRAMEWORK

# INDIAN REGULATORY FRAMEWORK (Chart 1.1)

MEANING OF LAW	SOURCES OF LAW	TYPES OF LAWS IN THE INDIAN LEGAL SYSTEM
<p>- Law is a set of <b>obligations and duties imposed by the government</b> for securing welfare and providing justice to society.</p> <p>- India's legal framework reflects the social, political, economic, and cultural aspects of our vast and diversified country.</p>	<p><b>I. THE CONSTITUTION OF INDIA:</b></p> <ul style="list-style-type: none"> <li>- The Constitution of India is the <b>foremost law</b> that deals with the framework within which our democratic system works, and our laws are made for the people, by the people.</li> <li>- The constitution is the <b>basis and source for all laws</b>.</li> <li>- The Constitution also provides for and protects certain <b>Fundamental rights of citizens</b>. It also lays down <b>Fundamental duties</b> as well as the <b>powers and duties of Governments, both Central and State</b>. The laws in India are interconnected with each other forming a hybrid legal system.</li> </ul> <p><b>II. STATUTES OR LAWS MADE BY LEGISLATURE:</b></p> <ul style="list-style-type: none"> <li>- Since India is a parliamentary democracy we elect our representatives to the parliament as well as to the legislative assemblies of various States.</li> <li>- These <b>representatives of the people make laws in parliament or in their state assemblies</b> as the case may be.</li> <li>- So, <b>Parliament is the ultimate law-making body</b>. The laws passed by parliament may apply throughout all or a portion of India, whereas the laws passed by state legislatures apply only within the borders of the states concerned.</li> <li>- Constitution divides the law-making power between the <b>Central Government and the various State Governments</b>. So, the Indian Constitution has three lists Viz., <b>Central (Union) List, State List and Joint (Concurrent) List</b>.</li> <li>- Depending on the list in which it figures a matter would become the subject for Central law or a State law.</li> <li>- For example, <b>Income Tax is a Central subject</b>. So, throughout India we have only one law for Income Tax which is implemented by the Central Government through the Ministry of Finance. We also have matters for which both Central as well as State Governments can pass laws. <b>Levy of stamp duty is such an example. Public order and Police is an example of matter in State List</b>.</li> </ul> <p><b>III. PRECEDENTS OR THE JUDICIAL DECISIONS OF VARIOUS COURTS</b></p> <ul style="list-style-type: none"> <li>- Judicial precedents refer to the <b>decisions given by courts in different cases</b>.</li> <li>- A judicial decision has a legal principle that is binding on the subordinate courts. <b>Once a court has delivered a judgement on a particular case, the courts subordinate to it must abide by the precedent while deciding on similar cases with similar facts</b>.</li> <li>- The authority of judicial precedents is based on the <b>doctrine of stare decisis</b>.</li> <li>- The term 'Stare Decisis' originates from Latin. It means <b>"to abide by things decided" or "to stand by that which is decided."</b></li> <li>- The same principle has been mentioned in <b>Article 141</b> of the Constitution. As per Article 141 of the Constitution of India, the Supreme Court's decisions are binding on all the courts across the country.</li> </ul> <p style="text-align: right; font-size: small;">Compiled By:CA Sahil Grover</p> <p><b>IV. CUSTOMS AND USAGES.</b></p> <ul style="list-style-type: none"> <li>- Custom can simply be explained as those <b>long-established practices or unwritten rules which have acquired binding or obligatory character</b>.</li> <li>- In ancient societies, the custom was considered as one of the most important sources of law; In fact, it was considered as the real source of law. With the passage of time and the advent of modern civilization, the importance of custom as a source of law diminished and other sources such as judicial precedents and legislation gained importance.</li> <li>- In India, <b>laws relating to marriage and divorce are mostly developed from customs</b> followed by different religious communities. Additionally, several communities belonging to the Scheduled Tribes category have their own customs related to marriage. As a result of that Section 2(2) of the Hindu Marriage Act, 1955 has exempted Scheduled Tribes from the application of this Act.</li> </ul>	<p><b>CRIMINAL LAW</b></p> <ul style="list-style-type: none"> <li>- Criminal law is concerned with laws pertaining to violations of the <b>rule of law or public wrongs and punishment of the same</b>.</li> <li>- Criminal Law is governed under the <b>Indian Penal Code, 1860, and the Code of Criminal Procedure, 1973 (Crpc)</b>.</li> <li>- The <b>Indian Penal Code, 1860</b>, defines the crime, its nature, and punishments whereas the <b>Criminal Procedure Code, 1973, defines exhaustive procedure</b> for executing the punishments of the crimes.</li> <li>- <b>Murder, rape, theft, fraud, cheating and assault</b> are some examples of criminal offences under the law.</li> </ul> <p><b>CIVIL LAW</b></p> <ul style="list-style-type: none"> <li>- Matters of <b>disputes between individuals or organisations</b> are dealt with under Civil Law.</li> <li>- Civil courts enforce the <b>violation of certain rights and obligations</b> through the institution of a <b>civil suit</b>.</li> <li>- Civil law primarily <b>focuses on dispute resolution rather than punishment</b>.</li> <li>- The act of process and the administration of civil law are governed by the <b>Code of Civil Procedure, 1908 (CPC)</b>.</li> <li>- Civil law can be further classified <b>into Law of Contract, Family Law, Property Law, and Law of Tort</b>.</li> <li>- Some examples of civil offences are <b>breach of contract, non-delivery of goods, non-payment of dues to lender or seller, defamation, breach of contract, and disputes between landlord and tenant</b>.</li> </ul> <p><b>COMMON LAW</b></p> <ul style="list-style-type: none"> <li>- A <b>judicial precedent</b> or a <b>case law is common law</b>. A judgment delivered by the Supreme Court will be binding upon the courts within the territory of India under <b>Article 141 of the Indian Constitution</b>.</li> <li>- The <b>doctrine of Stare Decisis</b> is the principle supporting common law.</li> <li>- It is a Latin phrase that means <b>"to stand by that which is decided."</b> The doctrine of Stare Decisis reinforces the obligation of courts to follow the same principle or judgment established by previous decisions while ruling a case where the facts are similar or "on all four legs" with the earlier decision.</li> </ul> <p><b>PRINCIPLES OF NATURAL JUSTICE</b></p> <ul style="list-style-type: none"> <li>- Natural justice, often known as <b>Jus Natural</b> deals with certain fundamental principles of justice going beyond written law.</li> <li>- Rules of Natural Justice.             <ul style="list-style-type: none"> <li>• <b>Nemo judex in causa sua</b> (Literally meaning "No one should be made a judge in his own cause, and it's a Rule against Prejudice),</li> <li>• <b>audi alteram partem</b> (Literally meaning "hear the other party or give the other party a fair hearing),</li> <li>• <b>reasoned decision</b> (i.e.order which is passed affecting the rights of an individual must be a speaking order.</li> </ul> </li> </ul>
<p><b>LAW MAKING PROCESS IN INDIA</b></p>		
<ul style="list-style-type: none"> <li>- When a law is proposed in parliament it is <b>called a Bill</b>.</li> <li>- After discussion and debate, the <b>bill is passed in both the houses of parliament i.e. Lok Sabha &amp; Rajya Sabha</b>.</li> <li>- It then has to <b>obtain the assent of the President of India</b>.</li> <li>- Finally, the law will be <b>notified by the Government in the publication called the Official Gazette of India</b>.</li> <li>- The law will become <b>applicable from the date mentioned in the notification as the effective date. Once it is notified and effective, it is called an Act of Parliament</b>.</li> </ul>		
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# INDIAN REGULATORY FRAMEWORK (Chart 1.2)

## ENFORCING THE LAW

- After a law is passed in parliament it has to be enforced. Somebody should monitor whether the law is being followed. This is the job of the executive.
- Depending on whether a law is a Central law or a State law the Central or State Government will be the enforcing authority.
- For this purpose government functions are distributed to various ministries. Some of the popular ministries are the Ministry of Finance, the Ministry of Corporate Affairs, the Ministry of Home Affairs, the Ministry of Law and Justice and so on.
- These Ministries are headed by a minister and run by officers of the Indian administrative and other services.
- The Government of India exercises its executive authority through a number of Government Ministries or Departments of State. A Ministry is composed of employed officials, known as civil servants, and is politically accountable through a minister.
- Most major Ministries are headed by a Cabinet Minister, who sits in the Union Council of Ministers, and is typically supported by a team of junior ministers called the Ministers of State. For example, the Income Tax Act is implemented and enforced by the Ministry of Finance through the Central Board for Direct Taxes coming under the Department of Revenue and is administered by the officers of the Indian Revenue Service.

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## MAJOR MINISTRIES AND THE LAWS WHICH ARE ENFORCED BY THEM

THE MINISTRY OF FINANCE	MINISTRY OF CORPORATE AFFAIRS (MCA)	MINISTRY OF HOME AFFAIRS (GRHA MANTRALAYA)	MINISTRY OF LAW AND JUSTICE
<p>- The Ministry of Finance (Vitta Mantralaya) is a Ministry within the Government of India concerned with the economy of India, serving as the Treasury of India</p> <p>- In particular, it concerns itself with taxation, financial legislation, financial institutions, capital markets, centre and state finances, and the Union Budget.</p> <p>- One of the important functions of the Finance Ministry is the presentation of the Union Budget. This annual event is eagerly awaited by professionals and the common man as it provides for the rates of taxes and budget allocations for the ensuing year.</p> <p><b>Constitution of the Ministry of Finance</b> Ministry of finance is the apex controlling authority of four Central Civil Services, namely:</p> <ul style="list-style-type: none"> <li>• Indian Revenue Service</li> <li>• Indian Audit and Accounts Service</li> <li>• Indian Economic Service and</li> <li>• Indian Civil Accounts Service.</li> </ul> <p>It is also the apex controlling authority of one of the central commerce services namely Indian Cost and Management Accounts Service.</p> <p><b>Departments under the Ministry of Finance</b></p> <ul style="list-style-type: none"> <li>• Department of Economic Affairs</li> <li>• Department of Expenditure</li> <li>• Department of Revenue</li> <li>• Department of Financial Services</li> <li>• Department of Investment and Public Asset Management</li> <li>• Department of Public Enterprises</li> </ul>	<ul style="list-style-type: none"> <li>- It is an Indian Government Ministry primarily concerned with administration of the Companies Act 2013, the Companies Act 1956, the Limited Liability Partnership Act, 2008, and the Insolvency and Bankruptcy Code, 2016.</li> <li>- It is responsible mainly for the regulation of Indian enterprises in the industrial and services sector.</li> <li>- The Ministry is mostly run by civil servants of the ICLS cadre (Indian Corporate Law Services)</li> <li>- These officers are elected through the Civil Services Examination conducted by Union Public Service Commission.(UPSC)</li> <li>- The highest post, Director General of Corporate Affairs (DGCoA), is fixed at apex Scale for the ICLS.</li> </ul>	<ul style="list-style-type: none"> <li>- It is a ministry of the Government of India .As an interior ministry of India, it is mainly responsible for the maintenance of internal security and domestic policy.</li> <li>- The Home Ministry is headed by Union Minister of Home Affairs.</li> </ul> <p><b>Departments of Ministry of Home Affairs</b></p> <ul style="list-style-type: none"> <li>• Department of Border Management</li> <li>• Department of Internal Security</li> <li>• Department of Jammu, Kashmir and Ladakh Affairs</li> <li>• Department of Home</li> <li>• Department of Official Language</li> <li>• Department of States</li> </ul> <p><b>Department of Official Language</b></p> <ul style="list-style-type: none"> <li>• Central Translation Bureau</li> <li>• Central Hindi Training Institute</li> <li>• Directorate of Central Operations</li> </ul>	<ul style="list-style-type: none"> <li>- It is a Cabinet Ministry in government of India</li> <li>- It deals with the             <ul style="list-style-type: none"> <li>• management of the legal affairs, through the Legislative Department</li> <li>• legislative activities through the Department of Legal Affairs</li> <li>• administration of justice in India through the Department of Justice</li> </ul> </li> <li>- The Department of Legal Affairs is concerned with advising the various Ministries of the Central Government while the Legislative Department is concerned with drafting of principal legislation for the Central Government</li> </ul> <p><b>Departments of Ministry of Law and Justice</b></p> <ul style="list-style-type: none"> <li>• Department of Legal Affairs</li> <li>• Legislative Department</li> <li>• Department of Justice</li> </ul>

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# INDIAN REGULATORY FRAMEWORK (Chart 1.3)

## REGULATORY AUTHORITIES

### Reserve Bank of India (RBI)

- It is **India's Central Bank and regulatory body** responsible for regulation of the Indian banking system.
- It is under the **ownership (administrative domain) of Ministry of Finance, Government of India.**
- It is responsible for the **control, issue and maintaining supply of the Indian rupee.**
- It also manages the country's main payment systems and works to promote its economic development.
- **Bharatiya Reserve Bank Note Mudran (BRBNM)** is a specialized division of RBI through which it prints and mints Indian currency notes (INR) in two of its **currency printing presses** located in **Nashik (Western India) and Dewas (Central India).**
- RBI established the **National Payments Corporation of India** as one of its specialized division to **regulate the payment and settlement systems in India.**
- **Deposit Insurance and Credit Guarantee Corporation** was established by RBI as one of its **specialized division for the purpose of providing insurance of deposits and guaranteeing of credit facilities to all Indian banks.**

### The Securities and Exchange Board of India (SEBI)

- It is the **regulatory body for securities and commodity market in India under the ownership (administrative domain) of Ministry of Finance within the Government of India.**
- It was **established on 12 April, 1988** as an executive body and was **given statutory powers on 30 January, 1992 through the SEBI Act, 1992.**
- The basic functions of the Securities and Exchange Board of India is to **protect the interests of investors in securities** and to **promote the development of, and to regulate the securities market** and for matters connected there with or incidental there to.

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### Insolvency and Bankruptcy Board of India (IBBI)

- It is the **regulator for overseeing insolvency proceedings and entities like Insolvency Professional Agencies (IPA), Insolvency Professionals (IP) and Information Utilities (IU) in India.**
- It was **established on 1 October 2016** and **given statutory powers through the Insolvency and Bankruptcy Code, which was passed by Lok Sabha on 5th May 2016.**
- It covers **Individuals, Companies, Limited Liability, Partnerships and Partnership firms.**
- The new code will **speed up the resolution process** for stressed assets in the country.
- It **attempts to simplify the process of insolvency and bankruptcy proceedings.**
- It handles the cases using **two tribunals like NCLT (National company law tribunal) and Debt recovery tribunal.**

## STRUCTURE OF THE INDIAN JUDICIAL SYSTEM

- When there is a dispute between citizens or between citizens and the Government, these disputes are resolved by the judiciary.
- **The functions of judiciary system of India are:**
  - Regulation of the interpretation of the Acts and Codes,
  - Dispute Resolution,
  - Promotion of fairness among the citizens of the land.
- **In the hierarchy of courts, the Supreme Court is at the top, followed by the High Courts and District Courts.**

### SUPREME COURT

- The Supreme Court is the **apex body of the judiciary.** It was established on **26th January, 1950.** The Chief Justice of India is the highest authority appointed under Article 126.
- The principal bench of the Supreme Court consists of seven members including the Chief Justice of India.
- Presently, the **number has increased to 34** including the Chief Justice of India due to the rise in the number of cases and workload.
- An individual can seek relief in the Supreme Court by filing a writ petition under Article 32.
- **Decisions of the Supreme Court are binding on all High Courts** under Article 141 of the Indian Constitution. In fact, a Supreme Court decision is the final word on the matter

### HIGH COURT

- The **highest court of appeal in each state and union territory** is the High Court.
- **Article 214** of the Indian Constitution states that **there must be a High Court in each state.** The High Court has appellant, original jurisdiction, and Supervisory jurisdiction. However, Article 227 of the Indian Constitution limits a High Court's supervisory power.
- In India, there are **25 High Courts**, one for each state and union territory. **Many states & UT** share a single High Court.
- An individual can seek remedies against violation of fundamental rights in High Court by filing a **writ under Article 226.**
- Decisions of a High Court are binding in the respective state but are only persuasive in other states.

### DISTRICT COURT

- Below the High Courts are the **District Courts.** The Courts of District Judge deal with **Civil law matters i.e. contractual disputes and claims for damages etc.,** The **Courts of Sessions** deals with Criminal matters.
- Under pecuniary jurisdiction, a civil judge can try suits valuing not more than Rupees 2 crore.
- Jurisdiction means the power to control. Courts get territorial Jurisdiction based on the areas covered by them. Cases are decided based on the local limits within which the parties reside or the property under dispute is situated

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### METROPOLITAN COURTS

- Metropolitan courts are established in metropolitan cities in consultation with the High Court where the population is **10 lakh or more.**
- **Chief Metropolitan Magistrate** has powers as **Chief Judicial Magistrate** and **Metropolitan Magistrate** has powers as **the Court of a Magistrate of the first class.**

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# CA SANCHIT GROVER

**THE INDIAN CONTRACT  
ACT, 1872**

# THE INDIAN CONTRACT ACT, 1872 (Chart 1.1)

## INTRODUCTION

- This Act extends to the **whole of India** except the State of J&K
- Came into force on the **1st Sep 1872**.
- The scheme of the Act may be divided into two main groups:
  - **General principles of the law of contract** (Secs. 1-75).
  - **Specific kinds of contracts, viz:**
    - o **Contracts of Indemnity and Guarantee** (Secs. 124-147).
    - o **Contracts of Bailment and Pledge** (Secs. 148-181).
    - o **Contracts of Agency** (Secs. 182-238).
- Before 1930 the Act also contained provisions relating to contracts of sale of goods and partnership. Sections 76- 123 (Chapter VII) relating to sale of goods were repealed in 1930 and a separate Act called the **Sale of Goods Act** was enacted.
- Similarly, Sections 239-266(Chapter XI) relating to partnership were repealed in 1932 when the **Indian Partnership Act** was passed.

## DEFINITION OF CONTRACT

• According to **Section 2(h)** of the Indian Contract Act: **"An agreement enforceable by law is a contract."** From the above definition, we find that a contract essentially consists of two elements:

- An agreement,
- and
- Legal obligation i.e. a duty enforceable by law.(Enforceability by law)

### AGREEMENT

As per **Section 2(e)**: **"Every promise and every set of promises, forming the consideration for each other, is an agreement."** Thus it is clear from this definition that a 'promise' is an agreement.

#### OFFER+ ACCEPTANCE = PROMISE

**OFFER (PROPOSAL):** 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. [Sec 2(a)].

**ACCEPTANCE:** 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.** [Sec 2(b)]

On analysing the above definition the following characteristics of an agreement become evident:

1. **Plurality of persons.** There must be two or more persons to make an agreement because one person cannot enter into an agreement with himself.
2. **Consensus-ad-idem.** Both the parties to an agreement must agree about the subject-matter of the agreement in the same sense and at the same time

### ENFORCEABILITY BY LAW

**According to Section 10**, all agreements are contracts if they are made by the free consent of the parties, competent to contract, for a lawful consideration with a lawful object, are not expressly declared by the Act to be void.

#### As Given By Section 10

1. Agreement
2. Free consent
3. Competency of the parties
4. Lawful consideration
5. Legal object

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#### Not Given By Section 10 But Are Also Considered Essential

1. Two parties
2. **Intention to create legal relationship**
3. **Fulfilment of legal formalities (Writing & registration)**
4. **Certainty of meaning(Sec 29)**
5. **Possibility of performance(Sec 56)**

### All contracts are agreements but all agreements are not contracts."

- Agreements of **moral, religious or social nature** e.g. a promise to lunch together at a friend's house or to take a walk together **are not contracts** because they are **not likely to create a duty enforceable by law** for the simple reason that the parties never intended that they should be attended by legal consequences.
- In **business agreements the presumption is usually that the parties intend to create legal relations.**
- Thus the Act restricts the use of the word 'contract' to only those agreements which give rise to legal obligations between the parties.
- The **law of contract deals only with such legal obligations which spring from agreements. Obligations which are not contractual in nature are outside the purview of the law of contract.** For example, obligation to maintain wife and children (status obligation), obligation to observe the laws of the land, and obligation to comply with the orders of a court of law do not fall within the scope of the Contract Act
- **Salmond** has rightly observed: **"The law of contracts is not the whole law of agreements, nor is it the whole law of obligations. It is the law of those agreements which create obligations, and those obligations, which have their source in agreements".**

### Intention to Create Legal Relationship

- There must be an **intention among the parties** that the agreement should be attended by legal consequences and create legal obligations.
- **Agreements of a social or domestic nature do not contemplate legal relations** and as such they do not give rise to a contract. An agreement to dine at a friend's house is not an agreement intended to create legal relations and therefore is not a contract. Agreements between husband and wife also lack the intention to create legal relationship and thus do not result in contracts.
- **Leading Case Law-Balfour Vs. Balfour**
- **In commercial agreements an intention to create legal relations is presumed.**
- But if the parties have expressly declared their resolve that the agreement is not to create legal obligation, even a business agreement does not amount to a contract.

### Writing and registration.

- According to the Indian Contract Act, a contract may **be oral or in writing.**
- But in **certain special cases** it lays down that the agreement, to be valid **must be in writing or/and registered.**
- For example, it requires that an **agreement to pay a time barred debt** must be in writing and an **agreement to make a gift for natural love and affection** must be in writing and registered (Sec. 25).

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TYPES OF CONTRACTS

VALIDITY/ENFORCEABILITY	FORMATION	PERFORMANCE
<p><b>1. Valid contract:</b> An agreement enforceable by law. An agreement becomes enforceable by law when all the essential elements of a valid contract as enumerated above are present.</p> <p><b>2. Voidable contract:</b> An agreement which is enforceable by law at the option of one or more of the parties thereto but not at the option of the other or others, is a voidable contract. [Sec 2(i)] Usually a contract becomes voidable when the consent of one of the parties to the contract is obtained by coercion, undue influence, misrepresentation or fraud. Such a contract is voidable at the option of the aggrieved party i.e., the party whose consent was so caused (Secs 19 and 19A).</p> <p><b>3. Void contract</b> A contract which ceases to be enforceable by law becomes void when it ceases to be enforceable. [Sec 2(j)]. A void contract is not void from its inception and that it is valid &amp; binding on the parties when originally entered but subsequent to its formation it becomes invalid and destitute of legal effect because of certain reasons like:</p> <ul style="list-style-type: none"> <li>- Supervening impossibility</li> <li>- Supervening illegality.</li> </ul> <p><b>4. Void agreement.</b> An agreement not enforceable by law is said to be void" [Sec. 2 (g)]. A void agreement does not give rise to any legal consequences and is void ab-initio. In the eye of law such an agreement is no agreement at all from its very inception.</p> <p><b>5. Unenforceable contract:</b> Contract is one which is valid in itself but is not capable of being enforced in a court of law because of some technical defect such as absence of writing, registration requisite stamp, etc or time barred by the law of limitation.</p> <p><b>6. Illegal or unlawful agreements:</b> Those that are forbidden by law &amp; are hence void. Because of the illegality of their nature they cannot be enforced by any court of law</p>	<p><b>1. Express Contracts</b> A contract would be an express contract if the terms are expressed by words or in writing. Section 9 provides that if a proposal or acceptance of any promise is made in words the promise is said to be express.</p> <p><b>2. Implied Contracts:</b> Implied contracts in contrast come into existence by implication. Most often the implication is by law and or by action. Section 9 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.</p> <p><b>3. Tacit Contracts:</b> Tacit contracts are those that are inferred through the conduct of parties. A classic example of tacit contract would be when cash is withdrawn by a customer of a bank from the automatic teller machine [ATM].</p> <p><b>4. E-Contracts:</b> When a contract is entered into by two or more parties using electronics means, such as e-mails is known as e-commerce contracts. In electronic commerce, different parties/persons create networks which are linked to other networks through EDI - Electronic Data Inter change. These are known as EDI contracts or Cyber contracts or mouse click contracts.</p> <p><b>5. Quasi-Contract:</b> A quasi-contract is not an actual contract but it resembles a contract. It is created by law under certain circumstances.</p>	<p><b>1. Executed Contract:</b> A contract is said to be executed when both the parties to a contract have, completely performed their share of obligation and nothing remains to be done by either party under the contract.</p> <p><b>2. Executory Contract:</b> In an executory contract the consideration is reciprocal promise or obligation. Such consideration is to be performed in future only and therefore these contracts are described as executory contracts.</p> <p><u>Unilateral or Bilateral are kinds of Executory Contracts and are not separate kinds.</u></p> <p><b>1. Unilateral Contract:</b> Unilateral contract is a one sided contract in which only one party has to perform his duty or obligation.</p> <p><b>2. Bilateral Contract:</b> A Bilateral contract is one where the obligation or promise is outstanding on the part of both the parties.</p>

S.No	Basis	Void Contract	Voidable Contract
1	Meaning	A Contract ceases to be enforceable by law becomes void when it ceases to be enforceable.	An agreement which is enforceable by law at the option of one or more of the parties thereto, but not at the option of the other or others, is a voidable contract.
2	Cause	A contract becomes void due to in law or change in circumstances beyond the contemplation of parties.	A contract becomes a voidable contract if the consent of a party was not free.
3	Performance of contract	A void contract cannot be performed.	If the aggrieved party does not, within reasonable time, exercise his right to avoid the contract, any party can sue the other for claiming the performance of the contract.
4	Rights	A void contract does not grant any right to any party.	The party whose consent was not free has the right to rescind the contract.

Basis of differences	Agreement	Contract
Meaning	Every promise and every set of promises, forming the consideration for each other. Offer + Acceptance	Agreement enforceable by law. Agreement + Legal enforceability
Scope	It's a wider term including both legal and social agreement	It is used in a narrow sense with the specification that contract is only legally enforceable agreement.
Legal obligation	It may not create legal obligation. An agreement does not always grant rights to the parties	Necessarily creates a legal obligation. A contract always grants certain rights to every party.
Nature	All agreement are not contracts.	All contracts are agreements

OFFER / PROPOSAL

LAPSE AND REVOCATION OF OFFER

DEFIITION [Sec 2(a)]

CLASSIFICATION OF OFFER

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.

The person making the 'proposal' or 'offer' is called the 'promisor' or 'offeror', the person to whom the offer is made is called the 'offeree' and the person accepting the offer is called the 'promisee' or 'acceptor'. [Sec 2(c)]

- 1. General offer:**  
It is an offer made to public at large with or without any time limit. In terms of Section 8 of the Act, anyone performing the conditions of the offer can be considered to have accepted the offer (*Carlill v. Carbolic Smoke Ball Co*). Until the general offer is retracted or withdrawn, it can be accepted by anyone at any time as it is a continuing offer.
- 2. Special/specific offer:**  
Where an offer is made to a particular and specified person, it is a specific offer. Only that person can accept such specific offer, as it is special and exclusive to him. [*Boulton v. Jones*]
- 3. Cross offer:**  
When two parties make identical offers to each other, in ignorance of each other's offer, the offers are 'cross-offers'. 'Cross-offers' do not constitute acceptance of one's offer by the other and as such there is no completed agreement.
- 4. Counter offer:**  
Upon receipt of an offer from an offeror, if the offeree instead of accepting it straightway, imposes conditions which have the effect of modifying or varying the offer, he is said to have made a counter offer. Counter offers amounts to rejection of original offer.
- 5. Standing or continuing or open offer:**  
An offer which is made to public at large and if it is kept open for public acceptance for a certain period of time, it is known as standing or continuing or open offer. Example: Tenders that are invited for supply of materials and goods.

- 1. An offer lapses after stipulated or reasonable time:**  
An offer lapses if acceptance is not communicated within the time prescribed in the offer, or if no time is prescribed, within a reasonable time [Sec.6(2)].
- 2. An offer lapses by not being accepted in the mode prescribed, or if no mode is prescribed, in some usual and reasonable manner:** If the offeree does not accept the offer according to the mode prescribed, the offer does not lapse automatically. It is for the offeror to insist that his proposal shall be accepted only in the prescribed manner and if he fails to do so he is deemed to have accepted the acceptance. [Sec 7]
- 3. An offer lapses by rejection:** An offer lapses if it has been rejected by the offeree. The rejection may be express i.e. by words spoken or written or implied. Implied rejection is one where either the offeree makes a counter offer, or where the offeree gives a conditional acceptance. A rejection is effective only when it comes to the knowledge of the offeror
- 4. An offer lapses by the death or insanity of the offeror or the offeree before acceptance:** Death or insanity of the offeror would not put an end to the offer until it comes to the notice of the acceptor before acceptance. An offeree's death or insanity before accepting the offer puts an end to the offer and his heirs cannot accept for him
- 5. An offer lapses by revocation:** An offer may be revoked at any time before acceptance by the communication of notice of revocation by the offeror to the other party [Sec. 6(1)]. Revocation must always be express and must be communicated by the offeror himself or his duly authorised agent to the other party.
- 6. Revocation by non-fulfilment of a condition precedent to acceptance:** An offer stands revoked if the offeree fails to fulfil a condition precedent to acceptance [Sec 6(3)]. Thus, where A, offers to sell his scooter to B, for Rs 4,000, if B joins the Lions Club within a week, the offer stands revoked and cannot be accepted by B, if B fails to join the Lions Club.
- 7. An offer lapses by subsequent illegality or destruction of subject matter:** An offer lapses if it becomes illegal after it is made, and before it is accepted. In the same manner, an offer may lapse if the thing, which is the subject matter of the offer, is destroyed or substantially impaired before acceptance.

LEGAL RULES REGARDING A VALID OFFER

- 1. An offer may be 'express' or 'implied'**
- 2. An offer must contemplate to give rise to legal consequences and be capable of creating legal relations:**  
If the offer does not intend to give rise to legal consequences, it is not a valid offer in the eye of law.
- 3. The terms of the offer must be certain and not loose or vague:** If the terms of the offer are not definite and certain, it does not amount to a lawful offer.
- 4. An invitation to offer is not an offer:** In the case of an 'invitation to receive offer' he person sending out the invitation does not make an offer but only invites the other party to make an offer His object is merely to circulate information that he is willing to deal with anybody who ,on such information, is willing to open negotiations with him. Such invitations for offers are therefore not offers in the eye of law and do not become agreements by their acceptance.  
**Leading Case Laws:** *Pharmaceutical Society of Great Britain v Boots Cash Chemists Ltd. Harvey vs. Facie:* It was held that the mere statement of the lowest price at which the vendor would sell contained no implied contract to sell to the person who had enquired about the price  
**Examples of invitation to offer to buy or sell:**
  - An invitation by a company to the public to subscribe for its shares.
  - Display of goods for sale in shop windows.
  - Advertising auction sales and
  - Quotation of prices

- 5. An offer may be 'specific' or 'general'.**
- 6. An offer must be communicated to the offeree:** An offer is effective only when it is communicated to the offeree. Until the offer is made known to the offeree, there can be no acceptance and no contract. Doing anything in ignorance of the offer can never be treated as its acceptance. **Leading Case law: Lalman Shukla Vs Gauri Datt**
- 7. An offer should not contain a term the non-compliance of which would amount to acceptance:** An offeror cannot say that if acceptance is not communicated up to a certain date, the offer would be presumed to have been accepted. If the offeree does not reply, there is no contract, because no obligation to reply can be imposed on him, on the grounds of justice.
- 8. Two identical cross-offers do not make a contract**

Basis	Offer	Invitation to offer
<b>Meaning</b>	Where a person shows his readiness to enter into a contract, it is called as an offer.	Where a person invites others to make an offer to him, it is called as an invitation to offer.
<b>Intention of the parties</b>	If a person who makes the statement has the intention to be bound by it as soon as the other accepts, he is making an offer.	If a person has the intention of negotiating on terms it is called invitation to offer
<b>Sequence</b>	An offer cannot be an act precedent to invitation to offer	An invitation to offer is always an act precedent to offer

ACCEPTANCE

COMMUNICATION OF OFFER, ACCEPTANCE & REVOCATION

**DEFIITION [Sec 2(b)]**  
 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'

RELATIONSHIP BETWEEN OFFER AND ACCEPTANCE

- According to **Sir William Anson** "Acceptance is to offer what a lighted match is to a train of gun powder".
- The effect of this observation is that **what acceptance triggers cannot be recalled or undone**. But there is a choice to the person who had the train to remove it before the match is applied. **It in effect means that the offer can be withdrawn just before it is accepted**. Acceptance converts the offer into a promise and then it is too late to revoke it. This means as soon as the train of gun powder is lighted it would explode. **Train of Gun powder [offer] in itself is inert, but it is the lighted match [the acceptance] which causes the gun powder to explode.**
- The significance of this is **an offer in itself cannot create any legal relationship but it is the acceptance by the offeree which creates a legal relationship. Once an offer is accepted it becomes a promise and cannot be withdrawn or revoked**. An offer remains an offer so long as it is not accepted but becomes a contract as soon as it is accepted.

1. **Communication of an offer:** The communication of an offer is complete when it comes to the knowledge of the person to whom it is made i.e., when the letter containing the offer reaches the offeree.(or when he reads the letter).
2. **Communication of an acceptance:** The communication of an acceptance has two aspects, viz., **as against the proposer and as against the acceptor**. 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. And
  - b) **as against the acceptor;** when it **comes to the knowledge of the proposer** i.e., when the letter of acceptance is received by the proposer.
3. **Communication of a revocation:** The communication of a revocation is complete:
  - a) **as against the person who makes it, when it is put into a course of transmission** to the person to whom it is made so as to be out of the power of the person revoking, i.e., when the letter of revocation is posted. And
  - b) **as against the person to whom it is made, when it comes to his knowledge,** i.e., when the letter of revocation is received by him.

LEGAL RULES REGARDING A VALID ACCEPTANCE

Time during which an offer or acceptance can be revoked.

1. **Acceptance must be given only by the person to whom the offer is made:** An offer made to a particular person can be validly accepted by him alone. Similarly an offer made to a class of persons (i.e. teachers) can be accepted by any member of that class. An offer made to the world at large can be accepted by any person who has knowledge of the existence of the offer.  
**Leading Case Law:** Boulton vs Jones.
2. **Acceptance must be absolute and unqualified:** In order to be legally effective it must be an absolute and unqualified acceptance of all the terms of the offer. **Even the slightest deviation from the terms of the offer makes the acceptance invalid. In effect a deviated acceptance is regarded as a counter offer in law.**
3. **Acceptance must be expressed in some usual and reasonable manner, unless the proposal prescribes the manner in which it is to be accepted [Sec. 7(2)]:** If the offeror prescribes no mode of acceptance, the acceptance must be communicated according to some usual and reasonable mode. If the offeror prescribes a mode of acceptance, the acceptance given accordingly will no doubt be a valid acceptance, even if the prescribed mode is funny. **Acc to Sec 7(2) in cases of deviated acceptances "the proposer may within a reasonable time after the acceptance is communicated to him, insist that his proposal shall be accepted in the prescribed manner and not otherwise; but if he fails to do so, he accepts the (deviated) acceptance.**
4. **Mere silence is not acceptance:** Law does not allow an offeror to prescribe 'silence' as the mode of acceptance. Thus, a person cannot say that if within a certain time acceptance is not communicated the offer would be considered as accepted.

**Section 5** provides "A proposal may be revoked at any time before the communication of its acceptance is complete as against the proposer, but not afterwards. An acceptance may be revoked at any time before the communication of the acceptance is complete as against the acceptor but not afterwards."

- To revoke an offer, the letter of revocation of offer must reach the offeree before he posts his acceptance.
- To revoke an acceptance, the letter of revocation should reach the offeror before the letter of acceptance reaches him.

Effect of delay or loss of letter of acceptance in postal transit.

- So far as the **offeror** is concerned, he **is bound by the acceptance the moment the letter of acceptance is posted**, although the letter is delayed or wholly lost through an accident of the post and the letter never in fact reaches him.
- But in order to bind the offeror, the **letter of acceptance must be correctly addressed, properly stamped and clearly posted.**
- So far as **the acceptor** is concerned, he **is not bound by the letter of acceptance till it reaches the offeror**. Thus the acceptor is at an advantage if the letter is delayed or lost in transit as the contract remains voidable at his option.

Accidental formation of contract

If the **letter of acceptance** and the **telegram of revocation of acceptance** are **delivered to the offeror at the same time**, in such situation the formation of contract will depend on a **matter of chance**. If the offeror **reads the letter of acceptance first** and then the telegram, a **binding contract will arise**. But if the offeror reads the telegram of revocation of acceptance first, there will be no binding contract because the communication of revocation comes to the offeror's notice first.

CONTRACTS OVER THE TELEPHONE

- When the parties negotiate a contract over telephone, **no question of revocation can possibly arise, for in such instantaneous communication, a definite offer is made and accepted at one and the same time.**
- **If the acceptance is not in fact communicated to the offeror because the telephone suddenly goes 'dead', there will be no contract.** The offeree, therefore, must make sure that his acceptance is received (heard and understood) by the offeror, otherwise there is no binding contract.

# THE INDIAN CONTRACT ACT, 1872 (Chart 1.5) -- CONSIDERATION

CONSIDERATION		DOCTRINE OF PRIVY OF CONTRACT	
MEANING	DEFINITION [Sec 2(d)]	<p>-The doctrine says that <b>only parties to a contract can enforce the contract. The parties stranger to a contract cannot sue and be sued.</b></p> <p>-Thus there is a <b>difference between a third party to consideration and third party to a contract; while the first can sue, the second cannot sue.</b></p> <p><b>Leading Case:</b> Dunlop Pneumatic Tyre Co. v Selfridge and Co.</p>	EXCEPTIONS TO RULE OF PRIVY OF CONTRACT
<ul style="list-style-type: none"> <li>• The <b>price paid by one party for the promise of the other.</b></li> <li>• An agreement is legally enforceable only when each of the parties to it <b>gives something and gets something.</b>(Quid pro quo) The something given or obtained is the price for the promise and is called 'consideration'.</li> <li>• <b>Subject to certain exceptions, gratuitous promises are not enforceable at law.</b></li> </ul>	<ul style="list-style-type: none"> <li>- When at the desire of the promisor,</li> <li>- the promisee or any other person</li> <li>- has done or abstained from doing or</li> <li>- does or abstains from doing or</li> <li>- promises to do or to abstain from doing something</li> <li>- such act or abstinence or promise is called a consideration for the promise.</li> </ul>	<ol style="list-style-type: none"> <li>1. In the case of <b>a trust</b>, the beneficiary can sue enforcing his right though he was not a party to the contract between the trustee and the settler.</li> <li>2. In the case of <b>family settlement</b>, if the terms of settlement are reduced in writing, members of the family who were not a party to the settlement can (also) enforce their claim.</li> <li>3. In the case of <b>certain marriage contracts</b> a female member can enforce a provision for marriage expense based on a petition made by the Hindu undivided family.</li> <li>4. Where there is an <b>assignment of a contract</b>, the assignee can enforce the contract for various benefits that would accrue to him on account of the assignment</li> <li>5. <b>Acknowledgement or estoppel</b> – 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</li> <li>6. In the case of <b>covenant running with the land</b>, 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</li> <li>7. <b>Contracts entered into through an agent:</b> 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</li> </ol>	
LEGAL REQUIREMENTS REGARDING A VALID CONSIDERATION			
<ol style="list-style-type: none"> <li>1. <b>Consideration must move at the desire of the promisor:</b> Acts done or services rendered voluntarily or at the desire of third party will not amount to valid consideration so as to support a contract. <b>Leading Case: Durga Prasad vs Baldeo</b> <b>Need not be for benefit of promisor:</b> This essential does not require that the consideration must confer 'some benefit' on the promisor. It would be enough if the act or forbearance or promise constituting the consideration was done or given at the promisor's request, the benefit may accrue to a third party.</li> <li>2. <b>Consideration may move from the promisee or any other person:</b> As long as there is a consideration for a promise, it is immaterial who has furnished it. It may move from the promisee or from any other person. This means that even a stranger to the consideration can sue on a contract provided he is a party to the contract. This is sometimes called as 'Doctrine of Constructive Consideration'. <b>Leading Case: Chinayya vs Ramayya</b></li> <li>3. <b>Consideration may consist of an act or abstinence.</b> Consideration may consist of either a positive act or abstinence i.e. a negative act.</li> <li>4. <b>Consideration may be past, present or future.</b> <ul style="list-style-type: none"> <li>• <b>Past consideration:</b> When something is done or suffered before the date of the agreement, at the desire of the promisor; it is called 'past consideration'</li> <li>• <b>Present consideration:</b> Consideration which moves simultaneously with the promise, is called 'present consideration' or 'executed consideration'.</li> <li>• <b>Future consideration.</b> When the consideration is to move at a future date, it is called 'future consideration' or 'executory consideration'</li> </ul> </li> </ol>	<ol style="list-style-type: none"> <li>5. <b>Executed and Executory consideration:</b> Where consideration consists of performance, it is called "executed" consideration. Where it consists only of a promise, it is executory.</li> <li>6. <b>Consideration must be 'something of value' but need not be 'adequate':</b> Law leaves the people free to make their own bargains. <b>Inadequacy of consideration is no bar to a valid contract unless it is an evidence of unfree consent.</b> If consideration is shockingly less and the other party alleges that his consent was not free than this inadequate consideration can be taken as an evidence in support of this allegation. <b>"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."</b> (Explanation 2 to Section 25).</li> <li>7. <b>Consideration must not be performance of something which one is legally bound to perform:</b> Consideration must not be performance of existing duty. <b>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.</b></li> <li>8. <b>Consideration must be real and not illusory:</b> Where consideration is physically impossible, illegal, uncertain or illusory, it is not real and therefore shall not be a valid consideration.</li> <li>9. <b>Consideration must not be unlawful, immoral, or opposed to public policy.</b> 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.</li> </ol>		
EXCEPTIONS TO THE RULE, "NO CONSIDERATION, NO CONTRACT"			
	<ol style="list-style-type: none"> <li>1. <b>Agreement made on account of natural love and affection [Sec. 25(1)]:</b> An agreement made without consideration is enforceable if it is <b>expressed in writing, and registered under the law</b> for the time being in force for the registration of documents, is made on account of natural love and affection, between parties standing in a near relation to each other <b>Leading Case:</b> Rajlaxhi Devi vs Bhootnaath</li> <li>2. <b>Agreement to compensate for past voluntary service [Sec.25(2)]:</b> A promise made without consideration is also valid, if it is a promise to compensate, wholly or in part, a person who has already voluntarily done something for the promisor or done something which the promisor was legally compellable to do. <b>The following essential factors must exist:</b> <ol style="list-style-type: none"> <li>i. The services should have been rendered voluntarily.</li> <li>ii. The services must have been rendered for the promisor.</li> <li>iii. The promisor must be in existence at the time when services were rendered.</li> <li>iv. The promisor must have intended to compensate the promisee.</li> </ol> <p>In order to attract this exception, it should be noted that the <b>promise must be to compensate a person who has himself done something for the promisor and not to a person who has done nothing for the promisor.</b></p> </li> <li>3. <b>Completed gift:</b> As between the donor and the donee, any gift actually made will be valid and binding even though without consideration"</li> </ol>	<ol style="list-style-type: none"> <li>4. <b>Agreement to pay a time-barred debt [Sec. 25(3)]:</b> Where there is an agreement, made in writing and signed by the debtor or by his authorised agent to pay wholly or in part a debt barred by the law of limitation, the agreement is valid even though it is not supported by any consideration. Before the exception can apply, <b>it is necessary that:</b> <ul style="list-style-type: none"> <li>• the debt must be such of which the creditor might have enforced payment but for the law for the limitation of suits</li> <li>• the promisor himself must be liable for the debt.</li> <li>• there must be an 'express promise to pay' a time barred debt as distinguished from a mere 'acknowledgment of a liability' in respect of a debt</li> <li>• the promise must be in writing and signed by the debtor or his agent. An oral promise to pay a time-barred debt is unenforceable.</li> </ul> </li> <li>5. <b>Contract of agency:</b> Section 185 of the Contract Act lays down that no consideration is necessary to create an agency.</li> <li>6. <b>Remission by the promisee, of performance of the promise (Sec. 63):</b> For compromising a due debt, i.e. agreeing to accept less than what is due, no consideration is necessary. Similarly, an agreement to <b>extend time for performance of a contract</b> need not be supported by consideration.</li> <li>7. <b>Contribution to charity:</b> A promise to contribute to charity, though gratuitous, would be enforceable, <b>if on the faith of promised subscription, the promisee takes definite steps in furtherance of the object and undertakes a liability, to the extent of liability incurred, not exceeding the promised amount of subscription.</b> But where the <b>promisee had done nothing</b> on the faith of the promise, <b>a promised subscription is not legally recoverable.</b></li> </ol>	



An essential ingredient of a valid contract is that the contracting parties must be 'competent to contract' (Sec. 10). Section 11 lays down that "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."

Thus the Section declares that a person is incompetent to contract under the following circumstances:

Compiled By:CA Sahil Grover

1. MINOR

Acc. to Sect 3 of the Majority Act, 1875, amended by the Majority (Amendment) Act. 1999, a person, domiciled in India, who is under 18 years of age is a minor.

LAW REGARDING MINOR'S AGREEMENTS

1. Agreement by a minor is absolutely void and inoperative as against him

Leading case: Mohori Bibi vs Dharmodos Ghosh

2. Beneficial agreements are valid contracts: Any agreement which is of some benefit to the minor and under which he is required to bear no obligation, is valid. In other words, a minor can be a beneficiary e.g., a payee, an endorsee or a promisee under a contract. Any money advanced by a minor can be recovered by him by a suit because he can take benefit under a contract.

3. No ratification on attaining the age of majority: Ratification means the subsequent adoption and acceptance of an act or agreement. A minor's agreement being a nullity and void- ab-initio has no existence in the eye of law. It cannot be ratified by the minor on attaining the age of majority.

4. Rule of estoppel does not apply to a minor: A minor is not estopped from pleading his infancy in order to avoid a contract, even if he has entered into an agreement by falsely representing that he was of full age. In other words, where an infant represents fraudulently or otherwise that he is of full age and thereby induces another to enter into a contract with him, then in an action founded on the contract, the infant is not estopped from setting up infancy.

5. No specific performance: A minor's agreement being absolutely void, there can be no question of the specific performance of such agreement.

6. Minor's liability for necessities:

- Sec 68 provides that "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 necessities 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."

- But a minor is not personally liable; it is his property only which is liable. If a minor owns no property, the supplier will lose the price of necessities.

- Where a minor owns property, the supplier will get a reasonable price & not price agreed to by minor.

- "What is a necessary article," is to be determined with reference to the status and circumstances of the particular minor. ( goods reasonably necessary for his support in the situation in life)

7. Partnership: A minor being incompetent to contract cannot be a partner in a partnership firm, but under Section 30 of the Indian Partnership Act, he can be admitted to the benefits of partnership with the consent of all the partners.

8. No insolvency: A minor cannot be declared insolvent as he is incapable of contracting debts and dues are payable from the personal properties of minor and he is not personally liable.

9. Contract by guardian are valid: Valid contract can be entered into with the guardian on behalf of the minor. Guardian must be competent to make the contract and the contract should be for the benefit of the minor.

10. Minor can be an agent: But he will not be liable to his principal for his acts

11. Minor cannot bind parent or guardian: In the absence of authority, express or implied, an infant is not capable of binding his parent or guardian, even for necessities. The parents will be held liable only when the child is acting as an agent for parents

12. Joint contract by minor and adult: The adult will be liable on the contract and not the minor

13. Minor as Shareholder: A minor, being incompetent to contract cannot be a shareholder of the company. If by mistake he becomes a member, the company can rescind the transaction and remove his name from register. But, a minor may, acting through his lawful guardian become a shareholder by transfer or transmission of fully paid shares to him.

14. Liability for torts: A tort is a civil wrong. A minor is liable in tort unless the tort in reality is a breach of contract. Thus, where a minor hired a horse for riding and injured it by over-riding, he wasn't held liable. But if the wrongful action is of a kind not contemplated by the contract, the minor may be held liable for tort. Thus, where a minor hired a horse for riding under express instructions not to jump, he was held liable when he lent the horse to one of his friends who jumped it, whereby it was injured & ultimately died.

15. Surety for a minor: In a contract of guarantee when an adult stands surety for a minor then he (the adult) is liable to the third party.

2. PERSONS OF UNSOUND MIND

- Sec 12 defines the term 'sound mind' as "A person is said to be of sound mind for the purpose of making a contract if, at the time when he makes it, he is capable of understanding it and of forming a rational judgment as to its effects upon his interests."

- According to this Section, therefore, the person entering into the contract must be a person who understands what he is doing and is able to form a rational judgment as to whether what he is about to do is to his interest or not.

- The Section further states that:

i. "A person who is usually of unsound mind, but occasionally of sound mind, may make a contract when he is of sound mind." Thus a patient in a lunatic asylum, who is at intervals of sound mind, may contract during those intervals.

ii. "A person who is usually of sound mind but occasionally of unsound mind, may not make a contract when he is of unsound mind." Thus, a sane man who is delirious from fever or who is so drunk that he cannot understand the terms of a contract, or form a rational judgment as to its effect on his interest, cannot contract whilst such delirium or drunkenness lasts.

- Burden of proof of 'unsound mind' is on the person who challenges the validity of the contract.

- Idiots, lunatics and drunken persons are examples of persons of unsound mind.

Effects of agreements made by persons of unsound mind.

- An agreement by a person of unsound mind is absolutely void and inoperative as against him but he can derive benefit under it.

- The property of a person of unsound mind is, however, always liable for necessities supplied to him or to any one whom he is legally bound to support, under Section 68

3. DISQUALIFIED PERSONS

1. Alien enemies:

An alien (citizen of a foreign country) living in India can enter into contracts with citizens of India during peace time only and that too subject to any restrictions imposed by the Govt. On the declaration of a war between his country and India, he becomes an alien enemy and cannot enter into contracts. "Alien friend can contract but an alien enemy can't contract."

2. Foreign sovereigns and ambassadors:

One has to be cautious while entering into contracts with them because whereas they can sue others to enforce the contracts entered upon with them, they cannot be sued without obtaining the prior sanction of the Central Government. Thus they are in a privileged position and are ordinarily considered incompetent to contract.

3. Convict:

A convict is one who is found guilty and is imprisoned. During the period of imprisonment, a convict is incompetent to enter into contracts, and to sue on contracts made before conviction. On the expiry of sentence, he is at liberty to institute a suit.

4. Insolvent:

An adjudged insolvent (before an 'order of discharge') is competent to enter into certain types of contracts i.e. he can incur debts, purchase property or be an employee but he cannot sell his property which vests in the Official Receiver. After the 'order of discharge,' he is just like an ordinary citizen.

5. Joint-stock company and corporation incorporated under a special Act (like L.I.C., U.T.I.):

A company/corporation is an artificial person created by law. It cannot enter into contracts outside the powers conferred upon it by its Memorandum of Association or by the provisions of its special Act, as the case may be. Again, being an artificial person (and not a natural person) it cannot enter into contracts of a strictly personal nature e.g., marriage.

# THE INDIAN CONTRACT ACT, 1872 (Chart 1.7)

**'Consent' defined:** Sec 13 provides "Two or more persons are said to consent when they agree upon the same thing in the same sense."  
Thus, consent involves identity of minds or consensus-ad-idem i.e., agreeing upon the same thing in the same sense. If, for whatever reason, there is no consensus-ad-idem among the contracting parties, there is no real consent & hence no valid contract.

**'Free Consent' defined:** Sec 14 lays down that "Consent is said to be 'free' when it is not caused by Coercion, as defined in Sec 15, or Undue influence, as defined in Sec 16, or Misrepresentation as defined in Sec 18; or Fraud, as defined in Sect 17 or Mistake, subject to the provisions of Sect 20, 21 and 22." Consent is said to be so caused when it would not have been given but for the existence of such coercion, undue influence, misrepresentation, fraud or mistake

## 1. COERCION [SEC 15]

## 2. UNDUE INFLUENCE [SEC 16]

## COERCION VS. UNDUE INFLUENCE

Basis	Coercion	Undue Influence
Nature of action	It involves the physical force or threat. The aggrieved party is compelled to make the contract	It involves moral or mental pressure.
Involvement of criminal action	It involves committing or threatening to commit and act forbidden by Indian Penal Code or detaining or threatening to detain property unlawfully.	No such illegal act is committed or a threat is given.  <i>Compiled By:CA Sahil Grover</i>
Relationship between parties	It is not necessary that there must be some sort of relationship between the parties.	Some sort of relationship between the parties is absolutely necessary.
Exercised by whom	Coercion need not proceed from the promisor nor need it be the directed against the promisor. It can be used even by a stranger to the contract.	Undue influence is always exercised between parties to the contract.
Enforceability	The contract is voidable at the option of the party whose consent has been obtained by the coercion.	Where the consent is induced by undue influence, the contract is either voidable or the court may set it aside or enforce it in a modified form.
Position of benefits received	In case of coercion where the contract is rescinded by the aggrieved party, as per Sec 64, any benefit received has to be restored back to the other party.	The court has the discretion to direct the aggrieved party to return the benefit in whole or in part or not to give any such directions.

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.

**Explanation-** It is immaterial whether the Indian Penal Code is or is not in force in the place where the coercion is employed

- Threat to shoot, murder, intimidation, threat to cause hurt, rape, defamation, giving wrong evidence, instigating to commit crime, theft, attempt to commit suicide are a few examples of acts forbidden by Indian Penal Code.

- The act constituting coercion may be directed at any person, and not necessarily at the other party to the agreement. Likewise it may proceed even from a stranger to the contract.

### Effect of Coercion

- A contract brought about by coercion is voidable at the option of the party whose consent was so caused (Sec. 19)

- The aggrieved party may either exercise the option to affirm the transaction and hold the other party bound by it or repudiate the transaction by exercising a right of rescission.

- If the aggrieved party opts to rescind a voidable contract, he must restore any benefit received by him under the contract to the other party from whom received.

- The burden of proof that coercion was used lies on the party who wants to set aside the contract on the plea of coercion

1. 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.

2. 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, e.g., the relationship between master and the servant, police officer and the accused;
- where he stands in a fiduciary relation to the other.
- 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. e.g. old illiterate persons

- Undue influence is presumed to exist under the circumstances mentioned above in sub-clauses (a), (b) and (c).
- In these cases the burden of proving that the person who was in a position to dominate the will of another did not use his position to obtain an unfair advantage, will lie upon the person who was in a position to dominate the will of the other [Sec. 16(3)].
- He can rebut or oppose the presumption by arguing (i) that full disclosure of facts was made. (ii) that the price was adequate, (iii) that the other party was in receipt of competent independent advice and his consent was free.

### Effect of Undue Influence

- 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 the court may seem just [Sec 19A]

**NO UNDUE INFLUENCE:** Every transaction where the terms are disadvantageous to one party isn't necessarily influenced by undue influence. Thus the mere fact the transaction is a hard bargain for one party doesn't always indicate undue influence, if the parties to such transaction were on equal footing and the transaction between them was a normal commercial transaction done in normal course of business.

## 5. MISTAKE [SEC 20, 21, 22]

Mistake as to fact

**Bilateral mistake**

Where both the parties to an agreement are under a mistake as to a matter of fact which is essential to the agreement, then the agreement is void. [Sec 20]

**Unilateral Mistake**

A contract is not voidable merely because it was caused by one of the parties to it being under a mistake as to a matter of fact. [Sec 22]

Mistake as to law

A contract is not voidable because it was caused by a mistake as to any law in force in India; but a mistake as to a law not in force in India has the same effect as a mistake of fact. [Sec 21]

**Mistake of Indian Law-Contract not voidable**

**Mistake of Foreign Law- Same effect as if Mistake of Fact**

## LOSS OF RIGHT OF RESCISSION

1. **Affirmation:** If after becoming aware of his right to rescind, the aggrieved party affirms the transaction either by express words or by an act which shows an intention to affirm it, the right of rescission is lost.

2. **Restitution not possible:** If the party seeking rescission is not in a position to restore the benefits he may have obtained under the contract, e.g., where the subject-matter of the contract has been consumed or destroyed, the right to rescind the contract cannot be exercised.

3. **Lapse of time:** It may be treated as evidence of affirmation where the aggrieved party fails to exercise his right promptly on discovering the representation to be untrue or on becoming aware of the fraud or coercion.

4. **Rights of third parties:** Since the contract is valid until rescinded, being a voidable contract, if before the contract is rescinded third parties, bonafide for value, acquire rights in the subject matter of the contract, those rights are valid against the party misled, and the right to rescind will no longer be available. Thus where a person obtains goods by fraud and, before the seller rescinds the contract, disposes them off to a bonafide party, the seller cannot then rescind.

# THE INDIAN CONTRACT ACT, 1872 (Chart 1.8)

Compiled By:CA Sahil Grover

**Representation** means a statement of fact made by one party to the other, either before or at the time of contract relating to some matter essential to the formation of the contract with an intention to induce the other party to enter into the contract. A representation when wrongly made may be either innocent or intentional or deliberate with an intent to deceive the other party. In law, for the former kind the term '**Misrepresentation**' and for the latter the term '**Fraud**' is used.

## 3. MISREPRESENTATION [SEC 18]

When a person makes a false statement which he himself believes to be true and he doesn't intend to deceive the other party, there is misrepresentation.

According to Section 18 'Misrepresentation' includes following cases:

- a) **Positive assertion of unwarranted statements of material facts believing them to be true:** If a person makes an explicit statement of fact not warranted by his information (i.e. without any reasonable ground) under an honest belief as to its truth though it is not true, there is misrepresentation.
- b) **Breach of duty which brings an advantage to the person committing it by misleading the other to his prejudice:** This clause covers those cases where a statement when made was true but subsequently before it was acted upon; it became false to the knowledge of the person making it. In such a case, the person making the statement comes under an obligation to disclose the change in circumstances to the other party, otherwise he will be guilty of misrepresentation.
- c) **Causing mistake about subject matter innocently:** If one of the parties induces the other, though innocently, to commit a mistake as to the quality or nature of the thing bargained, there is misrepresentation.

### Essentials of misrepresentation.

1. There should be a **representation, made innocently with an honest belief** as to its truth and without any desire to deceive the other party.
2. The representation **must relate to facts material to the contract.**
3. The representation **must be, or must have become untrue.**
4. The representation **must have been instrumental in inducing the other party to enter into a contract.**

### Effects of Misrepresentation

The aggrieved party has **two alternative courses:**

1. he can **rescind** the contract, treating the contract as voidable OR
2. he may **affirm** the contract and **insist that he shall be put in the position** in which he would have been if the **representation made had been true** (Sec. 19).

Misrepresentation **does not entitle** the aggrieved party to claim **damages** by way of interest or otherwise for expenses incurred

## 4. FRAUD [SEC 17]

'Fraud' includes **all acts committed by a person with an intention to deceive another person.**

**According to Section 17, 'fraud' means and includes any of the following acts committed by a party to a contract:**

1. **The representation that a fact is true when it is not true by one who does not believe it to be true:** Thus a false statement intentionally made is fraud. An absence of honest belief in the truth of the statement made is essential to constitute fraud.
2. **The active concealment of a fact by a person who has knowledge or belief of the fact.** Mere non-disclosure is not fraud where there is no duty to disclose. Caveat Emptor or 'Buyer Beware' is the principle in all contracts of sale of goods. As a rule the seller is not bound to disclose to the buyer the faults in the goods he is selling. The buyer must make all enquiries before he buys a good to ensure that the good suits his needs, In the absence of any enquiry from the buyer, the seller is not bound to disclose every defect in goods of which he may be aware.
3. **A promise made without any intention of performing it.** If a man while entering into a contract has no intention to perform his promise, there is fraud on his part.
4. **Any other act fitted to deceive:** All surprise, trick, cunning, dissembling and other unfair way that is used to cheat anyone is considered fraud and sub-section (4) is obviously intended to cover all those cases of fraud which cannot appropriately be covered by the other sub-sections.
5. **Any such act or omission as the law specially declares to be fraudulent:** This sub-section refers to the provisions in certain Acts which make it obligatory to disclose relevant facts. Example: Section 55 of the Transfer of Property Act, the seller of immovable property is bound to disclose to the buyer all material defects in the property (e.g., the roof has a crack) or in the seller's title (e.g., the property is mortgaged). An omission to make such a disclosure amounts to fraud.

### Effects of Fraud

The aggrieved party has following remedies:

1. He can **rescind the contract**, i.e., he can avoid the performance of the contract; contract being voidable at his option (Sec. 19);or
2. He can **ask for restitution and insist that the contract shall be performed**, and that he shall be **put in the position in which he would have been**, if the representation made had been true (Sec. 19).
3. The **aggrieved party can also sue for damages**, if any. Fraud is a 'civil wrong' hence compensation is payable.

### Can Silence be Fraudulent?

The **Explanation to Sec 17** deals with cases as to when '**silence is fraudulent**' or what is sometimes called '**constructive fraud.**' It declares that "mere silence as to facts likely to affect the willingness of a person to enter into a contract is not fraud, unless:

- i. 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
- ii. Silence is, in itself, equivalent to speech

**General rule:** Mere silence is not fraud because there is no duty cast by law on a party to a contract to make a disclosure to the other party, of material facts within his knowledge.

**Silence is fraudulent** if circumstances of the case are such that it is the **duty of the person keeping silence to speak**'. In other words, silence is fraudulent in contracts of 'utmost good faith' i.e. contracts '**uberrimae fidei**'.

Following contracts come within this category:

1. Fiduciary Relationship
2. Contracts of Insurance
3. Contracts of marriage
4. Share allotment contracts
5. Contracts of family settlement

**Silence is fraudulent** where the circumstances are such that "**silence is, in itself equivalent to speech.**" Where, for example, B says to A "If you do not deny it. I shall assume that the horse is sound." A says nothing. Hence A's silence is equivalent to speech. If the horse is unsound A's silence is fraudulent

### Special points

1. A deceit which doesn't deceive gives no ground for action. **Where a party to a contract commits fraud or misrepresentation, but the other party is not, in fact, misled by such fraud or misrepresentation, the contract cannot be avoided by the latter.** (Explanation to Section 19).
2. In cases of fraudulent silence, the contract is not voidable, if the party whose consent was so caused had the means of discovering the truth with ordinary diligence (Exception to Sec. 19).In case of fraud this is no defence i.e. contract is voidable even if the fraud could be discovered with ordinary diligence.
3. Fraud by a stranger to the contract does not affect contract

### FRAUD vs. MISREPRESENTATION

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
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.(except in case of fraudulent silence)	Party can always plead that the injured party had the means to discover the truth.

Compiled By:CA Sahil Grover

# THE INDIAN CONTRACT ACT, 1872 (Chart 1.9) - ILLEGAL/UNLAWFUL AGREEMENTS

According to **Section 23**, every agreement of which the object or consideration is unlawful is void and the consideration or the object of an agreement is unlawful in the following cases:

1. **If it is forbidden by law:** This clause refers to agreements which are declared illegal by law. If the consideration or object for a promise is such as is forbidden by law, the agreement is void.
2. **If it is of such a nature that, if permitted, it would defeat the provisions of any law:** This clause refers to cases where the object or consideration of an agreement is of such a nature that though not directly forbidden by law, it would indirectly lead to a violation of law whether enacted or otherwise (e.g. Hindu and Mohammedan Laws). Such an agreement is also void.
3. **If it is fraudulent:** An agreement whose object or consideration is to defraud others is unlawful and hence void.
4. **If it involves or implies injury to the person or property of another:** If the object or consideration of an agreement is injury to the person or property of another, it is void, being an unlawful agreement.
5. **If the court regards it as immoral:** An agreement whose object or consideration is immoral is illegal and therefore void. The scope of the word 'immoral' here extends to the following:
  - i. Sexual immorality e.g. illicit cohabitation or concubinage or prostitution
  - ii. Furtherance of sexual immorality.
  - iii. Interference with marital relations.
  - iv. Such acts which are against good public morals. Compiled By:CA Sahil Grover
6. **If the court regards it as 'opposed to public policy':** On the basis of decided cases on the subject the following agreements have been held by courts to be against public policy:
  - i. Trading with an alien enemy
  - ii. Agreements interfering with the course of justice.
  - iii. **Agreements for stifling criminal prosecution:** Any agreement which seeks to prevent the prosecution of a guilty party is opposed to public policy and is void. However, under the Indian Criminal Procedure Code there are certain compoundable offences (e.g. assault) which can be compromised and agreements for the compromise of such offences are valid.
  - iv. **Maintenance and Champerty.** 'Maintenance' may be defined as an agreement whereby a stranger promises to help another person by money or otherwise in litigation in which that third person has himself no legal interest. 'Champerty' is an agreement whereby a person agrees to assist another in litigation in exchange of a promise to hand over a portion of the proceeds of the action. Thus, in both cases financial or professional assistance is provided with a view to assisting another person in litigation but in case of champerty the party helping in litigation also shares in the gains of the litigation in addition to interest on money advanced or fees for professional services. Under the English Law both 'Maintenance' and 'Champerty' are absolutely void. The rules applied in India are as follows:
    - An agreement for supplying funds by way of 'maintenance' or 'champerty' is valid unless:
      - a) it is unreasonable so as to be unjust to the other party, or
      - b) it is made by a malicious motive like that of gambling in litigation and not with the bona fide object of assisting a claim believed to be just
  - v. **Traffic in public offices:** Agreements for sale or transfer of public offices or for appointments to public offices in consideration of money are illegal,
  - vi. **Agreements creating an interest opposed to duty:** An agreement which tends to create a conflict between interest and duty is illegal and void on the ground that it is opposed to public policy
  - vii. **Marriage brokerage agreements.** These are agreements for the payment of money in consideration of procuring for another in marriage a husband or a wife. Such agreements are illegal and void
  - viii. **Sale of public offices:** While appointing a person to certain important and high public office, merit alone should be the criteria. Any attempt to influence or any agreement to influence anyone in this regard should be seen as an act 'opposed to public policy'.
  - ix. **Agreement for the creation of monopolies**

Object or consideration unlawful in part	Effect of Illegal Agreements on Collateral Transactions
<ol style="list-style-type: none"> <li>1. When an agreement contains several distinct promises to do things legal and also other things illegal and <b>the legal part cannot be separated from the illegal part</b> (i.e. the consideration for different promises is a single sum of money), <b>the whole agreement is illegal and void (Sec. 24)</b></li> <li>2. Where there is reciprocal promise to do things legal and also other things illegal and <b>the legal part can be separated from the illegal part</b> (i.e. there is a separate consideration for different promises), <b>the legal part is a contract and the illegal part is a void agreement (Sec. 57)</b></li> <li>3. In the case of an <b>alternative promise, one branch of which is legal and the other illegal, the legal branch alone can be enforced (Sec. 58).</b>  <b>Example:</b> A and B agree that A shall pay B Rs. 1,000 for which B shall afterwards deliver to A either rice or smuggled opium. This is a valid contract to deliver rice and a void and unlawful agreement as to opium</li> </ol>	<p>Transactions which are <b>incidental or collateral to illegal agreements are also tainted with illegality</b> and therefore are not enforceable, provided the parties to the collateral transaction had the knowledge of the illegal or immoral design of the main or primary agreement.</p> <p style="text-align: center;"><b>No restitution is allowed.</b></p> <p>Parties to an illegal agreement cannot get any help from a court of law as <b>"no polluted hand shall touch the pure fountain of justice."</b> So <b>nothing can be recovered under an illegal agreement</b> and if something has been paid it cannot be recovered back <b>whether the illegal object has been carried out or has not been carried out is immaterial.</b> The rule of law is that "no action is allowed on an 'illegal agreement'".</p>

## VOID AGREEMENT vs. ILLEGAL AGREEMENT

Basis of distinction	Void agreement	Illegal agreement
1. Meaning	An agreement not enforceable by law is said to be a void agreement	An agreement which is forbidden (i.e., prohibited) by any law for the time being in force, is an illegal agreement.
2. One in another	All void agreements are not illegal.	An illegal agreement is always void.
3. Reason	If an agreement does not satisfy one or more requirements of Sec. 10, 29 and 56, it is void.	An agreement becomes an illegal agreement only if it is made against the provisions of any law for the time being in force.
4. Punishment	The parties are not liable to be punished.	In case of an illegal agreement, the parties are criminally liable.
5. Effect on collateral transactions	A transaction which is collateral to a void agreement, is not void.	A transaction which is collateral to an illegal agreement, is also illegal.

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# THE INDIAN CONTRACT ACT, 1872 (Chart 1.10) - EXPRESSLY DECLARED VOID AGREEMENTS

<b>1. Agreements in restraint of marriage [Sec 26]</b>	<b>2. Agreements in restraint of trade [Sec 27]</b>	<b>5. Wagering Agreements</b>	
<p><b>"Every agreement in restraint of the marriage of any person, other than a minor, is void."</b>[Sec 26].</p> <ul style="list-style-type: none"> <li>- The restraint may be general or partial but the agreement is void, and therefore, an agreement agreeing not to marry at all, or a certain person, or a class of persons, or for a fixed period, is void.</li> <li>- Agreement restraining the marriage of a minor is valid</li> <li>- A promise to marry a particular person does not imply any restraint of marriage, and is, therefore, a valid contract.</li> </ul>	<p><b>"Every agreement by which anyone is restrained from exercising a lawful profession, trade or business of any kind, is to that extent void."</b>[Sec 27]</p> <ul style="list-style-type: none"> <li>- An agreement whereby one of the parties agrees to close his business in consideration of the promise by the other party to pay a certain sum of money, is void, being an agreement is restraint of trade, and the amount is not recoverable, if the other party fails to pay the promised sum of money.</li> </ul> <p><b>Exceptions:</b> In these agreement in restraint is valid:</p> <ol style="list-style-type: none"> <li>1. <b>Sale of goodwill:</b> The seller of the 'goodwill' of a business can be restrained from carrying on a similar business, <b>within specified local limits</b>, so long as the buyer, or any person deriving title to the goodwill from him, <b>carries on a like business therein</b>, provided the <b>restraint is reasonable in point of time and space.</b></li> <li>2. <b>Partners' agreements:</b> An agreement in restraint of trade among the partners or between any partner and the buyer of firm's goodwill is valid in following cases:             <ol style="list-style-type: none"> <li>i. Restriction on existing partner not to carry any other business while he is partner.</li> <li>ii. Restriction on outgoing partner</li> <li>iii. Restrictions on partners upon or in anticipation of dissolution of firm.</li> <li>iv. Restrictions on partners in case of sale of goodwill of the firm</li> </ol> </li> <li>3. <b>Negative stipulations in service agreements:</b> An agreement of service by which a person binds himself <b>during the term of the agreement, not to take service with anyone else</b>, is not in restraint of lawful profession and is valid.</li> <li>4. <b>Trade combinations:</b> <ul style="list-style-type: none"> <li>- An agreement, the primary object of which is to regulate business and not to restrain it is valid. Thus, an agreement in the nature of a business combination between traders or manufacturers e. g., not to sell their goods below a certain price, to pool profits or output and to divide the same in an agreed proportion, does not amount to a restraint of trade. However an agreement attempts to create a monopoly, it would be void.</li> <li>- An agreement between manufacturer and a wholesale merchant that the entire production during a period will be sold by the manufacturer to the wholesale merchant is not in restraint of trade if the purchaser was bound to accept the whole quantity</li> </ul> </li> </ol> <p style="text-align: right; font-size: small;">Compiled By:CA Sahil Grover</p>	<p><b>Section 30</b> lays down that <b>agreements by way of wager are void</b>; and no suit shall be brought for recovering anything alleged to be won on any wager, or entrusted to any person to abide the result of any game or other uncertain event on which any wager is made.</p> <ul style="list-style-type: none"> <li>- Literally the word 'wager' means 'a bet': <b>something stated to be lost or won on the result of a doubtful issue</b>, and therefore, wagering agreements are nothing but ordinary betting agreements. "The <b>essence of wagering</b> is that <b>one party is to win</b> and the <b>other to lose upon a future event</b> which at the time of the contract is of an <b>uncertain nature</b> – that is to say, if the event turns out one way A will lose; but if it turns out the other way he will win."</li> </ul> <p><b>Exception:</b> A bet on a <b>horse race carrying a prize of Rs.500 or more</b> to the winners has been made valid under the exception.</p>	
<b>3. Agreements in restraint of legal proceedings [Sec 28]</b>	<p style="text-align: center;"><b>Essential features of a wager:</b></p> <ol style="list-style-type: none"> <li>(a) There must be a promise to pay money or money's worth.</li> <li>(b) The promise must be conditional on an event happening or not happening.</li> <li>(c) The event must be an uncertain one. If one of the parties has the event in his own hands, the transaction is not a wager.</li> <li>(d) Each party must stand to win or lose under the terms of agreement.</li> <li>(e) The stake must be the only interest which the parties have in the agreement.(No interest except winning the bet)</li> <li>(f) There must be common intention to bet at the time of making such agreement.</li> </ol>		
<p>Section 28 declares the following kinds of agreements void:</p> <ol style="list-style-type: none"> <li>a) An agreement by which a <b>party is restricted absolutely from taking usual legal proceedings</b>, in respect of any rights arising from a contract.</li> <li>b) An agreement which <b>limits the time within which one may enforce his contract rights</b>, without regard to the time allowed by the <b>Limitation Act.</b></li> </ol> <p><b>Exceptions:</b></p> <ol style="list-style-type: none"> <li>a) This Section does not affect the law relating to arbitration e.g., if the parties agree to refer to arbitration any dispute which may arise between them under the contract, such a contract is valid.</li> <li>b) The Section does not affect an agreement whereby parties agree "not to file an appeal" in a higher court.</li> <li>c) This Section does not prevent the parties to a contract from selecting one of the two courts which are equally competent to try the suit</li> </ol> <ul style="list-style-type: none"> <li>• <b>Curtailling the period of limitation:</b> Any agreement curtailing the period of limitation prescribed by the Limitation Act is also void under Section 28.</li> </ul> <p><b>Note:</b> Agreements <b>extending the period of limitation</b> prescribed by the Limitation Act are also <b>void</b>, not under this Section but <b>under Section 23</b>, as the object will be to defeat the provisions of the law.</p>	<p style="text-align: center;"><b>Transactions similar to Wager</b></p> <ul style="list-style-type: none"> <li>- <b>Lottery business</b> is a wagering transaction. Such a transaction is <b>not only void but also illegal</b> because <b>Section 294-A of the IPC</b> declares 'conducting of lottery' a punishable offence. If a lottery is authorised by the Govt., the persons running the lottery and the buyer of lottery ticket won't be guilty of a criminal offence, but the lottery remains a wager.</li> <li>- <b>Crossword Puzzles and Competitions:</b> Crossword puzzles in which <b>prizes depend upon the correspondence of the competitor's solution with a previously prepared solution</b> kept with the editor of a newspaper is a lottery and therefore, a <b>wagering transaction</b>. Crossword puzzles, picture competitions and athletic competitions where <b>prizes are awarded on the basis of skill and intelligence are the games of skill and hence such competitions are valid.</b></li> <li>- <b>Horse Race Transactions:</b> A horse race competition where prize payable to the bet winner is <b>less than 500, is a wager.</b></li> <li>- <b>Speculative transactions:</b> an agreement or a share market transaction where the parties <b>intend to settle the difference between the contract price and the market price of certain goods or shares</b> on a specified day, is a gambling and hence void</li> </ul>		<p style="text-align: center;"><b>Transactions resembling with wagering transaction but are not void</b></p> <p><b>Chit fund:</b> 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.</p> <p><b>Commercial transactions or share market transactions:</b> In these transactions in which delivery of goods or shares is intended to be given or taken, do not amount to wagers.</p> <p><b>Games of skill and Athletic Competition:</b> 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.</p> <p><b>A contract of insurance:</b> A contract of insurance is a type of contingent contract and is valid under law and these contracts are different from wagering agreements.</p>
<b>4. Uncertain Agreements [Sec 29]</b>	<p><b>COLLATERAL TRANSACTIONS:</b> Collateral transactions to void agreements are not void. Collateral transactions to illegal agreements are illegal and thus void. For example in a wagering transaction the broker is entitled to collect his brokerage</p>		
<p><b>Agreements, the meaning of which is not certain, or capable of being made certain, are void".</b> If the words used by the parties are vague or indefinite, the law cannot enforce the agreement</p>	<p><b>NO RESTITUTION:</b> No restitution of the benefit received is allowed in the case of expressly declared void agreements.</p>		

# THE INDIAN CONTRACT ACT, 1872 (Chart 1.11)

## INSURANCE CONTRACTS vs WAGERING AGREEMENTS

Basis	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	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	It is void and 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.

## CONTINGENT CONTRACTS

"A contingent contract is a contract to do or not to do something if some event collateral to such contract does or does not happen." [Sec 31]. Thus it is a contract, the performance of which is dependent upon the happening or non-happening of an uncertain event, collateral to such contract.

Essentials of Contingent Contract	Rules Regarding the Performance of Contingent Contracts
<ol style="list-style-type: none"> <li>The performance of such a contract <b>depends upon the happening or non-happening of some future uncertain event.</b></li> <li>The future <b>uncertain event is collateral</b> i.e. incidental to the contract. The event is not part of the contract. The event should be neither performance promised nor a consideration for a promise.</li> <li>The contingent <b>event should not be a mere 'will' of the promisor.</b> The event should be contingent in addition to being the will of the promisor.</li> <li>The <b>event must be uncertain.</b> Where the event is certain or bound to happen, the contract is due to be performed, then it is a not contingent contract.</li> </ol>	<ol style="list-style-type: none"> <li><b>Contingency is the "happening of an event"</b>: Where a contingent contract is made contingent on 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. [Sec 32]</li> <li><b>Contingency is the non-happening of an event</b>: Where a contingent contract is made contingent on a non-happening of an event, it can be enforced only when the happening of the event becomes impossible and not before. [Sec 33]</li> <li><b>Contingent on the future conduct of a living person</b>: 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 within any definite time, or otherwise then under further contingencies. [Sec 34]</li> <li><b>Contingency is happening of event within fixed time</b> 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 the time fixed, such event has not happened or if before the time fixed, such event becomes impossible. [Sec 35]</li> <li><b>Contingency is non happening of an event within fixed time</b> 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 if, before the time fixed has expired, if it becomes certain that such event will not happen. [Sec 35]</li> <li><b>Contingent on an impossible event</b>: A contingent agreement to do a thing or not to do a thing if an impossible event happens is void and hence is not obviously enforceable. The situation would not change even if the parties to the agreement are not aware of such impossibility. [Sec 36]</li> </ol>
Collateral event	
<ul style="list-style-type: none"> <li>Collateral event 'means an event which is "neither a performance directly promised as part of the contract, nor the whole of the consideration for a promise."</li> <li>It is incidental to the contract. The event is not part of the contract.</li> <li>Example : C contracts to pay Rs 100 to D for white-washing his house on the terms that no payment shall be made till the completion of the work, it is not a contingent contract because the event (D's completing the work) is not collateral to the contract, but is itself a reciprocal promise or is the very thing contracted for and is thus an integral part of the contract</li> </ul>	

## VOID AGREEMENTS vs. VOID CONTRACTS

Basis of distinction	Void agreement	Void Contract
Meaning	An agreement not enforceable by law is said to be a void i.e void agreement	A contract which ceases to be enforceable by law becomes void when it ceases to be enforceable.
Status at the time of formation	All the essentials of the contract are not satisfied at the time of formation of agreement .Thus it is a nullity since very beginning	All the essentials of the contract are satisfied at the time of formation of a contract ,which subsequently becomes void .Thus at the time of formation ,it is a valid contract
Restitution	No restitution is allowed in case of a expressly declared void agreements .or if the object or consideration of an agreement is unlawful.	Restitution is allowed in case of a void contract .In other words, any party who has obtained any benefit under a void contract, must restore it back to the other party.
Legal obligation	A void agreement does not create any legal obligations between the parties from the very beginning.	When legal obligations created under a contract come to an end subsequent to formation of the contract ,the contract becomes void

## CONTINGENT CONTRACT vs. WAGERING AGREEMENTS

Basis	Contingent contract	Wagering Agreement
Meaning	A contingent contract is a contract to do or not to do something with reference to a collateral event happening or not happening.	A wagering agreement is a promise to give money or money's worth with reference to an uncertain event happening or not happening.
Reciprocal promises	Contingent contract may not contain reciprocal promises.	A wagering agreement consists of reciprocal promises.
Uncertain event	In a contingent contract, the event is collateral.	In a wagering contract, the uncertain event is the core factor.
Nature of contract	Contingent contract may not be wagering in nature.	A wagering agreement is essentially contingent in nature.
Interest of contracting parties	Contracting parties have interest in the subject matter in contingent contract.	The contracting parties have no interest in the subject matter.
Effect of contract	Contingent contract is valid.	A wagering agreement is void.

- A contract is the result of an agreement enforceable by law. But in some cases there is no offer, no acceptance, no consensus ad-idem and in fact no intention on the part of parties to enter into a contract and still the law from the conduct and relationship of the parties, implies a promise imposing obligation on the one party and conferring a right in favour of the other.
- In other words under **certain special circumstances obligations resembling those created by a contract are imposed by law although the parties have never entered into a contract.** Such obligations imposed by law are referred to as '**Quasi-Contracts**' or '**Constructive Contracts**' under the English law, and "**certain relations resembling those created by contracts**" under the **Indian law.** A quasi-contract rests upon the equitable "**doctrine of unjust enrichment**" which declares that a person shall not be allowed to enrich himself unjustly at the expense of another. Quasi contracts are based on principles of **equity, justice and good conscience. Duty and not a promise or agreement is the basis of such contracts.**

**Claim for necessaries supplied to a person incapable of contracting or on his account (Sec. 68)**

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.

- The following points need to be emphasised:
- i. The Section **does not create any personal liability but only the estates are liable.**
  - ii. The things supplied must come within the category of '**necessaries**'. The word '**necessaries**' here covers **not only bare necessities of existence.** e.g. food and clothes, **but all things which are reasonably necessary to the incompetent person, having regard to his status in society.** e.g. watch, a radio, a bicycle may be included therein.
  - iii. Necessaries should be supplied only to such **incompetent person or to someone whom the incompetent person is legally bound to support,** such as his wife and children.
  - iv. Incompetent person's property is liable to **pay only a reasonable price for the goods or services** supplied and not the price which the incompetent person might have 'agreed to' (legally speaking an incompetent person cannot agree to anything).

**Reimbursement of person paying money due by another, in payment of which he is interested (Sec 69)**

A person who is interested in the payment of money which another is bound by law to pay and who therefore pays it, is entitled to be reimbursed by the other.

Conditions of Section 69:

- (a) **One person is legally bound to make a payment.**
- (b) **Some other person makes such payment.**
- (c) **The person making such payment is not legally bound to make such payment.**
- (d) **The person making such payment is interested in paying such amount.**

If all the conditions of Sec. 69 are satisfied, the person who is interested in paying such amount shall be entitled to recover the payment made by him

**Obligation of person enjoying benefit of non-gratuitous act (Sec.70)**

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 make compensation to the former in respect of, or to restore, the thing so done or delivered.

- The following three conditions must be fulfilled:
- a) A person has **lawfully done something for another person; or delivered something to another person.**
  - b) Such person must have **acted voluntarily; and non-gratuitously** i.e. it must have been done with the intention of being paid for.
  - c) **The other person has enjoyed the benefit of the act done for him; or the thing delivered to him.**

If the conditions of Sec. 70 are satisfied, there will be a quasi-contract between the parties. Consequently, the party who has done something or delivered a thing shall be entitled to recover its value from the person who obtained the benefit of the same.

**Liability of person to whom money is paid or thing delivered by mistake or under coercion [Sec.72].**

**"A person to whom money has been paid or anything delivered by mistake or under coercion must repay or return it".** Accordingly, if one party under a mistake pays to another party money which is not due by contract or otherwise, that money must be repaid

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**Difference between quasi contracts and contracts**

Basis of distinction	Quasi- Contract	Contract
Essential for the valid contract	The essentials for the formation of a valid contract are absent	The essentials for the formation of a valid contract are present
Obligation	Imposed by law	Created by the consent of the parties

**Responsibility of finder of goods (Sec. 71)**

"A person who finds goods belonging to another and takes them into his custody is subject to the same responsibility as a bailee."  
Thus an agreement is also implied by law between the owner and finder of the goods and the latter is deemed to be a bailee.

Duties of finder of goods:

- Finding true owner:** He must try to find out the real owner of the goods and must not appropriate the property to his own use. If the real owner is traced, he must restore the goods to him on demand. If he does not take these measures, he will be guilty of criminal misappropriation of the property under Section 403 of Indian Penal Code.
- Take reasonable care:** Further, till the goods are in possession of the finder, he must take as much care of the goods as **a man of ordinary prudence would under similar circumstances take of his own goods** of the same bulk, quality and value.

Rights of finder of goods (Sec 168 & 169)

- Recover expenses incurred:** He is entitled to receive from the true owner, all expenses incurred by him for preserving the goods or finding the true owner. He has a lien on the goods for the money so spent i.e. he can refuse to return the goods to the true owner until these moneys are paid. He is not entitled to file a suit for the recovery of such sums.
- Recover Reward:** He can file a suit against the owner to recover any reward which was offered by the owner for the return of the goods provided he came to know of the offer of reward before actually finding out the goods.
- Sell the goods:** The finder of goods is entitled to sell the goods if the owner cannot be found out or if he refuses to pay the lawful charges of the finder in the following two situations only:
  - a) when the thing is in danger of perishing or of losing the greater part of its value. Or
  - b) when the lawful charges of the finder amount to at least two-thirds of the value of goods found.
 He is entitled to sue to recover the deficit. In case of surplus it should be passed to the true owner.
- Right to retain possession against everyone except the true owner:** Till the true owner is found out, the finder of goods can retain possession of the goods against everybody in the world. No one except the real owner can claim possession of goods from the finder. If anybody deprives him of the possession of the goods, he can file a suit for damages for trespass



# THE INDIAN CONTRACT ACT, 1872 (Chart 1.13) - PERFORMANCE OF CONTRACT

"Performance of Contract" means fulfilling of their respective legal obligations created under the contract by both the promisor and the promisee. When a contract is duly performed by both the parties, the contract comes to a happy ending and nothing more remains. Performance by both parties is the normal and natural mode of discharging or terminating a contract.

## Who can Demand Performance?

- Only the **promisee (or his duly authorised agent)** can demand performance of the promise under a contract. (Rule- a person cannot acquire rights under a contract to which he is not a party")
- A **third party cannot demand performance** of the contract even if it was made for his benefit.
- In case of the **death of the promisee, his legal representatives** are entitled to enforce the performance of the contract against the promisor.

## By whom Contracts must be Performed?

### 1. By the promisor himself

In the case of a contract involving **personal skill, taste or credit**. e. g. a contract to paint a picture, a contract of agency or service, the promisor must himself perform the contract. **Section 40** states "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"

### 2. By the promisor or his agent:

In the case of a contract of impersonal nature; e.g., a contract of sale of goods or a contract to lend a sum of money, **the promisor himself or his agent** may perform the contract [Sec 40 (2)].

### 3. By the legal representatives:

In the case of contracts involving **personal skill**, the heirs or legal representatives of a deceased promisor are not bound to perform the contract. Such contracts come to an end on the death of the promisor. In the case of contracts not involving personal considerations, the legal representatives are bound to perform the contract. But their liability is limited to the estate of the deceased which has come to their hands. They are not personally liable.

### 4. Performance by a third person:

- **Section 41** lays down that if a promisee accepts performance of the promise from a third person, he cannot afterwards enforce it against the promisor.

- Where a promisee accepted lesser amount from a third party in full satisfaction of his claim, it was held that he cannot enforce the promise

- Thus under this Section performance of the promise by a stranger, once accepted by the promisee, discharges the promisor, although the latter has neither authorised nor ratified the act of the third party

## PERFORMANCE OF JOINT PROMISES

### Who can demand performance?

- **Section 45** which provides that when a promise is made to several persons jointly, then unless a contrary intention appears from the contract, the right to claim performance rests with all the promisees jointly and a single promisee cannot demand performance.
- When any one of the promisees dies, the right to claim performance rests with the legal representatives of such deceased person jointly with the surviving promisees. When all the promisees are dead, the right to claim performance rests with the legal representatives of all jointly.
- In brief, **so long as all the joint promisees are alive, the right to claim performance rests with all of them jointly and on the death of any promisee his legal representatives step into his shoes.**

### By whom Contracts must be Performed? [Liability of Joint Promisor & Promisee]

1. **All promisors must jointly fulfil the promise:** When two or more persons have made a joint promise (e.g. signed a promissory note jointly), then, unless a contrary intention appears by the contract, **all such persons must jointly fulfil the promise.**  
When any one of the joint promisors dies, his **legal representatives must jointly with the surviving promisors, fulfil the promise.** On the death of all the original promisors, **the legal representatives of all of them jointly must fulfil the promise (Sec. 42).**  
However **legal representatives are not personally liable.** Their liability is limited to the assets inherited by them.  
**Contracts involving personal skill come to an end on the death** of any of the joint promisors and the liability of performance does not fall on the legal representatives
2. **Any one or more of joint promisors may be compelled to perform:** The promisee is entitled, in the absence of express agreement to the contrary, to compel any one or more of such joint promisors to perform the whole of the promise (**Sec 43 para 1**). Thus the liability of joint promisors is "**joint and several**" as against the promisee.
3. **Right of contribution inter-se between joint promisors**  
If one of several joint promisors is made to perform the whole contract, he may require equal contribution from the other joint promisors unless a contrary intention appears from the contract. [**Sec 43 para 2**]
4. **Sharing of loss by default in contribution:** If any one of the joint promisors makes a default in making contribution, if any, the remaining joint promisors must bear the loss arising from such default in equal shares (**Sec.43, Para 3**).
5. **Effect of release of one joint promisor (Section 44):** In case of joint promise, if one of the joint promisors is released from his liability by the promisee, his liability to the promisee ceases but this does not discharge the other joint promisors from their liability; neither does it free the joint promisor so released from his liability to contribute to the other joint promisors (**Sec. 44**).

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## DISTINCTION BETWEEN SUCCESSION & ASSIGNMENT

Basis	Succession	Assignment
1. Meaning	The transfer of rights & liabilities of a deceased person to his legal representative is called as succession.	The transfer of rights by a person to another person is called assignment.
2. Time	Succession takes place on the death of a person.	Assignment takes place during the lifetime of a person.
3. Voluntary act	Succession is not a voluntary act.	Assignment is a voluntary act of the parties.
4. Written document	Succession may take place even without any written document.	Assignment requires execution of an assignment deed.
5. Scope	All the rights and liabilities of a person are transferred.	Only rights can be assigned.
6. Notice	No notice of succession is required to be given to any person.	Notice of assignment must be given to the creditor.
7. Consideration	No consideration is necessary for succession.	Consideration is a must for assignment.

## TIME AND PLACE FOR PERFORMANCE

- **Where prescribed by the promisee.** Where the time and place are prescribed by the promisee, the performance of the contract must be at the specified time and place.
- **Where not prescribed by the promisee.** If no time and place are prescribed by the promisee, then the contract must be performed:
  - a) **Within a reasonable time, on a working day and within the usual hours of business.** The question, "what is a reasonable time" is in each particular case, a question of fact. It depends either on special circumstances of each particular case or the usage of trade or the intention of parties at the time of entering into contract.
  - b) **At proper place e. g. at godown or shop and not at a public meeting or a fair.** "What is a proper place" is in each particular case, a question of fact. Generally speaking the promisor must ask the promisee where he would like the contract to be performed, and to perform it at such place (**Sec 49**)

## MODE OR MANNER OF PERFORMANCE.

"The performance of any promise may be made in any manner, which the promisee prescribes or sanctions" (**Sec. 50**). He has no right to substitute, for what he has been directed, something else, even if the substitute may be more beneficial to the promisee.

**EFFECTS OF FAILURE TO PERFORM CONTRACT WITHIN STIPULATED TIME**

- Section 55** lays down the following rules:
1. Where **"time is of the essence of the contract"** and there is failure to perform within the fixed time, the contract (or so much of it as remains unperformed) becomes **voidable at the option of the promisee**. He may rescind the contract and sue for the breach.
  2. Where **"time is not of the essence of the contract"** failure to perform within the specified time **does not make the contract voidable**. The promisee cannot rescind the contract and he will have to accept the delayed performance. But he would be **entitled to claim compensation** from the promisor for any loss caused to him by the delay. This rule is, however, subject to the condition that the promisor should **not delay the performance beyond a reasonable time**, otherwise the contract will become voidable at the option of the promisee.
  3. In case of a contract voidable on account of the promisor's failure to perform his promise within the agreed time or within a reasonable time, as the case may be, **if the promisee, instead of rescinding the contract, accepts the delayed performance, he cannot afterwards claim compensation** for any loss caused by the delay, unless, at the time of accepting the delayed performance, he gives notice to the **promisor of his intention to do so**.

**When is the time the essence of the contract?**

- "Time is of the essence of the contract,
- i. if the **parties to the contract have expressly agreed** to treat it as such, or
  - ii. if the **nature of transaction and the intention of parties were such** that the performance within a limited time was necessary.

**Note:**

- **Even where a time is specified** for the performance of a certain promise, **'time may not be of the essence of the contract'** and one has to look at the nature and construction of the contract and the intention of the parties in order to ascertain whether "time is of the essence of the contract" or not.
- Unless a different intention appears from the terms of the contract, ordinarily in commercial contracts the **time of delivery of goods is of the essence of the contract but not the time of payment of the price**.
- In transaction of sale of **gold, silver, blue chip shares, time of delivery is of essence**. Here time will be treated as essence of contract.
- In transaction involving **sale of land, redemption of mortgages, though certain time frame is fixed, any delay is not valued seriously** provided justice can be done to parties. Of course even in sale of land, time can be made as an essence of contract by express words.

**ORDER OF PERFORMANCE OF RECIPROCAL PROMISES**

A contract may consist of (i) an act and a promise or (ii) two promises one being the consideration for the other. The second type of contract which involves two promises, one promise from each to the other party is known as "Reciprocal promise".

**The performance of reciprocal promise can take in different forms-**

1. **Simultaneously performance of reciprocal promise [Sect 51]:** In this case, promises have to be performed simultaneously. The conditions and performances are concurrent. If one of the parties does not perform his promise, the other also need not perform his promise.
2. **Performance of reciprocal promise where the order is expressly fixed (Sec 52):** Where the order of performance is expressly fixed, the promise must be performed in that order only. Where 'A' promises to build a house for 'B' and 'B' promises to pay after construction, here 'A' must perform his promise before he can call upon 'B' to fulfill his promise of payment of money.
3. **Performance of reciprocal promise by implication:** Where the performance of reciprocal promise is not fixed expressly, sometimes the order is understood by implication.
4. **Effect of one party preventing another from performing promise [Section 53]:** When in a contract consisting of reciprocal promises one party prevents the other from performing his promise, the contract becomes voidable at the option of the party so prevented. Example: A and B contract that B shall execute certain work for A for Rs.1,000. B is ready and willing to do the work accordingly but A prevents him from doing so. The contract becomes voidable at the option of B and if he elects to rescind it he is entitled to recover from A compensation for any loss which he has incurred by its non-performance.
5. **Effects of default as to promise to be performed first [Sec 54]:** When a contract consists of reciprocal promises, such that one of them cannot be performed, or that its performance cannot be claimed till the other has been performed, and the promisor of the promise last mentioned fails to perform it, such promisor cannot claim the performance of the reciprocal promise, and must make compensation to the other party to the contract for any loss which such other party may sustain by the non-performance of the contract. Compiled By: CA Sahil Grover  
**Example:** A contracts with B to execute certain builder's work for a fixed price. B supplying the scaffolding and timber necessary for the work. B refuses to furnish any scaffolding or timber and the work cannot be executed. A need not execute the work and B is bound to make compensation to A for any loss caused to him by the non-performance of the contract.
6. **Position of legal and illegal parts of Reciprocal promises :** Section 57 of the Act provides that if reciprocal promises have two parts, the first part being legal and the second part being illegal, the legal part is a valid contract and the illegal part is void  
**Example:** Where 'A' agrees to sell his house to 'B' for Rs.50000/- and further 'A' insists and it is agreed that if the house is used as a gambling house, then 'B' would pay another Rs.75000/-. In this case the first part is valid as it is legal, the second part is void as it is illegal.
7. **Alternative promise one branch being illegal:** "In the case of the alternative promise, one branch of which is legal and the other illegal, the legal branch alone can be enforced"  
**Example:** A and B agree that A shall pay B Rs. 1,000 for which B shall afterwards deliver to A either rice or smuggled opium. This is a valid contract to deliver rice and a void and unlawful agreement as to opium

**APPROPRIATION OF PAYMENTS**

When a debtor who owes several debts to the same creditor, makes a payment which is insufficient to satisfy the whole indebtedness, the question arises. "as to which of the debts the payment is to be applied"?

**Sections 59 to 61 of the Contract Act answer this question and lay down the following rules:**

1. **Application of payment where debt to be discharged is indicated [Sec 59]:**
  - a) **Debtor's express instructions must be followed:** Appropriation is a right given to the debtor for his benefit. Thus if the debtor expressly states that the payment made by him is to be applied to the discharge of some particular debt, the creditor must act accordingly otherwise he should not accept the payment.
  - b) **Debtor's implied intention must be followed:** If there are no express instructions, then debtor's implied intention should be gathered from the circumstances attending the payment and appropriation must be done accordingly.
2. **Application of payment where debt to be discharged is not indicated [Sec 60]:** If there is no express or implied direction by the debtor regarding appropriation, then the creditor has got the option to apply the payment to any debt lawfully due from the debtor, including a debt which is barred by the Limitation Act.
3. **Application of payment when neither party appropriates [Sec 61]:** In terms of section 61 of the Act, where neither party appropriates:
  - a) the payment shall be applied in discharge of debts in order of time, and
  - b) if the debts are of equal standing the payment shall be applied in discharge of each proportionately.

The above appropriation takes place whether or not the debt is barred by limitation.
4. **When principal and interest both due:** If a payment has been made without expressly stating whether it is towards interest or principal, payment is to be applied towards interest first and then the balance to principal.

Discharge of a contract means termination of contractual relations between the parties to a contract. Where the rights and obligations arising out of a contract are extinguished the contract is said to be discharged or terminated. **The various modes of discharge are given below:**

1. DISCHARGE BY PERFORMANCE	2. DISCHARGE BY MUTUAL AGREEMENT	3. DISCHARGE BY LAPSE OF TIME
<p>Performance of contract is the principal and most usual mode of discharge of a contract. Performance may of two kinds:</p>	<p><b>1. Novation (Sec 62):</b> Novation means substitution of a new contract in place of the original contract. The new contract may be between the same parties; or between different parties. If parties are not changed then the nature of the obligation (i.e. material terms of the contract) must be altered substantially in the new substituted contract, for, a mere variation of some of the terms of a contract, while the parties remain the same is not "novation" but "alteration." The consideration for the new contract is the discharge of the original contract. Novation can't be compulsory. It can only be with the mutual consent of all the parties.</p>	<p>- The <b>Limitation Act</b> lays down that in case of breach of a contract legal action should be taken within at specified period, called the period of limitation, otherwise the promisee is debarred from instituting a suit in at court of law and the contract stands discharged. Thus in certain circumstances lapse of time may also discharge a contract</p>
<p><b>1. Actual Performance</b></p>	<p><b>2. Alteration (Sec 62)</b> Alteration means a change in one or more of the material terms of a contract with mutual consent of parties. A material alteration is one which alters the legal effect of the contract. e.g. a change in the amount of money to be paid or a change in the rate of interest. Immaterial alteration, e.g., correcting a clerical error in figures or the spelling of a name has no effect on the validity of the contract and does not amount to alteration in the technical sense. An alteration discharges the original contract and creates a new contract between the parties. However, the parties to the new contract remain the same. A material alteration made in a written contract by one party without the consent of the other will make the whole contract void and no person can maintain an action upon it.</p>	<p>- For example, the period of limitation for simple contracts is three years under the Limitation Act and therefore on default by debtor if the creditor does not file a suit of recovery against him within three years of default, the debt becomes time-barred on the expiry of three years and the creditor will be deprived of his remedy at law. This in effect implies discharge of contract.</p>
<p>- When each party to a contract fulfils his obligation arising under the contract within the time and in the manner prescribed it amounts to actual performance of the contract and the contract comes to an end or stands discharged.</p> <p>- But if one party only performs his promise, he alone is discharged. Such a party gets a right of action against the other party who is guilty of breach.</p>	<p>Compiled By:CA Sahil Grover</p>	<p>- Where "time is of essence in a contract", if the contract is not performed at the fixed time, the contract comes to an end, and the party not at fault need not perform his obligation and may sue the other party for damages</p>
<p><b>2. Attempted Performance [Tender]</b></p>	<p><b>3. Remission (Sec. 63):</b> Remission means waiver. Section 63 of the Act deals with remission. It provides that "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 it thinks fit". A contract is discharged by remission, i.e., where a promisee agrees to -</p>	<p><b>4. DISCHARGE BY OPERATION OF LAW</b></p>
<p>When the promisor offers to perform his obligation under the contract, but is unable to do so because the promisee does not accept the performance, it is called "attempted performance" or "tender." Thus "tender" is not actual performance but is only an 'offer to perform' the obligation under the contract.</p>	<p>(a) dispense with (wholly or in part) the performance of a promise made to him; or</p>	<p><b>1. Death:</b> Contracts involving personal skill, knowledge or ability of the deceased party are discharged automatically on the death of the promisor. In other contracts the rights and liabilities of the deceased person pass on to the legal representatives of the dead man.</p>
<p>A valid tender of performance is equivalent to performance and the contract comes to an end.</p>	<p>(b) extend the time for performance due by the promisor; or</p>	<p><b>2. Insolvency:</b> The insolvent is discharged from liability on all contracts entered into upto the date of insolvency.</p>
<p><b>Essentials of a valid tender</b></p>	<p>(c) accept a lesser sum instead of the sum due under the contract; or</p>	<p><b>3. Unauthorized material alteration:</b> An alteration which changes the substance (i.e., legal effect or basic character) of a contract is called as material alteration. A material alteration made in a written document or contract by one party without the consent of the other will make the whole contract void. Example: where the amount of money to be received is altered or an additional signature is forged.</p>
<p>- It must be unconditional. A conditional tender is no tender.</p>	<p>(d) accept any other consideration than agreed to in the contract.</p>	<p><b>4. Merger of rights:</b> Where an inferior right contract merges into a superior right contract, the former stands discharged automatically.</p>
<p>- It must be made at proper time and place.</p>	<p><b>No consideration</b> is necessary for remission.</p>	<p><b>Example:</b> Where a man holding property under a contract of tenancy buys the property, his rights as a tenant are merged into the rights of ownership and the contract of tenancy stands discharged by operation of law</p>
<p>- It must be of the whole obligation contracted for and not only of the part. Thus deciding of his own to pay in instalments and offering the first instalment was held an invalid tender as it was not of the whole amount due.</p>	<p><b>4. Rescission (Sec. 62):</b></p>	<p><b>5. DISCHARGE BY BREACH OF CONTRACT</b></p>
<p>- If the tender relates to delivery of goods, it must give a reasonable opportunity to the promisee for inspection of goods.</p>	<p>It means cancellation of a contract by one or all the parties to the contract. All the parties may mutually agree to bring the contract to an end. This is called as discharge of contract by rescission by mutual consent. An agreement of rescission releases the parties from their obligations arising out of the contract. In the case of rescission, the existing contract is cancelled by mutual consent without substituting a new contract in its place. There may also be an implied rescission of a contract, e.g., where there is non-performance of a contract by both the parties for a long period, without complaint, it amounts to an implied rescission.</p>	<p>Breach of contract by a party thereto is also a method of discharge of a contract because "breach" also brings to an end the obligations created by a contract on the part of each of the parties. Of course the aggrieved party, i.e., the party not at fault can sue for damages for breach of contract as per law; but the contract as such stands terminated.</p>
<p>- If there are several joint promisees, an offer to any one of them is a valid tender</p>	<p><b>Exception.</b></p>	<p><b>Breach of contract may be of two kinds:</b> <span style="float: right;">Compiled By:CA Sahil Grover</span></p>
<p>- In case of tender of money, exact amount should be tendered in the legal tender money.</p>	<p>Tender of money, however, does not discharge the contract. The money will have to be paid even after the refusal of tender, of course without interest from the date of refusal.</p>	<p><b>1. Actual breach; and 2. Actual breach.</b></p>
<p><b>Effect of refusal to accept valid tender</b></p>	<p>The contract is deemed to have been performed by the promisor, i.e., tenderer and the promisee can be sued for breach of contract. A valid tender, thus, discharges the contract.</p>	<p><b>1. Actual breach:</b> It occurs when a party fails to perform his obligation upon the date fixed for performance by the contract. It entitles the party not in default to elect to treat the contract as discharged and to sue the party at fault for damages for breach of contract.</p>
<p>The contract is deemed to have been performed by the promisor, i.e., tenderer and the promisee can be sued for breach of contract. A valid tender, thus, discharges the contract.</p>	<p></p>	<p><b>2. Anticipatory Breach:</b> An anticipatory breach of contract is a breach of contract occurring before the time fixed for performance has arrived. It may either be by words spoken or written or can also be implied from the conduct of parties.</p>
<p><b>Exception.</b></p>	<p></p>	<p><b>For example:</b> A person contracts to sell a particular horse to another on 1st of June and before that date he sells the horse to somebody else.</p>
<p>Tender of money, however, does not discharge the contract. The money will have to be paid even after the refusal of tender, of course without interest from the date of refusal.</p>	<p></p>	<p><b>Effects of Anticipatory Breach-Next Chart</b></p>

Effect of an anticipatory breach.

- When there is an anticipatory breach of contract, the promisee is excused from performance or from further performance.

- Further, it gives an option to the promisee (the aggrieved party) whereby:

1. He may either treat the contract as rescinded and sue the other party for damages for breach of contract immediately without waiting until the due date of performance OR
2. He may elect not to rescind but to treat the contract as still operative, and wait for the time of performance and then hold the other party responsible for the consequences of non-performance. But in that 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 reconsideration, 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.

**Exception:**  
The doctrine of anticipatory breach does not apply to contracts for the payment of a debt. Thus, if A borrows Rs.5,000 from B and signs a Promissory Note as evidence of the debt, same to be paid six months from date and if A notifies B two months before the due date that he will not pay the Note, A's renunciation will not entitle B to sue immediately. B must wait until the Note is due and if A then refuses to pay, B may file suit

IMPOSSIBILITY OF PERFORMNCE [SEC 56]

**An agreement to do an act impossible in itself is void.**  
**Contract to do act afterwards becoming impossible or unlawful:** A contract to do an act which, after the contract is made, becomes impossible, or, by reason of some event which the promisor could not prevent, unlawful, becomes void when the act becomes impossible or unlawful.

**Compensation for loss through non-performance of act known to be impossible or unlawful:** Where one person has promised to do something which he knew, or, with reasonable diligence, might have known, and which the promisee did not know, to be impossible or unlawful, such promisor must make compensation to such promisee for any loss which such promisee sustains through the non-performance of the promise.

**ANALYSIS OF SEC 56**

The impossibility of performance may be of the two types, namely (a) initial impossibility, and (b) subsequent impossibility

1. **Impossibility existing at the time of contract (Initial Impossibility):** When the parties agree upon doing of something which is obviously impossible in itself the agreement would be void. Impossible in itself means impossible in the nature of things. The fact of impossibility may be and may not be known to the parties.
  - i. **If known to the parties:** An agreement constituted, quite unknown to the parties, may be impossible of being performed and hence void.
  - ii. **If unknown to the parties:** Even where both the promisor and the promisee are ignorant of the impossibility the contract then too is void.
  - iii. **If known only to the promisor:** If the impossibility is not obvious and the promisor alone knows it is impossible to perform or even if he does not know but he should have known about the impossibility with reasonable diligence, the promisee is entitled to claim compensation for the loss suffered because of failure of the promisor to perform.
2. **Subsequent or Supervening impossibility:** 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. The effect of such impossibility is that it makes the contract void, and the parties are discharged from further performance of the contract.

Restitution under void agreement or contract that become void. [Sec 65]

Section 65 lays down that

- 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.

However, agreements which are known to be void or illegal, when they are entered into, are excluded from the purview of this Section. Similarly nothing can be recovered in case of expressly declared void agreements

6. DISCHARGE BY SUPERVENING IMPOSSIBILITY/ILLEGALITY

- Section 56, Para 2, declares: "A contract to do an act which, after the contract is made, becomes impossible, or, by reason of some event which the promisor could not prevent, unlawful, becomes void when the act becomes impossible or unlawful".

- In this case 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.

Effects of supervening impossibility

The contract is discharged, i.e., the contract becomes void. All the parties are discharged from their respective obligations. Restitution is allowed in terms of section 65

Cases where doctrine of supervening impossibility applies

1. **Accidental destruction of subject matter:** If the subject matter of the contract is accidentally destroyed, without any fault of any party, it amounts to supervising impossibility. Therefore, both the parties are excused from performance of the contract. **Leading Case : TAYLOR VS.CALDWELL**
2. **Incapacity to perform a contract of personal service:** Where a contract has to be personally performed by a party, disability or incapacity to perform caused due to circumstances beyond the control of such party (e.g., illness or death) amounts to supervening impossibility.
3. **Change of law:** Performance of a contract may also become impossible due to change in law subsequently. The law passed subsequently may prohibit the act which may form part as basis of contract. Here the parties are discharged from their obligations.
4. **Outbreak of war:** If one of the parties becomes an alien enemy due to outbreak of war, it amounts to supervening impossibility. All contracts entered into with an alien enemy during war are illegal and void-ab-initio. Contracts entered into before the outbreak of war are suspended during the war and may be revived after the war is over provided they have not already become time-barred. If a war is declared between the countries of the contracting parties then only the contract is suspended during war. If war is declared between the country of one of the parties to the contract and a third country, it will be treated as "difficulty in performance" only and does not discharge the contract.
5. **Non-existence or non-occurrence of things forming the basis of a contract:** If particular state of things, which forms the basis of a contract, ceases to exist or occur, the contract is discharged by supervening impossibility. **Leading Case: KRELL VS HENRY**

Cases not covered by supervening impossibility

1. **Commercial impossibility/ Difficulty in performance:** Where performance becomes difficult or burdensome, e.g., rise or fall in prices, depreciation or appreciation of currency, obstacles to the execution of the contract, execution of contract becoming more expensive or less profitable, availability of transport at exorbitant rates, etc., it does not amount to supervening impossibility and thus doesn't excuse performance.
2. **Default by third party:** Default by a third party on whose work or conduct the promisor relied does not amount to supervening impossibility.
3. **Strikes, riots or civil disturbances:** Strike by the workers, or outbreak of riots or some civil disturbances interrupting the performance of promise do not amount to supervening impossibility.
4. **Self-induced impossibility:** Impossibility arising due to a party's own conduct or act (i.e. a deliberate or a negligent act), is not supervening impossibility. Eg. lockout.
5. **Partial failure of objects or partial impossibility:** If a contract is made for fulfilment of several objects, the failure of one or more of them does not amount to supervening possibility. **Leading Case: H.B. Steamboat Co. v Hulton**

**1. RECISSION OF CONTRACT**

- Rescission means a right available to an aggrieved party to terminate a contract.
- When there is a breach of contract by one party, the other party may rescind the contract and need not perform his part of obligations under the contract and may sit quietly at home if he decides not to take any legal action against the guilty party.
- But in case the aggrieved party intends to sue the guilty party for damages for breach of contract he has to file a suit for rescission of the contract.
- When the court grants rescission, the aggrieved party is freed from all his obligations under the contract and becomes entitled to compensation for any damage which he has sustained through the non fulfilment of the contract (Sec. 75).
- Thus, applying to the court for 'rescission of the contract' is necessary for claiming damages for breach or for availing any other remedy. In practice a 'suit for rescission' is accompanied by a 'suit for damages' etc; in the same plaint

**2. SUIT FOR DAMAGES**

- Damages are a monetary compensation allowed to the injured party for the loss or injury suffered by him as a result of the breach of contract.
- The fundamental principle underlying damages is not punishment but compensation. By awarding damages the court aims to put the injured party into the position in which he would have been, had there been performance and not breach and not to punish the defaulter party. **As a general rule "compensation must be commensurate with the injury or loss sustained, arising naturally from the breach. If actual loss is not proved, no damages will be awarded."**

**KINDS OF DAMAGES** Compiled By: CA Sahil Grover

- 1. Ordinary Damages:** When a contract has been broken, the injured party can, as a rule, always recover from the guilty party ordinary or general damages. These are such damages as may **fairly and reasonably be considered as arising naturally and directly in the usual course of things** from the breach of contract itself. In other words, ordinary damages are restricted to the **"direct or proximate consequences"** of the breach of contract and remote or indirect losses, which are not the natural and probable consequence of the breach of contract are generally not regarded. **Leading Case: HADLEY VS. BAXENDALE**
- 2. Special damages:** are those which arise on account of the special or unusual circumstances affecting the plaintiff. In other words, they are such **remote losses which are not the natural and probable consequence of the breach of contract.** Unlike ordinary damages, special damages cannot be claimed as a matter of right. These can be claimed only if the special circumstances which would result in a special loss in case of breach of contract **are brought to the notice of the other party at the time when the contract is entered into.** Subsequent knowledge of the special circumstances will not create any special liability on the guilty party.
- 3. Exemplary or Vindictive Damages:** Such damages which are awarded with a view to punishing the guilty party for the breach and not by way of compensation for the loss suffered by the aggrieved party. These damages may be awarded only in two cases -
  - a) for **breach of promise to marry** because it causes injury to his or her feelings;
  - b) for **wrongful dishonour by a banker of his customer's cheque** because in this case the injury due to wrongful dishonour to the drawer of cheque is so heavy that it causes loss of credit and reputation to him. The damages could be very heavy if loss had been suffered by a businessman, when compared to a non-businessman customer. Similarly where the value of cheque is small the damages could be very heavy in comparison to a situation where the value of cheque is heavy.
- 4. Nominal Damages:** Nominal damages are awarded where the plaintiff has proved that there has been a breach of contract but he has not in fact suffered any real damage. It is **awarded just to establish the right to decree for the breach of contract.** The amount may be a rupee or even 10 paise
- 5. Damages for deterioration caused by delay:** In the case of deterioration caused to goods by delay, damages can be recovered from carrier even without notice. The word 'deterioration' not only implies physical damages to the goods but it may also mean loss of special opportunity for sale.
- 6. Pre-fixed damages:** Sometimes, parties to a contract stipulate at the time of its formation that on a breach of contract by any of them, a certain amount will be payable as damage. **It may amount to either liquidated damages (i.e., a reasonable estimate of the likely loss in case of breach) or a penalty (i.e., an amount arbitrarily fixed as the damages payable).** Section 74 provides that if a sum is named in a contract as the amount to be paid in case of a breach, the aggrieved party is entitled to receive from the party at fault a reasonable compensation not exceeding the amount so named (Section 74). Compiled By: CA Sahil Grover

**LIQUIDATED DAMAGES AND PENALTY**

- 'Liquidated damages' means a **sum fixed up in advance, which is a fair and genuine pre-estimate** of the probable loss that is likely to result from the breach.
- 'Penalty' means a **sum fixed up in advance, which is extravagant and unconscionable** in amount in comparison with the greatest loss that could conceivably be proved to have followed from the breach. It is imposed by way of punishment to prevent parties from committing the breach.
- Sometimes the parties fix up at the time of the contract the sum payable as damages in case of breach.
- In such a case, a distinction is made in **English Law** as to whether the provision amounts to 'liquidated damages' or a 'penalty'. Courts in England usually **allow 'liquidated damages'** as stipulated in the contract without any regard to the actual loss sustained. **'Penalty' clauses, however, are treated as invalid** and the courts in that case calculate damages according to the ordinary principles and allow only reasonable compensation
- Under the **Indian Law, Section 74 does away with the distinction between 'liquidated damages' and 'penalty'.** This Section lays down that the courts are not bound to treat the sum mentioned in the contract either by way of liquidated damages or penalty as the sum payable as damages for breach. Instead the courts are required to allow reasonable compensation so as to cover the actual loss sustained, not exceeding the amount so named in the contract.
- Thus, according to the Section, **the named sum, regardless whether it is a penalty or not, determines only the maximum limit of liability in case of the breach of contract.** 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.
- **Exception:** Where any **person gives any bond to the Central or State government for the performance of any public duty** or act in which the public are interested, on breach of the condition of any such instrument, he shall be liable to pay the whole sum mentioned therein.

**How to Calculate the Damage**

In case of a contract for sale of good,

- (i) where the **buyer breaks the contract**, the damages would be the **difference between contract price and market price as on the date of breach,**
- (ii) where the **seller breaks the contract**, the buyer can recover the **difference between market price and contract price as on date of breach.**

Any subsequent increase or decrease in the market price would not be taken note of.

**Duty to Mitigate Damage Suffered**

It is the duty of the injured party to mitigate damage suffered as a result of the breach of contract by the other party. He must use all reasonable means of mitigating the damage, just as a prudent man would under similar circumstances in his own case **He cannot recover any part of the damage traceable to his own neglect to mitigate**

**Cost of Suit**

The aggrieved party is entitled in **addition to the damages** to get the costs of getting the decree for damages from the defaulter party. The cost of suit for damages is in the **discretion of the court.**

LIQUIDATED DAMAGES vs PENALTY

Basis	Liquidated Damages	Penalty
1. Meaning	If the sum payable by the defaulting party in case of breach of a contract (as specified in the contract) represents a fair and genuine pre- estimate of the damages likely to result due to breach, such specified sum is called as liquidated damages. Thus, liquidated damages are based on probable loss.	If the sum payable by the defaulting party in case of breach of a contract (as specified in the contract) is not based on probable loss, and is disproportionate to the damages which are likely to result as a result of breach, such specified sum is called as penalty.
2. Purpose	Liquidated damages are imposed by way of compensation to the aggrieved party.	Penalty is imposed by way of punishment, so as to prevent a party from committing a breach
3. Validity in England	In England, liquidated damages are awarded in full (disregarding the actual damages suffered by the aggrieved party).	In England, no amount is awarded to any party, where a contract requires payment of penalty.
4. Validity in India	In India, the Courts do not differentiate between liquidated damages and penalty. Indian Courts restrict the damages to reasonable compensation so as to cover the actual loss suffered by aggrieved party (i.e. it is immaterial as to whether the specified sum is in the nature of liquidated damages or penalty).	

ORDINARY DAMAGES vs. LIQUIDATED DAMAGES

Basis	Ordinary Damages	Liquidated Damages
1. Meaning	Ordinary damages are determined by the Court. Ordinary damages are not specified by the parties in the contract. Ordinary damages means such damages as may fairly and reasonably be considered as arising naturally from the breach of contract.	If the sum payable by the defaulting party in case of breach of a contract (as specified in the contract) represents a fair and genuine pre- estimate of the damages likely to result due to breach, such specified sum is called as liquidated damages. Thus, liquidated damages are based on probable loss.
2. Purpose	The purpose of awarding damages is to compensate the loss caused to the aggrieved party.	The purpose of specifying the liquidated damages is to avoid uncertainty and expenses of proving damages in the Court.
3. Effect	The actual loss suffered by the aggrieved party due to breach of contract is allowed in the form of compensation, i.e., ordinary damages are allowed.	The liquidated damages act as a ceiling, i.e., the aggrieved party shall be allowed actual loss suffered by him or liquidated damages, whichever is less.

Compiled By: CA Sahil Grover

3. SUIT FOR SPECIFIC PERFORMANCE

- Specific performance means the **actual carrying out of the contract as agreed**. Under certain circumstances an aggrieved party may file a suit for specific performance i.e. for a decree by the court directing the defendant to actually perform the promise that he has made. Such a suit may be filed either instead of or in addition to a suit for damages.
- A decree for specific performance is **not granted for contracts of every description**. It is only **where it is just and equitable so to do**. i.e. where the legal remedy is inadequate or defective that the courts issue a decree for specific performance. It is usually granted in contracts connected with **land, buildings, rare articles and unique goods having some special value** to the party suing because of family association.
- Specific performance is **not granted, as a rule, in the following cases**:
  - o Where **monetary compensation is an adequate relief**. Thus the courts refuse specific performance of a contract to lend or to borrow money or where the contract is for the sale of goods easily procurable elsewhere.
  - o Where the **contract is for personal services** e.g a contract to marry or to paint a picture. In such contracts 'injunction' is granted in place of specific performance

4. SUIT FOR INJUNCTION

- 'Injunction' is an **order of a court restraining a person from doing a particular act**. It is a mode of securing the specific performance of the negative terms of the contract.
- To put it differently, where a party is in breach of negative term of the contract (i.e. where he is doing something which he promised not to do) the **court may by issuing an injunction restraint him from doing what he promised not to do**.
- Thus 'injunction' is a preventive relief

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5. SUIT UPON QUANTUM MERUIT

- Quantum Meruit i.e. **as much as the party doing the service has deserved**
  - Where one person has rendered service to another in circumstances which indicate an understanding between them that it is to be paid for although no particular remuneration has been fixed, the law will infer a promise to pay. It covers a case where the party injured by the breach had at time of breach done part but not all of the work which he is bound to do under the contract and seeks to be compensated for the value of the work done.
  - **For the application of this doctrine, two conditions must be fulfilled**:
    1. **It is only available if the original contract has been discharged.**
    2. **The claim must be brought by a party not in default.**
  - The object of allowing a claim on quantum meruit is to recompensate the party or person for value of work which he has done
- The claim for quantum meruit arises in the following cases:**
- a) When an agreement is discovered to be void or when a contract becomes void.
  - b) When something is done without any intention to do so gratuitously.
  - c) When one party abandons or refuses to perform the contract
  - d) Where there is an express or implied contract to render services but there is no agreement as to remuneration.
  - e) Where a contract is divisible and the party not in default has enjoyed the benefit of part performance.
  - f) When an indivisible contract for a lump sum is completely performed but badly the person who has performed the contract can claim the lump sum, but the other party can make a deduction for bad work

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# SPECIAL CONTRACTS



# INDEMNITY AND GUARANTEE (Chart 1.19)

## CONTRACT OF INDEMNITY

## CONTRACT OF GUARANTEE

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### Definition: Sec 124

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 other person** is called a "contract of indemnity". This is also known as typical form of contingent contract.

### RIGHTS OF INDEMNITY HOLDER - Sec 125

- a) **Right to recover damages:**  
He has the right to recover all the damages which he is compelled to pay in any suit in respect of any matter covered by the contract of indemnity.
- b) **Right to recover cost of suit:**  
He has the right to recover all the costs which he is compelled to pay, in bringing or defending such suit.
- c) **Right to recover sums paid as a compromise of the suit:**  
He has the right to recover all the sums which he has paid under the terms of a compromise of such suit.

### Definition:

A contract of guarantee is a contract to perform the promise made or discharge liability incurred by a third person in case of his default.

### Parties to contract:

- 1) **Surety**- person who gives the guarantee.
- 2) **Principal debtor**- person in respect of whose default the guarantee is given.
- 3) **Creditor**- person to whom the guarantee is given.

### Modes of guarantee:

Oral or written.

### ESSENTIALS AND LEGAL RULES FOR A VALID CONTRACT OF GUARANTEE

- 1) **Purpose:**
  - The purpose of a guarantee being to secure the payment of a debt, the existence of recoverable debt is necessary.
  - If there is **no principal debt, there can be no valid guarantee.**
- 2) **Consideration:**
  - A guarantee without consideration is void, but there need be no direct consideration between the surety and the creditor.
  - Even if the principal debtor is incompetent to contract, the guarantee is valid. But, if surety is incompetent to contract, the guarantee is void.
- 3) **Existence of a liability:**
  - There must be an existing liability or a promise whose performance is guaranteed.
  - The liability must be legally enforceable and not time barred.
- 4) **No misrepresentation or concealment:**
  - Any guarantee obtained by misrepresentation made by the creditor, or with his knowledge and assent, is invalid. (Sec 142)
  - Any guarantee which the creditor has obtained by means of keeping silence as to material circumstances, is invalid. (Sec 143)
- 5) **Writing not necessary:**  
Sec 126 expressly declares that a guarantee may be either oral or written.
- 6) **Must be conditional:**
  - The liability of surety is secondary and conditional.
  - The liability of surety arises only if the principal debtor makes a default.
- 7) **Joining of other Co-sureties:**  
Where a person gives a guarantee upon a contract that the creditor shall not act upon it until another person has joined in it as co-surety, the guarantee is not valid if that other person does not join. (Sec 144)
- 8) **Must have all the essentials of a valid contract:**
  - All the essentials of a valid contract must be present in the contract of guarantee.
  - **Exceptions:** Consideration received by the principal debtor is a sufficient consideration to the surety for giving the guarantee.

### NATURE AND EXTENT OF SURETY'S LIABILITY

- 1) **Surety's liability is coextensive with liability of principal debtor (Sec 128):**
  - The phrase "co-extensive with that of the principal debtor" shows the quantum of the surety's liability.
  - Accordingly the quantum of obligation of a surety is the same as that of a principal debtor unless there is a contract to the contrary. It will be neither more nor less although by a special contract it may
  - be made less than that of the principal debtor but never greater.
  - Where a debtor cannot be held liable on account of any defect in the document, the liability of the surety also ceases.
- 2) **Liability of surety is secondary and conditional:**  
Liability of a surety is secondary or contingent i.e. the surety is liable only on default of the principal debtor. Thus if the surety becomes insolvent before default by the principal debtor, the creditor cannot prove against the surety's "official receiver" in insolvency.
- 3) **Commencement of surety's liability:**
  - The liability of surety arises immediately on default by the principal debtor.
  - The creditor is not required to-
    - (a) first sue the principal debtor; or
    - (b) first give a notice to the principal debtor.
  - Where a creditor holds securities from the principal debtor for his debt the creditor need not first resort to these securities before suing the surety unless otherwise agreed.
- 4) **Surety's liability may be limited:**  
The surety may fix a limit on his liability upto which the guarantee shall remain effective.
- 5) **Surety's liability may be continuous:**
  - Surety may agree to become liable for a series of transactions of continuous nature.
  - However, the surety may fix -
    - (a) a limit on his liability upto which the guarantee shall remain effective;
    - (b) a time period during which the guarantee shall remain effective.
- 6) **Surety's liability may be conditional:**  
Surety may impose certain conditions in the contract of guarantee. Until those conditions are met, the surety shall not be liable.

### ESSENTIAL ELEMENTS OF CONTRACT OF INDEMNITY

- 1) All the essential elements of a valid contract must be present in a contract of indemnity. An indemnity given under coercion or for an illegal object cannot be enforced.
- 2) **Loss to one party:**  
In a contract of indemnity, a person (indemnifier) agrees to indemnify another person (indemnity holder) in case such other person incurs some loss or loss of such other person becomes certain.
- 3) **Indemnity by the promisor:**  
The purpose of contract of indemnity is to protect the indemnity holder from any loss that may be caused to him.
- 4) **Reason for loss:**  
The contract of indemnity must specify that indemnity holder shall be protected from the loss caused due to
  - Action of the promisor himself; or
  - Action of any other person;
 Thus, loss occasioned by the conduct of the promisee or accident or an act of God is not covered.

### Condition for (b) & (c):

- Indemnifier authorised him to bring or defend the suit; or
- Indemnity holder did not contravene the orders of the indemnifier and the indemnity holder acted as it would have been prudent for him to act in the absence of any contract of indemnity.

### TIME OF COMMENCEMENT OF INDEMNIFIER'S LIABILITY

The Indian Contract Act is silent on this point. It has been held that the indemnified can compel the indemnifier to make good his loss even before he has actually discharged his liability, provided his liability has become absolute.

**"Indemnity is not necessarily given by repayment after payment. Indemnity requires that the party to be indemnified shall never be called upon to pay."**

### TRIPARTITE AGREEMENT

- In a contract of guarantee there are 3 separate contracts
- one between the principal debtor and the creditor. (Primary contract)
  - The second between the creditor and the surety. (Secondary Contract) and
  - the third between the surety and the principal debtor wherein the principal debtor requests the surety to act as surety and impliedly promises to indemnify the surety in case the surety incurs liability. (Implied Contract)

Sec 145 'in every contract of guarantee there is an implied promise by the principal debtor to indemnify the surety and the surety is entitled to recover from the principal debtor whatever sum he has rightfully paid under the guarantee but no sum which he has wrongfully paid.'

### CONSIDERATION FOR GUARANTEE [Sec 126]

Sec 127 expressly provides and states that "anything done, or any promise made, for the benefit of the principal debtor, may be a sufficient consideration to the surety for giving the guarantee."

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# INDEMNITY AND GUARANTEE (Chart 1.20)

TYPES OF GUARANTEE	DISCHARGE OF A SURETY FROM LIABILITY		Compiled By:CA Sahil Grover	
<p><b>1) Specific Guarantee:</b> A guarantee which extends to a single debt/ specific transaction is called a specific guarantee. The surety's liability comes to an end when the guaranteed debt is duly discharged or the promise is duly performed.</p> <p><b>2) Continuing Guarantee [Sec 129]:</b> A guarantee which extends to a series of transaction is called a continuing guarantee. A surety's liability continues until the revocation of the guarantee.</p>	<p style="text-align: center;">(1) BY REVOCATION OF THE CONTRACT OF GUARANTEE</p>	<p style="text-align: center;">(2) BY CONDUCT OF THE CREDITOR</p>	<p style="text-align: center;">(3) BY INVALIDATION OF THE CONTRACT OF GUARANTEE</p>	
<p><b>CONTINUING GUARANTEE</b> [Sec 129,130 &amp; 131]</p>	<p><b>a) Notice of revocation by surety (Sec 130):</b></p> <ul style="list-style-type: none"> <li>• <b>Specific guarantee-</b> It can't be revoked once it is acted upon. Thus, it can be revoked only if liability to principal debtor has not accrued.</li> <li>• <b>Continuing guarantee-</b> It can be revoked only in respect of future transactions.</li> </ul> <p><b>b) Death of surety (Sec 131):</b></p> <ul style="list-style-type: none"> <li>• Death of the surety operates as a revocation of a continuing guarantee as to future transactions taking place after the death of surety.</li> <li>• However, the surety's estate remains liable for the past transactions which have already taken place before the death of the surety.</li> </ul> <p><b>c) By novation (Sec 62):</b> The surety under original contract is discharged if a fresh contract is entered into either between the same parties or between the other parties, the consideration being the mutual discharge of the old contract.</p>	<p><b>a) Variance in terms (Sec 133):</b></p> <ul style="list-style-type: none"> <li>• If subsequent to formation of contract, any variation made in the terms and conditions of contract of guarantee without the consent of surety then the surety shall be released for such transactions as take place after such variation.</li> <li>• Accepting further security for the same debt is not treated as variance in terms of contract.</li> </ul> <p><b>b) Release or discharge of principal debtor (Sec 134):</b> If-</p> <ul style="list-style-type: none"> <li>• the creditor makes a fresh contract with the principal debtor whereby the principal debtor is relieved from his liability; or</li> <li>• The creditor does any act or omission resulting in discharge of the principal debtor; Then the surety is discharged.</li> </ul> <p><b>c) Composition with principal debtor/ Not to sue the principal debtor/ Giving extension of time to principal debtor (Sec 135):</b></p> <ul style="list-style-type: none"> <li>• <b>Composition:</b> If the creditor makes a composition with the principal debtor, without consulting the surety, the latter is discharged. Composition inevitably involves variation of the original contract, and, therefore, the surety is discharged.</li> <li>• <b>Promise to give time:</b> When the time for the payment of the guaranteed debt comes, the surety has the right to require the principal debtor to pay off the debt. Accordingly, it is one of the duties of the creditor towards the surety not to allow the principal debtor more time for payment.</li> <li>• <b>Promise not to sue:</b> If the creditor under an agreement with the principal debtor promises not to sue him, the surety is discharged. <b>Cases where surety not discharged:</b></li> </ul> <ol style="list-style-type: none"> <li>1) Where a contract to give time to the principal debtor is made by the creditor with a third person, and not with the principal debtor, the surety is not discharged. [Sec 136]</li> <li>2) Mere forbearance on the part of the creditor to sue the principal debtor or to enforce any other remedy against him does not in the absence of any provision in the guarantee to the contrary, discharge the surety. [Sec 137]</li> </ol>	<p><b>d) Release by creditor of one of the co-sureties (Sec 138):</b> Where there are co-sureties, a release by the creditor of one of them does not discharge the others neither does it free the surety so released from his responsibility to other sureties.</p> <p><b>e) Creditor's act or omission impairing surety's eventual remedy (Sec 139):</b></p> <ul style="list-style-type: none"> <li>• If the creditor does any act which is inconstant with right of the surety, or omits to do any act which is duty to the surety requires him to do, and the eventual remedy of the surety himself against the principal debtor is thereby impaired, the surety is discharged.</li> <li>• It is the duty of the creditor to do every act necessary for the protection of the rights of the surety and if he fails in this duty, the surety is discharged.</li> <li>• A surety is entitled after paying off the creditor, to his indemnity from the principal debtor. If the creditors act or omission deprives the surety of the benefit of this remedy, the surety is discharged.</li> </ul> <p><b>f) Loss of security by a creditor (Sec 141):</b></p> <ul style="list-style-type: none"> <li>• A surety is entitled to benefit of every security which the creditor has against the principal debtor at the time when the contract of suretyship was entered into, whether the surety knows of the existence of such security or not; and</li> <li>• if the creditor loses ;or</li> <li>• without the consent of the surety, parts with such security,</li> <li>• the surety is discharged to the extent the value of the security.</li> </ul> <p>The word "loss" here means loss because of carelessness or negligence. Thus if the security is lost due to an act of God or enemies of the state or unavoidable accident, the surety would not be discharged. Again if the securities lost or parted with were obtained afterwards as a further security, the surety would not be discharged.</p>	<p><b>a) Guarantee obtained by misrepresentation invalid (Sec 142):</b> Any guarantee which has been obtained by means of misrepresentation made by the creditor, or with his knowledge and assent, concerning a material part of the transaction, is invalid.</p> <p><b>b) Guarantee obtained by concealment invalid (Sec 143):</b> When the creditor has obtained any guarantee by means of keeping silence as to material circumstances. The expression "keeping silence" implies intentional concealment of a material fact, as distinct from a mere non-disclosure thereof. There must exist some element of fraud.</p> <p><b>c) Guarantee on contract that creditor shall not act on it until co-surety joins (Sec 144):</b> Where a person gives a guarantee upon a contract that the creditor shall not act upon it until another person has joined in it as co-surety, the guarantee is not valid if that other person does not join.</p>
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# INDEMNITY AND GUARANTEE (Chart 1.21)

RIGHTS OF SURETY			LIABILITY OF TWO PERSONS, PRIMARILY LIABLE, NOT AFFECTED BY ARRANGEMENT BETWEEN THEM THAT ONE SHALL BE SURETY ON OTHER'S DEFAULT [SEC 132]	CONTRACT OF INDEMNITY vs. CONTRACT OF GUARANTEE								
RIGHTS AGAINST THE PRINCIPAL DEBTOR	RIGHTS AGAINST THE CREDITOR	RIGHTS AGAINST THE CO-SURETIES		Basis	Contract of Indemnity	Contract of Guarantee						
<p><b>1) Right of indemnity (Sec 145):</b></p> <ul style="list-style-type: none"> <li>In every contract of guarantee, there is an implied promise by the principal debtor to indemnify the surety.</li> <li>The surety is entitled to claim from the principal debtor all the sums which he has rightfully paid.</li> <li>The surety cannot recover such sums, which he has paid wrongfully.</li> <li>The surety cannot claim more than what he has actually paid to the creditor.</li> <li>Actual payment either in cash or by transfer of property is essential for asking the principal debtor to pay.</li> </ul> <p><b>2) Right of subrogation (Sec 140):</b></p> <ul style="list-style-type: none"> <li>When the surety pays off the debt on default of the principal debtor, he is invested with all the rights which the creditor had against the principal debtor.</li> <li>The surety steps into the shoes of the creditor and is entitled to all the remedies which the creditor could have enforced against the principal debtor.</li> <li>The surety may therefore claim the securities, if any, held by the creditor and sue the principal debtor, or may claim dividend in insolvency of the debtor.</li> </ul>	<p><b>1) Right to claim securities (Sec 141):</b></p> <ul style="list-style-type: none"> <li>The surety can at the time of payment, claim all the securities which the creditor had at the time of giving of guarantee.</li> <li>It is immaterial as to whether the surety had knowledge of such securities or not.</li> <li>If the securities are returned by the creditor to the principal debtor without the consent of surety or the securities are lost due to negligence of the creditor, the surety is discharged to the extent of value of the securities so returned.</li> <li>If the security is lost due to an Act of God or enemies of State or Unavoidable accident, the surety would not be discharged.</li> </ul> <p><b>2) Right of set off:</b></p> <p>If the creditor sues the surety, for payment of principal debtor's liability, the surety may have the benefit of the set off, if any, that the principal debtor had against the creditor.</p> <p><b>3) Right to share reduction:</b></p> <p>The surety has right to claim proportionate reduction in his liability if the principal debtor becomes insolvent.</p>	<ul style="list-style-type: none"> <li>Where a debt is guaranteed by more than one sureties, they are called co-sureties.</li> <li>In such a case all the co-sureties are liable to contribute towards the payment of the guaranteed debt as per agreement among them.</li> <li>If one of the co-sureties is compelled to pay the entire debt, he has a right of contribution from the other co-surety or co-sureties.</li> </ul> <div style="background-color: #d9534f; color: white; text-align: center; padding: 2px;"><b>RULES OF CONTRIBUTION</b></div> <p><b>1) Co-sureties liable to contribute equally (Sec 146):</b></p> <p>Sec 146 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".</p> <p><b>2) Liability of co-sureties bound in different sums (Sec 147):</b></p> <p>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.</p>	<p>Where two persons contract with a third person to undertake a certain liability, and also contract with each other that one of them shall be liable only on the default of the other, the third person not being a party to such contract the liability of each of such two persons to the third person under the first contract is not affected by the existence of the second contract, although such third person may have been aware of its existence.</p>	<p><b>Number of Parties to the contract</b></p> <p>2 parties namely the indemnifier [promisor] and the indemnified [promisee]</p>	<p><b>Number of contract(s)</b></p> <p>1 contract</p>	<p><b>3 parties</b> namely the creditor, principal debtor and surety</p> <p>3 contract; first between principal debtor and creditor, second between creditor and surety, and third between surety and principal debtor</p>	<p><b>Nature of liability</b></p> <p>The liability of the indemnifier is <b>primary and unconditional</b></p> <p>The liability of the surety is <b>secondary and conditional</b> as the primary liability is that of the principal debtor</p>	<p><b>Time of liability</b></p> <p>The liability of the indemnifier arises only on the <b>happening of a contingency</b></p> <p>The liability arises only on the <b>non-performance of an existing promise or non-payment of an existing debt.</b></p>	<p><b>Request to Act</b></p> <p>The indemnifier need not act at the request of indemnity holder</p> <p>The surety acts at the request of principal debtor</p>	<p><b>Right to sue third party</b></p> <p>Indemnifier cannot sue a third party for loss in his own name as there is no privity of contract. Such a right would arise only if there is an assignment in his favour</p> <p>Surety can proceed against principal debtor in his own right because he gets all the right of a creditor after discharging the debts</p>	<p><b>Purpose</b></p> <p>Reimbursement of loss</p> <p>For the security of the creditor</p>	<p><b>Competency to contract</b></p> <p>All parties must be competent to contract</p> <p>Where a minor is a principal debtor, the contract is still valid</p>

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# BAILMENT AND PLEDGE (Chart 1.22)

## CONTRACT OF BAILMENT

### Definition: Sec 148

- A 'bailment' is the **delivery of goods by one person to another** for some purpose, upon a contract that they shall, when the purpose is accomplished, be returned or otherwise disposed of according to the directions of the person delivering them.
- The person delivering the goods is called the "bailor".
- The person to whom they are delivered is called the "bailee".
- Examples:** hiring of goods, furniture, cycle, car, delivering of cloth to a tailor for making a suit, delivering a watch or scooter for repair, depositing goods for safe custody, etc.
- Explanation:** If a person already in possession of the goods of another contracts to hold them as a bailee, he thereby becomes the bailee, and the owner becomes the bailor of such goods, although they may not have been delivered by the way of bailment.

## ESSENTIAL ELEMENTS OF CONTRACT OF INDEMNITY

- Contract:** Bailment is based upon a contract. The contract may be express or implied. No consideration is necessary to create a valid contract of bailment.
- Delivery of goods:** It involves the delivery of goods from one person to another for some purposes. Bailment is only for moveable goods and never for immovable goods or money.
- Purpose:** The goods are delivered for some purpose. The purpose may be express or implied.
- Possession:** In bailment, possession of goods changes. Change of possession can happen by physical delivery or by any action which has the effect of placing the goods in the possession of bailee.
- Return of goods:** Bailee is obliged to return the goods physically to the bailor. The goods should be returned in the same form as given or may be altered as per bailor's direction.

## HOW THE DELIVERY TO BAALEE IS EFFECTED?

- As per Sec 149 the delivery to the bailee may be made by doing anything which has the effect of putting the goods in the possession of the intended bailee or of any person authorized to hold them on his behalf.
- The delivery of goods may be either 'actual' or 'constructive'.
- When the bailor hands over to the bailee physical possession of the goods, that is called 'actual delivery'. 'Constructive delivery', on the other hand, does not involve handing over the physical possession but something is done which has the effect of putting the goods in the possession of the 'bailee'.

## TYPES OF BAILMENT

### On the basis of benefit:

- For the exclusive benefit of bailor
- For the exclusive benefit of bailee
- For mutual benefit of bailor and bailee:

### On the basis of reward:

#### a) Gratuitous Bailment:

- Gratuitous bailment is one when the provider of service does it gratuitously i.e. free of charge. Such bailment would be either for the exclusive benefits of bailor or bailee.

#### b) Non-Gratuitous Bailment:

- Non gratuitous bailment means where both the parties get some benefit i.e. bailment for the benefit of both bailor & bailee.
- In the case of non-gratuitous bailment, some charges are paid by the bailee or by the bailor.  
**Examples:** giving the cycle on hire, payment of charges for the safe custody of goods in a godown.

## DUTIES OF BAILOR

### 1) Duty to disclose fault in goods (Sec 150):

#### a) Gratuitous bailment:

- Disclosure-** bailor is liable to disclose all the faults known to him which are material for use of the goods or may put the bailee to extraordinary risks.
- Effect of non-disclosure-** bailor shall be liable for damages for any loss caused to the bailee resulting directly from the faults known to him but not disclosed to the bailee. The bailor shall not be liable for damages arising to bailee from the defects of which the bailor was ignorant.

#### b) Non-Gratuitous bailment:

- Disclosure-** bailor is liable to disclose all the faults whether known to him or not.
- Effect of non-disclosure-** bailor shall be liable for damages for any loss caused to the bailee whether or not he was aware of the faults.

**Note:** If goods are of dangerous nature there is duty of disclose

### 2) Pay expenses (Sec 158):

#### a) Extraordinary Expenses:

- Bailor is liable to pay the extraordinary expenses. It is immaterial as to whether the bailment is gratuitous or non-gratuitous.

#### b) Ordinary Expenses:

- Bailee is not liable to pay the ordinary expenses.
- If bailment is gratuitous the bailor is liable to pay the ordinary expenses.

### 3) Indemnify the bailee for pre mature termination (Sec 159):

If the bailment is gratuitous and for a specific period then -

- the bailor may compel the bailee to return the goods before expiry of the period of bailment ;but
- the bailor shall indemnify the bailee for any loss incurred by the bailee.

### 4) Indemnify the bailee for defective title (Sec 164):

Bailor shall indemnify the bailee for any loss caused to bailee due to defective title of bailor.

### 5) Receive back the goods :

- It is the duty of the bailor to receive back the goods when returned by bailee after bailment expires. If he wrongfully refuses to receive back the goods he shall be liable to pay ordinary expenses of custody of goods

## DUTIES OF BAALEE

### 1) Take reasonable care (Sec 151 & 152):

- Bailee must take such care of goods as a man of ordinary prudence would under similar circumstances, take of his own goods.
- Bailee shall not be liable for any loss or destruction of goods if -
  - He is not negligent i.e. he has taken reasonable care or
  - The loss was caused due to an act of God or other unavoidable reasons.

### 2) Not to make unauthorized use of goods (Sec 153 & 154):

If the bailee makes an inconsistent use of goods then-

- The bailment becomes voidable at the option of the bailor (Sec 153) and
- The bailee shall be liable for any loss or damage even if such a loss is caused due to an act of God or other unavoidable reasons.

### 3) Not to mix goods (Sec 155, 156 & 157):

a) **Goods are mixed with bailor's consent-** The parties shall have a proportionate interest in such mixture.

b) **Goods are mixed without bailor's consent, but the goods are separable-** The bailee shall pay the expenses of separation and any damages incurred by the bailor.

c) **Goods are mixed without bailor's consent, and goods are not separable-** The bailee shall compensate the bailor for any loss caused to him.

### 4) Return the goods (Sec 160 & 161):

- Bailee must return the goods without waiting for demand from bailor if -
  - the time specified in the contract has expired or
  - the purpose specified in the contract is accomplished.
- If the goods are not returned, then-
  - the goods shall be at the risk of the bailee
  - the bailee shall be liable for any loss or damages.
- When there are several joint bailors, the bailee may return the goods to any one of the joint owners. (Sec 165)

### 5) Return accretion (Sec 163):

Bailee must return to the bailor any increase or profit or accretion (i.e. addition) to the goods bailed.

### 6) Not to setup Adverse Title:

Bailee must not set up a title adverse to that of the bailor. He must hold the goods on behalf of and for the bailor. He cannot deny the title of bailor.

## RIGHTS OF BAILOR

### a) Termination the bailment (Sec 153):

If the bailee does any act inconsistent with the terms and conditions of the contract of bailment then the bailment becomes voidable at the option of the bailor.

### b) Demand back the goods (Premature Termination) (Sec 159):

When the goods are lent gratuitously, the bailor can demand back the goods at any time even before the expiry of the time fixed or the achievement of the object. However, due to the premature return of the goods, if the bailee suffers any loss, the bailor has to compensate the bailee.

### c) File suit against wrongdoer (Sec 180 & 181):

Bailor has the right to sue -

- A third party who does any damages to the goods ; or
- A third party who deprives the bailee from using the goods;
- Both bailor and bailee have right to sue a third party who has deprived the bailee to the use or possession of goods bailed.
- Any relief obtained can be shared between the bailor and bailee according to their respective interest.

### d) Sue the bailee for enforcement of his duties:

The bailor may sue the bailee to enforce his duties like:

- right to claim damages for loss caused to the goods by the negligence of bailee;
  - right to claim compensation for loss caused by an unauthorized use of the goods bailed;
  - right to claim damages arising out of mixing the goods of the bailor with his own goods;
  - right to claim the increase of profit from the goods bailed which may have occurred from the goods value;
  - right to demand back goods.
- e) **Right to compensation:**  
If any damage is caused to the goods bailed because of the unauthorized use or mixing of the goods, the bailor has a right to claim compensation.

# BAILMENT AND PLEDGE (Chart 1.23)

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## RIGHTS OF BAILEE

### 1) Right to deliver the goods to any one of Joint Bailors (Sec 165):

If several joint owners bailed the goods, the bailee has a right to deliver them to any one of the joint owners unless there was a contract to the contrary.

### 2) Right to indemnity (Sec 164):

Bailee is entitled to be indemnified by the bailor for any loss arising to him by reasons that the bailor was not entitled to make the bailment or to receive back the goods or to give directions in respect to them.

### 3) Right to claim extraordinary expenses (Sec 158):

In case bailee is required to incur any extraordinary expenses, he can hold the bailor liable for such expenses.

### 4) Right to Apply to Court to Decide the Title to the Goods [Sec 167]:

If the goods bailed are claimed by the person other than the bailor, the bailee may apply to the court to stop its delivery and to decide the title to the goods.

### 5) Right to claim compensation in case of faulty goods (Sec 150):

- A bailee is entitled to receive compensation from the bailor for any loss caused to him due to the failure of the bailor to disclose any faults in the goods known to him.
- If the bailment is for hire, bailor will be liable to compensate even though he was not aware of the existence of such faults.

### 6) File suit against wrongdoer (Sec 180):

The bailee has the right to sue-

- A third party who does any damages to the goods ;or
- A third party who deprives the bailee from using the goods.

### 7) Right of Lien (Sec 170 & 171):

Bailee has the right to retain the goods delivered to him until the charges due to him are paid by the bailor.

## GENERAL LIEN AND PARTICULAR LIEN

- 'Particular lien' means the right to retain only that particular property in respect of which the charge is due
- 'General lien' means the right to retain all the goods of the other party until all the claims of the holder against the party are satisfied. In other words, this is a right to retain the goods of another as a security for a general balance of account.

### Bailee's particular lien

Sec 170 confers the right of particular lien upon a bailee and provides that "where the bailee has in accordance with the purpose of the bailment rendered any service involving the exercise of labour or skill in respect of the goods bailed, he has in the absence of a contract to the contrary, a right to retain such goods until he receives due remuneration for the services he has rendered in respect of them"

**Thus a bailee has a particular lien when the following conditions are fulfilled:**

- The bailee must have rendered some service in relation to the thing bailed and must be entitled to some remuneration for it which must not have been paid.
- The service rendered by the bailee must be one involving the exercise of labour or skill in respect of the goods bailed so as to confer an additional value on the article
- The services must have been performed in full in accordance with the directions of the bailor within the agreed time or a reasonable time.
- There must not be an agreement to perform the service on credit.
- The goods must be in possession of the bailee. If possession is lost, lien is also lost.
- There must not be a contract to the contrary.

### Notes:

- The bailee retaining the article to enforce his lien cannot charge for keeping it.
- The bailee cannot exercise his lien for the non-payment of extraordinary expenses incurred in relation to the thing bailed. He should sue for them.

### Bailee's general lien

Acc. to Sec 171, bailees coming within the following categories have a 'general lien' in the absence of a contract to the contrary: Bankers, factors, wharfingers, policy brokers and attorneys of law have general lien in respect of goods which come into their possession during the course of their profession.

## GENERAL LIEN vs PARTICULAR LIEN

General lien	Particular lien
Sec 171 of the Indian Contract Act, 1872 confer on Bailee the right of General Lien.	Sec 170 of the Indian Contract Act, 1872 confers on the Bailee, the right of particular lien.
General lien alludes to the right to keep possession of goods belonging to other against general balance of account.	Particular lien implies a right of the bailee to retain specific goods bailed for non-payment of amount.
It is not automatic but is recognized through on agreement. It is exercised by the bailee only by name.	It is automatic.
It can be exercised against goods even without involvement of labour or skill.	It comes into play only when some labour or skill is involved has been expended on the goods, resulting in an increase in value of goods.
Only such persons as are specified u/s 171, eg, Bankers, factors, wharfingers, policy brokers etc. are entitled to general lien.	Bailee, finder of goods, pledgee, unpaid seller, agent, partner etc are entitled to particular lien.

## GRATUITOUS BAILMENT vs NON-GRATUITOUS BAILMENT

Basis	Gratuitous Bailment	Non-Gratuitous Bailment
Meaning	Bailment without any charge or reward is gratuitous bailment	Bailment in which charges paid either by the bailee or the bailor in consideration of goods is called a non-gratuitous bailment
Consideration	No consideration is present	Consideration is always present
Liability for disclosure of undisclosed faults	Bailor is liable to disclose only such faults as known to him	Bailor is liable to disclose all faults whether known to him or not
Duty to pay ordinary necessary expense	Bailor is liable to reimburse to bailee all the necessary expenses incurred by bailee	Bailee is not entitled to recover any necessary/ordinary expenses incurred by him
Right of pre-mature termination of bailment	Bailor has the right to terminate the gratuitous bailment at anytime	Bailor has no right to terminate the non-gratuitous bailment before the expiry of period of bailment
Effects of Death of bailor or bailee	Death of bailor or bailee operates as automatic termination of gratuitous bailment	In case of non-gratuitous bailment, the bailment is not terminated by death of bailor or bailee.

## TERMINATION OF BAILMENT

### a) Expiry of fixed period:

If the period of bailment is fixed by the parties the bailment terminates on expiry of such fixed period.

### b) On fulfillment of the purpose:

If the goods were delivered for a specific purpose, a bailment shall terminate on the fulfillment of that purpose.

### c) By Notice:

- Where the bailee acts in a inconsistent manner, the bailor can always terminate the contract of bailment by giving a notice to the bailee.

- A gratuitous bailment can be terminated by the bailor at any time by giving a notice to the bailee.

However, the termination should not cause loss to the bailee in excess of the benefit derived by him. In case the loss exceeds the benefit derived by the bailee, the bailor must compensate the bailee for such a loss (Sec. 159)

### d) Death of bailor or bailee:

In case of gratuitous bailment the bailment terminates if the bailor or the bailee dies.

### e) Destruction of goods:

The bailment is terminated if the goods bailed are destroyed or there is a change in the nature of goods which makes it impossible to be used for the purpose of bailment.

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# BAILMENT AND PLEDGE (Chart 1.24)

## FINDER OF GOODS

Sec 71 clearly provides, "a person who finds goods belonging to another and takes them into his custody is subject to the same responsibility as a bailee."

## DUTIES OF FINDER

- (i) **Duty to find the true owner:**  
It is the duty of the finder to make reasonable efforts to find the true owner of the goods. If the finder fails in this duty, he will be liable as a trespasser or a thief.
- (ii) **Duty to take reasonable care of the goods as a bailee:**  
A finder must take as much care of the goods as a man of ordinary prudence would, under similar circumstances take of his own goods of the same description. If in spite of reasonable care, the goods are lost or destroyed he is not liable for any loss.

## RIGHTS OF FINDER

- 1) **Right to recover expenses (Sec 168):**  
Finder of goods has the right to recover the expenses voluntarily incurred by him for-
- Finding the true owner; and
  - Preserving the goods.
- Where the owner of goods refuses to pay compensation, 'finder' cannot sue for this compensation but, he has the right to retain the goods until he has been paid.
- 2) **Right to recover the reward (Sec 168):**  
He has a right to recover the reward declared by true owner for finding the goods.  
The right to receive reward is a primary and superior right and even more than the right to seek reimbursement of expenditure.
- 3) **Right of sale of Goods (Sec 169):**  
Finder has no right to sell the goods found in the normal course. However he has the right to sell the goods -
- if the real owner after reasonable efforts cannot be found or
  - if found the owner but he refuses to pay the lawful charges AND
- When the article is in danger of perishing and losing the greater part of the value; OR  
When the lawful charges of the finder amounts to 2/3<sup>rd</sup> or more of the value of the articles found.  
The true owner is however entitled to get the balance of sale proceeds (surplus, if any).
- 4) **Right to retain possession against everyone except the true owner:**  
No one except the real owner can claim possession of goods from the finder. If anybody deprives him of the possession of the goods, he can file a suit for damages for trespass.

## PLEDGE OR PAWN

**Definition:** "The bailment of goods as security for payment of a debt or performance of a promise is called 'pledge'. The bailor in this case is called the 'pawnor.' The bailee is called the 'pawnee' (Sec 172).

### Essentials of contract of pledge:

- There must be bailment for security for payment of debt/ performance of a promise.
- Goods must be the subject matter of the contract of pledge.
- The goods pledged must be in existence.
- There must be a delivery of goods from pawnor to pawnee.

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## RIGHTS OF PAWNEE

- a) **Retain the pledged goods (Sec 173):**  
Pawnee has the right to retain the goods pledged with him until he is paid -
- Money due under the pledge (or until the promise is performed)
  - Interest on debt and
  - Necessary expenses for preservation of goods.
- b) **Right of retainer for subsequent advances(Sec 174):**  
When the pawnee lends money to the same debtor after date of pledge without any further security the right of retainer over the pledged goods extends to subsequent advances.
- c) **Receive extraordinary expenses (Sec 175):**
- Pawnee has the right to recover extraordinary expenses incurred by him for preservation of goods pledged with him.
  - However he has no right to retain the goods but can sue the pawnor for recovery of such expenses in case of non payment of extraordinary expenses.
- d) **Right to sue the pawnor OR Rights to sell the goods (Sec 176):**  
If the pawnor fails to pay the debt or perform his promise, the pawnee has the right to-
- sue the pawnor and retain the goods pledged as a collateral security OR
  - sell the thing pledged after giving a reasonable notice to pawnor
- Conditions for sale of goods:**
- Pawnor has failed to pay the debt or perform his promise.
  - Pawnee has given a reasonable notice to the pawnor of his intention to sell the good.
  - Requirement of 'reasonable notice' is a statutory obligation and cannot be waived by an agreement.
  - A sale made without notice to pawnor is void, notwithstanding any contract to contrary
- Effect of sale of goods:**
- If sale proceeds < amount due- pawnee may recover the deficit from pawnor.
  - If sale proceeds > amount due- pawnee must pay the surplus to the pawnor.

## RIGHTS OF PAWNOR

- 1) **Redeem the goods pledged (Sec 177):**
- **Meaning of redemption:**  
Right to recover back the goods by making payment of the debt or performance of promise.
  - **Time for redemption:**  
Where time of redemption is fixed, the pawnor may exercise redemption
- a) within the time so fixed ; or  
b) Even after expiry of time so fixed, provided-
- The pawnee has not sold the goods and
  - The pawnor pays the pawnee all expenses arising on account of his default.
- 2) **Enforce Pawnee's duties:**  
Pawnor has right to enforce the duties of pawnee ,if the pawnee fails to fulfill his duties.
- 3) **Receive increase in goods:**  
Pawnor has the right to recover from pawnee any increase in goods pledged.
- 4) **Right to receive notice of sale:**  
In case of default by the pawnor to pay debt or perform his promise the pawnee has the right to sell the good, after giving a reasonable notice to the pawnor.If the pawnee fails to give notice ,the pawnor has the right to recover the loss incurred by him.
- 5) **Right to demand care of goods:**  
Pawnor has a right to demand a pawnee to take all reasonable care and preservation of the goods pledged.

## DUTIES OF PAWNOR

- a) **Pay the debt:**  
Pawnor is liable to pay the debt or perform his promise, as the case may be.
- b) **Pay deficit on sale:**  
If the pawnee sells the goods due to default by the pawnor, the pawnor must pay the deficit.
- c) **Pay extra ordinary expenses:**  
Pawnor is liable to pay to the pawnee any extraordinary expenses incurred by the pawnee for preservation of goods.
- d) **Disclose faults in goods:**  
Pawnor is liable to disclose all faults which may put pawnee to extraordinary risks.
- e) **Indemnify the Pawnee:**  
If loss is caused to the pawnee due to defect in pawnor's title to the goods the pawnor must indemnify the pawnee.

## DUTIES OF PAWNOR

- 1) **Not to use the goods/unauthorised use:**  
Pawnee has no right to use the goods unless authorized by pawnor.
- 2) **Return the goods:**  
Pawnee must return the goods if the Pawnor pays the debt or performs his promise.
- 3) **Take reasonable care:**  
Pawnee must take such care of goods pledged as a man of ordinary prudence would take care of his own goods.
- 4) **Not to mix goods:**  
Pawnee must not mix his own goods with the goods pledged.
- 5) **Return increase in goods:**  
Pawnee must return to the pawnor any accretion to the goods pledged with him.

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# BAILMENT AND PLEDGE

# CONTRACTS OF AGENCY

## PLEDGE BY NON OWNERS

## BAILMENT vs. PLEDGE

## AGENT AND PRINCIPAL (Sec 182)

## APPOINTMENT AND AUTHORITY OF AGENTS

- Pledge by mercantile agent (Sec 178):**  
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.  
The necessary conditions of validity under section 178 are as follows:
  - The person pledging the goods must be a mercantile agent.
  - He must be in possession either of the goods or the documents of title to goods.
  - Such possession must be with the consent of the owner.
  - Pledge must have been made in the ordinary course of business of a mercantile agent
  - Pledgee must act in good faith.
  - 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.
- Pledge by person in possession under voidable contract (Sec 178A):**  
When the pawnor has obtained possession of the goods pledged by him under a contract voidable u/s 19 or 19A, but the contract has not been rescinded at the time of the pledge, the pawnee acquires a good title to the goods provided he acts in good faith and without notice of the pawnor's defect of title.
- Pledge where pawnor has only a limited interest (Sec 179):**  
Where a person pledges goods in which he has only a limited interest i.e. pawnor is not the absolute owner of goods, the pledge is valid to the extent of that interest. Thus, a person having a lien over the goods may pledge them to the extent of his interest.
- Pledge by a co-owner in possession:**  
Where the goods are left in the possession of one of the co-owners with the consent of other owners. Such a co-owner may make a valid pledge of the goods in his possession.
- Pledge by seller or buyer in possession:**  
A seller, in whose possession, the goods have been left after sale or a buyer who with the consent of the seller, obtains possession of the goods, before sale, can make a valid pledge provided the pawnee acts in good faith and he has no knowledge of the defect in title of the pawnor.

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Basis	Bailment	Pledge
<b>Meaning</b>	Transfer of goods by one person to another for some specific purpose	Transfer of goods from one person to another as security for repayment of debt
<b>Terms Applicable</b>	<u>"Bailor"</u> person delivering the goods under a contract of bailment. <u>"Bailee"</u> person to whom the goods are delivered under a contract of bailment.	<u>"Pawnor"</u> person who delivers the good as security. <u>"Pawnee"</u> person to whom the goods are delivered as security.
<b>Purpose</b>	Any purpose as specified in the contract of bailment, eg: for safe custody, for repairs, for processing of goods.	Delivering the goods as security for repayment of debt or performance of promise
<b>Consideration</b>	Bailment may be made for consideration or without consideration	Pledge is always made for a consideration.
<b>Right to sell the goods</b>	Bailee has no right to sell the goods even if the charges of bailment are not paid to him The bailee's rights are limited to suing the bailor for his dues or to exercise lien on the goods bailed	Pawnee has right to sell the goods if the pawnor fails to redeem the goods
<b>Right to use of goods</b>	Bailee can use the goods only for a purpose specified in the contract and not otherwise	Pledgee or Pawnee cannot use the goods pledged

- Agent-** is a person employed to do any act for another or to represent another in dealings with third persons.
- Principal** is a person for whom such act is done, or who is represented.
- Agency-** contract which creates the relationship of 'principal' & 'agent'.

## GENERAL RULES OF AGENCY

- Whatever a person competent to contract may do by himself, he may do through an agent, except for acts involving personal skill and qualifications.
- He, who does through another, does by himself.** This Rule of Agency is based on the maxim "Quit facit per alium, facit per se" i.e., he who acts through an agent is himself acting".

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## TEST OF AGENCY

- Whether the person has the capacity to bind the principal and make him answerable to the third party.
  - Whether he can establish Privity of Contract between the principal and third parties.
- If the answer to these questions is in affirmative (Yes), then there is a relationship of agency.

## SALIENT FEATURES OF AGENCY

- Basis:**  
The basic essence of 'agency' is that the principal is bound by the acts of the agent and is answerable to third parties.
- Consideration not necessary:**  
Unlike other regular contracts, a contract of agency does not need consideration. In other words, the relationship between the 'principal' and 'agent' need not be supported by consideration.
- Capacity to employ an agent:**  
A person who is competent to contract alone can employ an agent. In other words, principal must be a major and of sound mind.
- Capacity to be an agent:**  
Any person can be an agent. Thus even a minor or a person of unsound mind can be appointed as an agent and therefore his contractual capacity is immaterial.

## Who may employ an agent?

According to Sec 183, "any person who is of the age of majority according to the law to which he is subject, and who is of sound mind, may employ an agent." Thus a minor or a person of unsound mind cannot appoint an agent.

## Who may be an agent?

Sec 184 provides that "as between the principal and third persons any person may become an agent, but no person who is not of the age of majority and of sound mind can become an agent, so as to be responsible to his principal according to the provisions in that behalf herein contained"

Since, agent is a mere connecting link between the principal and the third party, it is immaterial whether or not the agent is legally competent to contract. Thus, there is no bar to the appointment of a minor as an agent. However, in considering the contract of agency itself (i.e. the relation between principal and agent), the contractual capacity of the agent becomes important.

Thus, if the agent happens to be a person incapable of contracting, then the principal cannot hold the agent liable, in case of his misconduct or where the agent has been negligent in performance of his duties.

## Consideration Not Necessary

Acc. to Sec 185, no consideration is necessary to create an agency. The acceptance of the office of an agent is regarded as a sufficient consideration for the appointment.



## MODES OF CREATION OF AGENCY

### a) Agency by express agreement (Sec 187):

Normally agency is created by an **express agreement**, specifying the scope of the authority of agent. The **agent may be appointed either by word of mouth or by an agreement in writing**. However in certain cases, e.g. to execute a deed for sale or purchase of land, the **agent must be appointed by executing a formal 'power of attorney' on a stamped paper**.

### b) Agency by ostensible authority/ implied agreement (Sec 187):

- Where the authority of the principal is **inferred by the conduct of the principal**, there the agency through ostensible authority is born. It arises when there is no express agreement appointing a person as an agent, but instead the existence of agency is **inferred from the circumstances of the case or from the conduct of the parties on a particular occasion or from the relationship between parties**. **Implied agency includes the following:**

### a) Agency by estoppel (Sec 237):

***When an agent has without authority done acts or incurred obligations to third persons on behalf of his principal the principal is bound by such acts or obligations if he has by his words or conduct induced such third persons to believe that such acts and obligations were within the scope of the agent's authority.***

**An agency by estoppel may be created when following essentials are fulfilled:**

- principal must have made a representation;
- representation may be express or implied;
- representation must state that the agent has an authority to do certain act although really he has no authority;
- principal must have induced the third person by such representation;
- third person must have believed the representation and made the contract on the belief of such representation.

A principal cannot privately revoke or restrict the authority of his agent, which he has allowed in public

### b) Agency by necessity:

An agency of necessity arises due to some emergent circumstances. In emergency a person is authorised to do what he cannot do in ordinary circumstances.

**To constitute an agency by necessity following conditions must be fulfilled:**

- agent should be in a position of not being able to communicate in time with the principal
- there must have been an actual and definite commercial necessity
- agent must have acted bonafide & for benefit of principal
- agent must have adopted most reasonable and practicable course of action.

**c) Agency by Operation of Law:** When law treats one person as an agent of other. For example, a partner is the agent of the firm for the purposes of the business of the firm.

### d) Agency By Ratification (Sec 196):

- Ratification means the **subsequent adoption and acceptance of an act originally done without instructions or authority**.
- Where acts are done by one person on behalf of another, but without his knowledge or authority, he may elect to ratify or to disown such acts. If he ratifies them, the same effects will follow as if they had been performed by his authority.
- If a person (pretended agent) acts on behalf of another person (alleged principal) without the knowledge or consent of the alleged principal and afterwards the alleged principal accepts such as act, then Agency by ratification comes in to existence.
- Ratification may be **express or implied**.

#### **EFFECT OF RATIFICATION**

- Principal is bound by acts ratified by him as if such acts had been performed by his authority.
- Ratification relates back to the actual date of the act that is ratified (i.e. retrospective effect) and not from the date when the act was ratified.

#### **RULES OF RATIFICATION/ ESSENTIALS OF VALID RATIFICATION**

- Ratification may be expressed or Implied (Sec 197):** Ratification may be expressed or may be implied in the conduct of the person on whose behalf the acts are done.
- Knowledge requisite for valid ratification (Sec 198):** No valid ratification can be made by a person whose knowledge of the facts of the case is materially defective.
- Effect of ratifying unauthorized act forming part of a transaction (Sec 199):** Principal cannot ratify a part of the transaction which is beneficial to him and reject the rest. There can be ratification of an act in entirety or its rejection in entirety.
- Ratification of unauthorized act cannot injure third person (Sec 200):** When the interest of third parties is affected, the principle of ratification does not apply. **An act done by one person on behalf of another, without such other person's authority, which, if done with authority, would have the effect of subjecting a third person to damages, or of terminating any right or interest of a third person, cannot, by ratification, be made to have such effect.**
- Ratification within reasonable time:** Ratification must be made within a reasonable period of time.
- Communication of Ratification:** Ratification must be communicated to the other party.
- Act to be ratified must be valid:** Act to be ratified should not be void or illegal.

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## EXTENT OF AGENT'S AUTHORITY

The authority of an agent means his **capacity to bind the principal to third parties**. The agent can bind the principal only if he acts within the scope of his authority. The agent's authority is governed by **two principles:**

### 1) Agent's authority in normal circumstances:

#### • Actual authority:

An agent can do all such acts as have been assigned to him either expressly or impliedly and thereby bind the principal to third parties by acts done within the scope of his 'actual' or 'real' authority (Sec 186 and 226).

#### • Ostensible or apparent authority:

An agent can also bind the principal to third parties by acts done within his apparent authority (although the act is in excess of his actual authority), provided the third party acts bonafide and without knowledge of the limitation of the agent's apparent authority.

**Ostensible authority:** authority which the third parties dealing with the agent can presume to be with the agent in relation to a particular business ordinarily.

### 2) Authority in emergency:

An agent has authority in an emergency to do all such acts for the purpose of protecting his principal from loss as would be done by a **person of ordinary prudence in his own case, under similar circumstances** (Sec 189).

To constitute a valid agency in an emergency, **following conditions must be satisfied:**

- Agent should not be in a position or have any opportunity to communicate with his principal within the time available.
- There should have been actual and definite commercial necessity for the agent to act promptly.
- Agent should have acted bonafide and for the benefit of the principal.
- Agent should have adopted the most reasonable and practicable course under the circumstances,
- Agent must have been in possession of the goods belonging to his principal and which are the subject of contract.

## PRINCIPAL'S LIABILITY FOR AGENT'S ACT TO THIRD PARTIES

### 1) When agent acts within the scope of his authority:

- The principal is liable for all acts of the agent done within the scope of his 'actual' and 'apparent (ostensible) authority'.
- The principal is also liable for all such acts of the agent which are necessary for protecting the principal from loss in an emergency.

### 2) When agent exceeds his actual as well as apparent authority:

- In this case the principal has option either to disown the unauthorised acts or to ratify the same.
- Where he ratifies-** he becomes liable for those acts as if he had authorised them originally.
- Where he opts to disown them, the following rules shall apply-**
  - Where the excess is separable from the authorised portion, the principal is liable only for the authorised portion (Sec 227)
  - Where the excess is not separable from the authorised portion, the principal is not bound by the transaction. In such a case the principal is entitled to repudiate the whole transaction and the agent shall be personally liable for that. (Sec 228)

### 3) Liability for agent's misrepresentation or fraud (Sec 238):

The principal is liable for any fraud or misrepresentation done by the agent **within his authority** regardless of the fact that the act has resulted in benefit to the agent or the principal.

### 4) Principal is bound by notice given to agent:

- The principal is bound by the notice given to the agent. Knowledge of the agent is knowledge of the principal.
- But where knowledge is not acquired by the agent in the course of the agency business, it cannot be imputed to the principal.

**5) Liability by estoppel (Liability of principal inducing belief that agent's unauthorized acts were authorized [Sec 237]):** Where the agency is by the doctrine of estoppel, the principal is bound by the same doctrine. Such a principal is bound by the acts of the agent although the agent did not in fact possess any authority in relation to those acts.

# CONTRACTS OF AGENCY (Chart 1.27)

Compiled By: CA Sahil Grover

## DUTIES & OBLIGATIONS OF AGENT

- 1) **Duty to execute the mandate & follow instructions and customs:**
  - The first and foremost duty of every agent is to **carry out the mandate of his principal**.
  - The agent should **conduct the business of the principal as per directions of the principal or in the absence of any directions as per the custom prevalent in the business**.
  - The agent is **liable to the principal for any loss if he deviates from the above duty/ obligation** where he did not act according to instruction of the principal. [**Pannalal Jankidas Vs. Mohanlal**]
- 2) **Requirements as to skill and diligence:**
  - Agent must **act with reasonable diligence and to the best of his skill**.
  - If the agent **does not work with reasonable care, skill and diligence**, he must **make compensation to his principal** in respect of **direct consequences of his own neglect, want of skill or misconduct**.
- 3) **Duty to render proper accounts (Sec 213):**  
An agent is **bound to render proper accounts to his principal on demand**. Rendering accounts does not mean showing the accounts but the **accounts supported by vouchers**.
- 4) **Agent' duty to communicate with principal (Sec 214):**  
It is the duty of an agent, in cases of difficulty, to **use all reasonable diligence in communicating with his principal, and in seeking to obtain his instructions**.
- 5) **Duty not to deal on his own account/ Duty to Avoid Conflict of interest (Sec 215 and 216):**
  - An agent must **not deal on his own account** in the business of agency i.e. he **must not himself buy from or sell to his principal goods** he is asked to sell or buy on behalf of his principal, without obtaining the consent of his principal after disclosing all material facts to him.
  - If the agent violates this rule, the **principal may repudiate the transaction**, where it can be shown that any material fact has been knowingly concealed by the agent or that the dealings of the agent have been disadvantageous to the principal.
  - The principal is also **entitled to claim from the agent any benefit which may have resulted to him from the transaction**.
- 6) **Duty not to make any profit out of his agency except his remuneration:**
  - An agent stands in a fiduciary relation to his principal and therefore he **must not make any profit (secret profit)** out of his agency. He must **pay to his principal all moneys** (including illegal gratification, if any) **received by him on principal's account**.
  - He can, however, **deduct all moneys due to himself in respect of his remuneration or/and expenses properly incurred**.
- 7) **Agent's duty to pay sums received for principal (Sec 218):**  
Subject to such deductions, the agent is **bound to pay to his principal all sums received on his account**.
- 8) **Duty not to Delegate:** According to Sec 190, an agent **cannot lawfully employ to perform acts which he has expressly or impliedly undertaken to perform personally**, unless by the ordinary custom of trade a sub-agent may, or, from the nature of agency, a sub-agent, must be employed.
- 9) **Duty not to use any confidential information received in the course of agency against the principal.**

## RIGHTS OF AGENT

- a) **Right of remuneration:**
  - The agent in the normal course is **entitled for remuneration as per the contract**.
  - In the **absence of any agreed amount** of remuneration, he is **entitled for usual remuneration which is customary in the business**.
  - However he is **not entitled for any remuneration for acts done through misconduct/negligence**. In addition, he is **liable to compensate the principal for any loss caused by misconduct**.
- b) **Right of retain out of sums received on principal's account (Sec 217):**  
Agent may retain, out of any sums received on account of the principal in the business of the agency for following payments:
  - **all moneys due to himself in respect of advances made**
  - **in respect of expenses properly incurred by him** in conducting such business
  - **such remuneration as may be payable to him for acting as agent**.
- c) **Agent's lien on principal's property (Sec 221):**  
In the absence of any contract to the contrary, an agent is **entitled to retain the goods, papers and other property, whether movable or immovable, of the principal received by him, until the amount due to himself for commission, disbursement and services in respect of the same has been paid or accounted for him**.
  - **The conditions of this right are:**
    - 1) Agent should be **lawfully entitled to receive from the principal a sum of money by way of commission earned or disbursement made or services rendered**.
    - 2) **Property should belong to the principal and received by the agent in his capacity and during the course of his ordinary duties as agent**.
    - 3) **If the agent obtains possession of the property by unlawful means, he cannot exercise particular lien**.
    - 4) **Agent has only a particular lien**.
  - **The agent's right to lien is lost in the following cases:**
    - 1) **When the possession of the property is lost**.
    - 2) **When the agent waives his right**. Waiver may arise out of agreement express or implied.
    - 3) **The agent's lien is subject to a contract to the contrary**.
- d) **Right to indemnity:**
  - **Right of indemnification for lawful acts:** Compiled By: CA Sahil Grover
    - The **principal is bound to indemnify the agent against all consequences of lawful acts** done in exercise of his authority.
    - The **agent cannot claim indemnity in respect of acts which are apparently unlawful or criminal**.
  - **Right of indemnification against acts done in good faith:**  
An agent has a **right to be indemnified against the consequences of an act done in good faith** though it turns out to be injurious to the rights of third persons.
  - **Non-liability of employer of agent to do a criminal act:**  
Where **one person employs another to do an act which is criminal, the employer is not liable to the agent**, either upon an express or an implied promise, to **indemnify him against the consequences of that act**.
- e) **Right to compensation for injury caused by principal's neglect (Sec 225):**  
Principal must **make compensation to his agent in respect of injury caused to such agent by the principal's neglect or want of skill**. Thus, every principal owes to his agent the duty of care not to expose him to unreasonable risks.

## LIABILITY OF UNNAMED PRINCIPAL

- **"Unnamed principal"** means a **principal whose existence is disclosed by the agent but the name is not disclosed**.
- **On being discovered**, the **legal position of the unnamed principal is the same as where the principal is named**, unless there is a trade custom making the agent personally liable.
- Thus once it is disclosed by the agent that he is an agent, **the contract made by the agent binds the principal and the agent drops out of the transaction despite the fact that the principal for whom he acted has not been named**.
- If however the **agent declines to disclose the identity of the principal, he becomes personally liable on the contract**.
- Also if the **agent could not disclose the identity of the principal, say, because of his sudden death, his estate will be liable to third parties**.

## LIABILITY OF UNDISCLOSED PRINCIPAL

- 'Undisclosed Principal'** comes into play where an agent having the authority to contract, does not disclose the fact, **concealing not only the name of the principal but also the fact that there is a principal; here the agent gives an impression that he acts on his own**.
- In such a case **neither the existence nor the name of the principal is disclosed and the agent gives an impression to the third party as if he himself is the contracting party**
- The mutual rights, of principal, agent and third party are as follows:**
- a) **Agent is liable to third parties personally**.
  - b) Where the **third party** comes to know about the existence of the principal he **can sue the agent or the principal**. The **liability of the principal and agent is "joint and several"** in such a case. ***If the third party elects to sue the agent*** - claim remains **partially unsatisfied** he may afterwards **sue the principal for the balance**. ***If the third party decides to sue the principal*** - he must **allow the principal the benefit of all payments received by him from the agent**.
  - c) The **third party's interest would stand protected evenly, and would not suffer even if the principal surfaces and intervenes at a later date**. The principal, if he likes, may **intervene and sue the third party for non-performance of the contract** but he cannot exercise this right to the prejudice (disadvantage) of the third party. Principal must allow to the third party the benefits of all payments made by the third party to the agent.
  - d) **Third party has a right to refuse, if the principal discloses himself, on the ground that had he known about principal he would not have entered into the contract**.

# CONTRACTS OF AGENCY (Chart 1.28)

## PERSONAL LIABILITY OF AGENT

- 1) **Where the contract is made by an agent for the sale or purchase of goods for a merchant resident abroad/foreign principal:**  
Agent undertakes to be personally liable for the performances of such contract.
- 2) **Where the agent does not disclose the name of his principal or undisclosed principal: (Principal unnamed):**  
Agent undertakes to be personally liable.
- 3) **Non-existent or incompetent principal:**  
Where the principal, though disclosed, cannot be sued, the agent is presumed to be personally liable.
- 4) **Pretended agent:**  
If the agent pretends but is not an actual agent, and the principal does not rectify the act but disowns it, the pretended agent will be himself liable.
- 5) **When agent exceeds authority:**  
When the agent exceeds his authority, misleads the third person in believing that the agent he has the requisite authority in doing the act, then the agent can be made liable personally.
- 6) **Where the contract expressly provides for personal liability of the agent or where according to usage in trade agents are personally liable.**  
**Right of person dealing with agent personally liable [Sec 233]:**  
In cases where the agent is personally liable, a person dealing with him may hold either him or his principal, or both of them, liable.

## SUB AGENT

- **“Sub-agent”-** person employed by and acting under the control of the original agent in the business of the agency”. (Sec 191)
- **“Sub agency”** is a case where an agent appoints another agent. The person employed by an agent is called sub-agent.
- The appointment of sub agent is not lawful, because the agent is a delegatee and a delegatee cannot further delegate.  
**But there are certain exceptions to this general rule.** In following cases the agent can delegate his authority to another (i.e. can appoint a sub agent):
  - 1) If the terms of appointment originally contemplated it.
  - 2) Sometimes customs of the trade may provide for appointment of sub agents.
  - 3) Where in the course of the agent’s employment, unforeseen emergency arise making it necessary for him to delegate the authority. If the sub agent is appointed in any of above circumstances, then he is called as **‘properly appointed agent’**.

## POSITION OF SUB AGENT vis a vis THIRD PARTIES

- a) **Where sub-agent is properly appointed [Sec 192]**
  - Principal is bound and liable to third parties for the acts of the sub-agent. as if he were an agent originally appointed by the principal.
  - Agent is responsible to the principal for the acts of the sub-agent.
  - Sub-agent is responsible for his acts to the agent and not to the principal.
  - In case the sub-agent is guilty of fraud or wilful wrong, he is directly liable to the principal. In such a case the principal has the choice to sue either the agent or the sub-agent.
- b) **Where the sub -agent is not properly appointed [Sec 193]**
  - Principal is not liable for the acts of the sub-agent.
  - Agent is responsible for the acts of the sub-agent to the principal as well as to the third parties.
  - Sub-agent is not responsible to the principal at all. He cannot be held liable by the principal even for fraud or wilful wrong.
  - Sub -agent is responsible for his acts only to the agent (his employer).

## SUBSTITUTED AGENT

- When an agent has an express or implied authority of his principal to name another person to act for the principal and the agent names another person accordingly, such person is not a sub-agent but a substituted agent of the principal in respect of the business which is entrusted to him [Sec 194].
- **Thus an agent simply names or appoints a substituted agent at the request of the principal and thereafter drops out altogether from the scene**
- The substituted agent is directly responsible to the principal and a privity of contract is deemed between him and the principal.  
**Agent’s duty in naming such person [Sec 195]**
- Sec 195 imposes a duty on the original agent to act with reasonable care while naming a substituted agent. The Section lays down that “in selecting such agent for his principal, an agent is bound to exercise the same amount of discretion as a man of ordinary prudence would exercise in his own case; and if he does this, he is not responsible to the principal for the acts or negligence of the agent so selected
- Original agent must act with reasonable care in selecting a substituted agent.
- If he makes the selection carelessly he becomes liable to the principal for the negligence of the agent so selected.
- However, the original agent is not required to guarantee the integrity or solvency of the substituted agent.

## SUB-AGENT vs SUBSTITUTED AGENT

Sub Agent	Substituted Agent
Works under the control and directions of agent.	Works under the instructions of the principal.
Agent not only appoints a sub-agent but Agent delegates to sub agent a part of his own duties.	Agent does not delegate any part of his task to a substituted agent.
There is no privity of contract between the principal and the sub-agent.	Privity of contract is established between a principal and a substituted agent.
Sub agent is responsible to the agent alone and is not generally responsible to the principal	Substituted agent is responsible to the principal and not to the original agent who appointed him
Agent is responsible to the principal for the acts of the sub agent.	Agent is not responsible to the principal for the acts of the substituted agent.
Sub-agent has no right of action against the principal for remuneration due to him.	Substituted agent can sue the principal for remuneration due to him.
Sub-agents may be improperly appointed.	Substituted agents can never be improperly appointed.
Agent remains liable for the acts of the sub-agent as long as the sub-agency continues.	Agent’s duty ends once he has named the substituted agent.

# CONTRACTS OF AGENCY (Chart 1.29)

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SUBSTITUTED AGENT		IRREVOCABLE AGENCY
<p><b>(A) Termination by act of the Parties</b></p>	<p><b>(B) Termination by Operation of Law</b></p>	<p><b>When Termination of Agency Takes Effect - Sec 208</b></p>
<p>An agency comes to an end by act of the parties in the following cases:</p> <ol style="list-style-type: none"> <li><b>1) Agreement:</b> An agency, like any other contract, can be terminated at any time by the mutual agreement between the principal &amp; agent.</li> <li><b>2) Revocation by the principal:</b> Principal may revoke the authority of the agent at any time before the agent has exercised his authority so as to bind the principal, unless the agency is irrevocable. Revocation may be expressed or implied in the conduct of the principal (Sec. 207).</li> </ol> <p><b>Conditions for Revocation by the principal:</b></p> <ul style="list-style-type: none"> <li>Principal may revoke the authority at any time before the authority has been exercised so as to bind the principal. However, the principal cannot revoke the authority after the authority has been partly exercised.</li> <li>The principal may revoke it for the future. It cannot be revoked with regard to acts already done in the agency.</li> <li>Reasonable notice must be given for termination, otherwise the agent is entitled for compensation.</li> <li>Where there is an express or implied contract that the agency should be continued for any period of time, the principal must make compensation to the agent, for any previous revocation of the agency without sufficient cause.</li> <li>Even where the agent gets interested in the subject matter that would not be a ground for the principal to terminate the agency. The agency becomes an agency coupled with interest, which can't be revoked.</li> </ul> <ol style="list-style-type: none"> <li><b>3) Renunciation by the agent:</b> <ul style="list-style-type: none"> <li>An agency may also be terminated by an express renunciation by the agent because a person cannot be compelled to continue as agent against his will.</li> <li>Agent must give a reasonable notice of renunciation to the principal; otherwise he will be liable to compensate the principal for any damage resulting thereby.</li> <li>If the agency is for a fixed period and the agent renounces it without sufficient cause before the expiry of the period, he shall have to compensate the principal for the resulting loss, if any.</li> </ul> </li> </ol>	<p>An agency comes to an end automatically by operation of law in the following cases:</p> <ol style="list-style-type: none"> <li><b>1) Completion of the business of agency:</b> An agency is automatically and by operation of law terminated when its business is completed.</li> <li><b>2) Expiry of time:</b> If the agent is appointed for a fixed term, the expiration of the term puts an end to the agency, even though the business of the agency may not have completed.</li> <li><b>3) Death of the principal or the agent:</b> An agency is terminated automatically on the death of the principal or the agent. Agent must take all reasonable steps for the protection of the interests of the late principal entrusted to him. Section 209 states that when an agency is terminated by the principal dying or becoming of unsound mind, the agent is bound to take, on behalf of the representatives of his late principal, all reasonable steps for the protection and preservation of the interests entrusted to him.</li> <li><b>4) Insanity of the principal or the agent:</b> An agency also stands terminated when the principal or agent becomes of an unsound mind.</li> <li><b>5) Insolvency of the principal:</b> An agency is also terminated by the insolvency of the principal.</li> <li><b>6) Destruction of the subject-matter:</b> An agency which is created to deal with certain subject-matter will be terminated by the destruction of that subject-matter.</li> <li><b>7) Dissolution of a company:</b> If the principal or agent is an incorporated company; the agency automatically ceases to exist on dissolution of the company.</li> <li><b>8) Principal or agent becomes alien enemy:</b> If the principal and agent are nationals of two different countries and a war breaks out between the two countries, the contract of agency is terminated.</li> </ol>	<p><b>AGENCY COUPLED WITH INTEREST [Sec 202]</b></p> <ul style="list-style-type: none"> <li>Where the agent has himself an interest in the subject-matter of agency, the agency is said to be "coupled with interest."</li> <li>Such an agency is created with the object of protecting or securing any interest of the agent.</li> <li>In other words, when agency is created for securing some benefit to the agent over above his remuneration as an agent it is called as agency coupled with interest</li> <li>The interest should exist at the time of creation of agency. If the interest arises after the creation of agency then it would not be called as agency coupled with interest.</li> <li>Agency coupled with interest cannot be terminated to the prejudice of such interest.</li> <li>Agency coupled with interest does not terminate even on the death or insanity of the principal.</li> <li>Thus such agency is irrevocable to the extent of such interest.</li> </ul> <p><b>Termination of sub-agent's authority [Sec 210]</b></p> <p>The termination of the authority of an agent causes the termination of the authority of all sub-agents appointed by him.</p>
		<p>Where the agency cannot be terminated, it is called irrevocable agency.</p> <ol style="list-style-type: none"> <li><b>1) Where agency is coupled with interest -</b> agency cannot be terminated except where there is an express provision, to cause prejudice to the interest of the agent.</li> <li><b>2) Where the agent has incurred personal liability -</b> principal cannot revoke the agency leaving the agent to face the liability.</li> <li><b>3) Where the agent has partly exercised the authority -</b> the authority cannot be revoked.</li> </ol>
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# CA SANCHIT GROVER

**THE INDIAN  
PARTNERSHIP ACT, 1932**

# THE INDIAN PARTNERSHIP ACT, 1932 (Chart 1.1)

## INTRODUCTION

- This Act extends to the **whole of India** except the State of J&K
- Came into force on the **1st October, 1932**, except section 69 which shall come into force on the **1st October, 1933**.
- Contains **74 sections and 2 schedules**
- Earlier part of Contract Act. **Sections 239-366(Chapter XI) were repealed and reenacted as Indian Partnership Act, 1932.**

### Provisions of Indian Contract Act shall Apply

**Sec 2(e):** Expressions used but not defined in this Act and defined in the Indian Contract Act, 1872, shall have the meanings assigned to them in that Act.  
**Sec 3:** The unrepealed provisions of the Indian Contract Act, 1872, save in so far as they are inconsistent with the express provisions of this Act, shall continue to apply to firms.

## DEFINITION (SECTION 4)

### 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**.

Persons who have entered into partnership with one another are called individually, "**partners**" and collectively "**a firm**", and the name under which their business is carried on is called the "**firm-name**".

### PARTNERSHIP NOT CREATED BY STATUS (SEC 5)

The relation of partnership arises from contract and not from status

## ESSENTIAL ELEMENTS OF PARTNERSHIP

### 1. Association of two or more persons:

- at least **2 persons are necessary** to constitute a partnership.
- **Sec. 464 of the Companies Act, 2013 has put a limit of 50 partners in any association/partnership firm. (Partnership Act puts no limit)**
- **Only persons competent to contract** can enter into a contract of partnership.
- Persons may be **natural or artificial**.

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### 2. Contract:

- 'Contract' is the very foundation of partnership. It may, however, be either **express or implied**. Again, it may be **oral or in writing**.
- **Sec. 5 expressly provides that "the relation of partnership arises from contract and not from status."**

### 3. Business:

- **First**, there must exist a **business**. The term '**business**' is used in its widest sense and **includes every trade, occupation or profession [Sec. 2(b)]**. The existence of business is essential.
- **Secondly, the motive of the business is the "acquisition of gains. If the purpose is to carry on some charitable work, it will not be a partnership.**
- **Mere joint ownership not sufficient:** number of persons agree to share the income of a certain property or to divide the goods purchased in bulk amongst themselves, there is no partnership.

### 4. Sharing of profits:

- 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. **The partners may, however, agree to share profits in any ratio they like.**
- **Sharing of losses not necessary.** It is open to **one or more partners to agree to bear all the losses of the business.**
- **Section 13(b) however, provides that the partners are entitled to share equally in the profits earned, and shall contribute equally to the losses sustained by the firm, unless otherwise agreed.** Thus where nothing is said as to the sharing of losses, an agreement to share profits implies an agreement to share losses as well.

### 5. Mutual agency:

- Business must be carried on by **all the partners or any (one or more) of them acting for all**, that is, there must be mutual agency.
- Every partner is **both an agent and principal for himself and other partners i.e.,** he can bind by his acts the other partners and can be bound by the acts of other partners in the ordinary course of business.
- Enables every partner to carry on the business on behalf of others.
- **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.**

## Mode of Determining Existence of Partnership (Section 6)

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**.

**Cumulative effect of all relevant facts such as written or verbal agreement, real intention and conduct of the parties, other surrounding circumstances etc., are to be considered**

### Sharing of Profit not a conclusive test

Explanation II to Section 6 clearly states: "The receipt by a person of a share of the profits of a business, or of a payment contingent upon the earning of profits or varying with the profits earned by a business, does not of itself make him a partner with the persons carrying on the business; and, in particular, the receipt of such share or payment:

- a) by a lender of money to persons engaged or about to engage in any business,
- b) by a servant or agent as remuneration,
- c) by a widow or child of a deceased partner, as annuity, or
- d) by a previous owner or part owner of the business, as consideration for the sale of the goodwill or share thereof, does not of itself make the receiver a partner with the persons carrying on the business.

### Existence of Mutual Agency-Cardinal principle of partnership law,

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.



# THE INDIAN PARTNERSHIP ACT, 1932 (Chart 1.2)

## KINDS OF PARTNERSHIP

### WITH REGARD TO DURATION

#### AT WILL [SEC 7]

##### Conditions:

- i. **no fixed period** has been agreed upon for the duration of the partnership; **and**
- ii. there is **no provision** made as to the **determination of the partnership**
- 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.
- May be dissolved by any partner by giving notice in writing to all the other partners of his intention to dissolve the same.
- If this freedom to dissolve the firm at will is curtailed by agreement, (say, if the agreement provides that the partnership can be dissolved by mutual consent of all the partners only), it will not constitute a 'partnership at will.'

#### FIXED PERIOD

- Where a provision is made by a contract for the duration of the partnership, the partnership is called 'partnership for a fixed period'.
- Such a partnership comes to an end on the expiry of the fixed period

### WITH REGARD TO EXTENT OF BUSINESS

#### PARTICULAR PARTNERSHIP [SEC 8]

- When a partnership is formed for a particular or specific adventure or undertaking, e.g., for working a coal mine or producing a film, it is called a 'particular partnership'.
- It is automatically dissolved on the completion of the adventure (Sec. 42).
- Before such time the partnership would not be dissolved unless all the partners agree to it (Sec. 40).
- If the partners decide to continue such a partnership even after the completion of the specific adventure or undertaking then it becomes a 'partnership at will.'

#### GENERAL PARTNERSHIP

Where a partnership is constituted with respect to the business in general, it is called a general partnership.

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## PARTNERSHIP DEED

- Document in writing containing the various terms and conditions as to the relationship of the partners to each other is called the 'partnership deed'.
  - Document in which the respective rights and obligations of the members of a partnership are set forth.
  - Should be drafted with care and be stamped according to the provisions of the Stamp Act, 1899.
- It may contain the following information:
- Name of the partnership form.
  - Nature and place of the business of the firm.
  - Date of commencement of partnership.
  - Duration of the partnership firm.
  - Profit Sharing ratio of the partners.
  - Admission and Retirement of a partner.
  - Rates of interest on Capital, Drawings and loans.
  - Names of all the partners.
  - Capital contribution of each partner
- The terms laid down in the Deed may be varied by consent of all the partners, and such consent may be expressed or may be implied by a course of dealing [Sec. 11(1)].

## TYPES OF PARTNERS

### ACTIVE PARTNER

- Becomes partner by agreement
- Actively participates in the conduct of the partnership business.
- Acts as an agent of other partners for all acts done in the ordinary course of business.
- In event of his retirement, he must give a public notice in order to free himself of liabilities

### INCOMING PARTNER

- A person who is admitted as a partners into an already existing firm with the consent of all the existing partners.
- Not liable for any act of the firm done before his admission as a partner

### SLEEPING/DORMANT

- Becomes partner by agreement but does not actively participate in the conduct of the partnership business.
- share profits and losses and are liable to the third parties for all acts of the firm.
- Not required to give public notice of their retirement from the firm.

### OUTGOING PARTNER

- A partner who leaves a firm in which the rest of the partners continue to carry on business.
- Remains liable to third parties for all acts of the firm until public notice is given of his retirement.

### PARTNER BY HOLDING OUT [SECTION 28]

- Such a person is not a partner in that firm-no agreement, no sharing in profits and losses, no say in the management, may not be knowing exact place of business, but as he holds himself out to be a partner, he becomes responsible to outsiders as a partner on the principle of estoppel or holding out.
- 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'.
- 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.

### NOMINAL

- Lends his name to the firm, w/o having any real interest in it.
- Not entitled to share the profits of the firm.
- Neither invests in the firm nor takes part in the conduct of the business.
- Liable to third parties for all acts of the firm

### PARTNERS IN PROFIT ONLY

- Entitled to share the profits only without being liable for the losses
- Liability vis-a-vis third parties will be unlimited.

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**[Sec. 11(1)]:** "SUBJECT to the provisions of this Act, the mutual rights and duties of the partners of a firm may be determined by contract between the partners, and such contract may be express or may be implied by a course of dealing. Such contract may be varied by consent of all the partners, and such consent may be express or may be implied by a course of dealing".

Thus, except in cases where the Partnership Act makes a mandatory provision, the partners are entitled to agree to any terms and provide for their mutual rights and duties.

DUTIES OF PARTNER	RIGHTS OF PARTNER		PARTNERSHIP PROPERTY [SEC 14]
<p><b>GENERAL DUTIES OF PARTNERS (SECTION 9):</b> Partners are bound to <b>carry on the business of the firm to the greatest common advantage, to be just and faithful to each other, and to render true accounts and full information of all things affecting the firm</b> to any partner or his legal representative.</p> <p><b>DUTY TO INDEMNIFY FOR LOSS CAUSED BY FRAUD (SEC. 10):</b> Where a partner acts bonafide the loss caused by his <b>neglect or want of skill or omission is borne by the firm. But when the loss is caused by fraud committed against a third party by a partner, the same must be recovered from the guilty partner and cannot be shared among all the partners.</b></p> <p><b>DUTY TO ATTEND DILIGENTLY TO HIS DUTIES [SEC 12(b)]:</b> Every partner is bound to attend diligently to his duties in the conduct of the business.</p>	<p><b>CONDUCT OF THE BUSINESS (SECTION 12)</b> Subject to contract between the partners)</p> <p>a) every partner has a <b>right to take part in the conduct of the business;</b></p> <p>b) every partner is bound to attend diligently to his duties in the conduct of the business;</p> <p>c) any difference arising as to ordinary matters connected with <b>the business may be decided by majority of the partners, and every partner shall have the right to express his opinion</b> before the matter is decided, but <b>no change may be made in the nature of the business without the consent of all partners;</b> and</p> <p>d) Every partner has a <b>right to have access to and to inspect and copy any of the books of the firm.</b></p> <p>e) In the event of the <b>death of a partner, his heirs or legal representatives or their duly authorised agents</b> shall have a <b>right of access to and to inspect and copy any of the books of the firm.</b></p>	<p><b>MUTUAL RIGHTS AND LIABILITIES (SECTION 13)</b> <b>Subject to contract between the partners-</b></p> <p>a) a partner <b>is not entitled to receive remuneration</b> for taking part in the conduct of the business;</p> <p>b) the partners are <b>entitled to share equally in the profits earned, and shall contribute equally to the losses</b> sustained by the firm;</p> <p>c) where a partner is <b>entitled to interest on the capital subscribed by him</b> such interest shall be payable only out of profits.</p> <p>d) a partner making, for the purposes of the business, any <b>payment or advance beyond the amount of capital</b> he has agreed to subscribe, is entitled to <b>interest thereon at the rate of six percent per annum;</b></p> <p>e) the firm <b>shall indemnify a partner</b> in respect of <b>payments made and liabilities incurred by him-</b></p> <p>i. in the <b>ordinary and proper conduct of the business,</b> and</p> <p>ii. in <b>doing such act, in an emergency,</b> for the purposes of protecting the firm from loss, as would be done by a person of ordinary prudence, in his own case, under similar circumstances</p>	<p>- Also referred to as <b>'partnership property', 'partnership assets', 'joint stock', 'common stock'</b> or <b>'joint estate'</b>, denotes all property, rights and interests to which the firm, that is, all partners collectively, may be entitled.</p> <p>- In the absence of any agreement between the partners showing contrary intention, <b>'partnership property' is comprised of the following items:</b></p> <p>i. all property, rights and interests which partners may <b>have brought into the common stock as their contribution to the common business;</b></p> <p>ii. all the property, rights and interest <b>acquired or purchased by or for the firm,</b> or for the purposes and in the course of the business of the firm; and</p> <p>iii. <b>Goodwill of the business.</b></p> <p>- <b>Whether a particular property is or is not 'property' of the firm ultimately depends on the real intention or agreement of the partners.</b></p> <p>- <b>Mere fact that the property of a partner is being used for the purposes of the firm shall not by itself make it partnership property,</b> unless it is intended to be treated as such.</p> <p>- <b>Unless the contrary intention appears, property and rights and interests in property acquired with money belonging to the firm are deemed to have been acquired for the firm.</b></p> <p><b>Goodwill:</b> Section 14 does not define the term Goodwill. 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 levels of profits earned by undertaking belonging to the same class of business.</p>

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PERSONAL PROFITS EARNED BY PARTNERS [SEC 16]	MUTUAL RIGHTS & DUTIES OF PARTNERS AFTER CHANGE IN FIRM [SECTION 17]	APPLICATION OF THE PROPERTY OF THE FIRM (SECTION 15)
<p><b>1. Duty to account for personal profits derived:</b> Where 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 firm name, <b>he must account for that profit and pay it to the firm.</b></p> <p><b>2. Duty to account and pay for profits of competing business:</b> <b>Competing business:</b> - account for and pay to the firm all profits made. <b>Non-competing business:-</b>Retain the profits made. <b>Partnership Deed contains a restrictive clause prohibiting partners from carrying on any business other than that of the firm during partnership</b></p> <ul style="list-style-type: none"> <li>Such a <b>restraint is valid,</b> notwithstanding anything contained in <b>section 27</b> of the Indian Contract Act, 1872.</li> <li><b>Partner breaches</b> the clauses and carries on: <b>Competing Business:</b> Damages + account for profits made <b>Non-Competing Business:</b> Only Damages for breach of contract</li> </ul>	<p>a) <b>After change in the firm:</b> Where a change occurs in the constitution of a firm (<i>i.e.</i>, where a new partner is admitted or where a partner ceases to be a partner by retirement, expulsion, insolvency or death), the <b>mutual rights and duties of the partners in the reconstituted firm remain the same</b> as they were immediately before the change, as far as may be possible.</p> <p>b) <b>after the expiry of the term of the firm:</b> Where a firm constituted for a fixed term continues to carry on business after the expiry of that term, <b>the mutual rights and duties of the partners remain the same as they were before the expiry,</b> so far as they may be consistent with the incidents of partnership at will.</p> <p>c) <b>where additional undertakings are carried out:</b> where a firm constituted to carry out one or more adventures/undertakings carries out other adventures/undertakings <b>the mutual rights &amp; obligations in other adventure/undertaking are the same as those in respect of the original adventures or undertakings.</b></p>	<p>- Subject to contract between the partners, <b>the property of the firm shall be held and used by the partners exclusively for the purposes of the business.</b></p> <p>- In partnership, there is a <b>community of interest</b> which all the partners take in the property of the firm. But that <b>does not mean that during the subsistence of the partnership, a particular partner has any proprietary interest in the assets of the firm.</b></p>

# THE INDIAN PARTNERSHIP ACT, 1932 (Chart 1.4)

## PARTNER TO BE AGENT OF THE FIRM (SECTION 18)

- Section 18 declares that from the **point of view of the third parties a partner is an agent of the firm for the purposes of the business of the firm.**
- As such even if only one partner acts on behalf of the firm, the third party can make all the partners of the firm liable.
- However one partner can make other partners liable towards the third parties **only if he acts within the 'scope of his authority'**

EXPRESS AUTHORITY	IMPLIED AUTHORITY	AUTHORITY IN EMERGENCY [SEC 21]
When a partner is <b>expressly authorised by an agreement</b> of all the partners to do certain acts on behalf of the firm, it is called express authority of a partner.	An implied authority of a partner can be <b>inferred from the circumstances of the case.</b> Generally speaking, <b>such acts of a partner which are incidental to or usually done in the course of the proper conduct of the business</b> come within the scope of his implied or apparent or ostensible authority. <b>Firm is also bound by all acts of a partner done within the scope of his implied authority</b>	A partner has authority, <b>in an emergency, to do all such acts for the purpose of protecting the firm from loss as would be done by a person of ordinary prudence, in his own case,</b> acting under similar circumstances, and such acts bind the firm.

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SCOPE OF THE IMPLIED AUTHORITY OF A PARTNER.[SEC 19(1) read with SEC 22]	STATUTORY RESTRICTIONS ON IMPLIED AUTHORITY [SEC. 19(2)]	EXTENSION AND RESTRICTION OF PARTNERS' IMPLIED AUTHORITY (SECTION 20)
For an act to be covered within the implied authority it is necessary that: <ol style="list-style-type: none"> <li>The <b>act done must relate to the usual business of the firm</b>, that is, the act done by the partner must be within the scope of his authority and related to the normal business of the firm.</li> <li>The <b>act is such as is done for normal conduct of business of the firm.</b> The usual way of carrying on the business will depend on the nature and circumstances of each particular case [Section 19(1)].</li> <li>The act to be <b>done in the name of the firm</b> or in any other manner <b>expressing or implying an intention to bind the firm</b> (Section 22).</li> </ol>	<u>A partner does not have an implied authority to do following acts unless there is usage or custom or contract to the contrary:</u> <ol style="list-style-type: none"> <li><b>submit a dispute</b> relating to the business of the firm to <b>arbitration</b>;</li> <li><b>open a banking account</b> on behalf of the firm in his own name;</li> <li><b>compromise or relinquish</b> any claim or portion of a claim by the firm;</li> <li><b>withdraw a suit or proceeding</b> filed on behalf of the firm;</li> <li><b>admit any liability</b> in a suit or proceeding against the firm;</li> <li><b>acquire immovable property</b> on behalf of the firm;</li> <li><b>transfer immovable property</b> belonging to the firm; or</li> <li><b>enter into partnership</b> on behalf of the firm.</li> </ol>	<ul style="list-style-type: none"> <li>- The <b>implied authority</b> of a partner may be <b>extended or restricted by contract between the partners.</b></li> <li>- The restrictions imposed on the implied authority of a partner by agreement shall be <b>effective against a third party only if the third party knows about the restrictions.</b></li> <li>- Such extension or restriction is only possible with the <b>consent of all the partners.</b> Any one partner, or even a <b>majority</b> of the partners, <b>cannot restrict or extend</b> the implied authority.</li> </ul>

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Effect of admission by partner [Sec 23]	Effect of notice to acting partner [Sec 24]	LIABILITY OF PARTNERS TO THIRD PARTIES		
An admission or representation made by a partner concerning the affairs of the firm is evidence against the firm, if it is made in the ordinary course of business	<ul style="list-style-type: none"> <li>- Notice to a partner, <b>who habitually acts in the business of the firm,</b></li> <li>- of any matter relating to the affairs of the firm</li> <li>- operates as <b>notice to the firm,</b></li> <li>- <b>except in the case of a fraud on the firm,</b></li> <li>- committed by or with the consent of that partner</li> </ul>	<u>Liability of a Partner for Acts of the Firm (Sec. 25).</u> <ul style="list-style-type: none"> <li>- Every partner is liable, <b>jointly with all the other partners and also severally,</b> for all acts of the firm done while he is a partner.</li> <li>- <b>Creditor can sue all partners together, or can sue them separately.</b></li> <li>- Further, the <b>liability</b> of all the partners is <b>unlimited</b></li> <li>- As between the partners themselves, the partner paying for more than his share of the liability may <b>claim contribution from the others according to the terms of the partnership agreement.</b></li> </ul>	<u>Liability of the firm for wrongful acts of a partner (section 26)</u> <ul style="list-style-type: none"> <li>- The <b>firm is liable</b> to the same extent as the partner <b>for any loss or injury caused to a third party</b> by the <b>wrongful acts of a partner,</b> if they are done by the partner while <b>acting in the ordinary course of the business of the firm with the authority of the partners.</b></li> <li>- Thus <b>all the partners</b> in a firm are <b>liable to a third party</b> for <b>loss or injury</b> caused to him by the <b>negligent act of a partner</b> acting in the ordinary course of the business.</li> </ul>	<u>Liability of firm for misapplication by partners (Section 27)</u> <p>Where</p> <ol style="list-style-type: none"> <li>a partner acting within his apparent authority receives money or property from a third party and misapplies it, or</li> <li>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.</li> </ol> <p>Clause (a) covers the case where a partner acts within his authority and due to his authority as partner, <b>he receives money or property belonging to a third party and misapplies that money or property. It is not necessary that the money should have actually come into the custody of the firm.</b></p> <p>On the other hand, the provision of clause (b) would be attracted when <b>such money or property has come into the custody of the firm and it is misapplied by any of the partners.</b></p> <p><u>The firm would be liable in both the cases.</u></p>

**RIGHTS OF TRANSFEREE OF A PARTNER'S INTEREST (SECTION 29)**

- 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 cannot be 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.
- **Sec 29 thus provides** that **the 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.**

**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.**

**MINOR ADMITTED TO THE BENEFITS OF PARTNERSHIP [SECTION 30]**

- According to the Indian Contract Act an agreement by a minor is void *ab-initio* as against him but he can derive benefit under it. As such a **minor cannot be a full-fledged partner, he can at most be admitted to the benefits of a partnership.**
- Section 30 of the Partnership Act thus provides that though a minor cannot be a partner in a firm, but, with the *consent of all the partners* for the time being, he may be admitted to the benefits of partnership.

**RIGHTS & LIABILITIES OF MINOR ADMITTED TO BENEFITS**

**Rights of Minor Admitted to Benefits**

**During Minority**

- 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 elect to become partner, then his share is not liable for any acts of the firm after the date of the public notice served to that effect.**

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**Liabilities of Minor Admitted to Benefits**

**Before attaining majority (During Minority)**

- i. The **liability of the minor** is confined only to the extent of his share in the profits and the property of the firm.
- ii. Minor has **no personal liability** for the debts of the firm incurred during his minority.
- iii. Minor **cannot be declared insolvent**, but if the firm is declared insolvent his share in the firm vests in the Official Receiver/Assignee.

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**On 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.**
- Such minor shall **give notice to the Registrar that he has or has not become a partner.**

**If he elects to become 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)** are as follows:

- a) He becomes **personally liable to third parties for all acts of the firm done since he was admitted to the benefits of partnership.**
- b) His **share in the property and the profits of the firm remains the same** to which he was entitled as a minor.

**If he elects not to become a partner:**

- a) His **rights and liabilities continue to be those of a minor up to the date of giving public notice.**
- b) His **share shall not be liable** for any acts of the firm done after the date of the notice.
- c) He shall be **entitled to sue the partners for his share of the property and profits.**

INCOMING [SEC 31]	RETIREMENT [SEC 32]	EXPULSION [SEC 33]	INSOLVENCY [SEC 34]	DEATH [SEC 35]						
<p>Subject to contract between the partners, no person can be admitted as a partner into a firm without the <b>consent of all the existing partners.</b></p> <p><b>LIABILITY OF AN INCOMING PARTNER</b></p> <ul style="list-style-type: none"> <li>- <b>FUTURE DEBTS:</b> He is liable for the debts and acts of the firm <b>only from the date he is admitted as a partner.</b> He cannot be held liable for the acts of the old firm.</li> <li>- <b>PAST DEBTS:</b> <ul style="list-style-type: none"> <li>▪ He may, however, agree to be liable for debts existing prior to his admission but such agreeing will not give to a prior creditor the right of suing him because of 'absence of privity of contract.' He will be liable to other co-partners only.</li> <li>▪ The creditors can make him liable if he had agreed with them, expressly or impliedly, for being liable towards them for the past debts</li> </ul> </li> </ul> <p><b>In case of partnership of two partners:</b> This section does not apply to a partnership of two partners which is automatically dissolved by the death of one of them. In this event there is no partnership at all for any new partner to be introduced into it without the consent of others.</p>	<p>A partner is said to retire when he ceases to be a member of the firm without bringing to an end the subsisting relations between the other members, or between the firm and third parties.</p> <p><b>Sec 32(1):</b> 'A partner may retire:</p> <ol style="list-style-type: none"> <li>with the consent of all the other partners;</li> <li>in accordance with an express agreement by the partners; or</li> <li>where the partnership is at will, by giving notice in writing to all the other partners of his intention to retire.</li> </ol> <p><b>Liability of a retiring partner</b> <b>For acts done prior to retirement (Section 32(2)):</b> Continues to be liable for the acts of the firm done before his retirement. May free himself from his liability towards third parties for the debts of the firm incurred before his retirement by an agreement with such third parties and the partners of the reconstituted firm. Partners alone cannot give this freedom to the retiring partner. He may be discharged only if the creditors agree.</p> <p><b>Liability for acts of firm post retirement (Sec 32(3)):</b> Continues to be liable for the acts of the firm, even after retirement, until public notice is given of the fact of retirement. Similarly, the partners of the reconstituted firm continue to be liable for the acts of the retired partner though done after retirement, until public notice is given of the retirement.</p> <p><b>Public notice [Sec 32(4)]:</b> May be given either by the retiring partner or by any partner of the reconstituted firm.</p> <p><b>No public Notice:</b></p> <ul style="list-style-type: none"> <li>▪ A dormant or sleeping partner retires</li> <li>▪ If the partnership is at will, the partner by giving notice in writing to all the other partners of his intention to retire</li> </ul>	<p>A partner may not be expelled from a firm by any majority of the partners, save in the exercise in good faith of powers conferred by contract between the partners.</p> <p><b>Conditions</b></p> <ol style="list-style-type: none"> <li>the power of expulsion must have existed in a contract between the partners;</li> <li>the power has been exercised by a majority of the partners; and</li> <li>It has been exercised in good faith.</li> </ol> <p>If all these conditions are not present, the expulsion is not deemed to be in bonafide interest of the business of the firm.</p> <p><b>Test of good faith as required under Section 33(1) includes three things:</b></p> <ol style="list-style-type: none"> <li>The expulsion must be in the interest of the partnership.</li> <li>The partner to be expelled is served with a notice.</li> <li>He is given an opportunity of being heard.</li> </ol> <p>If a partner is otherwise expelled, the expulsion is null and void.</p> <p><b>The provisions of sub-section (2), (3) and (4) of section 32 shall apply</b> to an expelled partner as if he were a retired partner.</p>	<ul style="list-style-type: none"> <li>- 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.</li> <li>- The estate of the insolvent partner is not liable for the acts of the firm done after the date of order of adjudication.</li> <li>- The firm is also not liable for any act of the insolvent partner after the date of the order of adjudication.</li> <li>- 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</li> </ul>	<p><b>RIGHTS OF OUTGOING PARTNER TO CARRY ON COMPETING BUSINESS (SECTION 36)</b></p>	<p>(1) 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,</p> <ol style="list-style-type: none"> <li>use the firm name,</li> <li>represent himself as carrying on the business of the firm or</li> <li>solicit the custom of persons who were dealing with the firm before he ceased to be a partner.</li> </ol> <p><b>Agreement in restraint of trade-</b> A partner may make an agreement with his partners that on ceasing to be a partner he will not carry on any business similar to that of the firm within a specified period or within specified local limits and, notwithstanding anything contained in section 27 of the Indian Contract Act, 1872, such agreement shall be valid if the restrictions imposed are reasonable.</p>	<ul style="list-style-type: none"> <li>- Ordinarily, the effect of the death of a partner is the dissolution of the partnership but if the other partners so agree the firm may not be dissolved, unless the firm consists of only two partners</li> <li>- Where a firm is not dissolved, the estate of a deceased partner is not liable for any act of the firm done after his death.</li> <li>- His estate is liable only for liabilities undertaken during his life time.</li> <li>- No public notice of death is required to relieve the deceased partner's estate from future liabilities.</li> </ul>	<p><b>SHARE IN SUBSEQUENT PROFITS [SEC 37]</b></p>	<p><b>REVOCATION OF CONTINUING GUARANTEE [SEC 38]</b></p> <p>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.</p>	<p><b>Mutual rights and duties of partners after change in the Firm [SEC. 17(a)]</b></p>	<p>Subject to contract between the partners, where a change occurs in the constitution of a firm (admission, retirement, death, etc) the mutual rights and duties of the partners in the reconstituted firm remain the same as they were immediately before the change, as far as may be possible.</p>
				<p>If any member of a firm ceases to be a partner (death, retirement, insolvency, etc) &amp; the business of the firm is carried on without any final settlement of accounts with him, then, in the absence of a contract to the contrary, he or his legal representative has an option either:</p> <ol style="list-style-type: none"> <li>to claim 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 (i.e., to claim profits in capital ratio);</li> <li>Or</li> <li>to claim interest at the rate of 6 per cent per annum on the amount of his share in the property of the firm.</li> </ol>						

REGISTRATION OF FIRMS

Under the Partnership Act it is not compulsory for every partnership firm to get itself registered, but an unregistered firm suffers from a number of disabilities

PROCEDURE OF REGISTRATION

- An application in the prescribed form + prescribed fee--submitted to the Registrar of Firms of the State in which any place of business of the firm is situated or proposed to be situated.
- Must be signed by all the partners, or by their agents specially authorised in this behalf, and must contain the following particulars:
  1. The name of the firm.
  2. The place or principal place of business of the firm.
  3. The names of any other places where the firm carries on business.
  4. The date when each partner joined the firm.
  5. The names in full and permanent addresses of the partners.
  6. The duration of the firm.
- A firm name shall not contain any of the following words, namely:- 'Crown', 'Emperor', 'Empress', 'Empire', 'Imperial', 'King', 'Queen', 'Royal', or words expressing or implying the sanction, approval or patronage of Government except when the SG signifies its consent to the use of such words as part of the firm-name by order in writing.
- When the Registrar is satisfied that the provisions of Section 58 have been duly complied with, he shall record an entry of the statement in a Register called the Register of Firms & issue a certificate of Registration.
- Registration is deemed to be completed as soon as a proper application delivered to the Registrar. The recording of an entry in the register of firms is a routine duty of Registrar.
- If any change takes place in any of the particulars given above, it should be notified to the Registrar, who shall thereupon incorporate the necessary change in the Register of Firms.
- Registration may take place at any time during the continuance of the partnership firm. Where the firm intends to institute a suit in a court of law to enforce rights arising from any contract, registration must be effected before the suit is instituted otherwise the court shall not entertain the suit.
- Registration may also be effected even after a suit has been filed by the firm but in that case it is necessary to withdraw the suit, get the firm registered and then file a fresh suit.

CONSEQUENCES OF NON- REGISTRATION [SEC 69]

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:

- (i) No suit in a civil court by a partner against the firm or other co-partners (However, criminal proceedings can be brought by one partner against the other(s).)
- (ii) 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.  
Third party can sue the firm: In case of an unregistered firm, an action can be brought against the firm by a third party.
- (iii) 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.

**EXCEPTIONS:**  
Non-registration of a firm does not, however effect the following rights:

1. The right of third parties to sue the firm or any partner.
2. 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.
3. The power of an Official Assignee or Receiver or the Court, as the case may be, to realise the property of an insolvent partner and to bring an action therefore, if necessary, on behalf of the insolvent
4. The right to sue or claim a set-off if the value of suit does not exceed Rs.100 in value.
5. The right to suit and proceeding instituted by legal representatives or heirs of the deceased partner of a firm for accounts of the firm or to realise the property of the firm.

DISSOLUTION OF FIRM

The Indian Partnership Act distinguishes between:

- (a) Dissolution of firm, and
- (b) Dissolution of partnership.

**Section 39** provides that the dissolution of partnership between all the partners of a firm is called the 'dissolution of the firm.' Thus, the dissolution of firm means the discontinuation of the jural relation existing between all the partners of the firm.

When a particular partner goes out, but the remaining partners carry on the business of the firm, it is called 'dissolution of partnership.'

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 FIRM VS. DISSOLUTION OF PARTNERSHIP

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.

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**MODES OF DISSOLUTION OF PARTNERHIP**

**WITHOUT ORDER OF COURT  
[VOLUNTARY]**

- (i) Dissolution by agreement (Sec 40)**  
A firm may be dissolved with the consent of all the partners or in accordance with a contract between the partners.
- (ii) Compulsory dissolution (Section 41):**  
When some event has happened which makes it unlawful for the business of the firm to be carried on or for the partners to carry it on in partnership (e.g., when any partner, who is a citizen of a foreign country, becomes an alien enemy because of the declaration of war between his country and India).  
But if firm is carrying on more than one adventures or undertakings, the illegality of one or more shall not of itself cause the dissolution.
- (iii) Dissolution on the happening of certain contingencies (Section 42):**  
Subject to contract between the partners, a firm can be dissolved on the happening of any of the following contingencies:  
a) if constituted for a fixed term, by the expiry of that term;  
b) if constituted to carry out one or more adventures or undertakings, by the completion thereof;  
c) by the death of a partner; and  
d) by the adjudication of a partner as an insolvent
- (iv) Dissolution by notice of partnership at will (Section 43):**
- Where the partnership is at will, the firm may be dissolved by any partner giving notice in writing to all the other partners of his intention to dissolve the firm.
  - If the date is mentioned, the firm is dissolved as from the date mentioned in the notice as the date of dissolution, or if no date is so mentioned, as from the date of the communication of the notice.

**DISSOLUTION BY THE COURT (SECTION 44):**

- (a) 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.
- (b) 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.
- (c) 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.**
- (d) Persistent breach of agreement:** Where a partner other than the partner suing, wilfully 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
  - Holding more cash than allowed
  - Keeping erroneous A/Cs
  - Refusal to show accounts
- (e) 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, the court may dissolve the firm at the instance of any other partner.
- (f) 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.
- (g) 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-** Compiled By:CA Sahil Grover
- (i) Deadlock in the management.
  - (ii) Where the partners are not in talking terms between them.
  - (iii) Loss of substratum.
  - (iv) Gambling by a partner on a stock exchange.

**CONSEQUENCES OF DISSOLUTION**

- Liability for acts of partners done after dissolution (Section 45):**  
Notwithstanding the dissolution of a firm, the partners continue to be liable as such to third parties for any act done by any of them which would have been an act of the firm if done before the dissolution, until public notice is given of the dissolution. The notice may be given by the firm or any partner.  
**Exceptions (No Liability even if no notice):** the estate of a deceased partner or an insolvent partner, or a dormant partner.
- Right of partners to have business wound up after dissolution (Sec 46):**  
On the diss. of a firm every partner or his representative is entitled, as against all the other partners or their representative, to have the property of the firm applied in payment of the debts and liabilities of the firm, and to have the surplus distributed among the partners or their representatives according to their rights.
- Continuing authority of partners for purposes of winding up (Sec. 47):**  
After the diss. of the firm the authority of each partner to bind the firm, and other mutual rights and obligations of the partners, continue for the following two purposes:
  - a) to wind up the affairs of the firm, e.g., disposing of the property, realising amount due from debtors and paying to creditors and so on; &
  - b) to complete transactions begun but unfinished at the time of the diss., e.g., taking delivery of the goods ordered before dissolution and paying for them.
- Settlement of partnership accounts (Section 48):** Compiled By:CA Sahil Grover
  - Settled in the manner provided for in the partnership agreement.
  - **In the absence of any agreement, following rules shall apply:**
    - 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 their profit share ratio.
    - The assets of the firm, including any sums contributed by the partners to make up deficiencies of capital, shall be applied in the following manner and order:
      - i. In paying the debts of the firm to third parties.
      - ii. In paying to each partner rateably what is due to him from the firm for advances as distinguished from capital.
      - iii. In paying to each partner rateably what is due to him on account of capital.
      - iv. The residue, if any, shall be divided among the partners in profit sharing ratio.
- Payment of firm debts and of separate debts (Section 49):**  
Where both debts due from the firm and debts due from a partner in his individual capacity exist the following rules shall apply:
  - a) The **property of the firm** shall be applied for payment of the firm's debts first, and if there is any surplus, then the share of each partner shall be applied in payment of his separate debts or paid to him.
  - b) The **separate property of any partner** shall be applied first in the payment of his separate debts and surplus, if any, in the payment of debts of the firm.

# THE INDIAN PARTNERSHIP ACT, 1932 (Chart 1.9)

## IMPORTANT DIFFERENCES

### DIFFERENCES BETWEEN PARTNERSHIP & COMPANY

### DIFFERENCES BETWEEN PARTNERSHIP & HUF

Basis	Partnership	Joint Stock Company	Basis of difference	Partnership	Joint Hindu family
<b>Legal status</b>	A firm is not legal entity i.e., it has no legal personality distinct from the personalities of its constituent members.	A company is a separate legal entity distinct from its members ( <i>Saloman v. Saloman</i> ).	<b>Mode of creation</b>	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
<b>Agency</b>	In a firm, every partner is an agent of the other partners, as well as of the firm.	In a company, a member is not an agent of the other members or of the company, his actions do not bind either.	<b>Death of a member</b>	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.
<b>Distribution of profits</b>	The profits of the firm must be distributed among the partners according to the terms of the partnership deed.	There is no such compulsion to distribute its profits among its members. Some portion of the profits, but generally not the entire profit, become distributable among the shareholders only when dividends are declared.	<b>Management</b>	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.
<b>Extent of liability</b>	In a partnership, the liability of the partners is unlimited. This means that each partner is liable for debts of a firm incurred in the course of the business of the firm and these debts can be recovered from his private property, if the joint estate is insufficient to meet them wholly.	In a company limited by shares, the liability of a shareholder is limited to the amount, if any, unpaid on his shares, but in the case of a guarantee company, the liability is limited to the amount for which he has agreed to be liable. However, there may be companies where the liability of members is unlimited.	<b>Authority to bind</b>	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.
<b>Property</b>	The firm's property is that which is the "joint estate" of all the partners as distinguished from the 'separate' estate of any of them and it does not belong to a body distinct in law from its members.	In a company, its property is separate from that of its members who can receive it back only in the form of dividends or refund of capital.	<b>Liability</b>	In a partnership, the liability of a partner is unlimited.  <span style="color: blue;">Compiled By: CA Sahil Grover</span>	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
<b>Transfer of shares</b>	A share in a partnership cannot be transferred without the consent of all the partners.	In a company a shareholder may transfer his shares, subject to the provisions contained in its Articles. In the case of public limited companies whose shares are quoted on the stock exchange, the transfer is usually unrestricted.	<b>Calling for accounts on closure</b>	A partner can bring a suit against the firm for accounts, provided he also seeks the dissolution of the firm.	On the separation of the joint family, a member is not entitled to ask for account of the family business.
<b>Management</b>	In the absence of an express agreement to the contrary, all the partners are entitled to participate in the management.  <span style="color: blue;">Compiled By: CA Sahil Grover</span>	Members of a company are not entitled to take part in the management unless they are appointed as directors, in which case they may participate. Members, however, enjoy the right of attending general meeting and voting where they can decide certain questions such as election of directors, appointment of auditors, etc.	<b>Governing Law</b>	A partnership is governed by the Indian Partnership Act, 1932.	A Joint Hindu Family business is governed by the Hindu Law.
<b>Registration</b>	Registration is not compulsory in the case of partnership.	A company cannot come into existence unless it is registered under the Companies Act, 2013.	<b>Minor's capacity</b>	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.
<b>Winding up</b>	A partnership firm can be dissolved at any time if all the partners agree.	A company, being a legal person is either wound up by the National Company Law Tribunal or its name is struck off by the Registrar of Companies.	<b>Continuity</b>	A firm subject to a contract between the partners gets 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
<b>Number of membership</b>	According to section 464 of the Companies Act, 2013, the number of partners in any association shall not exceed 100. However, the Rule given under the Companies (Miscellaneous) Rules, 2014 restricts the present limit to 50.	A private company may have as many as 200 members but not less than two and a public company may have any number of members but not less than seven. A private Company can also be formed by one person known as one person Company.	<b>Number of Members</b>	In case of Partnership number of members should not exceed 50.	Members of HUF who carry on a business may be unlimited in number.
<b>Duration of existence</b>	Unless there is a contract to the contrary, death, retirement or insolvency of a partner results in the dissolution of the firm	A company enjoys a perpetual succession			



# THE INDIAN PARTNERSHIP ACT, 1932 (Chart 1.10)

## IMPORTANT DIFFERENCES

### DIFFERENCES BETWEEN PARTNERSHIP & CLUB

### DIFFERENCES BETWEEN PARTNERSHIP & JOINT OWNERSHIP

Basis of Difference	Partnership	Club
<b>Definition</b>	It is an association of persons formed for earning profits from a business carried on by all or any one of them acting for all.	A club is an association of persons formed with the object not of earning profit, but of promoting some beneficial purposes such as improvement of health or providing recreation for the members,
<b>Relationship</b>	Persons forming a partnership are called partners and a partner is an agent for other partners.	Persons forming a club are called members. A member of a club is not the agent of other members.
<b>Interest in the property</b>	Partner has interest in the property of the firm.	A member of a club has no interest in the property of the club.
<b>Dissolution</b>	A change in the partners of the firm affect its existence.	A change in the membership of a club does not affect its existence.

Basis of difference	Partnership	Co-ownership
<b>Formation</b>	Partnership always arises out of a contract, express or implied.	Co-ownership may arise either from agreement or by the operation of law, such as by inheritance.
<b>Implied agency</b>	A partner is the agent of the other partners.	A co-owner is not the agent of other co-owners.
<b>Nature of interest</b>	There is community of interest which means that profits and losses must have to be shared.	Co-ownership does not necessarily involve sharing of profits and losses.
<b>Transfer of interest</b>	A share in the partnership is transferred only by the consent of other partners.	A co-owner may transfer his interest or rights in the property without the consent of other co-owners.

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### DIFFERENCES BETWEEN PARTNERSHIP & JOINT OWNERSHIP

Basis of difference	Partnership	Association
<b>Meaning</b>	Partnership means and involves setting up relation of agency between two or more persons who have entered into a business for gains, with the intention to share the profits of such a business.	Association evolve out of social cause where there is no necessarily motive to earn and share profits. The intention is not to enter in a business for gains.
<b>Examples</b>	Partnership to run a business and earn profit thereon.	Members of charitable society or religious association or an improvement scheme or building corporation or a mutual insurance society or a trade protection association.

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**THE SALES OF GOODS  
ACT, 1930**

# THE SALES OF GOODS ACT, 1930 (Chart 1.1)

## INTRODUCTION

- This Act extends to the **whole of India** except the State of J&K
- Came into force on the **1st July 1930**
- Contains **66 sections**
- Earlier part of Contract Act. **Sections 76-123 (Chapter VII)** were repealed and reenacted as **Sales of Goods Act, 1930**

### Provisions of Indian Contract Act shall Apply

**Sec 2(15):** Expressions used but not defined in this Act and defined in the Indian Contract Act, 1872, shall have the meanings assigned to them in that Act.

**Section 3:** The unrepealed provisions of the Indian Contract Act, 1872, save in so far as they are inconsistent with the express provisions of this Act, shall continue to apply to contracts for the sale of goods.

## CONTRACT OF SALE [SECTION 4(1)]

- a **contract** whereby the **seller**
- **transfers or agrees to transfer**
- the **property in goods**
- to the **buyer**
- for a **price**.

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## ESSENTIAL ELEMENTS OF CONTRACT OF SALE OF GOODS

- Two parties:**
  - There must be **two distinct parties** to a contract of sale, *viz.*, a **buyer and a seller**, as a **person cannot buy his own goods**.
- Transfer of property:**
  - **Property** here means **'ownership'**.
  - To constitute a contract of sale the **seller must either transfer or agree to transfer the property in the goods to the buyer**.
  - A **mere transfer of possession** of the goods **cannot be termed as sale**
  - **Property:** The term 'property,' as used in the Sale of Goods Act, means **'general property' in goods as distinguished from 'special property'** [Sec. 2(11)].
- Goods:**
  - Subject-matter of the contract of sale must be 'goods'.
  - **GOODS:** [Sec 2(7)]
  - "goods means every **kind of movable property**
  - **other than**
  - **actionable claims and money;** Compiled By:CA Sahil Grover
  - **and includes**
    - o **stock and shares,**
    - o **growing crops, grass, &**
    - o **things attached to or forming part of the land which are agreed to be severed before sale or under the contract of sale.**
  - Goodwill, trademarks, copyrights, patent rights, water, gas, electricity, are all regarded as goods.
  - **Money'** means **current money**. Old and rare coins, however, may be treated as goods and sold as such.
  - 'Actionable claims' means **claims which can be enforced by a legal action or a suit, e.g., a book debt (i.e., a debt evidenced by an entry by the creditor in his Account Book)**
- Price:**
  - Consideration for a contract of sale must be money consideration called the 'price.' **Price means the money consideration for a sale of goods.** [Section 2(10)].
  - If goods are sold or exchanged for other goods, the transaction is **barter**, governed by the **Transfer of Property Act** and not a sale of goods under this Act. But if goods are **sold partly for goods and partly for money, the contract is one of sale**.
- Includes both a 'sale' and 'an agreement to sell.'** [A contract of sale may be absolute or conditional.] **[Sec 4(2)]**  
The term 'contract of sale' is a **generic term and includes both a 'sale' and an 'agreement to sell'**. Section 4(2) states that a contract of sale can be absolute or conditional.
- Other essentials of a contract:**  
**All other essential elements of a valid contract must be present in the contract of sale, e.g. competency of parties, legality of object and consideration etc.**

## SALE AND AGREEMENT TO SELL (SECTION 4)

The term '**contract of sale**' is a **generic term** and includes both a '**sale**' and an '**agreement to sell**'. Section 4(2) states that a contract of sale can be absolute or conditional.

### SALE:

- Where under a contract of sale the property in the goods is immediately transferred at the time of making the contract from the seller to the buyer, the contract is called a '**sale**' [Sec. 4(3)].
- It refers to an '**absolute sale**', *e.g.*, an outright sale on a counter in a shop.

### AGREEMENT TO SELL:

- Where under a contract of sale the transfer of 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**' [Sec. 4(3)].
- It is an executory contract and refers to a **conditional sale**.

### WHEN AGREEMENT TO SELL BECOMES SALE [SEC. 4 (4)]:

'An agreement to sell' becomes a '**sale**' when

- o the time elapses or
- o the conditions are fulfilled subject to which the property in the goods is to be transferred

## CONTRACT OF SALE HOW MADE (SECTION 5)

- 1) A contract of sale is made by **an offer to buy or sell goods** for a price and the **acceptance of such offer**. The contract may provide for the **immediate delivery of the goods or immediate payment of the price or both, or for the delivery or payment by instalments, or that the delivery or payment or both shall be postponed**.
- 2) Subject to the provisions of any law for the time being in force, a contract of sale may be made **in writing or by word of mouth, or partly in writing and partly by word of mouth or may be implied from the conduct of the parties**.

## EXISTING OR FUTURE GOODS (SECTION 6):

- 1) The goods which form the subject of a contract of sale may be either **existing goods**, owned or possessed by the seller, or **future goods**.
- 2) There may be a contract for the sale of goods **the acquisition of which by the seller depends upon a contingency** which may or may not happen.
- 3) **Where by a contract of sale the seller purports to effect a present sale of future goods, the contract operates as an agreement to sell the goods**.

# THE SALES OF GOODS ACT, 1932 (Chart 1.2)

## CLASSIFICATION OF GOODS

### EXISTING GOODS

Goods as are **in existence at the time of the contract of sale, i.e., those owned or possessed by the seller at the time of contract of sale.**

The existing goods may be of following kinds:

#### SPECIFIC GOODS

- Goods **identified and agreed upon at the time a contract of sale is made [Section 2(14)]**
- **Example:** 'A' had five cars of different models. He agreed to sell his 'Fiat' car to 'B' and 'B' agreed to purchase the same car. In this case, the sale is for specific goods as the car has been identified and agreed at the time of the contract of sale.

#### ASCERTAINED GOODS

- Goods which are **identified in accordance with the agreement after the contract of sale is made.**
- **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.**
- 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.'
- **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

#### UNASCERTAINED GOODS

- Goods which are **not specifically identified or ascertained at the time of making of the contract.** They are indicated or defined only by description or sample.
- **Example:** If A agrees to sell to B one packet of salt out of the lot of one hundred packets lying in his shop, it is a sale of unascertained goods because it is not known which packet is to be delivered. As soon as a particular packet is separated from the lot, it becomes ascertained or specific goods.

### FUTURE GOODS [SEC 2(6)]

- Goods to be manufactured, produced or acquired by the seller after the making of the contract of sale.
- These goods may be **either not yet in existence or be in existence but not yet acquired by the seller.**
- Contract for the sale of future goods is **always an agreement to sell.**

**Example:** T agrees to sell to S all the oranges which will be produced in his garden this year. It is contract of sale of future goods, amounting to 'an agreement to sell.'

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### CONTINGENT GOODS [SEC 6(2)]

- Goods, the acquisition of which by the seller depends upon an uncertain contingency.
- They are a **type of future goods** and therefore a contract for the sale of contingent goods also operates as 'an agreement to sell'
- A contract of sale of contingent goods is **enforceable only if the event on the happening of which the performance of the contract is dependent happens, otherwise the contract become void.**

**Example:** X agrees to sell to Y 25 bales of Egyptian cotton, provided the ship which is bringing them reaches the port safely. It is a contract for the sale of contingent goods. If the ship is sunk, the contract becomes void and the seller is not liable

## EFFECT OF PERISHING OF GOODS [SEC 7 & 8]

- Under these Sections the word '**perishing**' means **not only physical destruction of the goods but it also covers damage to goods so that the goods have ceased to exist in the commercial sense, i.e., their merchantable character as such has been lost, loss of goods by theft or where the goods have been lawfully requisitioned by the government.**
- Only the perishing of **specific and ascertained goods** affects a contract of sale.
- Where **unascertained goods** form the subject-matter of a contract of sale, their perishing **does not affect the contract** and the seller is bound to supply the goods from wherever he likes, otherwise be liable for breach of contract.

### Perishing of specific goods at/before making of the contract (Sec. 7)

- Where there is a contract for the sale of specific goods, **the contract is void if the goods without the knowledge of the seller have, at the time when the contract was made, perished or become so damaged as no longer to answer to their description contract.**
- This provision is based either on the ground of **mutual mistake** as to a matter of fact essential to the agreement, or on the ground of **impossibility of performance**, both of which render an agreement void *ab-initio*.
- **Example:** A agrees to sell to B a certain horse. It turns out that the horse was dead at the time of bargain, though neither party was aware of the fact. The agreement is void

### Perishing of specific goods before sale but after agreement to sell (Sec. 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 before the risk passes to the buyer, the agreement is thereby avoided, i.e., the contract of sale becomes void, and both parties are excused from performance of the contract.**
- If fault of either party causes the destruction of the goods, then the party in default is liable for non-delivery or to pay for the goods, as the case may be
- **Example:** A buyer took a horse on a trial for 8 days on condition that if found suitable for his purpose the bargain would become absolute. The horse died on the 3rd day without any fault of either party. *Held*, the contract, which was in the form of an agreement to sell, becomes void and the seller should bear the loss.

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## PRICE

### MODES OF FIXING THE PRICE (SECTION 9)

- **Money consideration for a sale of goods is known as 'price' [Sec. 2(10)].**
  - **Essential element in every contract of sale of goods, no valid sale can take place without a price.**
  - **Paid or promised to be paid in legal tender money**
1. It may be **expressly fixed by the contract itself.**
  2. It may be **fixed in accordance with an agreed manner provided by the contract.**
  3. It may be **determined by the course of dealings between the parties.**  
[For eg., if the buyer has been previously paying to particular seller the price prevailing on the date of placing the order,]
  4. If the price is **not capable of being determined in accordance with any of the above modes, the buyer is bound to pay to the seller a 'reasonable price.'**  
[What is a reasonable price is a question of fact dependent on the circumstances of each particular case.]

### AGREEMENT TO SELL AT VALUATION (SEC 10)

- Sec 10 provides for the **determination of price by a third party.**
- Where there is an agreement to sell goods on the terms that **price has to be fixed by the third party & he either does not or cannot make such valuation, the agreement will be void.**
- In case the **third party is prevented by the default of either party from fixing the price, the party at fault will be liable to the damages** to the other party who is not at fault.
- However, a **buyer who has received and appropriated the goods must pay a reasonable price for them**

**DOCUMENT OF TITLE TO GOODS [Sec. 2(4)].**

- "Any document which is used in the ordinary course of business as proof of the possession or control of goods, or authorizing or purporting to authorize, either by endorsement or by delivery, the possessor of the document to transfer or receive goods thereby represented is a document of title to goods".

- A document of title is a **proof of the ownership of the goods.**

- It **authorizes its holder to receive goods mentioned therein or to further transfer such right to another person by proper endorsement or delivery.**

- A document of title to goods contains an **undertaking on the part of the issuing authority to deliver the goods to the holder** thereof unconditionally.

Examples:  
Bill of lading, dock warrant, warehouse keeper's certificate, wharfinger's certificate, railway receipt

- There is a difference between a 'document showing title' and 'document of title'. A share certificate is a 'document showing title' but **not a document of title.** It merely shows that the person named in the share certificate is entitled to the share represented by it, but it does **not allow that person to transfer the share mentioned therein by mere endorsement on the back of the certificate and the delivery of the certificate.**

**STIPULATIONS AS TO TIME [SEC 11]**

Stipulations as to time in a contract of sale fall under the **following two heads:**

- 1) Stipulation relating to **time of delivery of goods.**
- 2) Stipulation relating to **time of payment of the price.**

**As regards the time fixed for the delivery of goods**

- Time of delivery of goods is usually held 'to be of the essence of the contract.'

- Thus if time is fixed for the delivery of goods and the seller makes a delay, the contract is voidable at the option of the buyer.

- In case of late delivery, therefore, the buyer may refuse to accept the delivery and may put an end to the contract.

**As regards the time fixed for the payment of the price**

- The **general rule** is that **'time is not deemed to be of the essence of the contract,' unless a different intention appears from the terms of the contract (Sec. 11).**

- Thus **even if the price is not paid as agreed, the seller cannot avoid the contract on that account. He has to deliver the goods** if the buyer tenders the price **within reasonable time** before resale of the goods.

- The **seller may, however, claim compensation** for the loss occasioned to him by the buyer's failure to pay on the appointed day.

**CONDITIONS & WARRANTIES**

DEFINITION [SEC 12]

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

CONDITION DEFINED

A 'condition' is a **stipulation essential to the main purpose of the contract, the breach of which gives the aggrieved party a right to repudiate the contract itself [Sec. 12(2)].**

WARRANTY DEFINED

A 'warranty' is a **stipulation collateral to the main purpose of the contract, the breach of which gives the aggrieved party a right to sue for damages only, and not to avoid the contract itself [Sec. 12(3)]**

A 'condition' forms the very basis of a contract of sale, the breach of which causes irreparable damage to the aggrieved party so as to entitle him even to repudiate the contract, whereas a 'warranty' is only of secondary importance, the breach of which causes only such damage as can be compensated for by damages.

**STIPULATION-CONDITION OR WARRANTY?**

- There is no hard and fast rule as to which stipulation is a condition and which one is a warranty.

- Section 12(4) lays down to the same effect, thus, **"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."**

- Thus the **court is not to be guided by the terminology of the parties** but has to **look to the intention of the parties** by referring to the terms of the contract, its construction and the surrounding circumstances

EXAMPLE: P goes to R, a horse dealer, and says, "I want a horse which can run at a speed of 30 kilometers per hour." The horse dealer points out a particular horse and says, "This will suit you." P buys the horse. Later on P finds that the horse can run only at a speed of 20 kilometers per hour. There is a breach of condition, P can repudiate the contract, return the horse to R and get back the price.

But if P says to R, "I want a good horse." R shows him a horse and says, "This is a good horse and it can run at a speed of 30 kilometers per hour," and P buys the horse and finds later on that it can run at a speed of 20 kilometers per hour only, there is a breach of warranty because the stipulation made by the seller did not form the very basis of the contract and was only subsidiary one. The seller gave the assurance about the running speed of the horse of his own without being asked by the buyer hence it is only of secondary importance.

WHEN CONDITION TO BE TREATED AS WARRANTY (SECTION 13)

- (i) Where the **buyer altogether waives the performance of the condition.** A party may for his own benefit, waive a stipulation.
- (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.  
Example: A agrees to supply B 10 bags of first quality sugar @ Rs.625 per bag but supplies only second quality sugar, the price of which is Rs.600 per bag. There is a breach of condition and the buyer can reject the goods. But if the buyer so elects, he may treat it as a breach of warranty, accept the second quality sugar and claim damages @ Rs.25 per bag.
- (iii) Where the **contract is non-severable and the buyer has accepted either the whole goods or any part thereof.**
- (iv) Where the **fulfillment of any condition or warranty is excused by law by reason of impossibility or otherwise.**

**DIFFERENCE BETWEEN CONDITIONS AND WARRANTIES**

Point of differences	Condition	Warranty
Meaning	A condition is essential to the main purpose of the contract.	It is only 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.

**EXPRESS AND IMPLIED CONDITIONS AND WARRANTIES (SECTION 14-17)**

Conditions' and 'Warranties' may be either express or implied. Express conditions are those, which are agreed upon between the parties at the time of contract and are expressly provided in the contract.- The implied conditions, on the other hand, are those, which are presumed by law to be present in the contract.

**Following conditions are implied in a contract of sale of goods unless the circumstances of the contract show a different intention**

Condition as to title [Section 14(a)]	Condition in a Sale by description [Sec 15]	Condition in a sale by sample (Sec. 17)	Condition in a sale by sample as well as by description (Sec. 15)
<p>In <b>every contract of sale</b>, unless there is an agreement to the contrary, the first implied condition on the part of the seller is that</p> <p>a) In case of a <b>sale, he has a right to sell the goods</b>, and</p> <p>b) In the case of an <b>agreement to sell, he will have right to sell the goods at the time when the property is to pass</b></p> <p>In simple words, the condition implied is that the <b>seller has the right to sell the goods at the time when the property is to pass.</b></p> <p>As a result of this condition, if <b>the seller's title turns out to be defective the buyer is entitled to reject the goods and to recover his price.</b></p>	<ul style="list-style-type: none"> <li>- Where there is a <b>contract of sale of goods by description</b>, there is an <b>implied condition</b> that the <b>goods shall correspond with the description.</b> (Sec 15)</li> <li>- The <b>buyer is not bound to accept and pay</b> for the goods which are <b>not in accordance with the description</b> of goods.</li> <li>- The <b>Act, however, does not define 'description'</b>. A sale has been deemed to be by the description                         <ul style="list-style-type: none"> <li>a) where the class or kind to which the goods belong has been specified, e.g., 'Egyptian cotton', "basmati rice", etc., and</li> <li>b) where the goods have been described by certain characteristics essential to their identification, e.g., jute bales of specified shipment, steel of specific dimension, etc.</li> </ul> </li> </ul>	<p>When under a contract of sale, <b>goods are to be supplied according to a sample</b> agreed upon, the implied conditions are:</p> <ul style="list-style-type: none"> <li>i. that the <b>bulk shall correspond with the sample in quality;</b></li> <li>ii. that the <b>buyer shall have a reasonable opportunity of comparing the bulk with the sample;</b></li> <li>iii. that the <b>goods shall be free from any defect, rendering them unmerchantable</b>, which would not be apparent on reasonable examination of the sample.</li> </ul> <p>In other words, <b>there should not be any latent defect in the goods.</b></p> <p>If the <b>defect is patent</b> one, that is, easily discoverable by the exercise of ordinary care, and the <b>buyer takes delivery after inspection, there is no breach of implied condition</b> and the buyer has no remedy.</p>	<ul style="list-style-type: none"> <li>- When <b>goods are sold by sample as well as by description</b>, there is an implied condition that the <b>bulk of the goods shall correspond both with the sample and with the description.</b></li> <li>- If the goods supplied correspond only with the sample and not with the description or vice versa, the buyer is entitled to reject the goods. <b>The bulk of the goods must correspond with both.</b></li> </ul> <p style="text-align: right;">Compiled By:CA Sahil Grover</p>
Condition as to fitness or quality [Sec. 16 (1)]	Condition as to merchantability [Sec. 16(2)]	Condition as to wholesomeness	
<p>Ordinarily, in a contract of sale there is <b>no implied condition or warranty as to quality or fitness</b> for any particular purpose of goods supplied; the rule of law being '<u>Caveat Emptor</u>', <i>that is, let the buyer beware.</i></p> <p>But an <b>implied condition is deemed to exist</b> on the part of the seller that the goods supplied shall be fit for the purpose for which the buyer wants them, <b>if the following conditions are satisfied:</b></p> <ul style="list-style-type: none"> <li>(i) The <b>buyer, expressly or impliedly, should make known to the seller</b> the particular purpose for which the goods are required;</li> <li>(ii) The <b>buyer should rely on the seller's skill or judgement;</b> and</li> <li>(iii) The goods sold must be <b>of a description which the seller deals in the ordinary course of his business</b>, whether he be the manufacturer or not</li> </ul> <p>The <b>purpose need not be told</b> expressly if the <b>goods are fit for one particular purpose only</b> or if the nature of the goods itself tells the purpose by implication. In such cases the purpose is deemed to be made known to the seller impliedly.</p> <p><b>Sale under patent or trade name:</b> Proviso to Section 16 (1) lays down that in the case of a contract for the sale of a specified article <b>under its patent or other trade name, there is no implied condition as to its fitness for any particular purpose.</b></p>	<p>Section 16(2) lays down another implied condition in such cases, that is, that the <b>goods should be of 'merchantable quality.'</b> This condition is implied <b>only where the sale is by description.</b></p> <p>For making this condition applicable, not only that the sale must be by description, but the <b>following conditions must also be satisfied:</b></p> <ul style="list-style-type: none"> <li>(i) The <b>seller should be a dealer in goods of that description</b>, whether he be the manufacturer or not; and</li> <li>(ii) The <b>buyer must not have any opportunity of examining the goods</b> or there must be <b>some latent defect</b> in the goods which would not be apparent on reasonable examination of the same.</li> </ul> <p><b>Merchantable Quality:</b></p> <p>The phrase 'merchantable quality' means that the goods are of such quality and in such condition that a <b>reasonable man, acting reasonably, would accept them under the circumstances of the case in performance of his offer to buy those goods</b>, whether he buys them for his own use or to sell again.</p> <p><b>Stated briefly, in order to be ' merchantable' the goods must be such as are reasonably saleable under the description by which they are known in the market.</b></p>	<p>This condition is implied only in a contract of sale of <b>eatables &amp; provisions.</b></p> <p>In such cases the <b>goods supplied must not only answer to description and be merchantable but must also be wholesome, i.e., free from any defect which render them unfit for human consumption.</b></p> <p style="text-align: right;">Compiled By:CA Sahil Grover</p>	



**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. Implied warranties are read into every contract of sale unless they are expressly excluded by the express agreement of the parties.

Sections 14 and 16 of the Sale of Goods Act, 1930 discloses the following implied warranties:

**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)]**

The second implied warranty is 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. If the goods are afterwards found to be subject to a charge and the buyer has to discharge the same, there is breach of warranty and the buyer is entitled to damages. If the buyer knows about the encumbrance on the goods at the time of entering into the contract, he becomes bound by the same and he is not entitled to claim compensation from the seller for discharging the same.

**3. Warranty as to quality or fitness by usage of trade [Sec 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. Warranty of disclosing the dangerous nature of goods to the ignorant buyer:**

The fourth implied warranty on the part of the seller is that in case the goods sold are of dangerous nature he will warn the ignorant buyer of the probable danger. If there is breach of this warranty the buyer is entitled to claim compensation for the injury caused to him.

**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.
- It is the duty of the buyer to satisfy himself before buying the goods that the goods will serve the purpose for which they are being bought.
- If the goods turn out to be defective or do not serve his purpose or if he depends on his own skill or judgment, the buyer cannot hold the seller responsible.

Section 16, states that, "*subject to the provisions of this Act or 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: The doctrine of Caveat Emptor is, however, subject to the following exceptions:

Fitness as to quality or use	Goods purchased under patent or brand name	Goods of Merchantable Quality
<p>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)].</p> <p><u>Following are the conditions to be satisfied: -</u></p> <ul style="list-style-type: none"> <li>-if the buyer had made known to the seller the purpose of his purchase, and</li> <li>-the buyer relied on the seller's skill and judgment, and</li> <li>-seller's business to supply goods of that description (Section 16).</li> </ul>	<p>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)].</p>	<p>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.</p> <p>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)].</p>
<p>Where the article can be used for only one particular purpose, the buyer need not tell the seller the purpose for which he required the goods. But where the article can be used for a number of purposes, the buyer should tell the seller the purpose for which he requires the goods, if he wants to make the seller responsible.</p>	<p><b>Goods sold by description</b></p> <p>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.</p>	<p><b>Sale by sample</b></p> <p>Where the goods are bought by sample, this rule of Caveat Emptor does not apply if the bulk does not correspond with the sample [Sec 17].</p>
<p>Where the article can be used for only one particular purpose, the buyer need not tell the seller the purpose for which he required the goods. But where the article can be used for a number of purposes, the buyer should tell the seller the purpose for which he requires the goods, if he wants to make the seller responsible.</p>	<p><b>Trade Usage</b></p> <p>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 [Sec 16(3)].</p>	<p><b>Goods by sample as well as description</b></p> <p>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].</p>
<p>Compiled By:CA Sahil Grover</p>	<p><b>Seller actively conceals a defect or is guilty of fraud</b></p>	
	<p>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.</p>	

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A. SPECIFIC OR ASCERTAINED GOODS	B. UNASCERTAINED GOODS	C. GOODS SENT ON APPROVAL OR "ON SALE OR RETURN" (SEC 24)
<ul style="list-style-type: none"> <li>- Where there is a contract for the sale of specific or ascertained goods the property in them is transferred to the buyer <b>at such time as the parties to the contract intend it to be transferred.</b> [sub-section (1)]</li> <li>- For the purpose of ascertaining the <b>intention of the parties regard shall be had to the terms of the contract, the conduct of the parties and the circumstances of the case.</b> [sub-section (2)]</li> <li>- Unless a different intention appears, the <b>rules contained in sections 20 to 24</b> are rules for ascertaining the intention of the parties as to the time at which the property in the goods is to pass to the buyer. [Sub- section (3)]</li> </ul>	<ul style="list-style-type: none"> <li>- The rule relating to transfer of property in <b>unascertained &amp; future goods is contained in Sec 18 &amp; 23.</b></li> <li>- Where there is a contract for the sale of unascertained goods, <b>no property in the goods is transferred to the buyer unless and until the goods are ascertained.</b> [Section 18]</li> <li>- <b>Sale of unascertained goods by description [Sec 23(1)]:</b> Where there is a contract for the sale of unascertained or future goods by description and goods of that description and in a deliverable state are <b>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,</b> the property in the goods thereupon passes to the buyer. Such assent may be express or implied, &amp; may be given either before or after the appropriation is made.</li> </ul>	<p>When goods are delivered to the buyer on approval or "on sale or return" or other similar terms, <b>the property therein passes to the buyer</b></p> <ul style="list-style-type: none"> <li>a) when he <b>signifies his approval or acceptance to the seller</b></li> <li>b) if he <b>does not signify his approval or acceptance to the seller but retains the goods without giving notice of rejection,</b> 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 <b>reasonable time;</b> or</li> <li>c) he does <b>something to the good which is equivalent to accepting the goods</b> e.g. he pledges or sells the goods.</li> </ul>
<p><b>When goods are in a deliverable state (Sec. 20)</b></p> <p>Where there is an <b>unconditional</b> (i.e., not subject to any condition precedent to be fulfilled by the parties) contract for the <b>sale of specific goods in a deliverable state,</b> the property in the goods passes to the buyer <b>as soon as the contract is made, and it is immaterial whether the time of payment of the price or the time of delivery of the goods, or both are postponed.</b></p> <p><b>Deliverable state:</b> The goods are said to be in a 'deliverable state' when they are in such a state that the buyer would, under the contract, be bound to take delivery of them [Sec. 2(3)].</p>	<p><b>SALE OF UNASCERTAINED GOODS AND APPROPRIATION</b></p> <p>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.</p> <p><b>The essentials are:</b></p> <ol style="list-style-type: none"> <li>There is a contract for the sale of unascertained or future goods.</li> <li>The goods should conform to the description and quality stated in the contract.</li> <li>The goods must be in a deliverable state.</li> <li>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.</li> <li>The appropriation must be made by:             <ol style="list-style-type: none"> <li>the seller with the assent of the buyer; or</li> <li>the buyer with the assent of the seller.</li> </ol> </li> <li>The assent may be express or implied.</li> <li>The assent may be given either before or after appropriation.</li> </ol> <p style="text-align: right;">Compiled By:CA Sahil Grover</p>	<p><b>SALE FOR CASH ONLY OR RETURN</b></p> <p>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., cash is paid for.</p> <p style="text-align: right;">Compiled By:CA Sahil Grover</p>
<p><b>When goods have to be put in deliverable state (Sec.21)</b></p> <p>Where there is a contract for the <b>sale of specific goods &amp; the seller is bound to do 'something' to the goods</b> for the purpose of putting them into a deliverable state, <b>the property does not pass until such thing is done and the buyer has notice thereof.</b></p> <p>The word 'something' here means an act like packing the goods, or loading them on rail or ship, or filling them in containers or polishing them in order to give a finished shape, etc.</p>	<p><b>DELIVERY TO CARRIER [SEC. 23(2)]</b></p> <ul style="list-style-type: none"> <li>- Where, in pursuance of the contract, <b>the seller delivers the goods to the buyer or to a carrier or other bailee</b> (whether named by the buyer or not) for the purpose of transmission to the buyer, <b>and does not reserve the right of disposal,</b> he is <b>deemed to have unconditionally appropriated the goods to the contract.</b>[Section 23(2)]</li> </ul>	
<p><b>When the goods have to be measured etc., to ascertain price (Sec. 22)</b></p> <p>Where there is a contract for the <b>sale of specific goods in a deliverable state,</b> but the <b>seller is bound to weigh, measure, test or do some other act or thing</b> with reference to the goods <b>for the purpose of ascertaining the price,</b> the property does not pass until such act or thing is done and the buyer has notice thereof.</p>	<p><b>RESERVATION OF RIGHT OF DISPOSAL (SEC 25)</b></p> <ul style="list-style-type: none"> <li>- This section preserves the right of disposal of goods to secure that the price is paid before the property in goods passes to the buyer.</li> <li>- Where there is contract of sale of specific goods or where the goods have been subsequently appropriated to the contract, <b>the seller may, by the terms of the contract or appropriation, as the case may be, reserve the right to dispose of the goods, until certain conditions have been fulfilled.</b></li> <li>- In such a case in spite of the fact that the goods have already been delivered to the buyer or to a carrier or other bailee for the purpose of transmitting the same to the buyer, the property therein will not pass to the buyer till the condition imposed, if any, by the seller has been fulfilled.</li> </ul> <p><b>Circumstances under which the right to disposal may be reserved:</b></p> <ol style="list-style-type: none"> <li>If the goods are shipped or delivered to a railway administration for carriage and by the bill of lading or railway receipt, as the case may be, the goods are deliverable to the order of the seller or his agent, then the seller will be prima facie deemed to have reserved to the right of disposal.</li> <li>Where the seller draws a bill on the buyer for the price and sends to him the bill of exchange together with the bill of lading or (as the case may be) the railway receipt to secure acceptance or payment thereof, the buyer must return the bill of lading, if he does not accept or pay the bill. And if he wrongfully retains the bill of lading or the railway receipt, the property in the goods does not pass to him.</li> </ol> <p><b>Thus section 25 deals with "conditional appropriation" as distinguished from 'unconditional appropriation' dealt with under Section 23 (2)</b></p>	

# THE SALES OF GOODS ACT, 1930 (Chart 1.7)

## RISK PRIMA FACIE PASSES WITH PROPERTY

According to **Sec 26**, the general rule is, **"unless otherwise agreed, the goods remain at the seller's risk until the property therein is transferred to the buyer, but when the property therein is transferred to the buyer, the goods are at the buyer's risk whether delivery has been made or not"**

**The aforesaid rule is, however, subject to two qualifications:**

- i. If **delivery has been delayed by the fault of the seller or the buyer**, the goods shall be at the risk of the party in default, as regards loss which might not have arisen but for the default.
- ii. The **duties and liabilities of the seller or the buyer as bailee of goods** for the other party remain unaffected even when the risk has passed generally

**The parties may, however, agree to the contrary.** For instance, the parties may agree that risk will pass sometime after or before the property has passed from the seller to the buyer.

## RULE OF TRANSFER OF TITLE ON SALE [SECTION 27]

- The general rule relating to the transfer of title on sale is that "the seller cannot transfer to the buyer of goods a better title than he himself has." If the title of the seller is defective the buyer's title will also be subject to the same defect.
- **Section 27** also lays down to the same effect and provides that **"where goods are sold by a person who is not the owner thereof and who does not sell them under the authority or with the consent of the owner, the buyer acquires no better title to the goods than the seller had"**.
- This rule is expressed by the maxim, **"nemo det quod non habet"** which means that **'no one can give what he has not got.'** Thus a buyer cannot get a good title to the goods unless he purchases the goods from a person who is the owner thereof or who sells them under the authority or with the consent of the owner.

### TRANSFER OF TITLE BY NON-OWNERS

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The above general rule as to title is subject to the following exceptions where the buyer gets a better title to the goods than what the seller himself possesses:

<b>Sale by a mercantile agent (Proviso to Sec. 27)</b>	<b>Sale by a joint owner (Sec. 28)</b>	<b>Sale by person in possession under voidable contract (Sec. 29)</b>	
<ul style="list-style-type: none"> <li>- A 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 [Sec. 2(9)].</li> <li>- <b>Thus as a rule a mercantile agent having an authority to sell goods conveys a good title to the buyer.</b></li> <li>- But by virtue of this provision (proviso to Sec. 27) a mercantile agent can convey a good title to the buyer even though he sells goods <i>without having any authority</i> from the principal to do so, <b>provided the following conditions are satisfied:</b> <ol style="list-style-type: none"> <li>i. he should be in <b>possession of the goods or documents of title to the goods</b> in his capacity as mercantile agent and with the consent of the owner,</li> <li>ii. he should <b>sell the goods while acting in the ordinary course of business</b> as a mercantile agent,</li> <li>iii. the buyer <b>should act in good faith without having any notice, at the time of the contract, that the agent has no authority to sell</b></li> </ol> </li> </ul>	<ul style="list-style-type: none"> <li>- If one of several <b>joint owners of goods has the sole possession of them by permission of the co- owners</b>, the property in the goods is <b>transferred to any person who buys them from such joint owner in good faith without notice of the fact that the seller has no authority to sell.</b></li> <li>- It may be noted that in the absence of this provision (<i>i.e.</i>, Sec. 28) the buyer would have obtained only the title of the co-owner and would have become merely a co-owner with the other co-owners. Hence the provision constitutes an exception to the rule - "no one can give what he has not got."</li> </ul>	<p>When a person has obtained <b>possession of the goods under a voidable contract</b> (on the ground of coercion, fraud, misrepresentation or undue influence) and <b>he sells those goods before the contract has been rescinded, the buyer of such goods acquires a good title to them provided the buyer acts in good faith and without notice of the seller's defect of title</b></p>	
	<b>Transfer of title by estoppel (Sec. 27).</b>	<b>Sale by one who has already sold the goods but continues in possession thereof [Sec 30(1)]</b>	<b>Sale by buyer obtaining possession before the property in the goods has vested in him [Sec 30(2)]</b>
	<p>When the true owner of the goods by his <b>conduct or words or by any act or omission leads the buyer to believe that the seller is the owner of the goods or has the authority to sell them</b>, he cannot afterwards deny the seller's authority to sell. The buyer in such a case gets a better title than that of the seller.</p>	<p>Where a seller, <b>after having sold the goods, continues to be in possession of the goods</b> or of the documents of title to them and again sells or pledges them either himself or through a mercantile agent, <b>he will convey a good title to the buyer or the pledgee</b> provided the buyer or the pledgee acts in good faith and without notice of the previous sale.</p>	<ul style="list-style-type: none"> <li>- Where a <b>buyer has agreed to buy the goods and has obtained possession of the same or the documents of title to them with the consent of the seller, resells or pledges</b> the goods either himself or through a mercantile agent, he will convey a good title to the buyer or the pledgee provided the person receiving the goods acts in good faith and without notice of any lien or other right of the original seller in respect of those goods.</li> <li>- A person who has got merely 'an option to buy,' as in a hire-purchase agreement, cannot convey a good title to a sub-buyer, however <i>bona fide</i>, for 'an option to buy' is not 'an agreement to buy'</li> </ul>
	<b>Resale by an unpaid seller [Sec. 54(3)].</b>	<b>Sale under the provisions of other Acts</b>	
	<p>Where an <b>unpaid seller, who has exercised his right of lien or stoppage in transit, resells the goods</b> (of which ownership has passed to the buyer), <b>the subsequent buyer acquires a good title</b> thereto as against the original buyer, even though the resale may not be justified in the circumstances, <i>i.e.</i>, <b>no notice of the resale has been given to the original buyer.</b></p>	<ol style="list-style-type: none"> <li>i. <b>Sale by an Official Receiver or Liquidator of the Company</b> will give the purchaser a valid title.</li> <li>ii. <b>Purchase of goods from a finder of goods will get a valid title</b> under certain circumstances [Section 169 of the Indian Contract Act, 1872]</li> <li>iii. <b>A sale by pawnee can convey a good title to the buyer</b> [Section 176 of the Indian Contract Act, 1872]</li> </ol>	
		Compiled By:CA Sahil Grover	

## THE SALES OF GOODS ACT, 1930 (Chart 1.8)

- Section 31: "It is the duty of the seller to deliver the goods and of the buyer to accept and pay for them, in accordance with the terms of the contract of sale". Thus, the performance of a contract of sale implies *delivery of goods* by the seller and *acceptance of the delivery* of goods and *payment* for them by the buyer, in accordance with the contract.
- The parties are free to provide any terms they like in their contract about the time, place and manner of delivery of goods, acceptance thereof and payment of the price. **But if the parties are silent and do not provide any thing regarding these matters in the contract then the rules contained in the Sale of Goods Act are applicable.**

### DELIVERY

- Delivery of goods means voluntary transfer of possession of goods from one person to another [Sec. 2(2)].
- If transfer of possession of goods is not voluntary, *i.e.*, possession is obtained under pistol point or by theft, there is no delivery.
- 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

Delivery of goods may be made in any of the following ways:

- 1) Actual delivery.**  
Where the goods are physically handed over by the seller (or his authorised agent) to the buyer (or his authorised agent), the delivery is said to be actual. For example, the seller of a car hands over the car to the buyer, there is actual delivery of the goods.
- 2) Constructive delivery or delivery by attornment:**  
It is effected without any change in the custody or actual possession of the thing. Such a delivery takes place when the person in possession of the goods of the seller acknowledges, in accordance with the seller's order that he holds the goods on behalf of the buyer and the buyer has assented to it. In such a delivery all the three parties, namely, the seller, the person holding the seller's goods and the buyer, must concur.
- 3) 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.

### RULES AS TO DELIVERY OF GOODS

- 1) Delivery may be either actual or symbolic or constructive (Sec. 33)**  
Delivery of goods sold may be made by doing anything which the parties agree shall be treated as delivery or which has the effect of putting the goods in the possession of the buyer or of any person authorised to hold them on his behalf. Thus, the delivery of the goods may be either *actual*, or *symbolic* or *constructive*
- 2) Delivery and payment are concurrent conditions (Sec. 32)**  
Unless otherwise agreed, delivery of the goods and payment of the price are *concurrent conditions*, that is, the seller should be ready and willing to deliver the goods to the buyer in exchange for the price and the buyer should be ready and willing to pay the price in exchange for possession of the goods simultaneously, just like in a cash sale over a shop counter.
- 3) Effect of part delivery, when property in goods is to pass on delivery (Sec. 34):** When a delivery of part of the goods has been made with the intention of delivering the rest also, the property in the whole of the goods is deemed to pass to the buyer as soon as some portion is delivered. But when a part of the goods is delivered with the intention of severing it from the whole, it is not regarded as delivery of the whole of the goods and the property is deemed to pass to the buyer in that portion of the goods only which has been delivered.  
*These rules are applicable only when passing of property has been made dependent on delivery of the goods.*
- 4) Buyer to apply for delivery (Sec. 35):**  
Although it is the duty of the seller to deliver the goods according to the contract, yet he is not bound to deliver them until the buyer applies for delivery. It is the duty of the buyer to demand delivery, and if he fails to do so, he cannot blame the seller for the non-delivery. The parties may, however, agree otherwise
- 5) Place of delivery [Sec. 36(1)]:**  
The place of delivery may be stated in the contract of sale, and where it is so stated, the goods must be delivered at the named place during business hours on a working day. But where no place is mentioned in the contract, the following rules must be followed:
  - i. In the **case of 'sale'**, - at the place at which they are at the time of the sale.
  - ii. In **"an agreement to sell"** - at the place where they are at the time of the agreement to sell.
  - iii. In the **case of future goods** - at the place at which they are manufactured or produced
- 6) Time of delivery [Section 36(2)] :**  
Where under the contract of sale the seller is bound to send the goods to the buyer, but no time for sending them is fixed, the seller is bound to send them within a reasonable time
- 7) Time for tender of delivery [Section 36(4)]**  
Demand of delivery by buyer or tender of delivery by seller may be treated as ineffectual unless made at a reasonable hour. What is reasonable hour is a question of fact.
- 8) Delivery of goods where they are in possession of a third party [Sec. 36(3)]:** Where the goods at the time of sale are in the possession of a third person, there is no delivery by the seller to the buyer unless and until such third person acknowledges to the buyer that he holds the goods on his behalf. Such a delivery is known as "constructive delivery" or "delivery by attornment" and requires the consent of all the three parties.
- 9) Expenses of delivery [Sec. 36(5)]:**  
Unless otherwise agreed, the expenses of and incidental to putting the goods into a deliverable state must be borne by the seller.
- 10) Delivery of wrong quantity [Section 37]:**
  1. Seller delivers a **quantity of goods less than he contracted to sell**, the buyer may reject them, but if the buyer accepts he shall pay for them at the contract rate.
  2. Seller delivers to the **buyer a quantity of goods larger than he contracted to sell**, the buyer may accept the goods included in the contract and reject the rest, or he may reject the whole. If the buyer accepts the whole of the goods, he shall pay for them at the contract rate.
  3. Where the seller delivers to **the buyer the goods he contracted to sell mixed with goods of a different description** not included in the contract, the buyer may accept the goods which are in accordance with the contract and reject, or may reject the whole.
- 11) Instalment deliveries (Sec 38):**  
Unless otherwise agreed, the buyer is not bound to accept delivery in instalments. The rights and liabilities in cases of delivery by instalments and payments thereon may be determined by contract.
- 12) Delivery to carrier[Sec 39(1)]:**  
Subject to the terms of contract, the delivery of the goods to the carrier for transmission to the buyer, is *prima facie* deemed to be delivery to the buyer.
- 13) Deterioration during transit (Section 40):**  
Where goods are delivered at a distant place, the liability for deterioration necessarily incidental to the course of transit will fall on the buyer, though the seller agrees to deliver at his own risk.
- 14) Buyer's right to examine the goods (Sec 41)**  
Where goods are delivered to the buyer, who has not previously examined them, he is entitled to a reasonable opportunity of examining them in order to ascertain whether they are in conformity with the contract.
- 15) Liability of buyer for neglecting/ refusing to take delivery of goods (Sec. 44):**  
When the seller is ready and willing to deliver the goods and requests the buyer to take delivery, and the buyer does not within a reasonable time after such request take delivery of the goods, he becomes 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.
- 16) Buyer not bound to return rejected goods (Section 43):**  
Unless otherwise agreed, where goods are delivered to the buyer and he refuses to accept them, having the right so to do, he is not bound to return them to the seller, but it is sufficient if he intimates to the seller that he refuses to accept them

ACCEPTANCE OF DELIVERY BY BUYER [SEC 42]

The mere fact that the buyer has taken the delivery of the goods does not amount to acceptance of them. According to Section 42, the buyer is deemed to have accepted the goods in either of the following circumstances, namely:

- 1) When he intimates to the seller that he has accepted the goods: Before intimating about acceptance the buyer has a right, under Section 41, to examine and test the goods in order to be sure as to whether they are in conformity with the contract regarding quality etc. He may even use the goods, if it is necessary for the purpose of testing. But if he is not satisfied, he must act promptly to inform the seller about rejection.
- 2) When he does any act in relation to the goods which is inconsistent with the ownership of the seller, e.g., consumes, uses, pledges or resells the goods or puts his mark on them
- 3) When, after the lapse of a reasonable time, he retains the goods without intimating the seller that he has rejected them. What is reasonable time is a question of fact

UNPAID SELLER

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Unpaid Seller Defined [Section 45(1)]:

The seller of goods is deemed to be an 'Unpaid Seller' when-

- a) The whole of the price has not been paid or tendered and the seller had an immediate right of action for the price.
- b) When a bill of exchange or other negotiable instrument has been received as conditional payment, and the condition on which it was received has not been fulfilled by reason of the dishonor of the instrument or otherwise.

The term 'seller' here includes any person who is in the position of a seller, as, for instance, an agent of the seller to whom the bill of lading has been endorsed, or a consignor or agent who has himself paid, or is directly responsible for, the price [Section 45(2)].

An unpaid seller has two-fold rights, viz.,:

1. Rights of unpaid seller against the goods, and
2. Rights of unpaid seller against the buyer personally.

RIGHTS OF UNPAID SELLER AGAINST GOODS

1. RIGHT OF LIEN

- 'Lien' is the right to retain possession of goods & refuse to deliver them to the buyer until the price due in respect of them is paid or tendered. An unpaid seller in possession of goods sold is entitled to exercise his lien on the goods in the following cases:
  - 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, even though the period of credit may not have yet expired.
- The unpaid seller's lien is a possessory lien, i.e., the lien can be exercised as long as the seller remains in possession of the goods.
- He may exercise his right of lien notwithstanding that he is in possession of the goods as agent or bailee for the buyer [Sec. 47(2)].
- The seller's lien when property has not passed to the buyer is termed as 'a right of withholding delivery.' Accordingly, Section 46(2) provides: "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 coextensive with his rights of lien and stoppage in transit where the property has passed to the buyer."
- **Part delivery (Section 48):** 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
- **Termination of lien: Section 49** provides that the unpaid seller of goods loses his lien thereon in the following cases:
  - 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. Where the buyer / his agent lawfully obtains possession of goods
  - iii. Where seller has waived the right of lien.
  - iv. By Estoppel i.e., where the seller so conducts himself that he leads third parties to believe that the lien does not exist.

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**Exception:** Right of lien is not lost by reason only that seller has obtained a decree for the price of the goods.

The right of lien, if once lost, will not revive if the buyer redelivers the goods to the seller for any particular purpose

2. RIGHT OF STOPPAGE OF GOODS IN TRANSIT

- The right of stoppage in transit means the right of stopping further transit of the goods while **they are with a carrier** for the purpose of transmission to the buyer, **resuming possession of them** and retaining possession until payment or tender of the price. Thus, in a sense this right is an extension of the right of lien because it entitles the seller to regain possession even when the seller has parted with the possession of the goods.
- The right of stoppage in transit is exercised only when the following conditions are fulfilled:
  - a) The seller must be unpaid.
  - (b) He must have parted with the possession of goods.
  - (c) The goods are in transit.
  - (d) The buyer has become insolvent.
  - e) The right is subject to provisions of the Act. [Section 50]

[Continued in next chart.....]

[Insolvent(Sec 2(8): A person is said to be insolvent when he ceases to pay his debts in the ordinary course of business, or cannot pay his debts as they become due, whether he has committed an act of insolvency or not]

3. RIGHT OF RESELL

The unpaid seller can exercise the right to re-sell the goods under the following conditions:

- i. **Where the goods are of a perishable nature:** In such a case the buyer need not be informed of the intention of resale.
  - ii. **Where he gives notice to the buyer of his intention to re-sell the goods:** If after the receipt of such notice the buyer fails within a reasonable time to pay or tender the price, the seller may resell the goods. It may be noted that in such cases, on the resale of the goods, the seller is also entitled to:
    - a) Recover the difference between the contract price and resale price, from the original buyer, as damages
    - b) Retain the profit if the resale price is higher than the contract price.
- When no notice is given:**  
The seller cannot recover the loss suffered on resale. If there is any profit on resale, he must return it to the original buyer.[Sec 54(2)]
- iii. **Where an unpaid seller who has exercised his right of lien or stoppage in transit resells the goods:** The subsequent buyer acquires the good title thereof as against the original buyer, despite the fact that the notice of re-sale has not been given by the seller to the original buyer.
  - iv. **A re-sale by the seller where a right of re-sale is sale expressly reserved in a contract of sale:** In such cases, the seller is not required to give notice of resale

2. RIGHT OF STOPPAGE OF GOODS IN TRANSIT

Duration of transit: (Sec. 51):

Goods are deemed to be in course of transit from the time when they are delivered to a carrier or other bailee for the purpose of transmission to the buyer, until the buyer or his agent takes delivery of them.

When does the transit come to an end?

- (i) When the buyer or his agent takes delivery after the goods have reached destination.
- (ii) When the buyer or his agent obtains delivery of the goods before their arrival at the appointed destination.
- (iii) When the goods have arrived at their destination and the carrier acknowledges to the buyer or his agent that he holds the goods on his behalf.
- (iv) When the goods have arrived at their destination but the buyer instead of taking delivery requests the carrier to carry the goods to some further destination and the carrier agrees to take them to the new destination.
- (v) Where goods are delivered to the carrier hired by the buyer, the transit comes to an end
- (vi) When the carrier wrongfully refuses to deliver the goods to the buyer or his agent.
- (vii) When part delivery of the goods has been made to the buyer with an intention of delivering the whole of the goods, transit will be at an end for the remainder of the goods also which are yet in the course of the transit
- (viii) Where the goods are delivered to a ship chartered by the buyer, the transit comes to an end.

HOW RIGHT OF STOPPAGE IS EXERCISED (SEC. 52).

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- The unpaid seller may exercise his right of stoppage in transit either:
  - a) by taking actual possession of the goods, or
  - b) by giving notice of his claim to the carrier or other bailee in whose possession the goods are.
- Such notice may be given either to the **person in actual possession of the goods, or to his principal.**
- In the **latter case, notice must be given well in advance** to enable the principal to communicate with his agent or servant in time, so as to prevent delivery to the buyer.
- It is the **duty of the carrier, after receiving due notice, not to deliver the goods to the buyer** but to redeliver them to, or according to the directions of the seller.
- If by **mistake he delivers the goods to the buyer, he can be made liable for conversion**
- The expenses of redelivery are to be borne by the seller.
- **Effect of stoppage:** The contract of sale is not rescinded when the seller exercises his right of stoppage in transit. The contract still remains in force and the buyer can ask for delivery of goods on payment of price.

RIGHTS OF UNPAID SELLER AGAINST THE BUYER (SECTIONS 55-61)

The rights of the seller against the buyer personally are called **rights in personam** and are in addition to his rights against the goods.

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 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)]

2) Suit for damages for non-acceptance (Sec. 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.** The seller's remedy in this case is a suit for damages rather than an action for the full price of the goods. **The damages are calculated in accordance with the rules contained in Section 73 of the Indian Contract Act.**

3) Repudiation of contract before due date (Sec 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 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.

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RIGHT OF LIEN Vs. RIGHT OF STOPPAGE IN TRANSIT

- (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, & (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 in transit.
- (v) Right of lien comes to an end as soon as the goods go out of the possession of the seller but the right of stopping in transit comes to an end as soon as the goods are delivered to the buyer.

EFFECTS OF SUB-SALE OR PLEDGE BY BUYER (SECTION 53)

- The unpaid seller's right of lien or stoppage in transit **is not affected by any sale or pledge of the goods which the buyer might have made.** This is based on the principle that a second buyer cannot stand in a better position than his seller. (The first buyer).  
**Example:** A sold certain goods to B of Mumbai and the goods are handed over to railways for transmission to B. In the meantime, B sold these goods to C for consideration. B becomes insolvent. A can still exercise his right of stoppage in transit  
**Exceptions:**
  - (i) When the **seller has assented to the sale or pledge which the buyer may have made.**
  - (ii) When a **document of title to goods (e.g., a bill of lading or railway receipt) has been issued or transferred to a buyer, and the buyer transfers the document to a person who takes the document in good faith** and for consideration, then,
    - a) if such last mentioned transfer was by **way of sale**, the unpaid seller's right of lien or stoppage in transit is defeated, and
    - b) if such last mentioned transfer was by **way of pledge**, the unpaid seller's right of lien or stoppage in transit can only be exercised subject to the rights of the pledgee.
 But in this case the unpaid seller may require the pledgee to satisfy his claim against the buyer first out of any other goods or securities of the buyer in the hands of the pledgee.

REMEDIES OF BUYER AGAINST THE SELLER	AUCTION SALE (SECTION 64)	INCLUSION OF INCREASED OR DECREASED TAXES IN CONTRACT OF SALE (SEC 64A)
<p><u>Modes of breach of contract by seller</u></p> <p>There can be a breach of contract by seller, where he:</p> <ol style="list-style-type: none"> <li>1) Fails to deliver the goods at the time or in manner prescribed</li> <li>2) Repudiates the contract</li> <li>3) Deliver non-conforming goods and buyer rejects and revokes acceptance.</li> </ol> <p><u>If the seller commits a breach of contract, the buyer gets the following rights against the seller:</u></p> <ol style="list-style-type: none"> <li>1) <u>Damages for non-delivery [Section 57]:</u> <ul style="list-style-type: none"> <li>- 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.</li> <li>- The damages are assessed in accordance with the rules contained in Section 73 of the Indian Contract Act, that is, the measure of damages shall be the estimated loss directly and naturally resulting, in the ordinary course of events, from the seller's breach of contract.</li> </ul> </li> <li>2) <u>Suit for specific performance (Sec. 58).</u> <p>Where there is breach of a contract for the sale of specific or ascertained goods, the buyer may file a suit for the specific performance of the contract. This remedy is discretionary and will only be granted when damages would not be an adequate remedy, for instance, the subject-matter of the contract is rare goods, say, a picture by a dead painter.</p> </li> <li>3) <u>Suit for breach of warranty (section 59):</u> <p>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 bases of such breach of warranty. But he may:</p> <ol style="list-style-type: none"> <li>(i) set up against the seller the breach of warranty in diminution or extinction of the price;(i.e. reduction in price) or</li> <li>(ii) sue the seller for damages for breach of warranty.</li> </ol> </li> <li>4) <u>Repudiation of contract before due date (Section 60):</u> <p>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.</p> </li> <li>5) <u>Suit for recovery of the price together with interest (Sec. 61).</u> <ul style="list-style-type: none"> <li>- If the buyer has already paid the price of the goods to the seller and the goods are not delivered or they are stolen one, he can sue the seller for the refund of the price and also for the interest at reasonable rate from the date of payment to the date of refund.</li> <li>- 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.</li> </ul> </li> </ol>	<p align="center"><b>AUCTION SALE (SECTION 64)</b></p> <ul style="list-style-type: none"> <li>- An 'Auction Sale' is a mode of selling property by inviting bids publicly and the property is sold to the highest bidder.</li> <li>- An auctioneer is an agent governed by the Law of Agency.</li> <li>- When he sells, he is only the agent of the seller. He may, however, sell his own property as the principal and need not disclose the fact that he is so selling.</li> </ul> <p><u>Rules of Auction sale:</u></p> <p>Section 64 of the Sale of Goods Act, 1930 provides following rules to regulate the sale by auction.</p> <ol style="list-style-type: none"> <li>(a) <b>Where goods are sold in lots:</b> Where goods are put up for sale in lots, each lot is <i>prima facie</i> deemed to be subject of a separate contract of sale.</li> <li>(b) <b>Completion of the contract of sale:</b> The sale is complete when the auctioneer announces its completion by the fall of hammer or in any other customary manner (say, by saying words like "one, two, three" or "going, going, gone ")and until such announcement is made, any bidder may retract from his bid.</li> <li>(c) <b>Right to bid may be reserved:</b> 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.</li> <li>(d) <b>Where the sale is not notified by the seller:</b> 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.</li> <li>(e) <b>Pretended bidding:</b> If the seller makes use of pretended bidding to raise the price, the sale is voidable at the option of the buyer</li> <li>(f) <b>Reserved price:</b> The sale may be notified to be subject to a reserve or upset price.</li> </ol> <p align="right">Compiled By:CA Sahil Grover</p>	<p align="center"><b>INCLUSION OF INCREASED OR DECREASED TAXES IN CONTRACT OF SALE (SEC 64A)</b></p> <ul style="list-style-type: none"> <li>- Where <b>after a contract has been made but before it has been performed, tax revision takes place.</b></li> <li>- Where tax is being imposed, increased, decreased or remitted in respect of any goods without any stipulations to the payment of tax, <b>the parties would become entitled to readjust the price of the goods accordingly.</b></li> <li>- Following taxes are applied on the sale or purchase of goods:             <ul style="list-style-type: none"> <li>• Any duty of customs or excise on goods,</li> <li>• Any tax on the sale or purchase of goods</li> </ul> </li> <li>- <b>The buyer would have to pay the increased price where the tax increases and may derive the benefit of reduction if taxes are curtailed. Thus, seller may add the increased taxes in the price. The effect of provision can, however, is excluded by an agreement to the contrary.</b></li> <li>- <b>It is open to the parties to stipulate anything regard to taxation</b></li> </ul> <p align="right">Compiled By:CA Sahil Grover</p>

# THE SALES OF GOODS ACT, 1932 (Chart 1.12)

## IMPORTANT DIFFERENCES

### DIFFERENCES BETWEEN SALE & AGREEMENT TO SELL

Basis of difference	Sale	Agreement to sell
<b>Transfer of property</b>	The property in the goods passes to the buyer immediately	Property in the goods passes to the buyer on future date or on fulfilment of some condition.
<b>Nature of contract</b>	It is an executed contract. i.e. contract for which consideration has been paid.	It is an executory contract. i.e. contract for which consideration is to be paid at a future date.
<b>Remedies for breach</b>	The seller can sue the buyer for the price of the goods because of the passing of the property therein to the buyer.	The aggrieved party can sue for damages only and not for the price, unless the price was payable at a stated date.
<b>Liability of parties</b>	A subsequent loss or destruction of the goods is the liability of the buyer.	Such loss or destruction is the liability of the seller.
<b>Burden of risk</b>	Risk of loss is that of buyer since risk follows ownership	Risk of loss is that of seller
<b>Nature of rights</b>	Creates Jus in rem	Creates Jus in personam
<b>Right of resale</b>	The seller cannot resell the goods.	The seller may sell the goods since ownership is with the seller
<b>In case of insolvency of seller</b>	The official assignee will not be able to take over the goods but will recover the price from the buyer  <i>Compiled By:CA Sahil Grover</i>	The official assignee will acquire control over the goods but the price will not be recoverable. The official assignee will acquire control over the goods but the price will not be recoverable.
<b>In case of insolvency of buyer</b>	The official assignee will have control over the goods	The official assignee will not have any control over the goods.

### DIFFERENCES BETWEEN SALE & HIRE PURCHASE

Basis of difference	Sale	Hire- Purchase
<b>Time of passing property</b>	Property in the goods is transferred to the buyer immediately at the time of contract.	The property in goods passes to the hirer upon payment of the last installment.
<b>Position of the party</b>	The position of the buyer is that of the owner of the goods.	The position of the hirer is that of a bailee till he pays the last installment.
<b>Termination of contract</b>	The buyer cannot terminate the contract and is bound to pay the price of the goods.	The hirer may, if he so likes, terminate the contract by returning the goods to its owner without any liability to pay the remaining installments.
<b>Burden of Risk of insolvency of the buyer</b>	The seller takes the risk of any loss resulting from the insolvency of the buyer.  <i>Compiled By:CA Sahil Grover</i>	The owner takes no such risk, for if the hirer fails to pay an installment, the owner has right to take back the goods.
<b>Transfer of title</b>	The buyer can pass a good title to a bona fide purchaser from him.	The hirer cannot pass any title even to a bona fide purchaser.
<b>Resale</b>	The buyer in sale can resell the goods	The hire purchaser cannot resell unless he has paid all the installments.

### DIFFERENCES BETWEEN SALE & BAILMENT

Basis of difference	Sale	Bailment
<b>Transfer of property</b>	The property in goods is transferred from the seller to the buyer.	There is only transfer of possession of goods from the bailor to the bailee for any of the reasons like safe custody, carriage etc.
<b>Return of goods</b>	The return of goods in contract of sale is not possible.	The bailee must return the goods to the bailor on the accomplishment of the purpose for which the bailment was made.
<b>Consideration</b>	The consideration is the price in terms of money.	The consideration may be gratuitous or non- gratuitous.



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# CA SANCHIT GROVER

# THE COMPANIES ACT, 2013

# THE COMPANIES ACT, 2013 (Chart 1.1)

## INTRODUCTION

- This Act repeals and replaces The Companies Act, 1956.
- Received the assent of President on **29<sup>th</sup> August, 2013**.
- **Sec 1 was notified on 30<sup>th</sup> Aug 2013**. Remaining sections were notified in phased manner on different dates
- Contains **470 sections** divided into **29 chapters** along with **7 schedules**.

## COMPANY-DEFINITION

### STATUTORY DEFINITION

As per **Sec. 2(20)** of the Companies Act, 2013, 'company' means a company incorporated

- Under this Act or
- Any of the previous Companies laws

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### AS DEFINED BY PROFESSOR HANEY

A company is an artificial person created by law having

- Separate identity
- Perpetual Succession
- Common seal (Now optional as per latest amendment)

## FEATURES OF A COMPANY

- **INCORPORATED ASSOCIATION:** formed and registered by complying with the prescribed formalities prescribed under the Act.
- **ARTIFICIAL PERSON:** not a natural person; not a fictitious person. A company exists only in eyes of law. Can own property, have banking account, raise loans, incur liabilities and enter into contracts. Can sue others and be sued in its own name.
- **SEPARATE LEGAL ENTITY:** A company is a legal entity separate from its members. It is known by its own name has rights and liabilities of its own.  
**Salomon v Salomon & Co. Ltd. ; Lee v Lee's Air Farming Ltd.**
- **PERPETUAL SUCCESSION:** 'Members may come and go, but the company goes on forever'. Death, insolvency, insanity etc. of any members does not affect the continuity of the Company.
- **LIMITED LIABILITY:** For the debts of the company, its creditors can sue it and not its members whose liability is limited to the unpaid amount on shares held by them or the guarantees provided by them to contribute on the winding up of the company, depending on the type of company.
- **COMMON SEAL:** Official signature of the Company. Companies (Amendment) Act, 2015 has made the provisions related to common seal as optional. 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.
- **TRANSFERABILITY OF SHARES:** Shares are movable property transferable in the manner provided in the Articles (Sec. 44). In a Private company - the right to transfer the shares is restricted. In a Public company – shares are freely transferable.
- **OWNERSHIP SEPARATE FROM MANAGEMENT:** Management of the company lies in the hands of elected representatives of members, commonly called as Board of Directors, who are appointed as well as removed by members
- **SEPARATE PROPERTY:** A Company can own and enjoy property in its own name. Members are not owners or co-owner of the company's property. **Members have no insurable interest in the property of the company (Macaura v. Northern Assurance Co. Ltd.)**

## LIFTING/PIERCING OF CORPORATE VEIL

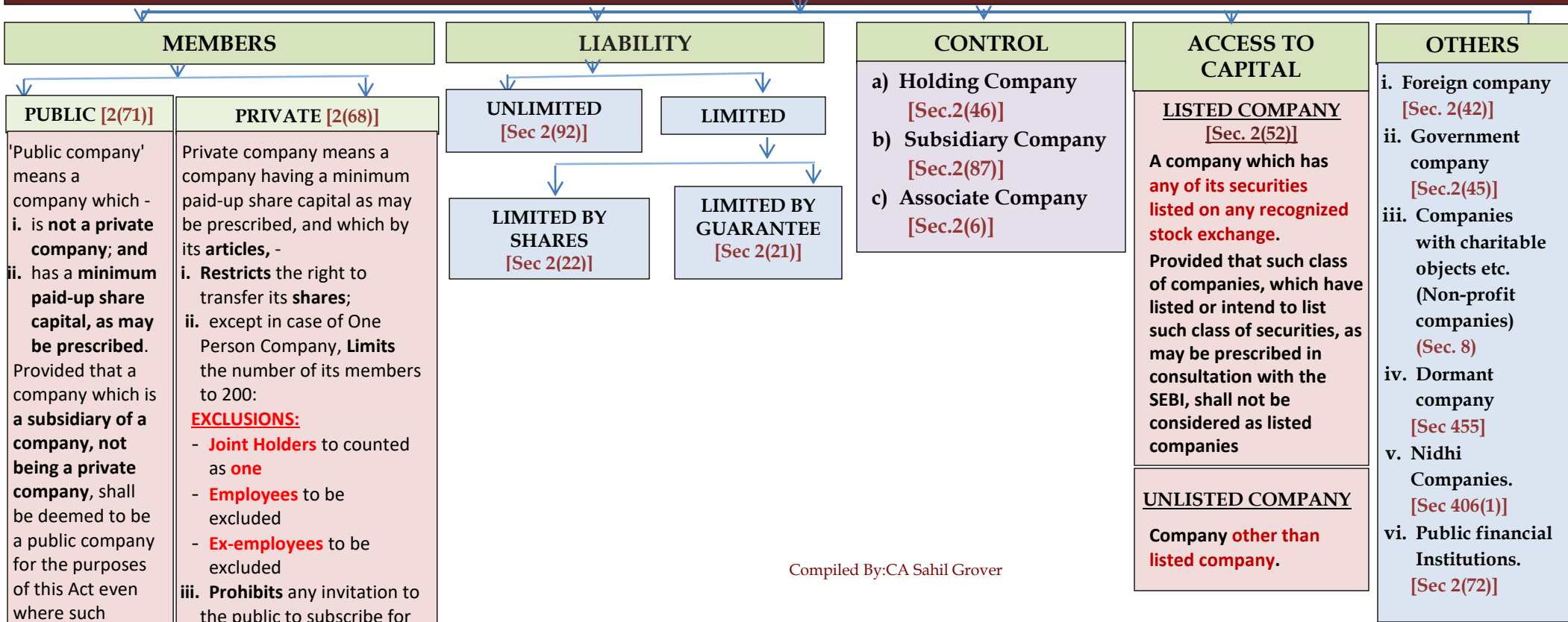
- Corporate Veil refers to a legal concept whereby the company is identified separately from the members of the company.
- Lifting of corporate veil means **ignoring the separate identity of a company**. It means **disregarding the corporate personality and looking behind the real persons who are in the control of the company**.
- Court has the discretion whether or not to lift the corporate veil. (Where the legal entity of a corporate body is **misused for fraudulent and dishonest purposes**)
- Under certain exceptional circumstances the courts may disregard or pierce the corporate veil of a company and hold persons controlling the affairs of the company liable for the acts of the company.

### Circumstances or the cases in which the Courts have disregarded the corporate personality are:

- **Protection of Revenue (To prevent evasion of taxation): (Re, Sir Dinshaw Maneckjee Pettit)**
- **Prevention of fraud or improper conduct: (Gilford Motor Co. Ltd. v Horne)**
- **Determining the character of the Company - whether an enemy company: (Daimler Co. Ltd. Vs Continental Tyre & Rubber Co. Ltd)**
- **To avoid a legal obligation or welfare legislation: (Workmen of Associated Rubber Industry Ltd. v Associated Rubber Industry Ltd.)**
- **Formation of subsidiaries to act as agents: (Merchandise Transport Limited vs. British Transport Commission)**
- **In quasi criminal cases**

## SECTION 1: Short Title, Extent, Commencement and Application

- (1) This Act may be called the **Companies Act, 2013**.
- (2) It extends to the **whole of India**.
- (3) This section shall come into force at once and the remaining provisions of this Act shall come into force on such date as the Central Government may, by notification in the Official Gazette, appoint and different dates may be appointed for different provisions.
- (4) The provisions of this Act shall apply to—
  - a) companies incorporated under this Act or under any previous company law;
  - b) Insurance companies, except in so far as the said provisions are inconsistent with the provisions of the Insurance Act, 1938 or the Insurance Regulatory and Development Authority Act, 1999.
  - c) banking companies, except in so far as the said provisions are inconsistent with the provisions of the Banking Regulation Act, 1949 ;
  - d) companies engaged in the generation or supply of electricity, except in so far as the said provisions are inconsistent with the provisions of the Electricity Act 2003,
  - e) any other company governed by any special Act, except in so far as the said provisions are inconsistent with the provisions of such special Act; and
  - f) such body corporate, incorporated by any Act for the time being in force, as the Central Government may, by notification, specify in this behalf.



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**SMALL COMPANY [Sec 2(85)]**

Small company means a company, **other than a public company** which satisfies **both** the following conditions:

- (i) **its paid-up share capital does not exceed**
  - **Rs. 50 lakhs**; or such higher amount as may be prescribed (not being more than **Rs. 10 crore**). [Prescribed amount -4 crores]
- (ii) **Its turnover(as per the profit and loss account for immediately preceding financial year )does not exceed**
  - **Rs. 2 crore** or such higher amount as may be prescribed (not being more than **Rs. 100 crore**). [Prescribed amount-40 crores]

**Certain companies not to be “small companies”**

A company shall not be a small company, if

- (i) It is a **public company**; or
- (ii) It is a **holding company** of any company; or
- (iii) It is a **subsidiary company** of any company
- (iv) It is a **company registered/s 8** (viz. it is a **non profit company**); or
- (v) It is a **company or a body corporate governed by any special Act** .

**Prescribed limits [Rule 2(t) of Companies (Specification of Definitions Details) Rules, 2014]**

For the purposes of sub-clause (i) and sub-clause (ii) of clause (85) of section 2 of the Act, **paid up capital and turnover** of the small company shall not exceed **Rs. 4 crores and rupees 40 crores respectively.**” (w.e.f. 15th September,2022)

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**ONE PERSON COMPANY [Sec 2(62)]**

‘One person company’ means a company which has only one person as a member. (Sec 2(62)  
(See next chart for detailed discussion)

**ONE PERSON COMPANY [Sec 2(62)]**

- 'One person company' means a company which has **only one person as a member**.
- Such a company is described **under section 3(1)(c) as a private company**. Thus all the provisions as are applicable to a private company shall also apply to "One Person Company". However certain provisions of the Act and the rules are applicable only to 'One Person company' and not to all private companies.

Specific provisions applicable to 'One Person Company'

- The memorandum must be **subscribed to by 1 person**.
- The memorandum shall state the **name of a person, who in the event of death of subscriber, shall become the member of the company**.
- The words '**One Person Company**' shall be mentioned in brackets **below the name**.
- Every **private company** shall have a minimum **of 2 members**. However 'One Person Company' shall have **1 member only**. The number of members shall exceed **200 in case of a private company**. However in 'One Person Company' shall have **1 member only**.
- Every private company shall have a minimum of **2 directors**. However, every 'One Person Company' shall have a **minimum of 1 director**.

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Provisions Relating To Incorporation of One Person Company

- 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 whether resident in India or not** (person who has stayed in India for a period of not less than **120 days** during the **immediately preceding one financial year**) shall be eligible to **incorporate** a OPC or be a **nominee** for the sole member of a OPC.
- A natural person **shall not be member of more than a OPC at any point of time and the said person shall not be a nominee of more than a OPC**
- Where a natural person being member in OPC becomes member in another such company by virtue of his being a nominee in that OPC, **such person shall meet the eligibility criteria (as given in point above) within a period of 180 days**.
- **No minor** shall become **member or nominee of the OPC**.
- Such Company **cannot be incorporated or converted into a company under section 8** of the Act.
- **It cannot carry out Non-Banking Financial Investment activities** including **investment in securities of any body corporate**.

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**PRIVATE COMPANY-EXEMPTIONS & PRIVILEGES**

- **Two or more persons** may form a private company as **against seven persons** in case of public company [Section 3(1)(b)].
- A private company **need not have more than 2 directors** as against **minimum 3 in case of a public company** [Section 149].
- A private company is **not required to have independent directors** [Section 149 (4)].
- A private company is **exempt from the provisions of having an audit committee** constituted by the Board of Directors [Section 177(1)]
- A private company is **exempt from the constitution of a Nomination & Remuneration Committee** [section 178(1)], as well as **Stakeholders Relationship Committee** [section 178 (5)].

**PRIVATE COMPANY vs. PUBLIC COMPANY**

1. **Minimum number of members:** In case of a private company minimum number of persons to form a **company is 2 while it is 7 in case of a public company**.
2. **Maximum number of members:** In case of private company, maximum number must not **exceed 200** whereas there is **no such restriction** on the maximum number of members in the case of a public company.
3. **Transferability of Shares:** As per Sec 44, the shares of any member in a company shall be movable property transferable in the manner provided by the articles of the company. In case of private company, by its very definition, articles of a **private company have to contain restrictions on transferability of shares**.
4. **Prospectus:** A **private company cannot issue a prospectus** while a **public company may, through prospectus; invite** the general public to subscribe for its securities.
5. **Minimum number of Directors:** A **private company** must have **atleast 2 directors**, whereas a **public company** must have at **least 3 directors**.
6. **Exemptions:** A **private company** has been granted **exemptions from several provisions of this Act** ( eg .appointment of independent directors, constitution of audit committee, Nomination & remuneration committees),whereas as no such exemptions are available to a public company.

**THE COMPANIES ACT, 2013 (Chart 1.4)**

ON BASIS OF LIABILITY		ON BASIS OF CONTROL																						
UNLIMITED [Sec. 2(92)]	LIMITED		HOLDING CO. [Sec. 2(46)].	SUBSIDIARY CO. [Sec. 2(87)].	ASSOCIATE CO. [Sec. 2(6)].																			
	BY SHARES [Sec. 2(22)].	BY GUARANTEE [Sec. 2(21)].																						
<ul style="list-style-type: none"> <li>A company not having any limit on the liability of its members. In such a company the liability of a member ceases when he ceases to be a member.</li> <li>The liability of each member extends to the whole amount of the company's debts and liabilities but he will be entitled to claim contribution from other members.</li> <li>In case the company has a share capital the AoA must state the amount of share capital and the amount of each share.</li> <li>So long as the company is a going concern the liability on the shares is the only liability which can be enforced by the company.</li> </ul>	When the liability of the members of a company is limited by its memorandum of association to <b>the amount (if any) unpaid on the shares held by them</b> , it is known as a company limited by shares.	Company having the liability of its members <b>limited by the memorandum to such amount as the members may respectively undertake by the memorandum to contribute to the assets of the company in the event of its being wound up.</b>	<p>'Holding company', <b>in relation to one or more other companies</b>, means a company of which such companies are subsidiary companies</p> <p><b>Explanation. – For the purposes of this clause, the expression “company” includes any ‘body corporate;’</b></p>	<p>'Subsidiary company' or 'subsidiary', <b>in relation to any other company</b> (that is to say the holding company), means a company <b>in which the holding company-</b></p> <p>i. <b>controls the composition of the Board of Directors;</b> or</p> <p>ii. <b>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.</b></p> <p><b>Explanation:</b> For the purposes of this clause, -</p> <p>a) A company shall be deemed to be a subsidiary company of the holding company <b>even if the control referred to in sub-clause (i) or sub-clause (ii) is of another subsidiary company of the holding company;</b></p> <p>b) the composition of a company's <b>Board of Directors shall be deemed to be controlled by another company</b> if that <b>other company by exercise of some power exercisable by it at its discretion can appoint or remove all or a majority of the directors.</b></p> <p>c) The expression 'company' shall include any 'body corporate'</p>	<p>'Associate Company' <b>in relation to another company</b>, means a company in which that <b>other company has a significant influence</b>, but which is <b>not a subsidiary company of the company</b> having such influence and <b>includes a joint venture company.</b></p> <p><b>'Significant influence':</b> The term "significant influence" means control of at <b>least 20% of total voting power</b>, or <b>control of or participation in business decisions under an agreement;</b></p> <p><b>Joint Venture:</b> The expression "joint venture" means <b>a joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the arrangement;</b></p>																			
	<table border="1"> <thead> <tr> <th>Basis of distinction</th> <th>Guarantee Company</th> <th>Company having Share Capital</th> </tr> </thead> <tbody> <tr> <td>Meaning :- Requirements as to memorandum</td> <td>If the memorandum states that the liability of members shall be limited to <b>the amount that they have respectively guaranteed to pay to the company in the event of winding up</b> of the company, the company is said to be a 'company limited by guarantee'.</td> <td>If the memorandum states that the liability of members shall be limited to <b>the unpaid amount on the shares held by them</b>, the company is said to be a 'company limited by shares'.</td> </tr> <tr> <td>Share capital</td> <td>A company limited by guarantee <b>may or may not have share capital.</b></td> <td>Such a company <b>must have share capital.</b></td> </tr> <tr> <td>Quantum of liability</td> <td>Every member shall be liable to pay the amount that he has <b>guaranteed to pay</b> to the company in the event of winding up of the company. Also, if the company <b>has a share capital</b>, the members are liable to <b>pay unpaid calls on shares</b> in addition to the guaranteed amount.</td> <td>Every member shall be liable to pay the <b>unpaid amount on the shares held by him.</b></td> </tr> <tr> <td>When does 'liability arise?</td> <td>The liability of a member shall arise only in the <b>event of winding up of the company</b>, i.e., in no case he can be compelled to pay guaranteed amount during the lifetime of the company.</td> <td>The liability of a member shall arise when a valid call is made <b>by the company</b>, i.e. during the lifetime of the Co. or in the event of winding up of the company.</td> </tr> <tr> <td>Suitability</td> <td>A guarantee company (having no share capital) is suitable in those cases where <b>initial capital requirement is not required</b> or where funds can be arranged from other sources like endowment, fees charges, donations or from borrowings.</td> <td>These companies are suitable in those cases where <b>initial capital requirement is high</b> and sufficient financial resources cannot be arranged by way of borrowings.</td> </tr> </tbody> </table>					Basis of distinction	Guarantee Company	Company having Share Capital	Meaning :- Requirements as to memorandum	If the memorandum states that the liability of members shall be limited to <b>the amount that they have respectively guaranteed to pay to the company in the event of winding up</b> of the company, the company is said to be a 'company limited by guarantee'.	If the memorandum states that the liability of members shall be limited to <b>the unpaid amount on the shares held by them</b> , the company is said to be a 'company limited by shares'.	Share capital	A company limited by guarantee <b>may or may not have share capital.</b>	Such a company <b>must have share capital.</b>	Quantum of liability	Every member shall be liable to pay the amount that he has <b>guaranteed to pay</b> to the company in the event of winding up of the company. Also, if the company <b>has a share capital</b> , the members are liable to <b>pay unpaid calls on shares</b> in addition to the guaranteed amount.	Every member shall be liable to pay the <b>unpaid amount on the shares held by him.</b>	When does 'liability arise?	The liability of a member shall arise only in the <b>event of winding up of the company</b> , i.e., in no case he can be compelled to pay guaranteed amount during the lifetime of the company.	The liability of a member shall arise when a valid call is made <b>by the company</b> , i.e. during the lifetime of the Co. or in the event of winding up of the company.	Suitability	A guarantee company (having no share capital) is suitable in those cases where <b>initial capital requirement is not required</b> or where funds can be arranged from other sources like endowment, fees charges, donations or from borrowings.	These companies are suitable in those cases where <b>initial capital requirement is high</b> and sufficient financial resources cannot be arranged by way of borrowings.	Compiled By:CA Sahil Grover
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# THE COMPANIES ACT, 2013 (Chart 1.5)

FOREIGN CO. [Sec. 2(42)]	GOVERNMENT COMPANY [Sec. 2(45)]	NIDHI [Sec. 406(1)]	COMPANIES WITH CHARITABLE OBJECTS [SEC. 8]
<p>Foreign company means any company or body corporate incorporated outside India which -</p> <p>a) has a place of business in India whether by itself or through an agent, physically or through electronic mode and</p> <p>b) conducts any business activity in India in any other manner.</p>	<p>Government Company means any company</p> <p>a) in which not less than 51% of the paid up share capital is held –</p> <p style="margin-left: 20px;">i. by the Central Government; or</p> <p style="margin-left: 20px;">ii. by any State Government or governments; or</p> <p style="margin-left: 20px;">iii. partly by the CG and partly by one or more SGs</p> <p>b) which is a subsidiary of a Government company.</p> <p><b>Explanation:-</b> For the purposes of this clause, the "paid up share capital" shall be construed as "<b>total voting power</b>", where shares with <b>differential voting rights</b> have been issued.</p>	<p>In this section, "<b>Nidhi</b>" or "<b>Mutual Benefit Society</b>" means a company which <b>the Central Government may, by notification in the Official Gazette, declare to be a Nidhi or Mutual Benefit Society, as the case may be.</b></p>	<p>A company may be formed u/s 8 if</p> <p>a) The <b>objects</b> of the company are to promote <b>commerce, art, science, sports, education research, social welfare, religion, charity, protection of environment or such other object.</b></p> <p>b) The company shall intend to <b>apply its profits in promoting its objects;</b> and</p> <p>c) The company intends to <b>prohibit the payment of dividend to its members.</b></p> <ul style="list-style-type: none"> <li>• <b>CG to issue the license on such conditions as it deems fit.</b></li> <li>• Company <b>shall not alter</b> the provisions of its <b>MoA or AoA</b> except with the <b>previous approval of the CG.</b></li> <li>• <b>CG may, after giving opportunity of being heard to company, revoke the licence</b> of the company where             <ul style="list-style-type: none"> <li>– the company <b>contravenes any of the requirements or conditions of this sections</b> or</li> <li>– where the <b>affairs of the company are conducted fraudulently, or violative</b> of the <b>objects</b> of the company or prejudicial to public interest,</li> </ul> </li> <li>• On revocation <b>Limited or Private Limited to be added to name.</b></li> <li>• <b>On revocation, Central Government may direct it to</b> <ul style="list-style-type: none"> <li>– <b>Convert its status and change its name</b></li> <li>– <b>Wind-up.</b> (If on winding up <b>any asset remains</b>, they may be <b>transferred to another company</b> registered under this section and having similar objects, , or <b>may be sold and proceeds thereof credited to the Insolvency and Bankruptcy Fund)</b></li> <li>– <b>Amalgamate with another company having similar object</b></li> </ul> </li> <li>• <b>Penalty:</b> If a <b>company makes any default the company: 10 lakh rupees to 1 crore rupees and the directors and every officer of the company who is in default-Rs.25000 -25L rupees, or with both.</b> And where it is proved that the affairs of the company were conducted fraudulently, every officer in default shall be liable for action <b>under section 447.</b></li> </ul>
<p><b>DORMANT COMPANY</b> [Sec.455].</p>		<p><b>PUBLIC FINANCIAL INSTITUTIONS [Sec 2(72)]</b></p>	
<p><b>1. Application by a company to the registrar for obtaining the status of dormant company</b></p> <p>a) A company may <b>make an application to the Registrar</b> so as to obtain the status of a dormant company in the following two cases:</p> <p style="margin-left: 20px;">i. It was <b>formed and registered under the Companies Act, 2013</b> for a <b>future project or to hold an asset or intellectual property</b> and it has <b>no significant accounting transaction.</b></p> <p style="margin-left: 20px;">ii. It is an <b>inactive company.</b></p> <p>b) The application shall be made to the Registrar in such manner as may be prescribed.</p> <p><b>2. 'Inactive company':</b> 'Inactive company' means –</p> <p>a) A company which <b>has not been carrying on any business or operation;</b> or</p> <p>b) A company which has <b>not made any significant accounting transaction</b> during the <b>last 2 financial years;</b> or</p> <p>c) A company which has <b>not filed financial statements and annual returns</b> during the <b>last 2 financial years.</b></p> <p><b>3. 'Significant accounting transaction':</b> Any transaction other than –</p> <p>a) <b>payment of fees by a company to the Registrar;</b></p> <p>b) <b>payments made by it to fulfill the requirements of this Act or any other law;</b></p> <p>c) <b>allotment of shares to fulfill the requirements of this Act; and</b></p> <p>d) <b>payments for maintenance of its office and records.</b></p> <p><b>4. Grant of status of dormant company by the Registrar:</b> After considering the application made by the company, the Registrar shall allow the status of a dormant company to the applicant company. The <b>Registrar shall issue a certificate in the prescribed form.</b></p> <p><b>5. Compliance requirements for a dormant company:</b> To retain its dormant status, a dormant company <b>shall have such minimum number of directors, file such documents and pay such annual fee as may be prescribed.</b> If a dormant company <b>fails to comply</b> with these requirements, the Registrar shall <b>strike off its name from the register of dormant companies.</b></p>		<p>As per <b>Section 2(72)</b> of the Companies Act, 2013 <b>the following institutions are to be regarded as public financial institutions:</b></p> <p>i. the <b>Life Insurance Corporation of India</b>, established under the Life Insurance Corporation Act, 1956;</p> <p>ii. the <b>Infrastructure Development Finance Company Limited,</b></p> <p>iii. <b>specified company referred to in the Unit Trust of India (Transfer of Undertaking and Repeal) Act, 2002;</b></p> <p>iv. institutions <b>notified by the Central Government under section 4A(2) of the Companies Act, 1956</b> so repealed under section 465 of this Act;</p> <p>v. such <b>other institution as may be notified by the Central Government in consultation with the Reserve Bank of India:</b></p> <p><b>Provided that no institution shall be so notified unless-</b></p> <p><b>A.</b> it has been <b>established or constituted by or under any Central or State Act; other than this Act or the previous company law;</b> or</p> <p><b>B.</b> not less than <b>fifty-one per cent of the paid-up share capital</b> is held or controlled by the <b>CG or by any SG(s) or partly by the CG and partly by one or more SG</b></p>	

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**PROMOTER**

**DEFINITION 2(69)**

‘Promoter’ means a person  
 a) who has been **named as such in a prospectus** or is **identified by the company in the annual return**; or  
 b) who has **control over the affairs of the company, directly or indirectly** whether as a **shareholder, director or otherwise**; or  
 c) In accordance with whose **advice, directions or instructions the Board of Directors of the company is accustomed to act.**

Provided that nothing in **sub-clause (c) shall apply to a person who is acting merely in a professional capacity.**

**DEFINITION GIVEN BY PALMER**

"Promoter is a person who **originates** a scheme for the formation of the company, **gets the memorandum and articles prepared**, executed and registered, and find the first directors, settle the terms of **preliminary contracts** and prospectus, and **makes arrangements for advertising and circulating the prospectus and placing the capital**

**FUNCTIONS**

- **Generating the idea of a starting a business** and forming a company, i.e. which business to be started.
- **Making a feasibility study** so as to determine whether the proposed business is profitable or not.
- **Taking decisions** regarding some fundamental questions, like -
  - a) **Whether to start** a new business or **to take over** an existing business by purchase of an existing undertaking.
  - b) **Nature of company** to be formed - whether it should be a **public company or a private company**; whether it should be a limited company or an unlimited company; whether the liability of members shall be limited by shares or by guarantee or by both.
  - c) The amount of **authorised capital** of the company.
  - d) Preparation of **memorandum, articles and other documents**
  - e) Arranging the **subscribers to memorandum**
  - f) **Filing the required documents** with the registrar
  - g) **Entering into negotiations** with the person who shall become the first directors of the company
  - h) **Entering into pre-incorporation contracts** (for the purpose of business of the company) on behalf of the company.
  - i) **Making arrangements for issue of shares**

**SECTION 3: FORMATION OF COMPANY**

- (1) A company may be formed for any **lawful purpose** by –
  - a) **7 or more persons**, where the company to be formed is to be a **public company**;
  - b) **2 or more persons**, where the company to be formed is to be a **private company**; or
  - c) **1 person**, where the company to be formed is to be **One Person Company** that is to say, a **private company**.
 by **subscribing their names or his name to a memorandum and complying with the requirements of this Act** in respect of registration.
- (2) A company formed under sub-section (1) may be either –
  - a) a company **limited by shares**; or
  - b) a company **limited by guarantee**; or
  - c) an **unlimited company**.

**SECTION 7: INCORPORATION OF COMPANY**

**Sec 7(1): Filing of the documents & information with the registrar**

Filed with the **registrar within whose jurisdiction the registered office of the company is proposed to be situated-**

- **MoA & AoA** of the company **duly signed by all the subscribers** to the memorandum.
- the **address for correspondence** till its RO is established;
- the **particulars** (names, including surnames or family names, residential address, nationality) **of every subscriber to the MoA along with proof of identity**,
- the **particulars of the persons mentioned in the articles as the first directors** of the company
- **Particulars of the interests of the persons mentioned in the articles as the first directors** of the company **in other firms or bodies corporate along with their consent to act as directors** of the company.
- **Declaration by person engaged in the formation of the company** (an advocate, a CA, CA or CS in practice), **and by a person named in the articles** (director, manager or secretary of the company), that all the requirements of this Act **and the rules made thereunder in respect of registration and matters precedent or incidental thereto have been complied with**
- **Declaration from each of the subscribers to the MoA and from persons named as the first directors**, if any, in the articles stating that-
  - he is **not convicted** of any offence in connection with the promotion, formation or management of any company, or
  - he **has not been found guilty of any fraud or misfeasance or of any breach of duty** to any company under this Act or any previous company law during the last five years,
  - and that **all the documents filed with the Registrar** for registration of the company contain information that is **correct and complete and true** to the best of his knowledge and belief;

**Sec 7(2):** Registrar on the basis of documents and information filed, shall register all the documents and information in the register and issue a **certificate of incorporation** in the prescribed form.(INC-11)

**Sec 7(3):** On and from the date mentioned in the certificate of incorporation, the **Registrar shall allot to the company a corporate identity number**, which shall be a **distinct identity for the company**.

**Sec 7(4):** Co. shall **maintain and preserve at its RO copies of all documents and info.** as originally filed, till its **dissolution**.

**Sec 7(5) & (6):** Furnishing any false or incorrect information or representation or by suppressing any material fact, **punishable u/s 447**.

**Sec 7(7): Order of the Tribunal**  
 Where a company got incorporated by furnishing false or incorrect info or by suppressing any material fact or info in any of the documents or declaration filed or made for incorporating such Co. or by any fraudulent action, **the Tribunal may, on an application made to it, on being satisfied that the situation so warrants, –**

- a) pass such orders, as it may think fit, for **regulation of the mngmt of the Co.including changes, if any, in its MoA and articles**, in public interest or in the interest of the company and its members and creditors; or
- b) direct that **liability of the members shall be unlimited**; or
- c) direct **removal of the name of the company from the register of companies**; or
- d) pass an order for the **winding up of the company**; or
- e) pass **such other orders as it may deem fit**

**Provided that before making any order, –**  
 - the company shall be given a **reasonable opportunity of being heard** in the matter; &  
 - the Tribunal shall **take into consideration the transactions entered into by the company, including the obligations, if any, contracted or payment of any liability.**

**SECTION 9: EFFECTS OF REGISTRATION**

- Date of incorporation:** The date mentioned in the CoI issued by the Registrar, shall be; the date of incorporation of the company.
- Body corporate:** From the date mentioned in the certificate of incorporation, the subscribers to MoA and all other persons, as may, from time to time, become members of the company, shall be a body corporate.
- Name:** The name, as mentioned in the memorandum, shall be the name of the company.
- Capacity to function:** The Company shall become capable of exercising all the functions of an incorporated company.
- Perpetual succession:** The Company shall have perpetual succession.
- Power to acquire:** The company shall have the power to **acquire, hold and dispose of the property** of any property kind, whether movable or immovable, tangible or intangible.
- Power to contract:** The company shall have the power to contract in its own name.
- Capacity to sue and be sued:** The company shall have the power to sue in its own name, and the company can be sued in its own name.

**MEMORANDUM OF ASSOCIATION**

**CONTENTS OF MoA [SEC 4(1)]**

**Statutory definition [Sec. 2(56)]**  
 'Memorandum of association of a company as originally framed or as altered from time to time in pursuance of any previous companies law or of this Act.

**As given by Palmer**  
 Memorandum contains the objects for which the company is formed and therefore, **identifies the possible scope of its operations** beyond which its actions cannot go. **It defines as well as confines the powers of the company.**

**OTHER POINTS**

- Also called as the **Charter of the company.**
- It is a **public document**, i.e. any person (whether a member of document of the company or not) can inspect it in the office of Registrar. **(S.399)**
- **Every company must have its own MoA.**
- **Enables shareholders, creditors and all those who deal with company to know what its powers are and what activities it can engage in.**
- **Company cannot depart from the provisions contained in the MoA. If it does so, it would be ultra vires the company & void.**

- Name Clause:**  
 It shall **state the name of the company.** In the case of a **public company**, the word '**limited**' shall be the last word of the name of the company. In the case of a **private company**, the words '**private limited**' shall be the last words of the name of the company. The requirement to use the word '**limited**' or the words '**private limited**', as the case may be, **shall not apply to a company registered u/s 8. In case of a govt. company** the word '**limited**' shall be the **last word** of the name of the company.
- Situation clause/Registered office Clause:** - states the **name of the State** in which the **registered office** of the company is proposed to be situated.
- Objects clause:** It shall state the **objects** for which the company is proposed to be incorporated and **any matter considered necessary in furtherance thereof.**
- Liability clause:** It shall state as to **whether the liability of members of the company is limited or unlimited.**  
 In case of a **company limited by shares**, it shall state that **liability of every member shall be limited to the amount unpaid on the shares held by him.**  
 In case of a **company limited by guarantee**, it shall state that **liability of every member shall be limited to the amount that he has undertaken to pay to the company, in the event of winding up of the company.**
  - The liability of a member shall **arise only if the company is wound up while he is a member or within 1 year of cessation of his membership.**
  - The liability of member shall be limited for payment of –
    - such debts**, as the company had incurred before he ceased to be a member;
    - expenses, costs and charges** of winding up of the company; and
    - adjustment of the **rights of the contributories** among themselves.
- Capital clause:** In case of a **company having a share capital**, capital clause shall state the **amount of share capital with which the company is registered** (viz. the authorized Share Capital) & the **division** of the authorized share capital into shares of a fixed amount.
- Subscription (Association) clause:** states the **no. of shares** which the subscribers to the MoA agree to subscribe which shall **not be less than 1 share**; & the **number of shares** each subscriber intends to take, indicated opposite his name.
- Nomination Clause:** In the **case of OPC**, the name of the person who in the event of death of the subscriber shall become the member of the company

**ARTICLES OF ASSOCIATION**

**Statutory Definition [Sec. 2(5)]**

'Articles' means the articles of association of a company as originally framed or as altered from time to time or applied in pursuance of any previous companies law or of this Act.

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**SECTION 5-ARTICLES**

- The articles of a company shall contain the **regulations for mgmt. of the company.**
- The articles shall also contain **such matters, as may be prescribed.** A company may **include any additional matter in its articles** which is considered necessary for the management of the company.

**Provision of Entrenchment**

- The articles may contain the **provisions for entrenchment**(to **protect something**), i.e. certain **specified provisions** of the articles can be altered only by complying with such **conditions or procedures as are more restrictive than those as are applicable in case of a SR.**
- These provisions for entrenchment shall only be made either **on formation of a company**, or by an **amendment in the articles agreed to by all the members of the company in the case of a private company** and by a **SR in the case of a public company.**
- Where the articles contain provisions for entrenchment, whether **made on formation or by amendment**, the company shall give notice to the Registrar of such provisions

- The articles of a company shall be in respective forms specified in **Tables F, G, H, I and J in Schedule I** as may be applicable to such company.
- A company may **adopt all or any of the regulations** contained in the model articles applicable to such company.
- In case of any company, which is **registered after the commencement of this Act**, in so far as the registered articles of such company **do not exclude or modify the regulations contained in the model articles** applicable to such company, **those regulations shall, so far as applicable, be the regulations of that company** in the same manner and to the extent as if they were contained in the duly registered articles of the company.
- Nothing in this section shall apply to the articles of a company registered under any previous company law unless amended under this Act.

MODEL FORMS OF MoA & AoA  
[SCHEDULE I]

**Form of Memorandum**

**Table A:** Memorandum of a **company limited by shares**

**Table B:** Memorandum of a **company limited by guarantee and having no share Capital**

**Table C:** Memorandum of a **company limited by guarantee and having a share capital**

**Table D:** Memorandum of an **unlimited company having no share capital**

**Table E:** Memorandum of an **unlimited company having a share capital.**

**Form of Articles**

**Table F:** Articles of a **company limited by shares**

**Table G:** Articles of a **company limited by guarantee and having a share capital**

**Table H:** Articles of a **company limited by guarantee and having no share capital**

**Table I:** Articles of an **unlimited company having a share capital**

**Table J:** Articles of an **unlimited company having no share capital.**

DIFFERENCE BETWEEN MOA & AOA

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

SEC 6: ACT TO OVERRIDE MOA & AOA

- the provisions of this Act shall have effect notwithstanding anything to the contrary contained in the memorandum or articles of a company, or in any agreement executed by it, or in any resolution passed by the company in general meeting or by its Board of Directors,
- any provision contained in the memorandum, articles, agreement or resolution shall, to the extent to which it is repugnant to the provisions of this Act. be void.

SEC 10: EFFECT OF MOA & AOA

- Subject to the provisions of this Act, the MoA & AoA shall, when registered, bind the Co. and the members thereof to the same extent as if they respectively had been signed by the Co.& by each member, and contained covenants on its and his part to observe all the provisions of the MoA & AoA.
- All money payable by any 'member to the company under the memorandum or articles shall be a debt due from him to the company.

**Company is bound to members:** If a company has committed breach of any terms and conditions of MoA or AoA, any member can sue the company, directors and the persons responsible for such breach.

**Members are bound to company:** Every member shall be bound to comply with the provisions contained in the MoA & AoA. In case of non-compliance, the company may sue a member.

**Members are not bound inter se (i.e., with each other):** There is no privity of contract between the members. However, a member may enforce his rights against another member through the company, but not directly.

**Company is not bound to outsiders:** The memorandum and the articles do not bind a company to the outsiders. This is based on the general rule of law that a stranger to a contract does not acquire any rights under the contract. Therefore, an outsider cannot take the help of the articles to establish a contract with the company. [Eley v Positive Govt. Security Life Assurance Co.]

DOCTRINE OF ULTRA VIRES

MEANING

Ultra means 'beyond' or 'in excess of' and vires means 'powers'. Thus, ultra vires means an act or transaction beyond or in excess of the powers of the company.

An act or transaction shall be ultra vires if-

- it is not permitted or authorised by the Companies Act, 2013
- it falls outside the object clause of memorandum; &
- its attainment is not incidental or ancillary to the attainment of main objects.

Effects of Ultra Vires Transactions

• **Void-ab-initio:**

An act which is ultra vires the company is void and of no legal effect. Neither the company nor the other contracting party derives any right under an ultra vires contract. Even ratification of an ultra vires contract by the whole body of shareholders doesn't make an ultra vires contract valid or enforceable.

• **No ratification or estoppel:**

An ultra vires contract can never be made binding on the company. It cannot become "Intravires" by reasons of estoppel, acquiescence, lapse of time, delay or ratification.

• **Injunction against the company:**

Any member may obtain an injunction order from the Court, i.e., an order of the Court restraining the company from proceeding with the ultra vires contract.

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• **Personal liability of Directors:**

If funds of the company are misapplied or wasted by entering into ultra vires transactions, the directors shall be personally liable to the company for breach of trust.

• **Ultra vires property:**

If the company acquires some property under an ultra vires transaction, the company has the right to hold that property and protect it against damage by other parties.

**Leading Case Law:** Ashbury Railway Carriage & Iron Company Ltd. V Richie

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**DOCTRINE OF CONSTRUCTIVE NOTICE**

Applicability of Doctrine

This doctrine operates in **favour of the company**, i.e., it creates a **presumption in favour of the company**. It operates against the persons dealing with the company.

Effect of the doctrine

- Once registered the MoA & AoA become **public documents** (Sec. 399). Therefore, every person dealing with the company is **presumed to have read the MoA & AoA**. Further, it is presumed that he has **understood the provisions** of memorandum and articles correctly, i.e. **in the right sense**.
- Thus, it is required of every person to **apprise himself with the requirements of the memorandum and articles, before entering into any contract with a company**.
- The doctrine prevents any person dealing with the company from **alleging that he did not know the provisions contained in the AoA & MoA**.
- If a person enters into a contract with the company in contravention of the provisions of the MoA & AoA, **he cannot enforce such a contract**.

Leading Case Law: **Kotla Venkataswamy vs. C Rammurthi**

**DOCTRINE OF INDOOR MANAGEMENT [TURQUAND RULE]**

Purpose of Doctrine

This doctrine **operates in favour of the outsiders**, i.e., this doctrine creates a **presumption in favour of the outsiders**. The doctrine of Indoor Management is the **exception to the doctrine of constructive notice**.

Meaning of the Doctrine

As per this doctrine, **outsiders dealing with the company are not required to enquire into the internal management** of the company. **Outsiders** dealing with the company **are entitled to assume** that as far as **internal proceedings of the company** are concerned, everything has been **done regularly**.

Effect of the Doctrine

If a **contract is entered into on behalf of the company** by any director or officer of the company, it is **enforceable** against the company, if **provisions contained in the MoA & AoA** have been complied with, **even though** while entering into such a contract, **some internal irregularity** had arisen of which the outsider was **unaware**.

**Leading Case law: Royal British Bank v Turquand**

Exceptions to the Doctrine

- **Knowledge of irregularity (Howard v Patent Ivory Manufacturing Company)**
- **Negligence -Suspicious circumstances or unusual magnitude of transactions (Anand Bihari Lal v Dinshaw & company) (Underwood v Bank of Liverpool)**
- **Forgery (Ruben v Great Fingall Consolidated Company)**

**SHARES AND SHARE CAPITAL**

**Concept of Capital**

In relation to a company limited by shares, **the word capital means share-capital**, i.e., the capital or figure in terms of so many rupees divided into shares of fixed amount. **In other words, the contributions of persons to the common stock of the company form the capital of the company**.

**In the domain of Company Law, the term 'capital' is used in the following senses:**

- a) **Nominal or authorised or registered capital [Sec 2(8)]**: means such capital as is authorised by the MoA of a company to be **the maximum amount of share capital of the company**. **At the time of registration of the company, the company has to pay fees to CG which is calculated with respect to authorised capital**.
- b) **Issued capital [Sec 2(50)]**: which means such capital as the company issues from time to time for subscription. **It is that part of authorised capital which is offered by the company for subscription and includes the shares allotted for consideration other than cash**. **Schedule III** makes it obligatory for a company to **disclose its issued capital in the balance sheet**
- c) **Subscribed capital [Sec 2(86)]**: defines "subscribed capital" as such **part of the capital which is for the time being subscribed by the members of company**. It is the nominal amount of shares taken up by the public.  
**Sec 60**: Where any notice, advertisement or other official communication or any business letter, bill head or letter paper of a company **states the authorised capital, the subscribed and paid-up capital must also be stated in equally conspicuous characters**. A default in this regard will make the **company and every officer who is in default** liable to pay penalty extending **Rs.10,000 and Rs.5,000** respectively.
- d) **Called-up capital [Sec 2(15)]**: means **such part of the capital, which has been called for payment**. It is the total amount called up on the shares issued.
- e) **Paid-up capital**: is the **total amount paid or credited as paid up on shares issued**. It is equal to called up capital less calls in arrears.

**KINDS OF SHARE CAPITAL (SEC. 43)**

- a) Preference share capital; and
  - b) Equity share capital
    - i. with **voting rights**; or
    - ii. with differential rights as to **dividend, voting or otherwise**, in accordance with such rules as may be prescribed by CG.
- a) **Preference share capital**: Share capital carrying a preferential right with respect to dividend and repayment of capital is termed as preference Share capital.
  - b) **Equity share capital**: Share capital which is not preference share capital is termed as equity share capital.

**NATURE OF SHARES (SEC 44)**

The shares and debentures shall be -

- a) **movable property**
- b) **transferable in the manner provided by the articles of the company**

**NUMBERING OF SHARES (SEC. 45)**

Every share shall be **distinguished by its distinctive number**.  
**Exception**: Shares held in **depository system** shall not have distinctive numbers

# AVJ ACADEMY

## CA - INTERMEDIATE

EARLY BIRD BATCH FOR MAY. 2025

AS PER NEW SYLLABUS

Starting from 8th July.2024



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GROVER  
TAXATION



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**LIMITED LIABILITY  
PARTNERSHIP ACT, 2008**

# THE LIMITED LIABILITY PARTNERSHIP ACT, 2008 (Chart 1.1)

## INTRODUCTION

- This Act extends to the **whole of India**
- The **Parliament passed the Limited Liability Partnership Bill on 12th December, 2008** and the President has assented the Bill on **7th January, 2009**.
- The **Limited Liability Act, 2008** has been amended through the **Limited Liability Partnership (Amendment) Act, 2021** dated **13th August, 2021**
- Contains **85 sections and 4 schedules**
- **The First Schedule** deals with mutual rights and duties of partners, as well limited liability partnership and its partners where there is absence of formal agreement with respect to them.
- **The Second Schedule** deals with conversion of a Firm into LLP.
- **The Third Schedule** deals with conversion of a private company into LLP.
- **The Fourth Schedule** deals with conversion of unlisted public company into LLP.
- **MCA & ROC** are entrusted with the task of administrating the LLP Act, 2008.

## DEFINITION & CONCEPT

- **Section 2(1)(n)** defines LLP as "**limited liability partnership means a partnership formed and registered under this Act.**"
- **Section 3** gives a comprehensive definition of an LLP giving its main essentials as '**A limited liability partnership is a body corporate, which is an artificial person, having a separate legal entity, with a perpetual succession, a common seal and carrying limited liability**'.
- LLP is a **new form of business entity** that enables professional expertise and entrepreneurial initiative to combine, organize and operate in an innovative and efficient manner.
- Initiated as an **alternative to the ' traditional partnership firm' on the one hand**, where partners are exposed to unlimited personal liability, and **'incorporated company' on the other**, which is burdened with statute based governance structure.
- **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.**
- 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.**

## SALIENT FEATURES OF LLP

### 1. **LLP is a body corporate:**

- **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.
- An LLP is **formed by the registration of an incorporation document** with the RoC of the State in which the registered office of the LLP is to be situated.

### 2. **Perpetual Succession:**

- **'Death, insanity, retirement or insolvency of partners has no impact on the existence of LLP. Partners may come and go but the LLP can go on forever.**

### 3. **Separate Legal Entity:**

- 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.
- It is **capable of entering into contracts and holding property in its own name.**
- It can **sue and be sued in its own name** by its partners as well as outsiders

### 4. **Mutual Agency:**

- **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.
- **In the absence of any such agreement**, the mutual rights and duties shall be governed by the provisions of the LLP Act, 2008.

### 6. **Artificial Legal Person:**

- A LLP is an **artificial legal person** because it is created by a legal process and is clothed with all rights of an individual.
- A LLP is **invisible, intangible, immortal** (it can be dissolved by law alone) but **not fictitious** because it really exists.

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### 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)].[not mandatory]**
- 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 except in case of unauthorized acts, fraud and negligence**

### 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. **Foreign LLPs:**

- **Section 2(1)(m)** defines foreign limited liability partnership "as a **limited liability partnership formed, incorporated, or registered outside India which established a place of business within India**".
- **Foreign LLP can become a partner in an Indian LLP.**

## ADVANTAGES OF LLP

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- LLP is organized and operates on the basis of an agreement.
- It provides flexibility without imposing detailed legal and procedural requirements
- It is easy to form
- In LLP form, all partners enjoy limited liability
- Flexible capital structure is there in this form
- It is easy to dissolve



# THE LIMITED LIABILITY PARTNERSHIP ACT, 2008 (Chart 1.2)

## SECTION 3: LIMITED LIABILITY PARTNERSHIP TO BE BODY CORPORATE.

1. A limited liability partnership is a **body corporate formed and incorporated under this Act** and is a legal entity separate from that of its partners.
2. A limited liability partnership shall **have perpetual succession.**
3. **Any change** in the partners of a limited liability partnership shall not affect the existence, rights or liabilities of the limited liability partnership.

## SECTION 4: NON-APPLICABILITY OF THE INDIAN PARTNERSHIP ACT, 1932

Save as otherwise provided, the provisions of the **Indian Partnership Act, 1932 shall not apply to a limited liability partnership.**

## SECTION 5: PARTNERS

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.**

## SECTION 6: MINIMUM NUMBER OF PARTNERS

- i. Every LLP shall have at **least 2 partners.**
- ii. If at any time the number of partners of a LLP is **reduced below two and the LLP carries on business for more than 6 months** while the number is so reduced, **the person, who is the only partner of the LLP during the time that it so carries on business after those 6 months and has the knowledge of the fact that it is carrying on business with him alone, shall be liable personally for the obligations of the LLP incurred during that period**

## SECTION 7: DESIGNATED PARTNERS

1. Every LLP shall have at **least 2 designated partners** who are individuals and **at least one of them shall be a resident in India.**

Provided that in case of a LLP in which **all the partners are bodies corporate or in which one or more partners are individuals and bodies corporate, at least 2 individuals who are partners of such LLP or nominees of such bodies corporate shall act as designated partners.**

Explanation: **Resident in India:** 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 120 days during the financial year.**

## SECTION 11: INCORPORATION DOCUMENT

1. For a LLP to be incorporated:
  - a) **2 or more persons** associated for **carrying on a lawful business** with a view to **profit** shall **subscribe their names** to an incorporation document;
  - b) the incorporation document shall be filed in such manner and with such fees, as may be prescribed with the **Registrar of the State in which the registered office of the LLP is to be situated;** and
  - c) **Statement to be filed:**
    - there shall be filed along with the incorporation document, a **statement in the prescribed form,**
    - made by either an **advocate, or a CS or a CA or a Cost Accountant,** who is engaged in the formation of the LLP and
    - by any **1 who subscribed his name to the incorporation document,**
    - that all the **requirements of this Act and the rules** made there under have **been complied with,** in respect of incorporation and matters precedent and incidental thereto.
2. The incorporation document shall –
  - a) be in a **form as may be prescribed;** Compiled By:CA Sahil Grover
  - b) state the **name of the LLP;**
  - c) state the **proposed business of the LLP;**
  - d) state the **address of the registered office of the LLP;**
  - e) state the **name and address of each of the persons who are to be partners of the LLP on incorporation;**
  - f) state the **name and address of the persons who are to be designated partners of the LLP on incorporation;**
  - g) contain such **other information** concerning the proposed LLP as may be **prescribed.**
3. **Punishment:** If a person makes a statement as discussed above which he –
  - a) knows to be **false;** or
  - b) does not **believe to be true,** shall be punishable
    - with **imprisonment** for a term which **may extend to 2 years and**
    - with **fine** which shall not be less than **Rs. 10,000 but which may extend to Rs.5 Lakhs**

## SECTION 12: INCORPORATION BY REGISTRATION

1. When the requirements imposed section 11 have been complied with the **Registrar shall retain the incorporation document & within 14 days register the incorporation document; and give a certificate that the LLP is incorporated by the name specified therein.**
2. The Registrar may **accept the statement delivered under Sec 11(1)(c)** as sufficient evidence that the requirement imposed by clause (a) of that sub-section has been complied with.
3. The certificate issued shall be **signed by the Registrar and authenticated by his official seal.**
4. The certificate shall be **conclusive evidence that the LLP is incorporated by the name specified therein.**

## SECTION 13: REGISTERED OFFICE OF LLP AND CHANGE THEREIN

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 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 default is made in complying with the requirements of this section, the **LLP and its every partner** shall be liable to a penalty of **Rs.500 for each day** during which the default continues, subject to a **maximum of Rs.50,000 for the LLP and its every partner.**

## SECTION 14: EFFECT OF REGISTRATION

- On registration, a LLP shall, by its name, be **capable of –**
- a) **suing and being sued;**
  - b) **acquiring, owning, holding and developing or disposing of property, whether movable or immovable, tangible or intangible**
  - c) having a **common seal, if it decides to have one; and**
  - d) **doing and suffering such other acts and things as bodies corporate may lawfully do and suffer**

# THE LIMITED LIABILITY PARTNERSHIP ACT, 2008 (Chart 1.3)

## SECTION 15: NAME

1. Every LLP shall have either the words **“limited liability partnership”** or the **acronym LLP** as the **last words of its name**.
2. **No LLP shall be registered by a name** which, in opinion of CG is—
  - a) **undesirable**; or
  - b) **identical or too nearly resembles** to that of any other LLP or a company or a registered trade mark of any other person under the Trade Marks Act, 1999.

## SECTION 16: RESERVATION OF NAME

1. **A person may apply** in such form and manner and accompanied by such fee as may be prescribed **to the Registrar for the reservation of a name set out in the application as—**
  - a) **the name of a proposed LLP**; or
  - b) **the name to which a LLP proposes to change its name**.
2. **Upon receipt of an application** under sub-section (1) and on **payment of the prescribed fee**, the Registrar may, **if he is satisfied**, subject to the rules prescribed by the CG in the matter, that the name to be reserved **is not one** which may be rejected on any ground referred to in section 15(2), **reserve the name for a period of 3 months from the date of intimation by the Registrar**.

## SECTION 17: CHANGE OF NAME OF LLP

1. Notwithstanding anything contained in sections 15 and 16, , if through inadvertence or otherwise, a **LLP, on its first registration or on its registration by a new name**, is registered by a **name which is identical with or too nearly resembles to—**
  - (a) that of any other **LLP 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 LLP or proprietor or company**, the **CG may direct such LLP to change its name** or new name within a period of **3 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 3 years** from the date of incorporation or registration or change of name of the LLP under this Act
2. Where a LLP changes its name or obtains a new name under sub-section (1), it shall **within a period of 15 days from the date of such change**, give **notice of the change to Registrar along with the order of the CG**, who shall carry out necessary changes in the certificate of incorporation and within **30 days of such change in the certificate of incorporation**, such LLP shall **change its name in the LLP agreement**.
3. If the LLP is in **default in complying** with any direction given under sub-section (1), the **CG shall allot a new name to the LLP** in such manner as may be prescribed and the **Registrar shall enter the new name in the register of LLPs** in place of the old name and **issue a fresh certificate of incorporation with new name**, which the **LLP shall use thereafter**.  
 Provided that nothing in this sub-section shall **prevent a LLP from subsequently changing its name in accordance with the provisions of Sec 16**.

## STEPS TO INCORPORATE LLP

- i. **Name reservation**: The first step to incorporate 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.
- ii. **Incorporate LLP**: After reserving a name, user has to file **e-Form 2** for incorporating a 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.
- iii. **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**.

## IMPORTANT DEFINITIONS

1. **Body Corporate [Sec 2(1)(d)]**: It means a company as defined in section 2(20) of Companies Act, 2013 and includes—
  - i. a LLP registered under this Act;
  - ii. a LLP incorporated outside India; and
  - iii. a company incorporated outside India,
 but does not include—
  - i. a corporation sole;
  - ii. a co-operative society registered under any law for the time being in force; and
  - iii. any other body corporate (not being a company as defined in section 2(20) of the Companies Act, 2013 or a LLP as defined in this Act), which the CG may, by notification in the OG specify in this behalf.
2. **Business [Sec 2(1)(e)]**: “Business” includes every trade, profession, service and occupation except any activity which the CG may by notification exclude.
3. **Designated Partner [Sec 2(1)(j)]**: “Designated partner” means any partner designated as such pursuant to section 7.
4. **Financial Year [Sec 2(1) (l)]**: “Financial year”, in relation to a LLP, means the period from the 1st day of April of a year to the 31st day of March of the following year. However, in the case of a LLP incorporated after the 30th day of September of a year, the financial year may end on the 31st day of March of the year next following that year.
5. **Foreign LLP [Sec 2(1)(m)]**: It means a LLP formed, incorporated or registered outside India which establishes a place of business within India.
6. **Limited liability partnership [Sec 2(1)(n)]**: Limited Liability Partnership means a partnership formed and registered under this Act.
7. **Limited Liability partnership agreement [Sec 2(1)(o)]**: It means any written agreement between the partners of the LLP or between the LLP and its partners which determines the mutual rights and duties of the partners and their rights and duties in relation to that LLP.
8. **Partner [Section 2(1)(q)]**: Partner, in relation to a LLP, means any person who becomes a partner in the LLP in accordance with the LLP agreement.
9. **Small LLP[Section 2(1)(ta)]**: It means a **limited liability partnership—**
  - (i) the contribution of which, does not exceed **25 lakh rupees** or such higher amount, **not exceeding 5 crore rupees**, as may be prescribed; and
  - (ii) the turnover of which, as per the Statement of Accounts and Solvency for the immediately preceding financial year, does not exceed **40 lakh rupees** or such higher amount, **not exceeding 50 crore rupees, as may be prescribed; or**
  - (iii) which meets such other requirements as may be prescribed, and fulfils such terms and conditions as may be prescribed

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# THE LIMITED LIABILITY PARTNERSHIP ACT, 2008 (Chart 1.4)

## DIFFERENCES BETWEEN LLP & PARTNERSHIP FIRM

	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.	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
9.	Liability	Liability of each partner limited to the extent to agreed contribution except in case of willful fraud.	Liability of each partner is unlimited.
10.	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.

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## DIFFERENCES BETWEEN LLP & COMPANY

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

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# CA SANCHIT GROVER

**THE NEGOTIABLE  
INSTRUMENTS ACT, 1881**

# THE NEGOTIABLE INSTRUMENTS ACT, 1881 (Chart 1.1)

INTRODUCTION	PAYABLE TO ORDER	INLAND INSTRUMENT (SEC 11)				
<ul style="list-style-type: none"> <li>- This is an Act to define and amend the law relating to Promissory Notes, Bills of Exchange and Cheques.</li> <li>- The Act applies to the whole of India.</li> <li>- The Act was amended several times.</li> <li>- Recent three amendments made in the N.I. Act were the Negotiable Instruments (Amendment and Miscellaneous Provisions) Act, 2002 and the Negotiable Instruments (Amendment) Act, 2015 and Negotiable Instruments (Amendment) Act, 2018.</li> </ul>	<ul style="list-style-type: none"> <li>- A negotiable instrument is payable to order when                             <ul style="list-style-type: none"> <li>(i) It is expressed to be so payable</li> <li>(ii) When it is expressed to be payable to a specified person and does not contain words prohibiting its transfer. (i.e. it is transferrable by Indorsement and delivery)</li> </ul> </li> <li><b>For example:</b></li> <li>(i) Pay A, (ii) Pay A or order, (iii) Pay to the order of A</li> <li>But it should not contain any words prohibiting transfer, e.g. "Pay to A only" or "Pay to A and none else" is not treated as 'payable to order' and therefore such a document shall not be treated as negotiable instrument because its negotiability has been restricted.</li> </ul>	<p>A negotiable instrument is an inland instrument if -</p> <ul style="list-style-type: none"> <li>• it is drawn or made in India and</li> <li>• it is payable in India or is drawn on a person resident in India</li> </ul> <p><b>Examples of inland instruments:</b></p> <ol style="list-style-type: none"> <li>a) A promissory note made in Chennai and payable in Delhi.</li> <li>b) A bill of exchange drawn in Delhi and made payable in Mumbai (although the drawee may be residing outside India).</li> <li>c) A bill of exchange drawn in Kanpur on a person resident in Kolkata (although it may be made payable in London).</li> <li>d) A, a resident of Agra, drew (i.e., made) a bill of exchange in Agra on B, a merchant in New York. And B accepted the bill of exchange as payable in Delhi. It is an inland bill of exchange. In this case, the bill of exchange was drawn in India and also payable in India.</li> <li>e) A, resident of Mumbai, drew a bill of exchange in Mumbai on B, a merchant in Mathura. And B accepted the bill of exchange as payable in London. It is also an inland bill of exchange. In this case, the bill of exchange was drawn in India on a person resident in India. It is immaterial that the amount is payable in London.</li> </ol> <p><b>Note:</b> An inland instrument remains inland even if it has been endorsed in a foreign country. For example: If the bills of exchange mentioned in above two examples, are endorsed in France, they will remain inland bills.</p>				
<p><b>NEGOTIABLE INSTRUMENT-DEFINITION [Sec 13]</b></p> <ul style="list-style-type: none"> <li>• Negotiable instrument means a promissory note or Bill of exchange or Cheque payable either to order or to the bearer.</li> <li>• The word negotiable means 'transferable by delivery' and the word instrument means 'a written document'.</li> <li>• "Negotiable instrument" literally means 'a written document transferable by delivery.'</li> <li>• Sec 13 does not define a negotiable instrument although it mentions only three kinds of negotiable instruments namely, bills, notes and cheques. But it does not necessarily follow that there can be no other negotiable instruments than those enumerated in the Act.</li> <li>• In India, Government promissory notes, delivery orders, railway receipts for goods and banker drafts have been held to be negotiable by usage or custom.</li> </ul>	<p style="text-align: center;"><b>PAYABLE TO BEARER</b></p> <ul style="list-style-type: none"> <li>- A negotiable instrument is payable to bearer when                             <ul style="list-style-type: none"> <li>(i) it is expressed to be so payable e.g. pay bearer</li> <li>(ii) When the only or last indorsement on the instrument is an indorsement in blank</li> </ul> </li> <li><b>For example:</b></li> <li>(i) "Pay to A or bearer", (ii) "Pay bearer"</li> <li>Also where an instrument is originally 'payable to order,' it may become 'payable to bearer' if indorsed in blank by the payee.</li> </ul> <p style="text-align: right; font-size: small;">Compiled By: CA Sahil Grover</p>					
<p style="text-align: center;"><b>CHARACTERISTICS OF NEGOTIABLE INSTRUMENT</b></p> <ol style="list-style-type: none"> <li>1) It is necessarily in writing.</li> <li>2) It should be signed.</li> <li>3) It is freely transferable from one person to another.</li> <li>4) Holder's title is free from defects.</li> <li>5) It can be transferred any number of times till its satisfaction.</li> <li>6) Every negotiable instrument must contain either a promise or order to pay money. Also, the promise or order must be unconditional.</li> <li>7) The promise or order to pay must consist of money only (nothing in addition or substitution of money).</li> <li>8) The sum payable, time of payment, the payee must be certain.</li> <li>9) The instrument should be delivered. Mere drawing of instrument does not create liability.</li> </ol>	<p style="text-align: center;"><b>TIME AND DEMAND INSTRUMENTS</b></p> <table border="1" style="width: 100%; border-collapse: collapse;"> <thead> <tr> <th style="width: 50%;">TIME INSTRUMENTS</th> <th style="width: 50%;">DEMAND INSTRUMENTS</th> </tr> </thead> <tbody> <tr> <td style="vertical-align: top;">                     An instrument which is payable -                     <ol style="list-style-type: none"> <li>a) After a fixed period or</li> <li>b) After sight or</li> <li>c) On a specified day or</li> <li>d) On the happening of an event which is certain to happen.</li> </ol> </td> <td style="vertical-align: top;">                     An instrument which is payable                     <ol style="list-style-type: none"> <li>a) On demand or</li> <li>b) At sight or</li> <li>c) in which no time for payment is specified.</li> </ol> </td> </tr> </tbody> </table> <p><b>Notes:</b></p> <ul style="list-style-type: none"> <li>- There can only be a 'time bill' or a 'time note' but not a 'time cheque', the reason being that a cheque cannot be expressed to be payable otherwise than on demand.</li> <li>- The maturity of a P/note or bill of exchange is the date at which it falls due</li> <li>- A negotiable instrument which is payable otherwise than on demand is entitled to 3 days of grace. A demand instrument is not entitled to any days of grace.</li> <li>- In a P/N or BOE the expressions "at sight" &amp; "on presentment" means on demand.</li> <li>- The expression "after sight" means,                             <ul style="list-style-type: none"> <li>• in a P/N, after presentment for sight, and,</li> <li>• in a BOE after acceptance, or noting or protest for non-acceptance</li> </ul> </li> <li>- As per the provisions of the RBI Act, 1934:                             <ul style="list-style-type: none"> <li>• A promissory note - cannot be made payable to bearer</li> <li>• A bill of exchange - cannot be made payable to bearer on demand.</li> <li>• A Cheque- is always payable on demand</li> </ul> </li> </ul> <p style="text-align: right; font-size: small;">Compiled By: CA Sahil Grover</p>	TIME INSTRUMENTS	DEMAND INSTRUMENTS	An instrument which is payable - <ol style="list-style-type: none"> <li>a) After a fixed period or</li> <li>b) After sight or</li> <li>c) On a specified day or</li> <li>d) On the happening of an event which is certain to happen.</li> </ol>	An instrument which is payable <ol style="list-style-type: none"> <li>a) On demand or</li> <li>b) At sight or</li> <li>c) in which no time for payment is specified.</li> </ol>	<p style="text-align: center;"><b>FOREIGN INSTRUMENT (SEC 12)</b></p> <p>A negotiable instrument which is not an inland instrument is called as foreign instrument.</p> <p><b>Examples of foreign instruments:</b></p> <ol style="list-style-type: none"> <li>a) A promissory note made in India but made payable in Germany on a person residing outside India.</li> <li>b) A bill of exchange drawn in India, on a person residing outside India, and made payable outside India.</li> <li>c) A bill drawn outside India and made payable in India.</li> <li>d) A bill drawn outside India, on a person residing in India.</li> </ol> <p><b>Liability of maker/ drawer of foreign bill (Section 134):</b> In the absence of a contract to the contrary, the liability of the</p> <ul style="list-style-type: none"> <li>- maker or drawer of a foreign promissory note or bill of exchange or cheque is regulated in all essential matters by the law of the place where he made the instrument</li> <li>- and the respective liabilities of the acceptor and indorser by the law of the place where the instrument is made payable</li> </ul>
TIME INSTRUMENTS	DEMAND INSTRUMENTS					
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# THE NEGOTIABLE INSTRUMENTS ACT, 1881 (Chart 1.2)

PROMISSORY NOTE (SECTION 4)	BILL OF EXCHANGE (SECTION 5)	CHEQUE (SECTION 6)
<p>A "promissory note" is an instrument in writing (not being a bank note or a currency note) containing an unconditional undertaking signed by the maker, to pay a certain sum of money only to a certain person or the order of a certain person or to the bearer of the instrument.</p> <p style="text-align: center;"><b><u>PARTIES TO A PROMISSORY NOTE</u></b></p> <p><b>Maker:</b> The person who makes the promissory note. He is the debtor and his liability is primary and unconditional</p> <p><b>Payee:</b> The person to whom money is to be paid is named in the promissory note</p>	<p>A bill of exchange is an instrument in writing, containing an unconditional order signed by the maker, directing a certain person to pay a certain sum of money only to a certain person; or the order of a certain person; or the bearer of the instrument.</p> <p style="text-align: center;"><b><u>PARTIES TO A BILL OF EXCHANGE</u></b></p> <p><b>Drawer:</b> The person who draws the bill (i.e. the person who makes the bill) is called as drawer. His liability is secondary and conditional.</p> <p><b>Drawee:</b> The person on whom the bill is drawn is called as drawee. The person directed by the drawer to pay is called the 'drawee'. On acceptance of the bill:-</p> <ol style="list-style-type: none"> <li>he is called as acceptor</li> <li>he becomes liable for the payment of bill .</li> <li>his liability is primary and unconditional.</li> </ol> <p><b>Payee:</b> The person named in the instrument, to whom or to whose order the money is, by the instrument, directed to be paid.</p>	<p>A Cheque is a bill of exchange drawn on a specified banker and not expressed to be payable otherwise than on demand (i.e. it is always payable on demand) and it includes the electronic image of a truncated cheque &amp; a cheque in the electronic form.</p> <p style="text-align: center;"><b><u>PARTIES TO A CHEQUE</u></b></p> <p><b>Drawer:</b> Person who draws the cheque (i.e. debtor). His liability is primary and conditional.</p> <p><b>Drawee:</b> The specific bank on whom the cheque is drawn. He makes the payment of the cheque. In case of a cheque, drawee is always a banker.</p> <p><b>Payee:</b> Person named in the instrument (i.e. the person in whose favour cheque is issued) to whom money is to be paid. The payee may be the drawer himself or a third party.</p>
CHARACTERISTICS OF PROMISSORY NOTE	CHARACTERISTICS OF BILL OF EXCHANGE	CHARACTERISTICS OF CHEQUE
<ol style="list-style-type: none"> <li><b><u>In writing:</u></b> An oral promise to pay is not sufficient. There is no prescribed form or language for this; even the word 'promise' need not be used. What is necessary is that whatever language is used, it must clearly show that the maker is unconditionally bound to pay the sum.</li> <li><b><u>Express promise to pay:</u></b> There must be an express promise to pay. Mere acknowledgement of indebtedness is not sufficient. <span style="float: right;">Compiled By:CA Sahil Grover</span></li> <li><b><u>Definite and unconditional promise:</u></b> Instruments payable on performance or non-performance of a particular act or on the happening or non-happening of an event, are not promissory notes. If a promise to pay is dependent upon an event which is certain to happen, although the time of its happening is uncertain, the promise to pay is unconditional.</li> <li><b><u>Signed by maker:</u></b> A promissory note must be signed by maker. The signatures may be made on any part of the instrument and need not be at the bottom.</li> <li><b><u>Promise to pay a certain sum:</u></b> The sum of money promised to be payable must be certain and definite. The amount payable must not be capable of contingent additions or subtractions. But, according to Sec 5, Para 3, the sum does not become indefinite merely because: <ul style="list-style-type: none"> <li>there is a promise to pay the amount with interest, provided the rate of interest is stated;</li> <li>the amount is to be paid at an indicated rate of exchange or according to the course of exchange; or</li> <li>The amount is payable by instalments, even with a provision that on default being made in payment of an installment, the balance unpaid shall become due.</li> </ul>                     If the amount undertaken or ordered to be paid is stated differently in figures and in words, the amount stated in words shall be the amount undertaken or ordered to be paid.(Section 18)                 </li> <li><b><u>Promise to pay money only:</u></b> "I promise to pay B Rs. 500 and to deliver to him my black horse on 1st January next". It is not a valid promissory note since the promisor is required to deliver his black horse also, which is not "money".</li> <li><b><u>Maker &amp; Payee must be certain:</u></b> The name of payee must be specified in the promissory note, otherwise it will be invalid. As per RBI Act P/N cannot be made payable to bearer</li> <li><b><u>Stamped:</u></b> A promissory note must be stamped in accordance with the provisions of the Indian Stamp Act and such stamp must be duly cancelled by maker's signatures or initials or otherwise.</li> </ol>	<ol style="list-style-type: none"> <li>It must be in writing.</li> <li>It must contain an express order to pay.</li> <li>The order to pay must be definite and unconditional.</li> <li>It must be signed by the drawer.</li> <li>The sum contained in the order must be certain.</li> <li>The order must be pay money only.</li> <li>The drawer, drawee and payee must be certain. As per the provisions of the RBI Act, 1934, a bill of exchange cannot be made payable to bearer on demand.</li> <li>It must be stamped.</li> </ol>	<ul style="list-style-type: none"> <li>A cheque is a species of bill of exchange. Thus, it should fulfil all the essential characteristics of a bill of exchange.</li> <li>It must be drawn on a specified banker.</li> <li>It must be payable on demand.</li> </ul> <p><b>Meaning of 'Truncated cheque':</b> A truncated cheque means a cheque which is truncated during the course of clearing cycle either by the clearing house or bank whether paying or receiving payment immediately on generation of an electronic image for transmission, substituting the further physical movement of the cheque in writing.</p> <p><b>Meaning of 'a cheque in electronic form':</b> "Cheque in the electronic form" means a cheque drawn in electronic form by using any computer resource, and signed in a secure system with a digital signature (with /without biometric signature) and asymmetric crypto system or with electronic signature, as the case may be</p> <p><b>Duties of collecting banker:</b> The collecting banker shall verify with due diligence and ordinary care the prima facie genuineness of the cheque to be truncated as to whether any fraud, forgery or tampering is apparent on the face of the instrument</p> <p><b>Presentment of truncated Cheque:</b> In case of any reasonable suspicion about the genuineness of the electronic image of a truncated cheque (e.g. suspicion as to fraud, forgery, tempering or destruction of the instrument) the paying banker is entitled to demand any further information regarding the truncated cheque or demand the presentment of truncated cheque itself for verification</p>
PROCESS OF BILL OF EXCHANGE	<pre> graph TD     A[Mr. Sam (Drawer)] --&gt; B[Drawer receives payment and transaction is completed]     B --&gt; C[Sold goods to Mrs. Reeta (Drawee) and draws a BoE]     C --&gt; D[The BoE is delivered to Reeta and is accepted by her unconditionally.]     D --&gt; E[On maturity drawer presents the instrument to drawee for payment]     E --&gt; B                     </pre>	

# THE NEGOTIABLE INSTRUMENTS ACT, 1881 (Chart 1.3)

DIFFERENCES BETWEEN ELECTRONIC & TRUNCATED CHEQUE	
ELECTRONIC CHEQUE	TRUNCATED CHEQUE
It means a <b>cheque drawn in electronic form</b> by using any computer resource, and <b>signed in a secure system with a digital signature</b> (with/without biometric signature) and asymmetric crypto system <b>or with electronic signature</b> , as the case may be.	It means a cheque which is <b>truncated during the course of clearing cycle</b> either by the clearing house or bank whether paying or receiving payment immediately on generation of an electronic image <b>for transmission, substituting the further physical movement of the cheque in writing.</b>
<b>Paper is not used</b> at any stage in creation of an electronic cheque.	It is nothing, but a <b>paper cheque</b> , which is truncated during the clearing cycle.
<b>Digital signatures must be used</b> to create an electronic image	<b>No digital signature</b> is used.
The <b>original writing</b> of an electronic cheque is <b>in electronic form.</b>	The <b>original writing</b> of a truncated cheque is <b>on paper, duly signed in ink.</b>

DIFFERENCES BETWEEN A PROMISSORY NOTE AND BILL OF EXCHANGE		
Basis	Promissory Note (Sec 4)	Bill of Exchange (Sec 5)
<b>Meaning</b>	It is an instrument in writing (not being a bank-note or a currency note) containing an unconditional undertaking signed by the maker, to pay a certain sum of money only to, or to the order of, a certain person, or to the bearer of the instrument.	It is an instrument in writing containing an unconditional order, signed by the maker, directing a certain person to pay a certain sum of money only to, or to the order of a certain person or to the bearer of the instrument.
<b>Nature of Instrument</b>	<b>There is a promise to pay money.</b>	<b>There is an order for making payment.</b>
<b>Parties</b>	<b>2 parties:</b> <b>Maker-</b> Person who makes the promissory note. His liability is primary and unconditional. <b>Payee-</b> Person to whom money is to be paid is named in the promissory note.  <span style="color: orange;">Compiled By:CA Sahil Grover</span>	<b>3 parties:</b> <b>Drawer-</b> Person who draws the bill (i.e. the person who makes the bill). His liability is secondary and conditional. <b>Drawee-</b> Person on whom the bill is drawn. On acceptance of the bill:- <ul style="list-style-type: none"> <li>• he is called as acceptor</li> <li>• he becomes liable for the payment of bill</li> <li>• his liability is primary and unconditional .</li> </ul> <b>Payee-</b> Person named in the instrument, to whom or to whose order the money is, by the instrument, directed to be paid.
<b>Acceptance</b>	<b>It does not require any acceptance</b> , as it is signed by the person who is liable to pay.	<b>It need a acceptance from the drawee.</b>
<b>Payable to bearer</b>	<b>It cannot be made payable to bearer.</b>	<b>It can be drawn payable to bearer.</b> However, it cannot be payable to bearer on demand.
<b>Nature of Liability</b>	The liability of the maker of a note is <b>primary and absolute.</b>  <span style="color: orange;">Compiled By:CA Sahil Grover</span>	The liability of the drawer of a bill is <b>secondary and conditional.</b> He would be liable if drawee, after accepting the bill fails to pay the money due provided notice of dishonour is given to the drawer within the prescribed time.

DIFFERENCES BETWEEN BILL OF EXCHANGE AND CHEQUE		
Basis	Bill of Exchange	Cheque
<b>Drawee</b>	Any person (including a banker) can be a drawee.	Only a banker can be a drawee.
<b>Liability of drawer</b>	Secondary and conditional. However, until a bill is accepted, the liability is primary.	The liability of drawer is always primary.
<b>Payable to bearer on demand</b>	A bill cannot be made payable to bearer on demand.	A cheque can be made payable to bearer on demand.
<b>Maturity date</b>	A bill may be payable on demand or otherwise than on demand.	A cheque is always payable on demand.
<b>Validity period</b>	No validity period.	3 months from the date of its issue.
<b>Stamping</b>	A bill must be stamped.	A cheque does not require stamping.
<b>Acceptance</b>	A bill requires acceptance if it is payable certain period after sight, or it contains an express term requiring acceptance.	No acceptance is required.
<b>Days of grace</b>	3 days of grace are allowed in case of every bill payable otherwise than on demand.	No days of grace are allowed.
<b>Crossing</b>	A bill cannot be crossed.	A cheque can be crossed.
<b>Criminal liability for dishonour</b>	No criminal liability on drawer.	The drawer of a cheque is criminally liable.



- SIMILARITIES**

  - Both are the **bills of exchange.**
  - Both have **3 parties**, the drawer, drawee and the payee.
  - **Drawer and payee may be one and the same person** in both instruments.
  - Both must **written and signed.**
  - Both must contain an **unconditional order to pay a certain sum of money.**
  - Both may be **indorsed.**



# THE NEGOTIABLE INSTRUMENTS ACT, 1881 (Chart 1.4)

NEGOTIATION [SECTION 14]	IMPORTANCE OF DELIVERY IN NEGOTIATION [SEC 46]	DISHONOUR OF CHEQUES FOR INSUFFICIENCY OF FUNDS IN THE ACCOUNTS [SEC 138]
<p>It means transfer of a negotiable instrument to any other person so as to constitute that person the holder of such negotiable instrument.</p> <p><b>Who can Negotiate?</b> Every maker, drawer, payee or indorsee</p> <p><b>Methods of negotiation:</b></p> <p>a) <b>Negotiation by delivery-</b></p> <ul style="list-style-type: none"> <li>• A bearer instrument may be negotiated by delivery.</li> <li>• The delivery must be voluntary and with an intention of transferring the ownership of the instrument to the transferee.</li> <li>• Mere delivery without the intention of passing the property is not sufficient to constitute a complete negotiation.</li> </ul> <p><b>Example:</b></p> <ul style="list-style-type: none"> <li>- If a person delivers a negotiable instrument to his servant for safe custody or to his solicitor for filing a suit, the delivery does not amount to negotiation and the servant or the solicitor acquires no title to the instrument.</li> <li>- A, the holder of a negotiable instrument payable to bearer, which is in the hands of A's banker, who is at the time the banker of B, directs the banker to transfer the instrument to B's credit in the banker's account with B. The banker does so, and accordingly now possesses the instrument as B's agent. The instrument has been negotiated, and B has become the holder of it.</li> </ul> <p style="text-align: right; color: #FF8C00;">Compiled By:CA Sahil Grover</p> <p>b) <b>Negotiation by Indorsement and delivery</b> An order instrument can be negotiated only by way of Indorsement and Delivery</p>	<ul style="list-style-type: none"> <li>- Delivery of an instrument is essential whether the instrument is payable to bearer or order for effecting the negotiation.</li> <li>- The delivery must be <b>voluntary</b> and the <b>object of delivery should be to pass the property</b> in the instrument to the person to whom it is delivered.</li> <li>- The delivery can be, <b>actual or constructive</b>.</li> <li>- <b>Actual delivery</b> takes place when the instrument changes hand physically.</li> <li>- <b>Constructive delivery</b> takes place when the instrument is delivered to the agent, clerk or servant of the indorsee on his behalf or when the indorser, after indorsement, holds the instrument as an agent of the indorsee.</li> <li>- The delivery is essential not only at the time of negotiation but also at the time of making or drawing of negotiable instrument. The rights in the instrument are not transferred to the indorsee unless after the indorsement the same has been delivered</li> <li>- If the holder of a negotiable instrument payable to order makes the indorsement but dies before delivering the same to the indorsee, the negotiation is not complete and his legal representative cannot negotiate the same by mere delivery thereof.</li> <li>- It is so because there is no valid delivery since the instrument has not been voluntarily delivered by the deceased himself.</li> <li>- Thus, delivery with the intention of passing the property in the instrument to the person to whom it is delivered is an essential formality to complete any contract on a negotiable instrument whether it be a contract of making, Indorsement or acceptance (Sec. 46).</li> <li>- Section 46 also lays down that when an instrument is conditionally or for a special purpose only, the property in it does not pass to the transferee, even though it is indorsed to him, unless the instrument is negotiated to a holder in due course.</li> </ul>	<ul style="list-style-type: none"> <li>- Where any cheque drawn by a person on an account maintained by him with a banker for payment of any amount of money to another person from out of that account</li> <li>- for the discharge, in whole or in part, of any debt or other liability,</li> <li>- is returned by the bank unpaid, either because of the –</li> <li>- amount of money standing to the credit of that account is insufficient to honor the cheque, or that it exceeds the amount arranged to be paid from that account by an agreement made with that bank,</li> <li>- Such person shall be deemed to have committed an offence and shall, be punished</li> <li>- with imprisonment for a term which may extend to two years, or</li> <li>- with fine which may extend to twice the amount of the cheque, or with both.</li> </ul> <p style="text-align: center; color: #FF8C00;"><b>Conditions to be complied to attract Sec 138</b></p> <ol style="list-style-type: none"> <li>i. The cheque should have been <b>dishonoured due to insufficiency of funds</b> standing to the credit of the account on which the cheque was drawn or for the reason that the amount of cheque drawn on the account exceeds the sanctioned limit of overdraft.</li> <li>ii. The cheque should have been issued by the drawer in favour of another person for the <b>discharge of legally enforceable debt or other liability</b>, in whole or in part. Therefore, when any cheque issued for meeting social obligations, such as <b>charity, marriage presents, birthday gifts. etc., is dishonoured for want of funds</b>, the drawer would not be deemed to have committed an offence. However, the court shall presume that the holder of a cheque received the cheque in the discharge of a liability, unless the contrary is proved by the accused drawer.(Sec 139)</li> <li>iii. Cheque should have been <b>presented to the bank within a period of 3 months from the date</b> on which it is drawn or <b>within the period of its validity, whichever is earlier</b>.</li> <li>iv. Payee or HDC of the cheque should have made a demand for the <b>payment within 30 days</b> of the receipt of information by him from the bank regarding the return of the cheque as unpaid/ bounced.</li> <li>v. Drawer of such cheque should have failed to make the payment to the payee or HDC of the cheque <b>within 15 days of the receipt of the said notice of demand</b>. If the drawer does not pay till the expiry of the 15 days time, the cause of action arises on 16th day.</li> <li>vi. Payee or HDC of the cheque dishonoured should have made a <b>written complaint of the offence to a Court not subordinate to that of a Metropolitan Magistrate or a First Class Judicial Magistrate, within 1 month of the date on which the cause of action arose</b>. However, if the complainant satisfies the court that he had sufficient cause for not making a complaint within the prescribed period of one month, the court is empowered to condone the delay.</li> </ol> <p style="text-align: right; color: #FF8C00;">Compiled By:CA Sahil Grover</p>
INDORSEMENT [SECTION 15]		
<p><b>Indorsement means</b></p> <ul style="list-style-type: none"> <li>- signing on the face/back of negotiable instrument or on a slip of a paper annexed to the negotiable instrument (known as allonge)</li> <li>- by the holder of negotiable instrument</li> <li>- for the purpose of negotiating such negotiable instrument.</li> </ul> <p>The person making the Indorsement is called an 'indorser' and the person to whom the instrument is indorsed is called an 'indorsee.'</p>		
ESSENTIAL REQUIREMENTS OF VALID INDORSEMENT		
<ol style="list-style-type: none"> <li>a) <b>Writing:</b> Indorsement must be in writing.</li> <li>b) <b>Signed:</b> Indorsement must be signed. The indorsement may be made by the indorser either by merely signing his name on the instrument or by specifying in addition to his signature, the person to whom or to whose order the instrument is payable.</li> <li>c) <b>By holder:</b> Indorsement shall be valid only if the negotiable instrument is signed by the holder.</li> </ol>		

# THE NEGOTIABLE INSTRUMENTS ACT, 1881 (Chart 1.5)

## PRESUMPTION IN FAVOUR OF HOLDER [SECTION 139]

When a cheque is dishonoured, it shall be presumed, unless the contrary is proved, that the holder of a cheque received the cheque of the nature referred to in section 138 for the discharge, in whole or in part, or any debt or other liability. Presumption prescribed here is a "rebuttable presumption". The effect of this presumption is to place the evidential burden on the accused.

## DEFENCE WHICH MAY NOT BE ALLOWED IN ANY PROSECUTION UNDER SEC 138 [SECTION 140]

It shall not be a defense in a prosecution of an offence under section 138 that the drawer had no reason to believe when he issued the cheque that the cheque may be dishonoured on presentment for the reasons stated in that section.

## EFFECT OF STOP PAYMENT

Where the drawer makes 'stop payment' order to the banker (i.e. he countermands payment) resulting in dishonor of cheque, it has the same effect as if the cheque had been dishonored due to insufficiency of funds. Thus the proceedings u/s 138 may be initiated against the drawer. (Modi Cements Ltd. Vs. Kuchil Kumar Nandi)

### Example:

X issued a post-dated cheque to Y on the account of discharge of its liability. Further, X instructed to the bank to stop the payment due to unavailability of the adequate amount in the account. Here, in this instance section 138 of the Act is attracted as when a cheque is dishonoured on account of stop payment instructions sent by the drawer to his banker in respect of a post- dated cheque irrespective of insufficiency of funds in the account

## PRESENTMENT OF NEGOTIABLE INSTRUMENTS

**Presentation means showing the instrument to the drawee, acceptor or maker for acceptance, sight or payment. There are three kinds of presentments:**

1. Presentment of bills of exchange for acceptance. [Sec 61]
2. Presentment of promissory notes for sight. [Sec 62]
3. Presentment of negotiable instrument for payment. [Sec 64]

Compiled By: CA Sahil Grover

### PRESENTMENT FOR ACCEPTANCE [Sec 61]

- Sec 61 provides as follows:
  - A bill of exchange payable after sight must [if no time or place is specified therein for presentment]
  - be presented to the drawee thereof for acceptance [if he can, after reasonable search, be found]
  - by a person entitled to demand acceptance,
  - within a reasonable time after it is drawn, and in business hours on a business day
- In default of such presentment, no party thereto is liable thereon to the person making such default.
- If the drawee cannot, after reasonable search, be found, the bill is dishonoured.
- If the bill is directed to the drawee at a particular place, it must be presented at that place, and if at the due date for presentment he cannot, after reasonable search, be found there, the bill is dishonored. (If no place is mentioned in the bill, it may be presented at the usual place of business of the drawee or his residence).
- Where authorised by agreement or usage, a presentment through the post office by means of a registered letter is sufficient.

Compiled By: CA Sahil Grover

### Analysis of section:

- Presentment for acceptance' is necessary in case of bills of exchange only. But it is not every bill which has to be presented for acceptance.
- A bill of exchange 'payable on demand', or 'payable on the expiry of certain period after date' (say, payable three months after date), or 'payable on the date of happening of an event which is certain to happen' (say, on the death of Mr. X) need not be presented for acceptance and it becomes due for payment even otherwise.
- The following bills, however, must be presented for acceptance in order to charge the parties with liability:
  - a) A bill payable at a specified period after sight. Such a bill must be presented to the drawee for sight or acceptance in order to fix the maturity of the bill. (Sec. 61)
  - b) A bill in which there is an express stipulation that it shall be presented for acceptance before it is presented for payment.
- Even where presentation is optional, it is advisable to present the bill to the drawee for his acceptance in order to get the additional security of the acceptor's name on the bill, or an immediate right of recourse against the drawer and the endorsers, if any, in case the bill is dishonoured by non-acceptance
- From the drawer's point of view also presentment for acceptance is desirable, for if acceptance is refused, he may, on receiving early notice of dishonour, be able to get his effects out of the hands of the drawee.

### Drawee's time for deliberation [Section 63]:

- Sec. 63 provides that the holder of a bill must allow the drawee 48 hours (excluding of public holidays) to consider whether he will or will not accept the bill.
- If the holder allows more time, all the previous parties not consenting to such allowance are discharged from liability to such holder. (Sec 83) If the drawee does not return the accepted bill within forty-eight hours the holder should treat the bill as dishonoured.

### PRESENTMENT FOR SIGHT [Sec 62]

- "Presentment for sight" is necessary only in the case of a promissory note which is made payable at a certain period after sight, so that the maturity of the note may be ascertained.
- According to Section 62, "a promissory note, payable at a certain period after sight, must be presented to the maker thereof for sight (if he can after reasonable search be found) by a person entitled to demand payment, within a reasonable time after it is made and in business hours on a business day.
- In default of such presentment, no party thereto is liable thereon to the person making such default."

### PRESENTMENT FOR PAYMENT [Sec 64]

- Promissory note, bill of exchange and cheques must be presented for payment on the due dates to the maker, acceptor or drawee thereof respectively by or on behalf of the holder.
- On default of such presentment the parties thereto, other than the maker, acceptor or drawee, are not liable thereon to the holder of the instrument. [Sec. 64(1)]

### Presentment by whom?

- The presentment for payment is to be made by the person who can give valid discharge to the debtor, i.e. either by the holder or by his authorised agent, or in case of his death or insolvency, by his legal representative or Official Assignee, as the case may be.
- Where authorised by agreement or trade usage, a presentment through the post office by means of a registered letter is sufficient. [Sec. 64(1)]

### Presentment to whom?

- The presentment for payment of P/notes, BOE & cheques must be made to the maker, acceptor or drawee thereof respectively
- It may also be made to the duly authorized agent of the maker, acceptor or drawee, as the case may be, or, where the maker, acceptor or drawee has died, to his legal representative, or, where he has been declared an insolvent, to his Official Assignee

# THE NEGOTIABLE INSTRUMENTS ACT, 1881 (Chart 1.6)

RULES REGARDING TIME OF PRESENTMENT FOR PAYMENT	RULES REGARDING PLACE OF PRESENTMENT FOR PAYMENT	WHEN PRESENTMENT FOR PAYMENT UNNECESSARY (SEC. 76)
<p><b>1. Hours for presentment:</b> Presentment for payment must be made during the usual hours of business and if payable at a bank, during the usual banking hours (Sec. 65).</p> <p><b>2. Presentment for payment of instrument payable after date or sight:</b> A negotiable instrument payable otherwise than on demand, <i>i.e.</i>, payable at a specified period after date or sight thereof, must be presented for payment at maturity (Sec. 66). Earlier presentment is premature and ineffective, and even a day's delay would discharge the parties thereto except one which is primarily liable</p> <p><b>3. Presentment for payment of promissory note payable by instalments (Sec 67):</b> A promissory note payable by instalments must be presented for payment on the third day after the date fixed for payment of each instalment (thus every instalment is entitled to three days of grace). Non-payment of single instalment has the same effect as non-payment of a note at maturity. Thus, if a single instalment is not paid the whole of the note can be treated as dishonoured by non-payment.</p> <p><b>4. Presentment of instrument payable on demand (Secs. 73 and 74):</b> A negotiable instrument payable on demand must be presented for payment <b>within a reasonable time</b> after it is received by the holder, otherwise the parties thereto except one which is primarily liable will be discharged from their liability</p> <p><b>5. Presentment of cheque to charge drawer (Section 72):</b> A cheque, which is always payable on demand, should be presented for payment <b>not only within a reasonable time</b> after delivery thereof <b>but also before the relation between the drawer and his banker has been altered to the prejudice of the drawer (i.e., before the bank has failed)</b>, otherwise even the party primarily liable, namely, the drawer will also be discharged from his liability to the extent of loss suffered by him on account of the delay (Secs. 72 and 84).</p>	<p><b>1. Instrument payable at specified place (Secs. 68 and 69):</b></p> <ul style="list-style-type: none"> <li>- Where in an instrument the precise address of the place of payment has been indicated by the maker, drawer or acceptor, it must be presented at that place for payment (Secs. 68 and 69).</li> <li>- However, if alternative places of payment have been mentioned then the instrument may be presented for payment at either of the places.</li> <li>- Thus, acceptor will also be discharged in case an instrument is not presented at the specified place.</li> <li>- "Specified place" implies the precise address of the place; the mere mention of a big city like 'Madras' is not sufficient.</li> </ul> <p><b>2. Presentment where no exclusive place specified (Sec. 70):</b> Where no place of payment has been indicated, the note or the bill must be presented at the place of business (if any), or at the usual residence of the maker, drawee or acceptor, as the case may be.</p> <p><b>3. Presentment when maker, etc., has no known place of business or residence (Section 71):</b> If the maker, drawee or acceptor of a negotiable instrument has no known place of business or fixed residence, and no place is specified in the instrument for presentment for acceptance or payment such presentment may be made to him in person wherever he can be found.</p>	<p>No presentment for payment is necessary, and the instrument may be taken to be dishonoured on the due date for presentment, in any of the following cases:</p> <ol style="list-style-type: none"> <li><b>1. When presentment is intentionally prevented:</b> Where the maker, acceptor or drawee intentionally does something which prevents the holder from presenting the instrument, e.g., where a promissory note is lost and the maker refuses to give a duplicate.</li> <li><b>2. Place of business closed:</b> If the instrument is payable at the payer's place of business and he closes such place on a business day during the usual business hours.</li> <li><b>3. Payer absents from place of payment:</b> If the instrument is payable at some other specified place, neither the payer nor any person authorised to make payment attends at such place during the usual business hours.</li> <li><b>4. When the payer cannot be found:</b> If the instrument is not payable at any specified place and the payer cannot after due search be found.</li> <li><b>5. Waiver of presentment:</b> If the person entitled to the presentment, namely, the payer waives the presentment and promises to pay even though no presentment is made. Such waiver may be made either expressly or impliedly. An express waiver may be made before maturity by expressly adding in the instrument such words as 'presentment waived'. An implied waiver will be inferred from the conduct of the maker, acceptor or drawee, when after maturity             <ul style="list-style-type: none"> <li>- he makes a part payment on account of the amount due on the instrument or</li> <li>- promises to pay the amount due thereon in whole or in part.</li> <li>- or otherwise waives his right to take advantage of any default in presentment for payment</li> </ul> </li> <li><b>6. Where drawer could not suffer damage:</b> Where the drawer is not likely to suffer damage by non-presentment for payment e.g., where drawee is a fictitious person or one incompetent to contract or where the drawer and the drawee are the same person, the presentment is excused as against the drawer and a holder can make the drawer liable without presentation</li> </ol>
<p><b>Liability of banker for negligently dealing with bill presented for payment (Section 77):</b> When a bill of exchange, accepted payable at a specified bank, has been duly presented there for payment and dishonoured, if the banker so negligently or improperly keeps. deals with or delivers back such bill as to cause loss to the holder. he must compensate the holder for such loss.</p>		
<p><b>RULES OF COMPENSATION (SECTION 117)</b></p>		
<p><b>WHEN DELAY IN PRESENTMENT IS EXCUSED (SEC. 75A)</b></p> <ul style="list-style-type: none"> <li>- Delay in presentment (for acceptance or payment) is excused if the same is caused by circumstances beyond the control of the holder, and not imputable to his default, misconduct or negligence.</li> <li>- Example- delay on account of impracticability of transmitting the instrument to the place of payment because of postal strike is excusable.</li> <li>- But when the cause of delay ceases to operate, presentment must be made within a reasonable time.</li> </ul>	<p>The compensation payable in case of dishonour of promissory note, bill of exchange or cheque, by any party liable to the holder or any endorsee, shall be determined by the following rules:</p> <ol style="list-style-type: none"> <li>a) the holder is entitled to the amount due upon the instrument, together with the expenses properly incurred in presenting, noting &amp; protesting it;</li> <li>b) when the person charged resides at a place different from that at which the instrument was payable, the holder is entitled to receive such sum at the current rate of exchange between the two places;</li> <li>c) an endorser who, being liable, has paid the amount due on the same is entitled to the amount so paid with interest at 18% per annum from the date of payment until tender or realisation thereof, together with all expenses caused by the dishonour &amp; payment;</li> <li>d) when the person charged and such endorser reside at different places, the endorser is entitled to receive such sum at the current rate of exchange between the two places.</li> <li>e) the party entitled to compensation may draw a bill upon the party liable to compensate him, payable at sight or on demand, for the amount due to him, together with all expenses properly incurred by him. Such bill must be accompanied by the instrument dishonoured and the protest thereof (if any). If such bill is dishonoured, the party dishonouring the same is liable to make compensation thereof in the same manner as in the case of the original bill.</li> </ol>	

INCHOATE INSTRUMENT [Sec. 20]
<ul style="list-style-type: none"> <li>- An incomplete or blank negotiable instrument properly stamped and signed is termed as an 'inchoate instrument'.</li> <li>- The drawer/ maker/ acceptor/ indorser of a negotiable instrument may sign and deliver the instrument to another person in his capacity leaving the instrument, either wholly blank or having written on it the word incomplete. Such an instrument is called an inchoate instrument and this gives a power to its holder to make it complete by writing any amount either within limits specified therein or within the limits specified by the stamp's affixed on it</li> <li>- Sec 20 provides that "where one person signs and delivers to another a paper stamped in accordance with the law relating to negotiable instruments, either wholly blank or having written thereon an incomplete negotiable instrument, he thereby gives prima facie authority to the holder thereof to make or complete, as the case may be, upon it a negotiable instrument, for any amount specified therein and not exceeding the amount covered by the stamp. The person so signing shall be liable upon such instrument, in the capacity in which he signed the same, to any holder in due course for such amount. But a person other than a holder in due course cannot recover from the person delivering the instrument anything in excess of the amount intended by him to be paid thereunder."</li> </ul> <p><b>Liability on drawing inchoate instrument:</b> The person signing and delivering the inchoate instrument is liable both to a holder and holder in due course. However, there is a difference in their respective rights:</p> <ul style="list-style-type: none"> <li>• The holder of such an instrument cannot recover the amount in excess of the amount intended to be paid by the signor.</li> <li>• The holder in due course can, however, recover any amount on such instrument provided it is covered by the stamp affixed on the instrument.</li> </ul> <p>It is to be emphasized that delivery of a stamped paper to the holder is necessary for the application of this Section, otherwise the maker or acceptor will not be liable even to a subsequent holder in due course</p>

AMBIGUOUS INSTRUMENTS
<ul style="list-style-type: none"> <li>- An instrument, which in form is such that it may either be treated as a bill of exchange or as a promissory note, is an ambiguous instrument.</li> <li>- In such a case, the holder may either treat it as a bill of exchange or a promissory note, but once he has made his choice the instrument shall henceforth be treated accordingly. (Sec. 17)</li> <li>- Sec 17 of the Act, reads as: "Where an instrument may be construed either as a promissory note or bill of exchange, the holder may at his election treat it as either, and the instrument shall be hence forward treated accordingly."</li> </ul> <p><b>Examples:</b></p> <ol style="list-style-type: none"> <li>Where in a bill the drawer and the drawee are the same person. Thus, where a bill is drawn by an agent, acting within the scope of his authority, upon his principal, the holder may, at his option treat it as a note or a bill because the drawer and the drawee are the same person in the eye of law. But where drawer and payee are the same, e.g., where a bill is drawn payable to the drawer's order, it is not an ambiguous instrument and is a valid bill of exchange.</li> <li>Where in a bill the drawee is a fictitious person or a person not having the capacity to contract. Thus, where P draws a bill on Q and negotiates it away, and Q is a fictitious or a minor drawee, the holder may treat the bill as a note made by P.</li> </ol>

SOME TOPICS FOR EXTRA READING FOR BETTER UNDERSTANDING	
<p><b>Meaning of 'holder' (Sec. 8)</b></p> <ol style="list-style-type: none"> <li>He must be entitled to the possession of negotiable instrument in his own name.</li> <li>He must be entitled to receive or recover the amount due on negotiable instrument from the parties liable on negotiable instrument.</li> </ol> <p><b>Meaning of 'holder in due course' (Sec. 9)</b></p> <ol style="list-style-type: none"> <li>He must be a holder.</li> <li>He must have become the holder for a valuable consideration.</li> <li>He must have obtained the possession of negotiable instrument before maturity.</li> <li>He must take the negotiable instrument complete and regular on the face of it</li> <li>He must have obtained the negotiable instrument in good faith i.e. without sufficient cause to believe that any defect existed in the title of the person from whom he derived his title.</li> </ol>	<p style="text-align: center;"><b>ACCEPTANCE</b></p> <p><b>Meaning of acceptance</b> The drawee signs the bill and delivers it to the holder of the bill or gives notice of acceptance to the holder of bill.</p> <p><b>Effect:</b> The drawee becomes the acceptor.</p> <p><b>Essentials of a valid acceptance</b></p> <ol style="list-style-type: none"> <li>Written (whether on the face or back of the bill).</li> <li>Signed (Signature without the word 'accepted' is also valid).</li> <li>Signing on the bill.</li> <li>Delivery or intimation to the holder that the bill has accepted.</li> </ol> <p><b>Types of acceptance</b></p> <ol style="list-style-type: none"> <li><b>General</b> - Acceptance of bill without any qualification.</li> <li><b>Qualified</b> - Acceptance of bill subject to some qualification.</li> </ol> <p><b>Examples of qualified acceptance:</b></p> <ol style="list-style-type: none"> <li>Where acceptance is conditional, declaring the payment to be dependent on the happening of an event therein stated.</li> <li>Where the drawee accepts the bill only for a part of the sum ordered to be paid.</li> <li>Where the drawee agrees to make the payment at a time other than that the time stated in the bill.</li> <li>Where, no place of payment being specified in the bill, the drawee agrees to make the payment at a specified place</li> </ol> <p><b>Effect of qualified acceptance</b></p> <ol style="list-style-type: none"> <li>Holder may object to the qualified acceptance, it shall be treated that the bill is dishonoured due to non-acceptance.</li> <li>He may give his consent to the qualified acceptance- all the prior parties not consenting to it, are discharged.</li> </ol>
<p><b>DISHONOUR OF NEGOTIABLE INSTRUMENTS</b></p> <p><b>DISHONOUR BY NON -ACCEPTANCE [Sec 91]</b></p> <ul style="list-style-type: none"> <li>• <b>Meaning:</b> A bill is dishonoured by non-acceptance if it is duly presented for acceptance, but the bill is not accepted.</li> <li>• <b>Cases in which a bill is dishonoured by non-acceptance:</b> <ol style="list-style-type: none"> <li>Where a bill is not accepted by the drawee within 48 hours of presentment of bill.</li> <li>In case there are two or more drawees who are not partners, if the bill is not accepted by all the drawees.</li> <li>Where the drawee is a fictitious person.</li> <li>When the drawee cannot be found even after a reasonable search.</li> <li>When the drawee is incompetent to contract.</li> <li>Where the drawee gives a qualified acceptance and the holder does not give his consent to qualified acceptance.</li> </ol> </li> <li>• <b>Effects:</b> The holder gets immediate rights to sue all the prior parties, without waiting for the maturity of the bill.</li> <li>• <b>Non-applicability:</b> A promissory note or a cheque cannot be dishonoured by non-acceptance since a promissory note or a cheque does not require any acceptance.</li> </ul> <p style="text-align: right;">Compiled By:CA Sahil Grover</p>	
<p><b>DISHONOUR BY NON PAYMENT [SECTION 92]</b> A promissory note, bill of exchange and cheque is said to be dishonoured by non-payment when the maker of the note, acceptor of the bill or drawee of the cheque makes default in payment upon being duly required to pay the same (Sec. 92).</p>	

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