PAPER – 2
BUSINESS LAWS

INDEX

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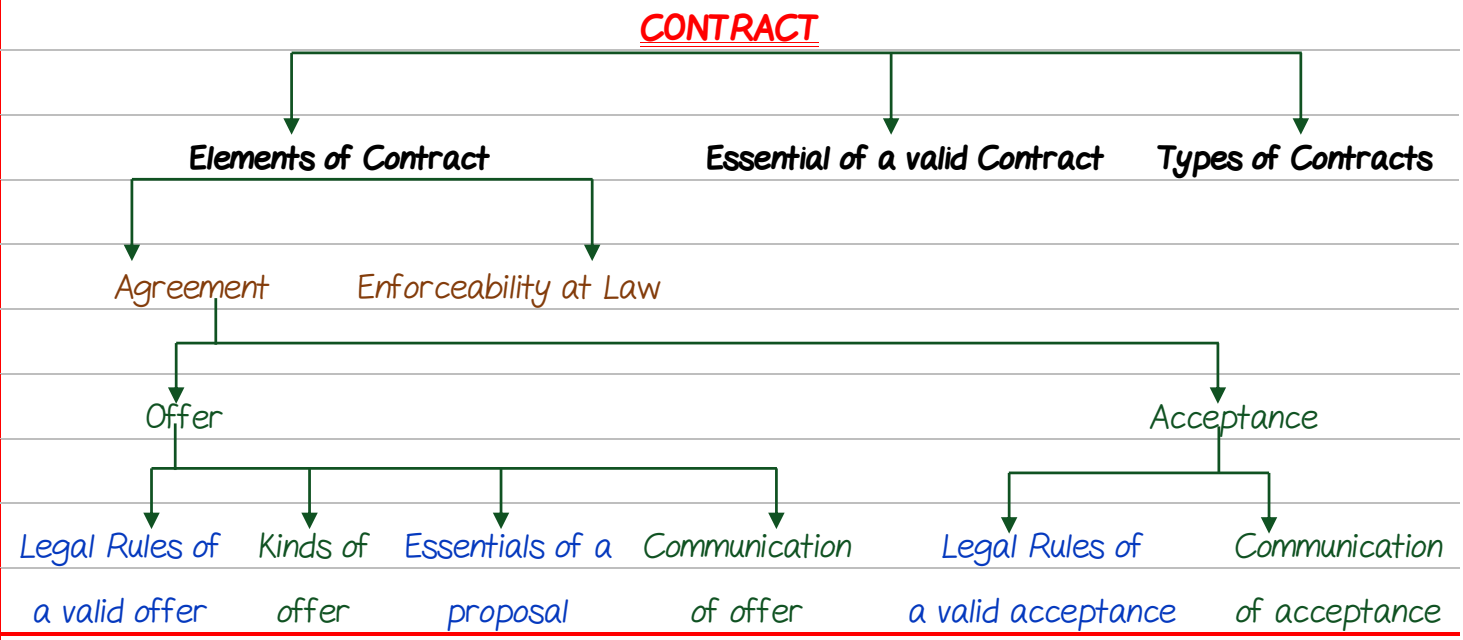
CHAPTER 1 THE INDIAN CONTRACT ACT, 1872

UNIT – 1

NATURE OF CONTRACT



THE LAW OF CONTRACT: INTRODUCTION

The Law of Contract constitutes the most important branch of mercantile or commercial law. It affects everybody, more so, trade, commerce and industry. It may be said that the contract is the foundation of the civilized world. The law relating to contract is governed by the Indian Contract Act, 1872. It came into force on September 01, 1872. The preamble to the Act says that it is an Act "to define and amend certain parts of the law relating to contract". It extends to the whole of India.

The Act mostly deals with the general principles and rules governing contracts. The Act is divisible into two parts. The first part (Section 1-75) deals with the general principles of the law of contract, and therefore applies to all contracts irrespective of their nature. The second part (Sections 124-238) deals with certain special kinds of contracts, e.g., Indemnity and guarantee, bailment, pledge, and agency.

As a result of increasing complexities of business environment, innumerable contracts are entered into by the parties in the usual course of carrying on their business. 'Contract' is the most usual method of defining the rights and duties in a business transaction. This branch of law is different from other branches of law in a very important aspect. It does not prescribe so many rights and

duties, which the law will protect or enforce; instead it contains a number of limiting principles subject to which the parties may create rights and duties for themselves. The Indian Contract Act, 1872 codifies the legal principles that govern 'contracts'. The Act basically identifies the ingredients of a legally enforceable valid contract in addition to dealing with certain special type of contractual relationships like indemnity, guarantee, bailment, pledge, quasi contracts, contingent contracts etc. It basically defines the circumstances in which promises made by the parties to a contract shall be legally binding on them.

This unit refers to the essentials of a legally enforceable agreement or contract. It sets out rules for the offer and acceptance and revocation thereof. It states the circumstances when an agreement is voidable or enforceable by one party only, and when the agreements are void, i.e. not enforceable at all.

WHAT IS A CONTRACT?

The term contract is defined under section 2(h) of the Indian Contract Act, 1872 as- "an agreement enforceable by law".

The contract consists of two essential elements:

(i) an agreement, and

(ii) its enforceability by law.

(i) **Agreement -** The term 'agreement' given in Section 2(e) of the Act is defined as- "every promise and every set of promises, forming the consideration for each other".

To have an insight into the definition of agreement, we need to understand promise.

Section 2 (b) defines promise as-"when the person to whom the proposal is made signifies his assent there to, the proposal is said to be accepted. Proposal when accepted, becomes a promise".

The following points emerge from the above definition:

1. when the person to whom the proposal is made
2. signifies his assent on that proposal which is made to him
3. the proposal becomes accepted
4. accepted proposal becomes promise

Thus, we say that an agreement is the result of the proposal made by one party to the other party and that other party gives his acceptance thereto of course for mutual consideration.

Agreement = Offer/Proposal + Acceptance

(ii) **Enforceability by law** – An agreement to become a contract must give rise to a legal obligation which means a duly enforceable by law.

Thus, from above definitions it can be concluded that –

Contract = Accepted proposal/Agreement + Enforceability by law

On elaborating the above two concepts, it is obvious that contract comprises of an agreement which is a promise or a set of reciprocal promises, that a promise is the acceptance of a proposal giving rise to a binding contract. Further, section 2(h) requires an agreement capable of being enforceable by law before it is called 'contract'. Where parties have made a binding contract, they created rights and obligations between themselves.

Example 1: A agrees with B to sell car for Rs. 2 lacs to B. Here A is under an obligation to give car to B and B has the right to receive the car on payment of Rs. 2 lacs and also B is under an obligation to pay Rs. 2 lacs to A and A has a right to receive Rs. 2 lacs.

Example 2: Father promises his son to pay him pocket allowance of Rs. 500 every month. But he refuses to pay later. The son cannot recover the same in court of law as this is a social agreement. This is not created with an intention to create legal relationship and hence it is not a contract.

So, Law of Contract deals with only such legal obligations which has resulted from agreements. Such obligation must be contractual in nature. However, some obligations are outside the purview of the law of contract.

Example 3: An obligation to maintain wife and children, an order of the court of law etc. These are status obligations and so out of the scope of the Contract Act.

Difference between Agreement and 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.

ESSENTIALS OF A VALID CONTRACT

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As given by Section 10 of Indian Contract Act, 1872	Not given by Section 10 but are also considered essential
1. Agreement	1. Two parties
2. Free consent	2. Intention to create legal relationship
3. Competency of the parties	3. Fulfilments of legal formalities
4. Lawful consideration	4. Certainty of meaning
5. Legal object	5. Possibility of performance
6. Not expressly declared to be void [as per Section 24 to 30 and 56]	

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

Since section 10 is not complete and exhaustive, so there are certain others sections which also contains requirements for an agreement to be enforceable. Thus, in order to create a valid

contract, the following elements should be present:

1. **Two Parties**: One cannot contract with himself. A contract involves at least two parties- one party making the offer and the other party accepting it. A contract may be made by natural persons and by other persons having legal existence e.g. companies, universities etc. It is necessary to remember that identity of the parties be ascertainable.

   Example 4: To constitute a contract of sale, there must be two parties- seller and buyer. The seller and buyer must be two different persons, because a person cannot buy his own goods. In State of Gujarat vs. Ramanlal S & Co. when on dissolution of a partnership, the assets of the firm were divided among the partners, the sales tax officer wanted to tax this transaction. It was held that it was not a sale. The partners being joint owner of those assets cannot be both buyer and seller.

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

   Example 5: A husband agreed to pay to his wife certain amount as maintenance every month while he was abroad. Husband failed to pay the promised amount. Wife sued him for the recovery of the amount. Here, in this case, wife could not recover as it was a social agreement and the parties did not intend to create any legal relations. (Balfour v. Balfour)

   Example 6: Lekhpal promises to pay Rs. 5 lakhs to his son if the son passes the CA exams. On passing the exams, the son claims the money. Here, the son could not recover as it was a social agreement.

   Example 7: A sold goods to B on a condition that he must pay for the amount of goods within 30 days. Here A intended to create legal relationship with B. Hence the same is contract. On failure by B for making a payment on due date, A can sue him in the court of law.

3. **Other Formalities to be complied with in certain cases**: A contract may be written or spoken. As to legal effects, there is no difference between a written contract and contract made by word of mouth. But in the interest of the parties the contract must be written. In case of certain contracts some other formalities have to be complied with to make an agreement

legally enforceable.

For eg. Contract of Insurance is not valid except as a written contract. Further, in case of certain contracts, registration of contract under the laws which is in force at the time, is essential for it to be valid, e.g. in the case of immovable property.

Thus, where there is any statutory requirement that any contract is to be made in writing or in the presence of witness, or any law relating to the registration of documents must be complied with.

4. **Certainty of meaning**: The agreement must be certain and not vague or indefinite.

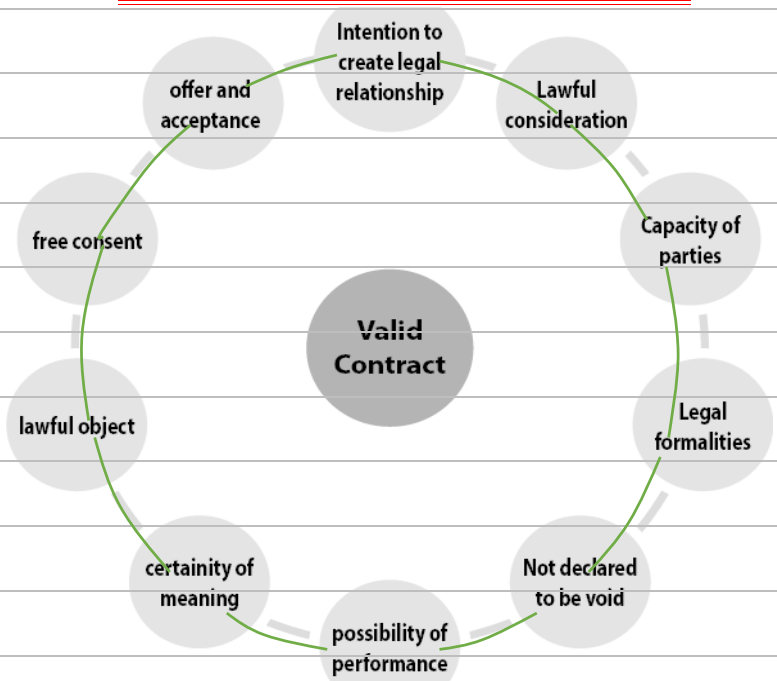
Example 8: A agrees to sell to B a hundred tons of oil. There is nothing certain in order to show what kind of oil was intended for.

Example 9: XYZ Ltd. agreed to lease the land to Mr. A for indefinite years. The contract is not valid as the period of lease is not mentioned.

5. **Possibility of performance of an agreement**: The terms of agreement should be capable of performance. An agreement to do an act impossible in itself cannot be enforced.

Example 10: A agrees with B to discover treasure by magic. The agreement cannot be enforced as it is not possible to be performed.

Essential elements of a valid contract



According to Section 10 of the Indian Contract Act, 1872, the following are the essential elements of a Valid Contract:

I. **Offer and Acceptance or an agreement**: An agreement is the first essential element of a valid contract. According to Section 2(e) of the Indian Contract Act, 1872, "Every promise and every set of promises, forming consideration for each other, is an agreement" and according to Section 2(b) "A proposal when accepted, becomes a promise". An agreement is an outcome of offer and acceptance.

II. **Free Consent**: Two or more persons are said to consent when they agree upon the same thing in the same sense. This can also be understood as identity of minds in understanding the terms viz consensus ad idem. Further such a consent must be free. Consent would be considered as free consent if it is not caused by coercion, undue influence, fraud, misrepresentation or mistake.

Example 11: A, who owns two cars is selling red car to B. B thinks he is purchasing the black car. There is no consensus ad idem and hence no contract.

To determine consensus ad idem the language of the contract should be clearly drafted. Thus, if A says B " Will you buy my red car for Rs. 30000? " and B says "yes" to it. There is said to be consensus ad idem i.e. the meaning is taken in same sense by both the parties.

Example 12: A threatened to shoot B if he (B) does not lend him Rs.2000 and B agreed to it. Here the agreement is entered into under coercion and hence not a valid contract.

(Students may note that the terms coercion, undue influence, fraud, misrepresentation, mistake are explained in the coming units)

III. **Capacity of the parties**: Capacity to contract means the legal ability of a person to enter into a valid contract. Section 11 of the Indian Contract Act specifies that every person is competent to contract who

(a) is of the age of majority according to the law to which he is subject and

(b) is of sound mind and

(c) is not otherwise disqualified from contracting by any law to which he is subject. A person competent to contract must fulfil all the above three qualifications.

Qualification (a) refers to the age of the contracting person i.e. the person entering into contract must be of 18 years of age. Persons below 18 years of age are considered minor, therefore, incompetent to contract.

Qualification (b) requires a person to be of sound mind i.e. he should be in his senses so that he understands the implications of the contract at the time of entering into a contract. A lunatic, an idiot, a drunken person or under the influence of some intoxicant is not supposed to be a person of sound mind.

Qualification (c) requires that a person entering into a contract should not be disqualified by his status, in entering into such contracts. Such persons are an alien enemy, foreign sovereigns, convicts etc. They are disqualified unless they fulfil certain formalities required by law.

Contracts entered by persons not competent to contract are not valid.

IV. **Consideration**: It is referred to as 'quid pro quo' i.e. 'something in return'. A valuable consideration in the sense of law may consist either in some right, interest, profit or benefit accruing to one party, or some forbearance, detriment, loss or responsibility given, suffered or undertaken by the other.

Example 13:- A agrees to sell his books to B for Rs. 100.

B's promise to pay Rs. 100 is the consideration for A's promise to sell his books. A's promise to sell the books is the consideration for B's promise to pay Rs. 100.

V. **Lawful Consideration and Object**: The consideration and object of the agreement must be lawful.

Section 23 states that consideration or object is not lawful if it is prohibited by law, or it is such as would defeat the provisions of law, if it is fraudulent or involves injury to the person or property of another or court regards it as immoral or opposed to public policy.

Example 14: 'A' promises to drop prosecution instituted against 'B' for robbery and 'B' promises to restore the value of the things taken. The agreement is void, as its object is unlawful.

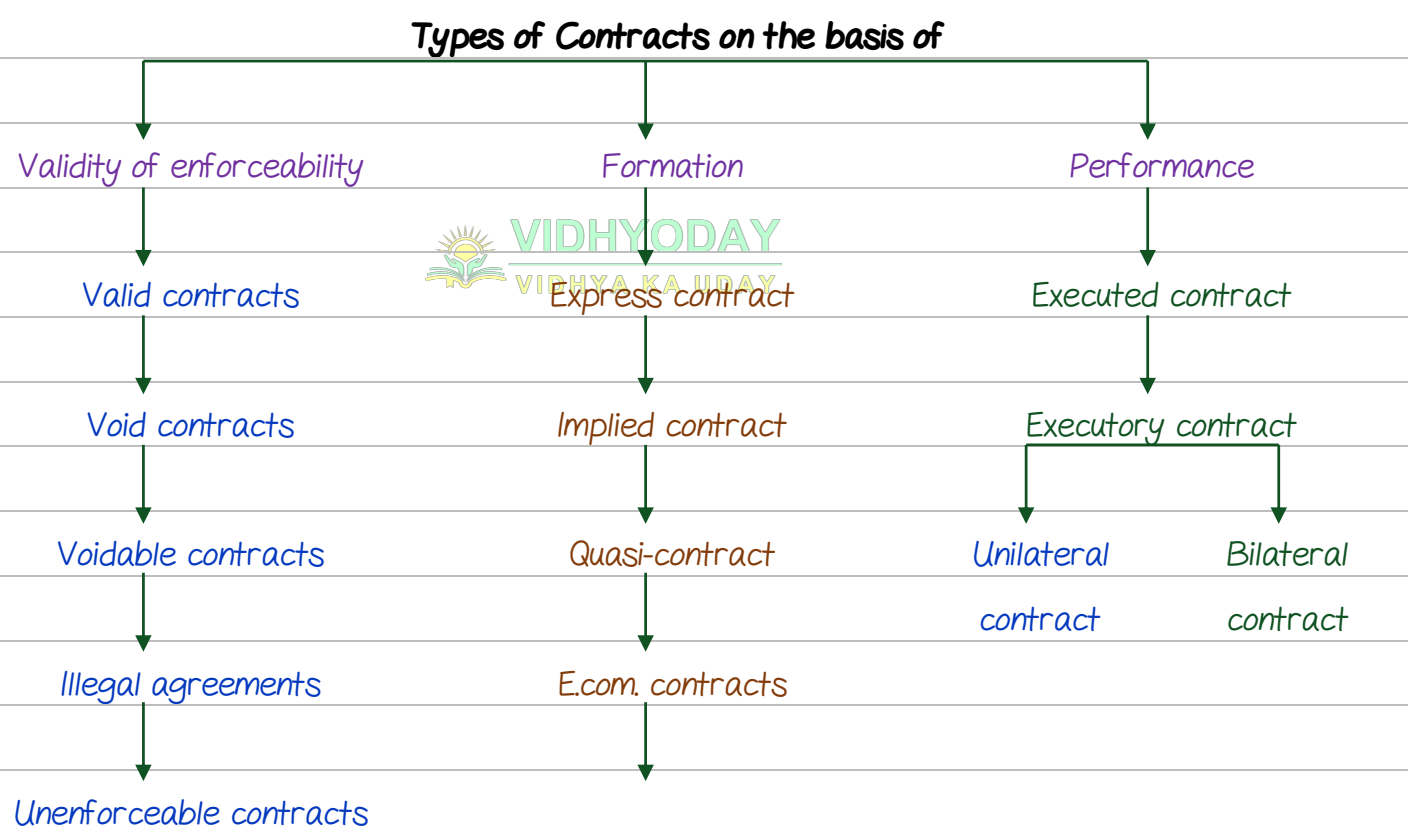
Example 15: A agrees to sell his house to B against 100 kgs of cocaine (drugs). Such agreement is illegal as the consideration is unlawful.

VI. **Not expressly declared to be void**: The agreement entered into must not be which the law declares to be either illegal or void. An illegal agreement is an agreement expressly or impliedly prohibited by law. A void agreement is one without any legal effects.

Example 16: Threat to commit murder or making/publishing defamatory statements or entering into agreements which are opposed to public policy are illegal in nature. Similarly, any agreement in restraint of trade, marriage, legal proceedings, etc. are classic examples of void agreements.

TYPES OF CONTRACT

Now let us discuss various types of contracts.



I. On the basis of the validity

1. **Valid Contract**: An agreement which is binding and enforceable is a valid contract. It contains all the essential elements of a valid contract.

   Example 17: A ask B if he wants to buy his bike for Rs.10,000. B agrees to buy bike. It is agreement which is enforceable by law. Hence, it is a valid contract.

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

Example 18: Mr. X agrees to write a book with a publisher. Such contract is valid. But after few days, X dies in an accident. Here the contract becomes void due to the impossibility of performance of the contract. Thus, a valid contract when cannot be performed because of some uncalled happening becomes void.

Example 19: A contracts with B (owner of the factory) for the supply of 10 tons of sugar, but before the supply is effected, the fire caught in the factory and everything was destroyed. Here the contract becomes void.

It may be added by way of clarification here that when a contract is void, it is not a contract at all but for the purpose of identifying it, it has to be called a [void] contract.

3. **Voidable Contract**: Section 2(i) defines that "an agreement which is enforceable by law at the option of one or more parties thereto, but not at the option of the other or others is a voidable contract".

This in fact means where one of the parties to the agreement is in a position or is legally entitled or authorized to avoid performing his part, then the agreement is treated and becomes voidable. Such a right might arise from the fact that the contract may have been brought about by one of the parties by coercion, undue influence, fraud or misrepresentation and hence the other party has a right to treat it as a voidable contract.

Example 20: X promise to sell his scooter to Y for Rs. 1 Lac. However, the consent of X has been procured by Y at a gun point. X is an aggrieved party and the contract is voidable at his option but not on the option of Y. It means if X accepts the contract, the contract becomes a valid contract then Y has no option of rescinding the contract.

At this juncture it would be desirable to know the distinction between a Void Contract and a Voidable Contract. These are elaborated hereunder:

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.	**Enforceability**	A void contract cannot be enforced at all.	It is enforceable only at the option of aggrieved party and not at the option of other party.
3	**Cause**	A contract becomes void due to change 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.
4	**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.
5	**Rights**	A void contract does not grant any legal remedy to any party.	The party whose consent was not free has the right to rescind the contract within a reasonable time. If so rescinded it becomes a void contract. If it is not rescinded it becomes a valid contract

4. **Illegal Contract**: It is a contract which the law forbids to be made. The court will not enforce such a contract but also the connected contracts. All illegal agreements are void but all void agreements are not necessarily illegal. Despite this, there is similarity between them is that in both cases they are void ab initio and cannot be enforced by law.

Example 21: Contract that is immoral or opposed to public policy are illegal in nature. Similarly, if R agrees with S, to purchase brown sugar, it is an illegal agreement. According to Section 2(g) of the Indian Contract Act, "an agreement not enforceable by law is void". The Act has specified various factors due to which an agreement may be considered as void agreement. One of these factors is unlawfulness of object and consideration of the contract

i.e. illegality of the contract which makes it void. The illegal and void agreement differ from each other in the following respects:

Basis of difference	Void agreement	Illegal agreement
Scope	A void agreement is not necessarily illegal.	An illegal agreement is always void.
Nature	Not forbidden under law.	Are forbidden under law.
Punishment	Parties are not liable for any punishment under the law.	Parties to illegal agreements are liable for punishment
Collateral Agreement	It's not necessary that agreements collateral to void agreements may also be void. It may be valid also.	Agreements collateral to illegal agreements are always void.

5. **Unenforceable Contract**: Where a contract is good in substance but because of some technical defect i.e. absence in writing, barred by limitation etc. one or both the parties cannot sue upon it, it is described as an unenforceable contract.

Example 22: A bought goods from B in 2015. But no payment was made till 2019. B cannot sue A for the payment in 2019 as it has crossed three years and barred by Limitation Act. A good debt becomes unenforceable after the period of three years as barred by Limitation Act.

Communicated

II. On the basis of the formation of contract

1. **Express Contracts**: A contract would be an express contract if the terms are expressed by words or in writing. Section 9 of the Act provides that if a proposal or acceptance of any promise is made in words, the promise is said to be express.

Example 23: A tells B on telephone that he offers to sell his house for Rs. 2 lacs and B in reply informs A that he accepts the offer, this is an express contract.

2. **Implied Contracts**: Implied contracts in contrast come into existence by implication. Most often the implication is by action or conduct of parties or course of dealings between them. Section 9 of the Act contemplates such implied contracts when it lays down that in so far as such proposal or acceptance is made otherwise than in words, the promise is said to be implied.

By conduct

Example 24: Where a coolie in uniform picks up the luggage of A to be carried out of the railway station without being asked by A and A allows him to do so, it is an implied contract and A must pay for the services of the coolie detailed by him.

Example 25: A drinks a coffee in restaurant. There is an implied contract that he should pay for the price of coffee.

Tacit Contracts: The word Tacit means silent. Tacit contracts are those that are inferred through the conduct of parties without any words spoken or written. A classic example of tacit contract would be when cash is withdrawn by a customer of a bank from the automatic teller machine [ATM]. Another example of tacit contract is where a contract is assumed to have been entered when a sale is given effect to at the fall of hammer in an auction sale. It is not a separate form of contract but falls within the scope of implied contracts.

(Auction Sale)

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

Example 26: Obligation of finder of lost goods to return them to the true owner or liability of person to whom money is paid under mistake to repay it back cannot be said to arise out of a contract even in its remotest sense, as there is neither offer and acceptance nor consent. These are said to be quasi-contracts.

4. **E-Contracts**: 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. This helps in doing business transactions using electronic mode. These are known as EDI contracts or Cyber contracts or mouse click contracts.

III. On the basis of the performance of the contract

1. **Executed Contract**: The consideration in a given contract could be an act or for bearance.When the act is done or executed or the forbearance is brought on record, then the contract is an executed contract.

Example 27: When a grocer sells a sugar on cash payment it is an executed contract because both the parties have done what they were to do under the contract.

2. **Executory Contract**: 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.

Example 28: Where G agrees to take the tuition of H, a pre-engineering student, from the next month and H in consideration promises to pay G Rs. 1,000 per month, the contract is executory because it is yet to be carried out.

Unilateral or Bilateral are kinds of Executory Contracts and are not separate kinds.

(a) **Unilateral Contract**: Unilateral contract is a one sided contract in which one party has performed his duty or obligation and the other party's obligation is outstanding.

Example 29: M advertises payment of award of Rs. 5000 to any one who finds his missing boy and brings him. As soon as B traces the boy, there comes into existence an executed contract because B has performed his share of obligation and it remains for M to pay the amount of reward to B. This type of Executory contract is also called unilateral contract.

(b) **Bilateral Contract**: A Bilateral contract is one where the obligation or promise is outstanding on the part of both the parties.

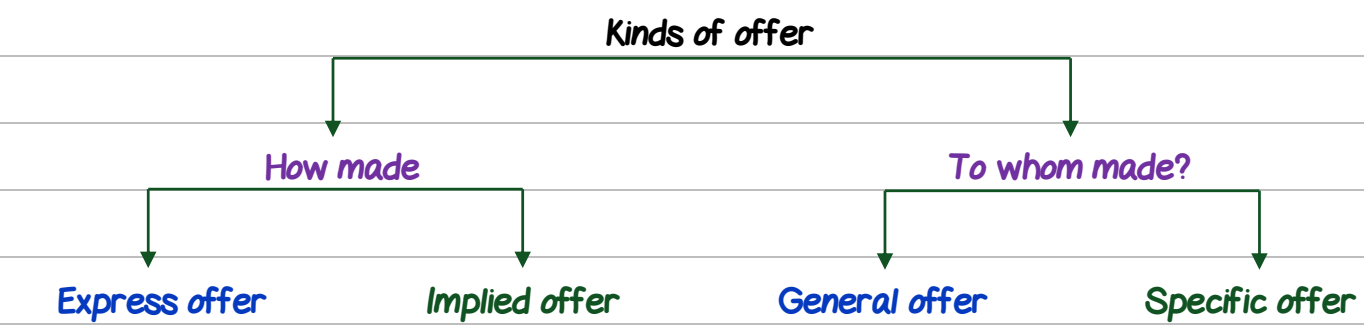
Example 30: A promises to sell his plot to B for Rs.1 lacs cash down, but B pays only Rs. 25,000 as earnest money and promises to pay the balance on next Sunday. On the other hand, A gives the possession of plot to B and promises to execute a sale deed on the receipt of the whole amount. The contract between the A and B is executory because there remains something to be done on both sides. Such Executory contracts are also known as Bilateral contracts.

(Advance Money)

PROPOSAL / OFFER [SECTION 2(a) OF THE INDIAN CONTRACT ACT, 1872]

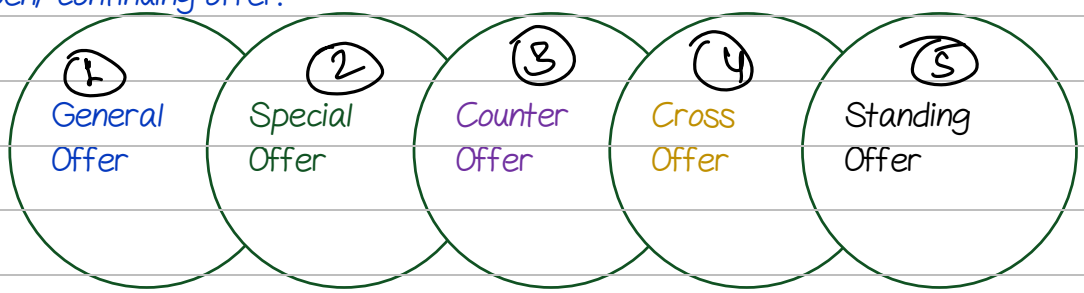
Definition of Offer/Proposal:

According to Section 2(a) of the Indian Contract Act, 1872, "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".



CLASSIFICATION OF OFFER

An offer can be classified as general offer, special/specific offer, cross offer, counter offer, standing/ open/ continuing offer.



Now let us examine each one of them.

(a) **General offer**: It is an offer made to public at large and hence anyone can accept and do the desired act (Carlill v. Carbolic Smoke Ball Co.). In terms of Section 8 of the Act, anyone performing the conditions of the offer can be considered to have accepted the offer. Until the general offer is retracted or withdrawn, it can be accepted by anyone at any time as it is a continuing offer.

Case Law: Carlill Vs. Carbolic Smoke Ball Co. (1893)

Facts: In this famous case, Carbolic Smoke Ball Co. advertised in several newspapers that a reward of £100 would be given to any person who contracted influenza after using the smoke balls produced by the Carbolic Smoke Ball Co. according to printed directions. One lady, Mrs. Carlill, used the smoke balls as per the directions of company and even then, suffered from influenza. Held, she could recover the amount as by using the smoke balls she had accepted the offer.

(b) **Special/specific offer**: When the offer is made to a specific or an ascertained person, it is known as a specific offer. Specific offer can be accepted only by that specified person to whom the offer has been made. [Boulton v. Jones]

Example 36: 'A' offers to sell his car to 'B' at a certain cost. This is a specific offer.

(c) **Cross offer**: When two parties exchange identical offers in ignorance at the time of each other's offer, the offers are called cross offers. There is no binding contract in such a case because offer made by a person cannot be construed as acceptance of the another's offer.

Example 37: If A makes a proposal to B to sell his car for Rs. 2 lacs and B, without knowing the proposal of A, makes an offer to purchase the same car at Rs. 2 lacs from A, it is not an acceptance, as B was not aware of proposal made by A. It is only cross proposal (cross offer). And when two persons make offer to each other, it cannot be treated as mutual acceptance. There is no binding contract in such a case.

(d) **Counter offer**: When the offeree offers to qualified acceptance of the offer subject to modifications and variations in the terms of original offer, he is said to have made a counter offer. Counter-offer amounts to rejection of the original offer. It is also called as Conditional Acceptance.

Example 38: 'A' offers to sell his plot to 'B' for Rs.10 lakhs. 'B' agrees to buy it for Rs. 8 lakhs. It amounts to counter offer. It will result in the termination of the offer of 'A'. If later on 'B' agrees to buy the plot for Rs. 10 lakhs, 'A' may refuse.

(e) **Standing or continuing or open offer**: An offer which is allowed to remain open for acceptance over a period of time is known as standing or continuing or open offer. Tenders that are invited for supply of goods is a kind of standing offer.

Essential of a valid offer

1. **It must be capable of creating legal relations**: Offer must be such as in law is capable of being accepted and giving rise to legal relationship. If the offer does not intend to give rise to legal consequences and creating legal relations, it is not considered as a valid offer in the eye of law. A social invitation, even if it is accepted, does not create legal relations because it is not so intended.

2. **It must be certain, definite and not vague**: If the terms of an offer are vague or indefinite, its acceptance cannot create any contractual relationship. Thus, where A offers to sell B 100 quintals of oil, there is nothing whatever to show what kind of oil was intended. The offer is not capable of being accepted for want of certainty.

3. **It must be communicated to the offeree**: An offer, to be complete, must be communicated to the person to whom it is made, otherwise there can be no acceptance of it. Unless an offer is communicated, there can be no acceptance by it. An acceptance of an offer, in ignorance of the offer, is not acceptance and does not confer any right on the acceptor.
   This can be illustrated by the landmark case of **Lalman Shukla v. GauriDutt**
   Facts: G (Gauridutt) sent his servant L (Lalman) to trace his missing nephew. He then announced that anybody who traced his nephew would be entitled to a certain reward. L traced the boy in ignorance of this announcement. Subsequently when he came to know of the reward, he claimed it. Held, he was not entitled to the reward, as he did not know the offer.

4. **It must be made with a view to obtaining the assent of the other party**: Offer must be made with a view to obtaining the assent of the other party addressed and not merely with a view to disclosing the intention of making an offer.

5. **It may be conditional**: An offer can be made subject to any terms and conditions by the offeror.
   Example 39: Offeror may ask for payment by RTGS, NEFT etc. The offeree will have to accept all the terms of the offer otherwise the contract will be treated as invalid.

6. **Offer should not contain a term the non-compliance of which would amount to acceptance**: Thus, one cannot say that if acceptance is not communicated by a certain time the offer would be considered as accepted.
   Example 40: A proposes B to purchase his android mobile for Rs.5000 and if no reply by him in a week, it would be assumed that B had accepted the proposal. This would not result into contract.

7. **The offer may be either specific or general**: Any offer can be made to either public at large or to the any specific person. (Already explained in the heading types of the offer)

8. **The offer may be express or implied**: An offer may be made either by words or by conduct.

   Example 41: A boy starts cleaning the car as it stops on the traffic signal without being asked to do so, in such circumstances any reasonable man could guess that he expects to be paid for this, here boy makes an implied offer.

9. **Offer is Different from a mere statement of intention,** an invitation to offer, a mere communication of information, a prospectus and Advertisement.

   (i) A statement of intention and announcement.

   Example 42: A father wrote his son about his wish of making him the owner of all his property is mere a statement of intention.

   Example 43: An announcement to give scholarships to children scoring more than 95% in 12^{th} board is not an offer.

   (ii) Offer must be distinguished from an answer to a question.

   Case Law: Harvey vs. Facie [1893] AC 552

   In this case, Privy Council succinctly explained the distinction between an offer and an invitation to offer. In the given case, the plaintiffs through a telegram asked the defendants two questions namely,

   (i) Will you sell us Bumper Hall Pen? and

   (ii) Telegraph lowest cash price.

   The defendants replied through telegram that the "lowest price for Bumper Hall Pen is £ 900". The plaintiffs sent another telegram stating "we agree to buy Bumper Hall Pen at £ 900". However, the defendants refused to sell the property at the price.

   The plaintiffs sued the defendants contending that they had made an offer to sell the property at £ 900 and therefore they are bound by the offer.

   However, the Privy Council did not agree with the plaintiffs on the ground that while plaintiffs had asked two questions, the defendant replied only to the second question by quoting the price but reserved their answer with regard to their willingness to sell. Thus, they made no offer at all. Their Lordships 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.

The above decision was followed in Mac Pherson vs Appanna [1951] A.S.C. 184 where the owner of the property had said that he would not accept less than £ 6000/- for it. This statement did not indicate any offer but indicated only an invitation to offer.

(iii) A statement of price is not an offer: Quoting the price of a product does not constitute it as offer. (refer case of Harvey Vs. Facie as discussed above)

Example 44: The price list of goods does not constitute an offer for sale of certain goods on the listed prices. It is an invitation to offer.

(iv) An invitation to make an offer or do business. In case of "an invitation to make an offer", the person making the invitation does not make an offer rather invites the other party to make an offer. His objective is to send out the invitation that he is willing to deal with any person who, on the basis of such invitation, is ready to enter into contract with him subject to final terms and conditions.

Example 45: An advertisement for sale of goods by auction is an invitation to the offer. It merely invites offers/bids made at the auction.

When goods are sold through auction, the auctioneer does not contract with anyone who attends the sale. The auction is only an advertisement to sell but the items are not put for sale though persons who have come to the auction may have the intention to purchase.

Similar decision was given in the case of Harris vs. Nickerson (1873).

Similarly, Red Herring Prospectus issued by a company, is only an invitation to the public to make an offer to subscribe to the securities of the company.

10. A statement of price is not an offer

What is invitation to offer?

An offer should be distinguished from an invitation to offer. An offer is definite and capable of converting an intention into a contract. Whereas an invitation to an offer is only a circulation of an offer, it is an attempt to induce offers and precedes a definite offer. An invitation to offer is an act precedent to making an offer. Acceptance of an invitation to an offer does not result in the contract and only an offer emerges in the process of negotiation.

When a person advertises that he has stock of books to sell or houses to let, there is no offer to be bound by any contract. Such advertisements are offers to negotiate-offers to receive

offers. In order to ascertain whether a particular statement amounts to an 'offer' or an 'invitation to offer', the test would be intention with which such statement is made. Does the person who made the statement intend to be bound by it as soon as it is accepted by the other or he intends to do some further act, before he becomes bound by it. In the former case, it amounts to an offer and in the latter case, it is an invitation to offer.

Difference between offer and invitation to make an offer:

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

In order to ascertain whether a particular statement amounts to an offer or an invitation to offer, the test would be intention with which such statement is made. The mere statement of the lowest price which the vendor would sell contains no implied contract to sell at that price to the person making the inquiry.

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. Thus, the intention to be bound is important factor to be considered in deciding whether a statement is an 'offer' or 'invitation to offer.'

Following are instances of invitation to offer to buy or sell:

(i) An invitation by a company to the public to subscribe for its shares.

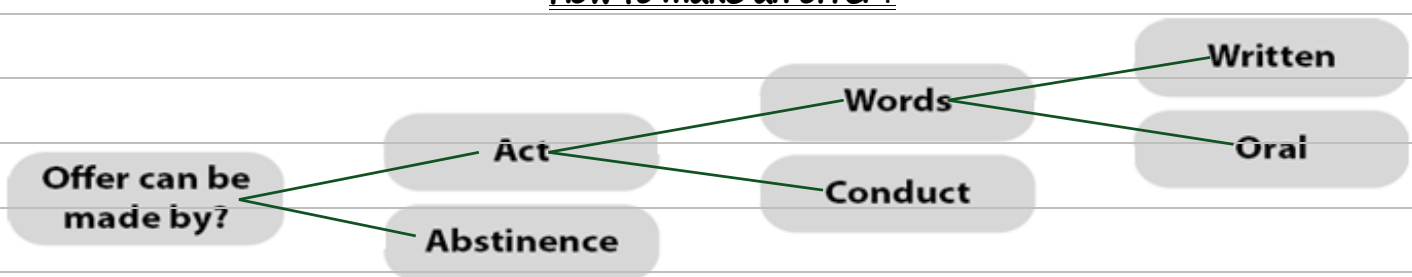
(ii) Display of goods for sale in shop windows.

(iii) Advertising auction sales and

(iv) Quotation of prices sent in reply to a query regarding price.

Basis	Offer	Invitation to offer
Meaning	Section 2(a) of the Act, an offer is the final expression of willingness by the offeror to be bound by the offer should the other party chooses to accept it.	Where a party without expressing his final willingness proposes certain terms on which he is willing to negotiate he does not make an offer, but only invites the other party to make an offer on those terms.
Intention of the parties	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
Sequence	An offer cannot be an act precedent to invitation to offer	An invitation to offer is always an act precedent to offer

How to make an offer?



ACCEPTANCE

Definition of Acceptance: In terms of Section 2(b) of the Act, 'the term acceptance' is defined as follows:

"When the person to whom the proposal is made signifies his assent thereto, proposal is said to be accepted. The proposal, when accepted, becomes a promise".

Legal Rules regarding a valid acceptance

1. **Acceptance can be given only by the person to whom offer is made**: In case of a specific offer, it can be accepted only by the person to whom it is made. [Boulton vs. Jones (1857)]

   Case Law: Boulton vs. Jones (1857)

   Facts: Boulton bought a business from Brocklehurst. Jones, who was Broklehurst's creditor, placed an order with Brocklehurst for the supply of certain goods. Boulton supplied the goods even though the order was not in his name. Jones refused to pay Boultan for the goods because by entering into the contract with Blocklehurst, he intended to set off his debt against Brocklehurst. Held, as the offer was not made to Boulton, therefore, there was no contract between Boulton and Jones.

   In case of a general offer, it can be accepted by any person who has the knowledge of the offer. [Carlill vs. Carbolic Smoke Ball Co. (1893)]

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

   M offered to sell his land to N for £280. N replied purporting to accept the offer but enclosed a cheque for £ 80 only. He promised to pay the balance of £ 200 by monthly instalments of £ 50 each. It was held that N could not enforce his acceptance because it was not an unqualified one. [Neale vs. Merret [1930] W. N. 189].

   A offers to sell his house to B for Rs. 1,00,000/-. B replied that, "I can pay Rs. 80,000 for it. The offer of 'A' is rejected by 'B' as the acceptance is not unqualified. B however changes his mind and is prepared to pay Rs. 1,00,000/-. This is also treated as counter offer and it is upto A whether to accept it or not. [Union of India v. Bahulal AIR 1968 Bombay 294].

   Example 46: 'A' enquires from 'B', "Will you purchase my car for Rs. 2 lakhs?" If 'B' replies "I shall purchase your car for Rs. 2 lakhs, if you buy my motorcycle for Rs. 50000/-, here 'B' cannot be considered to have accepted the proposal. If on the other hand 'B' agrees to purchase the car from 'A' as per his proposal subject to availability of valid Registration

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

3. **The acceptance must be communicated**: To conclude a contract between the parties, the acceptance must be communicated in some perceptible form. Any conditional acceptance or acceptance with varying or too deviant conditions is no acceptance. Such conditional acceptance is a counter proposal and has to be accepted by the proposer, if the original proposal has to materialize into a contract. Further when a proposal is accepted, the offeree must have the knowledge of the offer made to him. If he does not have the knowledge, there can be no acceptance. The acceptance must relate specifically to the offer made. Then only it can materialize into a contract. The above points will be clearer from the following examples:

Brogden vs. Metropolitan Railway Co. (1877)

Facts: B a supplier, sent a draft agreement relating to the supply of coal to the manager of railway Co. viz, Metropolitian railway for his acceptance. The manager wrote the word "Approved" on the same and put the draft agreement in the drawer of the table intending to send it to the company's solicitors for a formal contract to be drawn up. By an oversight the draft agreement remained in drawer. Held, that there was no contract as the manager had not communicated his acceptance to the supplier, B.

Where an offer made by the intended offeree without the knowledge that an offer has been made to him cannot be deemed as an acceptance thereto. (Bhagwandas v. Girdharilal)

A mere variation in the language not involving any difference in substance would not make the acceptance ineffective. [Heyworth vs. Knight [1864] 144 ER 1210].

Example 47: A proposed B to marry him. B informed A's sister that she is ready to marry him. But his sister didn't inform A about the acceptance of proposal. There is no contract as acceptance was not communicated to A.

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

not in the prescribed manner, the proposer is presumed to have consented to the acceptance.

Example 48: If the offeror prescribes acceptance through messenger and offeree sends acceptance by email, there is no acceptance of the offer if the offeror informs the offeree that the acceptance is not according to the mode prescribed. But if the offeror fails to do so, it will be presumed that he has accepted the acceptance and a valid contract will arise.

5. **Time**: Acceptance must be given within the specified time limit, if any, and if no time is stipulated, acceptance must be given within the reasonable time and before the offer lapses. What is reasonable time is nowhere defined in the law and thus would depend on facts and circumstances of the particular case.

Example 49: A offered to sell B 50 kgs of bananas at Rs. 500. B communicated the acceptance after four days. Such is not a valid contract as bananas being perishable items could not stay for a period of week. Four days is not a reasonable time in this case

Example 50: A offers B to sell his house at Rs. 10,00,000. B accepted the offer and communicated to A after 4 days. Held the contract is valid as four days can be considered as reasonable time in case of sell of house.

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

Case Law: Felthouse vs. Bindley (1862)

Facts: F (Uncle) offered to buy his nephew's horse for £30 saying "If I hear no more about it I shall consider the horse mine at £30." The nephew did not reply to F at all. He told his auctioneer, B to keep the particular horse out of sale of his farm stock as he intended to reserve it for his uncle. By mistake the auctioneer sold the horse. F sued him for conversion of his property. Held, F could not succeed as his nephew had not communicated the acceptance to him.

Example 51: 'A' subscribed for the weekly magazine for one year. Even after expiry of his subscription, the magazine company continued to send him magazine for five years. And also 'A' continued to use the magazine but denied to pay the bills sent to him. 'A' would be liable to pay as his continued use of the magazine was his acceptance of the offer.

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

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

Example 52: when a tradesman receives an order from a customer and executes the order by sending the goods, the customer's order for goods constitutes the offer, which has been accepted by the trades man subsequently by sending the goods. It is a case of acceptance by conduct.

Example 53: When a cobbler sits with a brush and polish, a person giving his shoes for polishing constitutes as acceptance by conduct.

COMMUNICATION OF OFFER AND ACCEPTANCE

The importance of 'offer' and 'acceptance' in giving effect to a valid contract was explained in the previous paragraphs. One important common requirement for both 'offer' and 'acceptance' is their effective communication. Effective and proper communication prevents avoidable revocation and misunderstanding between parties.

When the contracting parties are face-to-face, there is no problem of communication because there is instantaneous communication of offer and acceptance. In such a case the question of revocation does not arise since the offer and its acceptance are made instantly.

The difficulty arises when the contracting parties are at a distance from one another and they utilise the services of the post office or telephone or email (internet). In such cases, it is very much relevant for us to know the exact time when the offer or acceptance is made or complete.

The Indian Contract Act, 1872 gives a lot of importance to "time" element in deciding when the offer and acceptance is complete.

Communication of offer: In terms of Section 4 of the Act, "the communication of offer is complete when it comes to the knowledge of the person to whom it is made"

Example 54: Where 'A' makes a proposal to 'B' by post to sell his house for Rs. 5 lakhs and if the letter containing the offer is posted on 10th March and if that letter reaches 'B' on 12th March the offer is said to have been communicated on 12th March when B received the letter.

Thus, it can be summed up that when a proposal is made by post, its communication will be complete when the letter containing the proposal reaches the person to whom it is made.

Mere receiving of the letter is not sufficient, he must receive or read the message contained in the letter.

He receives the letter on 12th March, but he reads it on 15th of March. In this case offer is communicated on 15th of March, and not 12th of March.

Communication of acceptance: There are two issues for discussion and understanding. They are:

The modes of acceptance and when is acceptance complete?

Let us, first consider the modes of acceptance. Section 3 of the Act prescribes in general terms two modes of communication namely, (a) by any act and (b) by omission, intending thereby, to communicate to the other or which has the effect of communicating it to the other.

Communication by act would include any expression of words whether written or oral. Written words will include letters, telegrams, faxes, emails and even advertisements. Oral words will include telephone messages. Again communication would include any conduct intended to communicate like positive acts or signs so that the other person understands what the person 'acting 'or 'making signs' means to say or convey.

Communication of acceptance by 'omission' to do something. Such omission is conveyed by a conduct or by forbearance on the part of one person to convey his willingness or assent. However, silence would not be treated as communication by 'omission'.

Example 55: A offers Rs. 50000 to B if he does not arrive before the court of law as an evidence to the case. B does not arrive on the date of hearing to the court. Here omission of doing an act amounts to acceptance.

Communication of acceptance by conduct. For instance, delivery of goods at a price by a seller to a willing buyer will be understood as a communication by conduct to convey acceptance. Similarly, one need not explain why one boards a public bus or drop a coin in a weighing machine. The first act is a conduct of acceptance against its communication to the offer by the public transport authority to carry any passenger. The second act is again a conduct conveying acceptance to use

the weighing machine kept by the vending company as an offer to render that service for a consideration.

The other issue in communication of acceptance is about the effect of act or omission or conduct. These indirect efforts must result in effectively communicating its acceptance or non acceptance. If it has no such effect, there is no communication regardless of which the acceptor thinks about the offer within himself. Thus, a mere mental unilateral assent in one's own mind would not amount to communication. Where a resolution passed by a bank to sell land to 'A' remained uncommunicated to 'A', it was held that there was no communication and hence no contract. [Central Bank Yeotmal vs Vyankatesh (1949) A. Nag. 286].

Let us now come to the issue of when communication of acceptance is complete. In terms of Section 4 of the Act, it is complete,

post Box

(i) As against the proposer, when it is put in the course of transmission to him so as to be out of the power of the acceptor to withdraw the same;

(ii) As against the acceptor, when it comes to the knowledge of the proposer.

Where a proposal is accepted by a letter sent by the post, the communication of acceptance will be complete as against the proposer when the letter of acceptance is posted and as against the acceptor when the letter reaches the proposer.

For instance in the above example, if 'B' accepts, A's proposal and sends his acceptance by post on 14th, the communication of acceptance as against 'A' is complete on 14th, i.e. when the letter is posted. As against 'B' acceptance will be complete, when the letter reaches 'A'.

Here 'A' the proposer will be bound by B's acceptance, even if the letter of acceptance is delayed in post or lost in transit. The golden rule is proposer becomes bound by the contract, the moment acceptor has posted the letter of acceptance. But it is necessary that the letter is correctly addressed, adequately stamped and duly posted. In such an event the loss of letter in transit, wrong delivery, non delivery etc., will not affect the validity of the contract.

However, from the view point of acceptor, he will be bound by his acceptance only when the letter of acceptance has reached the proposer. So it is crucial in this case that the letter reaches the proposer. If there is no delivery of the letter, the acceptance could be treated as having been completed from the viewpoint of proposer but not from the viewpoint of acceptor. Of course this will give rise to an awkward situation of only one party to the contract, being treated

as bound by the contract though no one would be sure as to where the letter of acceptance had gone.

Acceptance over telephone or telex or fax: When an offer is made of instantaneous communication like telex, telephone, fax or through e-mail, the contract is only complete when the acceptance is received by the offeree, and the contract is made at the place where the acceptance is received (Entores Ltd. v. Miles Far East Corporation). However, in case of a call drops and disturbances in the line, there may not be a valid contract.

Communication of special conditions: Sometimes there are situations where there are contracts with special conditions. These special conditions are conveyed tacitly and the acceptance of these conditions are also conveyed by the offeree again tacitly or without him even realizing it.

Example 56: Where a passenger undertakes a travel, the conditions of travel are printed at the back of the tickets, sometimes these special conditions are brought to the notice of the passenger, sometimes not. In any event, the passenger is treated as having accepted the special condition the moment he bought his ticket.

When someone travels from one place to another by air, it could be seen that special conditions are printed at the back of the air ticket in small letters [in a non-computerized train ticket even these are not printed] Sometimes these conditions are found to have been displayed at the notice board of the Airlines office, which passengers may not have cared to read. The question here is whether these conditions can be considered to have been communicated to the passengers of the Airlines and can the passengers be treated as having accepted the conditions. The answer to the question is in the affirmative and was so held in Mukul Datta vs. Indian Airlines [1962] AIR cal. 314 where the plaintiff had travelled from Delhi to Kolkata by air and the ticket bore conditions in fine print. But such terms and condition should be reasonable.

Example 57: Where a launderer gives his customer a receipt for clothes received for washing. The receipt carries special conditions and are to be treated as having been duly communicated to the customer and therein a tacit acceptance of these conditions is implied by the customer's acceptance of the receipt [Lily White vs. R. Mannuswamy [1966] A. Mad. 13].

CASE LAW: Lilly White vs. Mannuswamy (1970)

Facts: P delivered some clothes to drycleaner for which she received a laundry receipt containing a condition that in case of loss, customer would be entitled to claim 15% of the market price of value of the article, P lost her new saree. Held, the terms were unreasonable and P was entitled to recover full value of the saree from the drycleaner.

In the cases referred above, the respective documents have been accepted without a protest and hence amounted to tacit acceptance.

Standard forms of contracts: It is well established that a standard form of contract may be enforced on another who is subjectively unaware of the contents of the document, provided the party wanting to enforce the contract has given notice which, in the circumstances of a case, is sufficiently reasonable. But the acceptor will not incur any contractual obligation, if the document is so printed and delivered to him in such a state that it does not give reasonable notice on its face that it contains certain special conditions. In this connection, let us consider a converse situation. A transport carrier accepted the goods for transport without any conditions. Subsequently, he issued a circular to the owners of goods limiting his liability for the goods. In such a case, since the special conditions were not communicated prior to the date of contract for transport, these were not binding on the owners of goods [Raipur transport Co. vs. Ghanshyam [1956] A. Nag.145].

COMMUNICATION OF PERFORMANCE

We have already discussed that in terms of Section 4 of the Act, communication of a proposal is complete when it comes to the knowledge of the person to whom it is meant. As regards acceptance of the proposal, the same would be viewed from two angles. These are:

(i) from the viewpoint of proposer and

(ii) the other from the viewpoint of acceptor himself

From the viewpoint of proposer, when the acceptance is put into a course of transmission, when it would be out of the power of acceptor. From the viewpoint of acceptor, it would be complete when it comes to the knowledge of the proposer.

At times the offeree may be required to communicate the performance (or act) by way of

acceptance. In this case it is not enough if the offeree merely performs the act but he should also communicate his performance unless the offer includes a term that a mere performance will constitute acceptance. The position was clearly explained in the famous case of Carlill Vs Carbolic & Smokeball Co. In this case the defendant a sole proprietary concern manufacturing a medicine which was a carbolic ball whose smoke could be inhaled through the nose to cure influenza, cold and other connected ailments issued an advertisement for sale of this medicine. The advertisement also included a reward of $100 to any person who contracted influenza, after using the medicine (which was described as 'carbolic smoke ball'). Mrs. Carlill bought these smoke balls and used them as directed but contracted influenza. It was held that Mrs. Carlill was entitled to a reward of $100 as she had performed the condition for acceptance. Further as the advertisement did not require any communication of compliance of the condition, it was not necessary to communicate the same.

The court thus in the process laid down the following three important principles:

(i) an offer, to be capable of acceptance, must contain a definite promise by the offeror that he would be bound provided the terms specified by him are accepted;

(ii) an offer may be made either to a particular person or to the public at large, and

(iii) if an offer is made in the form of a promise in return for an act, the performance of that act, even without any communication thereof, is to be treated as an acceptance of the offer

REVOCATION OF OFFER AND ACCEPTANCE

If there are specific requirements governing the making of an offer and the acceptance of that offer, we also have specific law governing their revocation.

In term of Section 4, communication of revocation (of the proposal or its acceptance) is complete.

(i) 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 who makes it, and

(ii) as against the person to whom it is made, when it comes to his knowledge.

The above law can be illustrated as follows: If you revoke your proposal made to me by a telegram, the revocation will be complete, as far as you are concerned when you have dispatched the telegram. But as far as I am concerned, it will be complete only when I receive the telegram.

As regards revocation of acceptance, if you go by the above example, I can revoke my acceptance (of your offer) by a telegram. This revocation of acceptance by me will be complete when I dispatch the telegram and against you, it will be complete when it reaches you.

But the important question for consideration is when a proposal can be revoked? And when can an acceptance be revoked? These questions are more important than the question when the revocation (of proposal and acceptance) is complete.

Ordinarily, the offeror can revoke his offer before it is accepted. If he does so, the offeree cannot create a contract by accepting the revoked offer.

Example 58: The bidder at an auction sale may withdraw (revoke) his bid (offer) before it is accepted by the auctioneer by fall of hammer.

An offer may be revoked by the offeror before its acceptance, even though he had originally agreed to hold it open for a definite period of time. So long as it is a mere offer, it can be withdrawn whenever the offeror desires.

Example 59: X offered to sell 50 bales of cotton at a certain price and promised to keep it open for acceptance by Y till 6 pm of that day. Before that time X sold them to Z. Y accepted before 6 p.m., but after the revocation by X. In this case it was held that the offer was already revoked.

In terms of Section 5 of the Act a proposal can be revoked at any time before the communication of its acceptance is complete as against the proposer. An acceptance may be revoked at any time before the communication of acceptance is complete as against the acceptor.

Example 60: A proposes, by a letter sent by post, to sell his house to B. B accepts the proposal by a letter sent by post. A may revoke his proposal at any time before or at the moment when B posts his letter of acceptance, but not afterwards. Whereas B may revoke his acceptance at any time before or at the moment when the letter communicating it reaches A, but not afterwards.

An acceptance to an offer must be made before that offer lapses or is revoked.

The law relating to the revocation of offer is the same in India as in England, but the law relating to the revocation of acceptance is different.

In English law, the moment a person expresses his acceptance of an offer, that moment the contract is concluded, and such an acceptance becomes irrevocable, whether it is made orally or through the post. In Indian law, the position is different as regards contract through post.

Contract through post- As acceptance, in English law, cannot be revoked, so that once the letter

of acceptance is properly posted the contract is concluded. In Indian law, the acceptor or can revoke his acceptance any time before the letter of acceptance reaches the offeror, if the revocation telegram arrives before or at the same time with the letter of acceptance, the revocation is absolute.

Contract over Telephone- A contract can be made over telephone. The rules regarding offer and acceptance as well as their communication by telephone or telex are the same as for the contract made by the mutual meeting of the parties. The contract is formed as soon as the offer is accepted but the offeree must make it sure that his acceptance is received by the offeror, otherwise there will be no contract, as communication of acceptance is not complete. If telephone unexpectedly goes dead during conversation, the acceptor must confirm again that the words of acceptance were duly heard by the offeror.

Revocation of proposal otherwise than by communication: When a proposal is made, the proposer may not wait indefinitely for its acceptance. The offer can be revoked otherwise than by communication or sometimes by lapse.

Modes of revocation of offer

(i) **By notice of revocation**:

Example 61: A offered B to sell goods at Rs. 5,000 through a post but before B could accept the offer A received highest bid for the goods from C. So, A revoked the offer to B by informing B over the telephone and sold goods to C.

(ii) **By lapse of time**: The time for acceptance can lapse if the acceptance is not given within the specified time and where no time is specified, then within a reasonable time. This is for the reason that proposer should not be made to wait indefinitely. It was held in Ramsgate Victoria Hotel Co. Vs Montefiore (1866 L.R.Z. Ex 109), that a person who applied for shares in June was not bound by an allotment made in November. This decision was also followed in India Cooperative Navigation and Trading Co. Ltd. Vs Padamsey Prem Ji. However, these decisions now will have no relevance in the context of allotment of shares since the Companies Act, 2013 has several provisions specifically covering these issues.

(iii) **By non-fulfilment of condition precedent**: **Where the acceptor fails to fulfill a condition** precedent to acceptance the proposal gets revoked. This principle is laid down in Section 6 of

the Act. The offeror for instance may impose certain conditions such as executing a certain document or depositing certain amount as earnest money. Failure to satisfy any condition will result in lapse of the proposal. As stated earlier 'condition precedent' to acceptance prevents an obligation from coming into existence until the condition is satisfied. Suppose where 'A' proposes to sell his house to be 'B' for Rs. 5 lakhs provided 'B' leases his land to 'A'. If 'B' refuses to lease the land, the offer of 'A' is revoked automatically.

(iv) **By death or insanity**: Death or insanity of the proposer would result in automatic revocation of the proposal but only if the fact of death or insanity comes to the knowledge of the acceptor.

(v) By counter offer

(vi) By the non-acceptance of the offer according to the prescribed or usual mode

(vii) By subsequent illegality.

UNIT – 2

CONSIDERATION

WHAT IS CONSIDERATION?

Consideration is the price agreed to be paid by the promisee for the obligation of the promisor. The word consideration was described in a very popular English case of Misa v. Currie as:

"A valuable consideration in the sense of law may consist either in some right, interest, profit or benefit accruing to one party (i.e. promisor) or forbearance, detriment, loss or responsibility given, suffered or undertaken by the other (i.e. the promisee)."

Section 2(d) defines consideration as follows:

"When at the desire of the promisor, the promisee or any other person has done or abstained from doing, or does or abstains from doing or promises to do or abstain from doing something, such an act or abstinence or promise is called consideration for the promise".

LEGAL RULES REGARDING CONSIDERATION

(i) **Consideration must move at the desire of the promisor**: Consideration must be offered by the promisee or the third party at the desire or request of the promisor. This implies "return" element of consideration. Contract of marriage in consideration of promise of settlement is enforceable.

An act done at the desire of a third party is not a consideration.

In Durga Prasad v. Baldeo, D (defendant) promised to pay to P (plaintiff) a certain commission on articles which would be sold through their agency in a market. Market was constructed by P at the desire of the C (Collector), and not at the desire of the D. D was not bound to pay as it was without consideration and hence void.

Example 5: R saves S's goods from fire without being asked to do so. R cannot demand any reward for his services, as the act being done voluntary.

(ii) **Consideration may move from promisee or any other person**: In India, consideration may proceed from the promisee or any other person who is not a party to the contract. The definition of consideration as given in Section 2(d) makes that proposition clear. According to

the definition, when at the desire of the promisor, the promisee or any other person does something such an act is consideration. In other words, there can be a stranger to a consideration but not stranger to a contract.

Example 6: An old lady made a gift of her property to her daughter with a direction to pay a certain sum of money to the maternal uncle by way of annuity. On the same day, the daughter executed a writing in favour of the brother agreeing to pay annuity. The daughter did not, however, pay the annuity and the uncle sued to recover it. It was held that there was sufficient consideration for the uncle to recover the money from the daughter. [Chinnayya vs. Ramayya (1882)]

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

Example 7: A pays Rs. 5,000 to B and B promises to deliver to him a certain quantity of wheat within a month. In this case, A pays the amount, whereas B merely makes a promise. Therefore, the consideration paid by A is executed, whereas the consideration promised by B is executory.

(iv) **Consideration may be past, present or future**: The words "has done or abstained from doing" [as contained in Section 2(d)] are a recognition of the doctrine of past consideration. In order to support a promise, a past consideration must move by a previous request. It is a general principle that consideration is given and accepted in exchange for the promise. The consideration, if past, may be the motive but cannot be the real consideration of a subsequent promise. But in the event of the services being rendered in the past at the request or the desire of the promisor, the subsequent promise is regarded as an admission that the past consideration was not gratuitous.

Example 8: 'A' performed some services to 'B' at his desire. After a week, 'B' promises to compensate 'A' for the work done by him. It is said to be past consideration and A can sue B for recovering the promised money.

Example 9: A cash sale of goods is an example of present consideration. The consideration is immediately made against delivery of goods.

(v) **Consideration need not be adequate**: Consideration need not to be of any particular value. It need not be approximately of equal value with the promise for which it is exchanged but it must be something which the law would regard as having some value. Something in return need not be equal to something given. It can be considered a bad bargain of the party.

It may be noted in this context that Explanation 2 to Section 25 states that an agreement to which the consent of the promisor is freely given is not void merely because the consideration is inadequate.

But as an exception if it 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.

Example 10: X promises to sell a house worth Rs.6 lacs for Rs.1 lacs only, the adequacy of the price in itself shall not render the transaction void, unless the party pleads that transaction takes place under coercion, undue influence or fraud.

Best 'EXAMPLE'

(vi) **Performance of what one is legally bound to perform**: (consideration must not be performance of existing duty) The performance of an act by a person who is legally bound to perform the same cannot be consideration for a contract. Hence, a promise to pay money to a witness is void, for it is without consideration. Hence, such a contract is void for want of consideration. Similarly, an agreement by a client to pay to his counsel after the latter has been engaged, a certain sum over and above the fee, in the event of success of the case would be void, since it is without consideration.

But where a person promises to do more that he is legally bound to do, such a promise provided it is not opposed to public policy, is a good consideration. It should not be vague or uncertain.

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

Examples 11: A man promises to discover treasure by magic, bringing the dead person to live again. This transaction can be said to be void as it is illusory.

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

Example 12: ABC Ltd. promises to give job to Mr. X in a Government bank against payment of Rs. 50,000 is void as the promise is opposed to public policy.

SUIT BY A THIRD PARTY TO A CONTRACT

Though under the Indian Contract Act, 1872, the consideration for an agreement may proceed from a third party, the third party cannot sue on contract. Only a person who is party to a contract can sue on it.

Thus, the concept of stranger to consideration is a valid and is different from stranger to a contract.

Example 13: P who is indebted to Q, sells his property to R and R promises to pay off the debt amount to Q. If R fails to pay, then in such situation Q has no right to sue, as R is a stranger to contract.

The aforesaid rule, that stranger to a contract cannot sue is known as a "doctrine of privity of contract", is however, subject to certain exceptions. In other words, even a stranger to a contract may enforce a claim in the following cases:

1. In the case of trust, a beneficiary can enforce his right under the trust, though he was not a party to the contract between the settler and the trustee.

2. In the case of a family settlement, if the terms of the settlement are reduced into writing, the members of family who originally had not been parties to the settlement may enforce the agreement.

Example 14: Two brothers X and Y agreed to pay an allowance of Rs. 20,000 to mother on partition of joint properties. But later they denied to abide by it. Held their mother although stranger to contract can require their sons for such allowance in the court of law.

3. In the case of certain marriage contracts/arrangements, a provision may be made for the benefit of a person, he may file the suit though he is not a party to the agreement.

   Example 15: Mr. X's wife deserted him for ill-treating her. Mr. X promised his wife's father Mr. Puri that he will treat her properly or else pay her monthly allowance. But she was again ill-treated by her husband. Held, she has all right to sue Mr. X against the contract made between Mr. X and Mr. Puri even though she was stranger to contract.

4. **In the case of assignment of a contract,** when the benefit under a contract has been assigned, the assignee can enforce the contract but such assignment should not involve any personal skill.

5. **Acknowledgement or estoppel** – where the promisor by his conduct acknowledges himself as an agent of the third party, it would result into a binding obligation towards third party.

   Example 16: If L gives to M Rs.20,000 to be given to N, and M informs N that he is holding the money for him, but afterwards M refuses to pay the money. N will be entitled to recover the same from the former
   i.e. M.

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

   Example 17: One owner of the land having two land adjacent to each other. One was agricultural land. He sold the other land containing a condition that it can never be used for Industrial purpose so as to protect the other agricultural land from pollution. Such condition is attached with the land so who so ever is the successor of land has to abide by it. Such are called restrictive covenants and all successor are bind to it.

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

VALIDITY OF AN AGREEMENT WITHOUT CONSIDERATION

The general rule is that an agreement made without consideration is void (Section 25). In every valid contract, consideration is very important. A contract may only be enforceable when consideration is there. However, the Indian Contract Act contains certain exceptions to this rule. In the following cases, the agreement though made without consideration, will be valid and enforceable.

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

   (i) It must be made out of natural love and affection between the parties.

   (ii) Parties must stand in near relationship to each other.

   (iii) It must be in writing.

   (iv) It must also be registered under the law.

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

   Example 18: A husband, by a registered agreement promised to pay his earnings to his wife. Held the agreement though without consideration, was valid.

   Example 19: A out of natural love and affection promises to give his newly wedded daughter- in -law a golden necklace worth Rs. 5,00,000. 'A' made the promise in writing and signed it and registered. The agreement is valid.

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

   (i) The services should have been rendered voluntarily.

   (ii) The services must have been rendered for the promisor.

   (iii) The promisor must be in existence at the time when services were rendered.

   (iv) The promisor must have intended to compensate the promisee.

   Example 20: P finds R's wallet and gives it to him. R promises to give P Rs.10,000. This is a valid contract.

Example 21: Mr. X had helped his nephew Mr. Y to fight a case in the court of law using his knowledge and intellect. After Mr. Y won the case, he promised Mr. X to pay Rs. 10,000. Held, this is a valid contract as it is compensation to past services.

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

   Example 22: A is indebted to C for Rs.60,000 but the debt is barred by the Limitation Act. A sign a written promise now to pay Rs.50,000 in final settlement of the debt. This is a contract without consideration, but enforceable.

4. **Agency**: According to Section 185 of the Indian Contract Act, 1872, no consideration is necessary to create an agency.

5. **Completed gift**: In case of completed gifts, the rule no consideration no contract does not apply. Explanation (1) to Section 25 states "nothing in this section shall affect the validity as between the donor and donee, of any gift actually made." Thus, gifts do not require any consideration.

6. **Bailment**: No consideration is required to affect the contract of bailment. Section 148 of the Indian Contract Act, 1872, defines bailment as the delivery of goods from one person to another for some purpose. This delivery is made upon a contract that post accomplishment of the purpose, the goods will either be returned or disposed of, according to the directions of the person delivering them. No consideration is required to affect a contract of bailment

   Example 23: Mr. A hand over the keys of his godown to Mr. Y as Mr. Y had deposited his goods in the same. Mr. Y gets possession of godown but not the ownership. As soon as Mr. Y lifts his goods from godown he is liable to hand over the keys back to Mr. A.

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

UNIT 3

OTHER ESSENTIAL ELEMTNS OF A CONTRACT

CAPACITY TO CONTRACT

Meaning: Capacity refers to the competence of the parties to make a contract. It is one of the essential elements to form a valid contract.

Who is competent to contract (Section 11)

"Every person is competent to contract who is of the age of majority according to the law to which he is subject, and who is of sound mind and is not disqualified from contracting by any law to which he is subject".

(A) **Age of Majority: In India, the age of majority is regulated by the Indian Majority Act, 1875. Every person domiciled in India shall attain the age of majority on the completion of 18 years of age and not before. The age of majority being 18 years, a person less than that age even by a day would be minor for the purpose of contracting.**

Law relating to Minor's agreement/Position of Minor

1. **A contract made with or by a minor is void ab-initio**: A minor is not competent to contract and any agreement with or by a minor is void from the very beginning.

   In the leading case of Mohori Bibi vs. Dharmo Das Ghose (1903), "A, a minor borrowed Rs. 20,000 from B and as a security for the same executed a mortgage in his favour. He became a major a few months later and filed a suit for the declaration that the mortgage executed by him during his minority was void and should be cancelled. It was held that a mortgage by a minor was void and B was not entitled to repayment of money. Further money lender's request for repayment of amount advanced to the minor as part of consideration for the mortgage was also not accepted.

   It is especially provided in Section 10 that a person who is incompetent to contract cannot make a contract within the meaning of the Act.

2. **No ratification after attaining majority**: A minor cannot ratify the agreement on attaining majority as the original agreement is void ab initio and a void agreement can never be ratified.

   Example 1: X, a minor makes a promissory note in the name of Y. On attaining majority, he cannot ratify it and if he makes a new promissory note in place of old one, here the new promissory note which he executed after attaining majority is also void being without consideration.

3. **Minor can be a beneficiary or can take benefit out of a contract**: Though a minor is not competent to contract, nothing in the Contract Act prevents the minor from making the other party bound to him r. Thus, a promissory note duly executed in favour of a minor is not void and can be sued upon by him, because he though incompetent to contract, may yet accept a benefit.

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

   Example 2: A mortgage was executed in favour of a minor. Held, he can get a decree for the enforcement of the mortgage.

4. **A minor can always plead minority**: A minor can always plead minority and is not stopped to do so even where he has taken any loan or entered into any contract by falsely representing that he was major. Rule of estoppel cannot be applied against a minor. It means he can be allowed to plea his minority in defence.

   Example 3: A, a minor has falsely induced himself as major and contracted with Mr. X for loan of Rs.20,000. When Mr. X asked for the repayment A denied to pay. He pleaded that he was a minor so cannot enter into any contract. Held, A cannot be held liable for repayment of amount. However, if he has not spent the same, he may be asked to repay it but the minor shall not be liable for any amount which he has already spent even though he received the same by fraud. Thus, a minor can always plead minority and is not estopped from doing so even where he had produced a loan or entered into some other

contract by falsely representing that he was of full age, when in reality he was a minor.

5. **Liability for necessaries**: The case of necessaries supplied to a minor or to any other person whom such minor is legally bound to support is governed by section 68 of the Indian Contract Act. A claim for necessaries supplied to a minor is enforceable by law. But a minor is not liable for any price that he may promise and never for more than the value of the necessaries. There is no personal liability of the minor, but only his property is liable.

To render minor's estate liable for necessaries two conditions must be satisfied.

(i) The contract must be for the goods reasonably necessary for his support in the station in life.

(ii) The minor must not have already a sufficient supply of these necessaries.

Necessaries mean those things that are essentially needed by a minor. They cannot include luxuries or costly or unnecessary articles. Necessaries extend to all such things as reasonable persons would supply to an infant in that class of society to which the infant belongs. Expenses on minor's education, on funeral ceremonies come within the scope of the word 'necessaries'.

The whole question turns upon the minor's status in life. Utility rather than ornament is the criterion.

Example 4: Shruti being a minor purchased a laptop for her online classes of Rs.70,000 on credit from a shop. But her assets could pay only Rs.20,000. The shop keeper could not hold Shruti personally liable and could recover only amount recoverable through her assets i.e. upto Rs. 20,000.

6. **Contract by guardian -** how far enforceable: Though a minor's agreement is void, his guardian can, under certain circumstances enter into a valid contract on minor's behalf. Where the guardian makes a contract for the minor, which is within his competence and which is for the benefit of the minor, there will be valid contract which the minor can enforce. But all contracts made by guardian on behalf of a minor are not valid. For instance, the guardian of a minor has no power to bind the minor by a contact for the purchase of

immovable Property. But a contract entered into by a certified guardian (appointed by the Court) of a minor, with the sanction of the court for the sale of the minor's property, may be enforced by either party to the contract.

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

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 shall never be held personally liable.

9. **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.

10. **Minor can be an agent**: A minor can act as an agent. But he will not be liable to his principal for his acts. A minor can draw, deliver and endorse negotiable instruments without himself being liable.

    Example 5: A minor can have an account in the bank. He can draw a cheque for his purchases. But he shall not be liable for cheque bounces nor can he be sued under court of law for any fraud done from his account.

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 necessaries. The parents will be held liable only when the child is acting as an agent for parents.

    Example 6: Richa a minor entered into contract of buying a scooty from the dealer and mentioned that her parents will be liable for the payment of scooty. The dealer sent a letter to her parents for money. The parents will not be liable for such payment as the contract was entered by a minor in their absence and out of their knowledge.

12. **Joint contract by minor and adult**: In such a case, the adult will be liable on the contract and not the minor. In Sain Das vs. Ram Chand, where there was a joint purchase by two purchasers, one of them was a minor, it was held that the vendor could enforce the contract against the major purchaser and not the minor.

13. **Surety for a minor**: In a contract of guarantee when an adult stands surety for a minor then he (adult) is liable to third party as there is direct contract between the surety and the third party.

    Example 7: Mr. X guaranteed for the purchase of a mobile phone by Krish, a minor. In case of failure for payment by Krish, Mr. X will be liable to make the payment.

14. **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 though his lawful guardian become a shareholder by transfer or transmission of fully paid shares to him.

15. **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 borrowed a horse for riding only he was held liable when he lent the horse to one of his friends who jumped and killed the horse. Similarly, a minor was held liable for his failure to return certain instruments which he had hired and then passed on to a friend.

(B) Person of sound mind: According to Section 12 of Indian Contract Act, "a person is said to be of sound mind for the purposes of making a contract if, at the time when he makes it is capable of understanding it and of forming a rational judgement as to its effect upon his interests"

A person who is usually of unsound mind, but occasionally of sound mind, may make a contract when he is of sound mind.

A person who is usually of sound mind, but occasionally of unsound mind, may not make a

contract when he is of unsound mind.

Example 8: A patient in a lunatic asylum, who is at intervals, of sound mind, may contract during those intervals.

Example 9: 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 judgement as to its effect on his interests, cannot contract whilst such delirium or drunkenness lasts.

Position of unsound mind person making a contract: A contract by a person who is not of sound mind is void.

Person who is usually of Unsound Mind but occasionally of Sound Mind may make a Contract when he is of Sound Mind.

⇓

Person who is usually of Unsound Mind but occasionally of Unsound Mind may make a Contract when he is of Unsound Mind.

(C) Contract by disqualified persons:

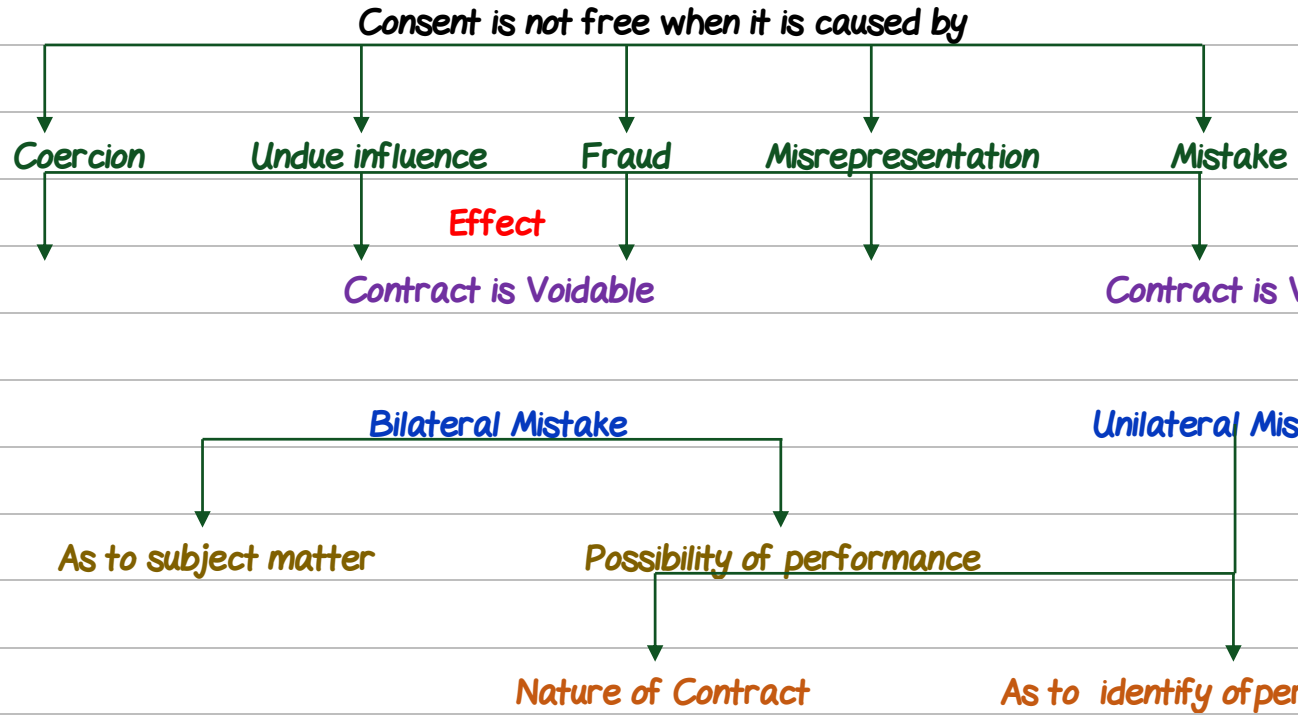
Besides minors and persons of unsound mind, there are also other persons who are disqualified from contracting, partially or wholly, so that the contracts by such person are void.

Incompetency to contract may arise from political status, corporate status, legal status, etc.

The following persons fall in this category:

Foreign Sovereigns and Ambassadors, Alien enemy, Corporations, Convicts, Insolvent etc.

FREE CONSENT



Definition of Consent according to Section 13:

"two or more persons are said to consent when they agree upon the same thing in the same sense."

Parties are said to have consented when they not only agreed upon the same thing but also agreed upon that thing in the same sense. 'Same thing' must be understood as the whole content of the agreement. Consequently, when parties to a contract make some fundamental error as to the nature of the transaction, or as to the person dealt with or as to the subject-matter of the agreement, it cannot be said that they have agreed upon the same thing in the same sense. And if they do not agree in the same sense, there cannot be consent. A contract cannot arise in the absence of consent.

If two persons enter into an apparent contract concerning a particular person or ship, and it turns out that each of them, misled by similarity of name, had a different person or ship in his mind, no contract would exist between them as they were not ad idem, i.e., of the same mind. Again, ambiguity in the terms of an agreement, or an error as to the nature of any transaction or as to the subject-matter of any agreement may prevent the formation of any contract on the ground of absence of consent. In the case of fundamental error, there is really no consent

whereas, in the case of mistake, there is no real consent.

As has been said already, one of the essential elements of a contract is consent and there cannot be a contract without consent. Consent may be free or not free. Only free consent is necessary for the validity of a contract.

Definition of 'Free Consent' (Section 14)

Consent is said to be free when it is not caused by:

1. Coercion, as defined in Section 15; or
2. Undue Influence, as defined in Section 16; or
3. Fraud, as defined in Section 17; or
4. Misrepresentation, as defined in Section 18 or
5. Mistake, subject to the provisions of Sections 20, 21, and 22.

When consent to an agreement is caused by coercion, fraud, misrepresentation, or undue influence, the agreement is a contract voidable at the option of the party whose consent was so caused. When the consent is vitiated by mistake, the contract becomes void.

ELEMENTS VITIATING FREE CONSENT

We shall now explain these elements one by one.

(I) Coercion (Section 15)

"Coercion' is the committing, or threatening to commit, any act forbidden by the Indian Penal Code or the unlawful detaining, or threatening to detain any property, to the prejudice of any person whatever, with the intention of causing any person to enter into an agreement."

Effects of coercion under section 19 of Indian Contract Act, 1872

(i) Contract induced by coercion is voidable at the option of the party whose consent was so obtained.

(ii) As to the consequences of the rescission of voidable contract, the party rescinding a void contract should, if he has received any benefit, thereunder from the other party to the contract, restore such benefit so far as may be applicable, to the person from whom it was received.

(iii) A person to whom money has been paid or anything delivered under coercion must repay or return it. (Section 72)

Example 10: Where husband obtained a release deed from his wife and son under a threat of committing suicide, the transaction was set aside on the ground of coercion, suicide being forbidden by the Indian Penal Code. The threat of suicide amounts to coercion within Section 15.

Example 11: An agent refused to give books of accounts to the principal unless he frees him from all his liabilities. The principal had to give the release deed. Held, the contract was under coercion by unlawful detaining of the principal's property.

(II) Undue influence (Section 16)

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

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

(a) Where he holds a real or apparent authority over the other; or

(b) Where he stands in a fiduciary relationship to the other; or

(c) Where he makes a contract with a person whose mental capacity is temporarily or permanently affected by reason of age, illness or mental or bodily distress for example, an old illiterate person.

Example 12: A having advanced money to his son, B, during his minority, upon B's coming of age obtains, by misuse of parental influence, a bond from B for a greater amount than the sum due in respect of the advance. A employs undue influence.

Example 13: A, a man enfeebled by disease or age, is induced by B's influence over him as his medical attendant, to agree to pay B an unreasonable sum for his professional services. B employs undue influence.

Ex. 14: A, being in debt to B, the money-lender of his village, contracts a fresh loan on terms which appear to be unconscionable. It lies on B to prove that the contract was not induced by undue influence.

Example 15: A applies to a banker for a loan at a time when there is a stringency in money market. The banker declines to make the loan except at an unusually high rate of interest. A accepts the loan on these terms. This is a transaction in the ordinary course of business, and the contract is not induced by undue influence.

Power to set aside contract induced by undue influence- (Section 19A)

When consent to an agreement is caused by undue influence, the agreement is a contract voidable at the option of the party whose consent was so caused.

Any such contract may be set aside either absolutely or, if the party who was entitled to avoid it has received any benefit thereunder, upon such terms and conditions as to the Court may seem just.

Example 22: A, a money lender advances Rs. 1,00,000 to B, an agriculturist, and by undue influence induces B to execute a bond for Rs. 2,00,000 with interest at 6 percent per month. The court may set aside the bond, ordering B to repay Rs. 1,00,000 with such interest as may seem just.

Case study: A student was induced by his teacher to sell his brand-new car to the latter at less than the purchase price to secure more marks in the examination. Accordingly, the car was sold. However, the father of the student persuaded him to sue his teacher. State on what ground the student can sue the teacher?

Yes, the student can sue his teacher on the ground of undue influence under the provisions of Indian Contract Act, 1872. A contract brought as a result of coercion, undue influence, fraud or misrepresentation would be voidable at the option of the person whose consent was caused.

(III) Fraud (Section 17)

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

1. the suggestion, as a fact, of that which is not true, by one who does not believe it to be true;
2. the active concealment of a fact by one having knowledge or belief of the fact;
3. a promise made without any intention of performing it;

4. any other act fitted to deceive;
5. any such act or omission as the law specially declares to be fraudulent.

Explanation to Section 17

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

Example 23: A sell, by auction, to B, a horse which A knows to be unsound, A says nothing to B about the unsoundness of the horse. This is not fraud by A.

Example 24: B is A's daughter and has just come of age. Here, the relation between the parties would make it A's duty to tell B if the horse is unsound.

Example 25: B says to A –"If you do not deny it, I shall assume that the horse is sound". A says nothing. Here A's silence is equivalent to speech.

Example 26: A and B being traders, enter into a contract. A has private information of a change in prices which would affect B's willingness to proceed with the contract. A is not bound to inform B.

Effect of Fraud upon validity of a contract:

When the consent to an agreement in caused by the fraud, the contract is voidable at option of the party defrauded and he has the following remedies:

1. He can rescind the contract within a reasonable time.
2. He can sue for damages.
3. He can insist on the performance of the contract on the condition that he shall be put in the position in which he would have been had the representation made been true.

Mere silence is not fraud

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

Example 27: H sold to W some pigs which were to his knowledge suffering from fever. The pigs were sold 'with all faults' and H did not disclose the fact of fever to W. Held there was no fraud. [Word vs. Hobbs. (1878)].

Example 28: A sells by auction to B, a horse which A knows to be unsound, A says nothing to B about the unsoundness of horse. This is not fraud by A.

Silence is fraud when:

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

   Following contracts come within this category:

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

   Example 29: A broker was asked to buy shares for client. He sold his own shares without disclosing this fact. The client was entitled to avoid the contract or affirm it with a right to claim secret profit made by broker on the transaction since the relationship between the broker and the client was relationship of utmost good faith. (Regier V. Campbell Staurt)

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

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

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

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

2. **Where the silence itself is equivalent to speech**: For example, A says to B "If you do not deny it, I shall assume that the horse is sound." A says nothing. His silence amounts to speech. In case of fraudulent silence, contracts are not voidable if the party whose consent was so obtained had the means of discovering the truth with ordinary diligence

(Exception to section 19)

(IV) Misrepresentation (Section 18)

Misrepresentation means and includes -

1. the positive assertion, in a manner not warranted by the information of the person making it, of that which is not true, though he believes it to be true;
2. any breach of duty which, without an intent to deceive, gains an advantage to the person committing it, or any one claiming under him; by misleading another to his prejudice or to the prejudice of any one claiming under him;
3. causing, however, innocently, a party to an agreement to make a mistake as to the substance of the thing which is the subject of the agreement.

Difference between Coercion and Undue influence

Basis of difference	Coercion	Undue Influence
Nature of action	It involves the physical force or threat. The aggrieved party is compelled to make the contract against its will.	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.
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 Section	The court has the discretion to direct the aggrieved party to return the

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

Legal effects of agreements without free consent - (Section 19)

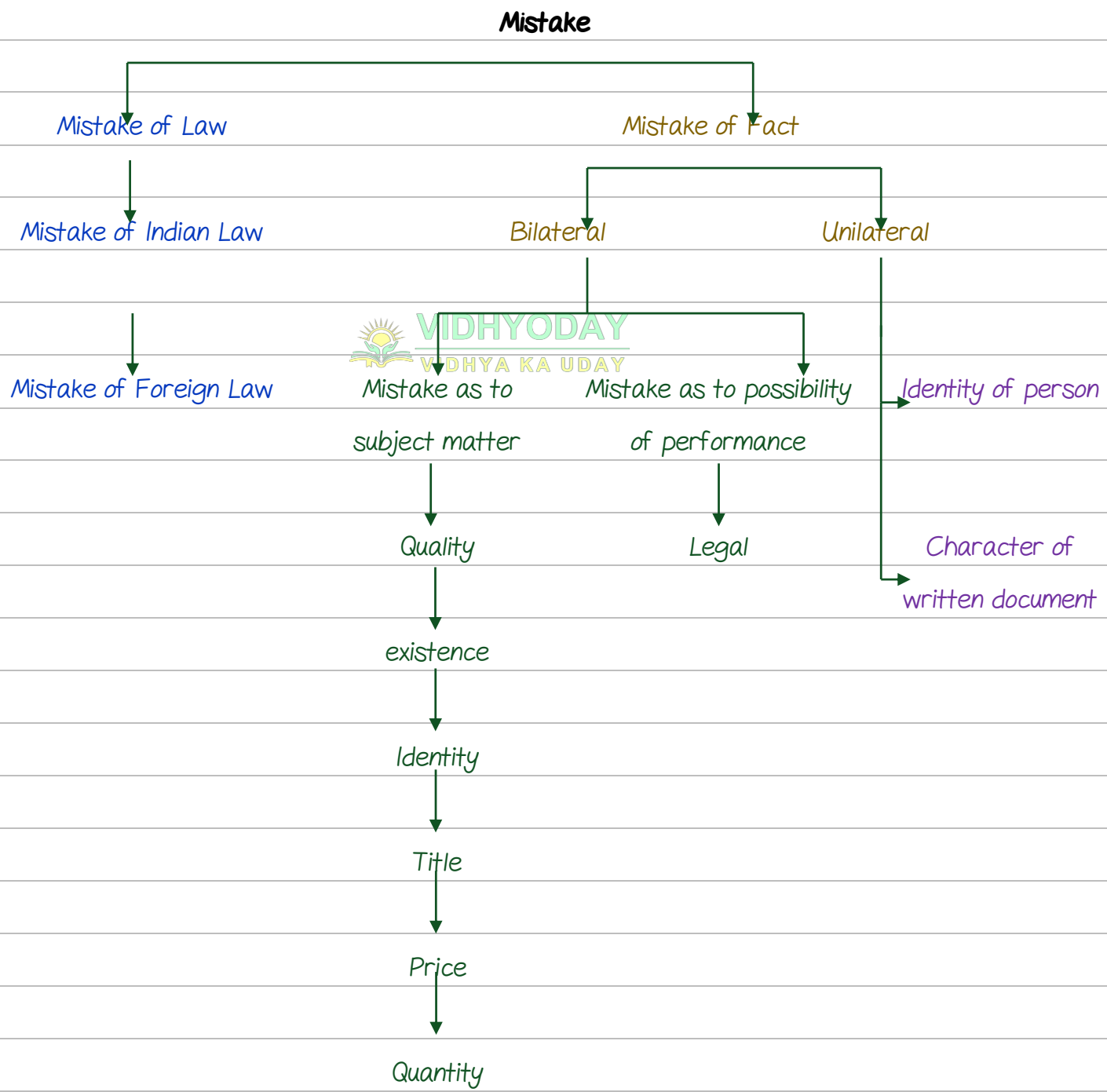
When consent to an agreement is caused by coercion, fraud or misrepresentation, the agreement is a contract voidable at the option of the party whose consent was so caused.

A party to contract, whose consent was so caused by fraud or misrepresentation may, if he thinks fit, insist that the contract shall be performed, and that he shall be put in the position in which he would have been if the representation made had been true.

Exception - If such consent was caused by misrepresentation or by silence, fraudulent within the meaning of section 17, the contract is not voidable, if the party whose consent was so caused had the means of discovering the truth with ordinary diligence.

Explanation to Section 19 - A fraud or misrepresentation which did not cause the consent to a contract of the party on whom such fraud was practiced, or to whom such misrepresentation was made, does not render a contract voidable.

Example 34: A, intending to deceive B, falsely represents that 500 maunds of indigo are made annually at A's factory, and thereby induces B to buy the factory. The contract is voidable at the option of B. This is because when consent to an agreement is caused by coercion, fraud or misrepresentation, the agreement is a contract voidable at the option of the party whose consent was so caused.



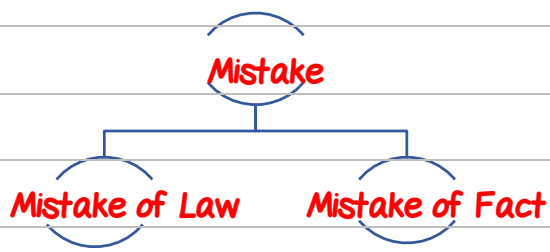
Mistake: Mistake may be defined as innocent or erroneous belief which leads the party to misunderstand the others. Mistake may be either Bilateral or Unilateral.

Bilateral mistake is when both the parties to a contract are under a mistake.

Unilateral mistake is when only one party to the contract is under a mistake.

Effect of mistake on validity of a contract:

Mistake is some unintentional act, omission or error, arising from unconsciousness, ignorance or forgetfulness, imposition or misplaced confidence. It may be of two kinds-



It is essential for the creation of a contract that both the parties should agree to the same thing in the same sense. Thus, if two persons enter into a contract, each of them thinking about a different subject matter, no contract will arise. As a result, a mistake may lead a contract towards voidness. Its effect can be broadly studied as under:

(i) **Mistake of Law**: A mistake of law does not render a contract void as one cannot take excuse of ignorance of the law of his own country. But if the mistake of law is caused through the inducement of another, the contract may be avoided. Mistake of foreign law is excusable and is treated like a mistake of fact. Contract may be avoided on such mistake.

(ii) **Mistake of fact**: Where the contracting parties misunderstood each other and are at cross purposes, there is a bilateral or mutual mistake. Where both the parties to an agreement are under a mistake as to a matter of fact essential to the agreement, the agreement is void.

Example 36: A offers to sell his Ambassador Car to B, who believes that A has only Fiat Car, agrees to buy the car. Here, the two parties are thinking about different subject matter so that there is no real consent and the agreement is void.

LEGALITY OF OBJECT AND CONSIDERATION

Which considerations and objects are lawful, and those which are not (Section 23):

The consideration or object of an agreement is lawful, unless-

1. It is forbidden by law; or
2. Is of such a nature that, if permitted, it would defeat the provisions of any law; or
3. Is fraudulent; or
4. Involves injury to the person or property of another; or
5. The court regards it as immoral; or
6. Opposed to public policy.

In each of these cases, the consideration or object of an agreement is said to be unlawful. Every agreement of which the object or consideration is unlawful is void.

Example 37: A, B and C enter into an agreement for the division among them of gains acquired, or to be acquired, by them by fraud. The agreement is void, as its object, viz., acquisition of gains by fraud is unlawful.

Example 38: A promises to B to abandon a prosecution which he had instituted against B for robbery and B promises in lieu thereof to restore the value of the property robbed. The agreement is void as its object, namely, the stifling of prosecution, is unlawful.

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

The following is an example of the agreement which is void because of unlawful consideration.

Example 39: A promises to obtain for B an employment in the public service and B promises, in return, to pay Rs.1,00,000 to A. The agreement is void. The consideration, being opposed to public policy, is unlawful.

Under Section 23 of the Indian Contract Act, in each of the following cases the consideration or object of an agreement is said to be unlawful:

(i) **When consideration or object is forbidden by law**: Acts forbidden by law are those which are punishable under any statute as well as those prohibited by regulations or orders made in exercise of the authority conferred by the legislature.

Example 40: A licence to cut grass is given to X by the Forest Department under the Forest Act. One of the terms of licence is that the licencee should not assign his interest under the licence without the permission of the Forest Officer, and a fine is prescribed for a breach of this condition. But the observance of the conditions of the licence is not obligatory under the Forest Act. If X in breach of the condition, agrees to assign his interest under the licence to B, that agreement will be valid. Here, the assignment is not prohibited by law, the condition against assignment has been imposed only for administrative purpose or solely for the protection of revenue.

Example 41: A father had arranged for marriage of his 17 years boy and took dowry from the girl's parents. Such marriage contract cannot take place as in India the minimum age for boy marriage is 21 years and dowry is not permissible in Indian law. Such is not a valid contract as the consideration and object both are forbidden by law.

(ii) **When consideration or object defeats the provision of law**: The words 'defeat the provisions of any law' must be taken as limited to defeating the intention which the law has expressed. The court looks at the real intention of the parties to an agreement. If the intention of the parties is to defeat the provisions of law, the court will not enforce it.

Legislative enactment would be defeated by an agreement by a debtor not to plead limitation, as the object is to defeat the provisions of the Limitation Act. The Hindu Law is defeated by an agreement to give son in adoption in consideration of annual allowance to the natural parents.

(iii) **When it is fraudulent**: Agreements which are entered into to promote fraud are void. For example, an agreement for the sale of goods for the purpose of smuggling them out of the country is void and the price of the goods so sold, cannot be recovered.

(iv) **When consideration defeats any rule for the time being in force in India**.

(v) **When consideration involves injury to the person or property of another**: The general term

"injury" means criminal or wrongful harm. In the following examples, the object or consideration is unlawful as it involves injury to the person or property of another.

Example 42: An agreement to print a book in violation of another's copyright is void, as the object is to cause injury to the property of another. It is also void as the object of the agreement is forbidden by the law relating to copyright.

Example 43: A promises to repay his debt by doing manual labour daily for a special period and agrees to pay interest at an exorbitant rate in case of default. Here A's promise to repay by manual labour is the consideration for the loan, and this consideration is illegal as it imposes what, in substance, amounts to slavery on the part of A. In other words, as the consideration involves injury to the person A, the consideration is illegal. Here, the object too is illegal, as it seeks to impose slavery which is opposed to public policy. Hence, the agreement is void.

(vi) **When consideration is immoral**: The following are the examples of agreements where the object or consideration is unlawful, being immoral.

Example 44: Where P had advanced money to D, a married woman to enable her to obtain a divorce from her husband and D had agreed to marry him as soon as she could obtain the divorce, it was held that P was not entitled to recover the amount, since the agreement had for its object the divorce of D from her husband and the promise of marriage given under these circumstances was against good morals.

(vii) **When consideration is opposed to public policy**: The expression 'public policy' can be interpreted either in a wide or in a narrow sense. The freedom to contract may become illusory, unless the scope of 'public policy' is restricted. In the name of public policy, freedom of contract is restricted by law only for the good for the community. In law, public policy covers certain specified topics, e.g., trading with an enemy, stifling of prosecutions, champerty, maintenance, interference with the course of justice, marriage brokerage, sales of public offices, etc. Agreements tending to create interest against duty, agreements tending to create monopolies and agreements not to bid at an auction are also opposed to public policy. An attempt to enlarge the scope of the doctrine is bound to result in the curtailment of individual freedom of contract.

Agreements opposed to public policy

Some of the agreements which are held to be opposed to public policy are-

1. **Trading with enemy**: Any trade with person owing allegiance to a Government at war with India without the licence of the Government of India is void, as the object is opposed to public policy. Here, the agreement to trade offends against the public policy by tending to prejudice the interest of the State in times of war.

   Example 45: India entered in war like situation with China. Mr. A from India entered into contract with China for import of toys. Such contract is void as China is alien enemy of India. The contract if made before such war like situation may be suspended or dissolved. Like India felt apps like tik tok and PUBG will provide some internal information of the country, hence such apps were banned and any contract with them were dissolved.

2. **Stifling Prosecution**: An agreement to stifle prosecution i.e. "an agreement to present proceedings already instituted from running their normal course using force" tends to be a perversion or an abuse of justice; therefore, such an agreement is void. The principle is that one should not make a trade of felony. The compromise of any public offence is generally illegal. Under the Indian Criminal Procedure Code, there is, however, a statutory list of compoundable offences and an agreement to drop proceeding relating to such offences with or without the permission of the Court, as the case may be, in consideration the accused promising to do something for the complainant, is not opposed to public policy. Thus, where A agrees to sell certain land to B in consideration of B abstaining from taking criminal proceeding against A with respect to an offence which is compoundable, the agreement is not opposed to public policy. But, it is otherwise, if the offence is uncompoundable.

3. **Maintenance and Champerty**: Maintenance is an agreement in which a person promises to maintain suit in which he has no interest.

   Example 46: A offer B Rs. 2000, if he sues C for a case which they could have settled mutually under provisions of law, just to annoy C. Such agreement is maintenance agreement. Champerty is an agreement in which a person agrees to assist another in litigation in-

exchange of a promise to hand over a portion of the proceeds of the action.

Example 47: A agrees to pay expenses to B if he sues C and B agrees to pay half of the amount received from result of such suit. This is an agreement of champerty. The agreement for supplying funds by way of Maintenance or Champerty is valid unless

(a) It is unreasonable so as to be unjust to other party or

(b) It is made by a malicious motive like that of gambling in litigation or oppressing other party by encouraging unrighteous suits and not with the bonafide object of assisting a claim believed to be just.

4. **Trafficking relating to Public Offices and titles**: An agreement to trafficking in public office is opposed to public policy, as it interferes with the appointment of a person best qualified for the service of the public. Public policy requires that there should be no money consideration for the appointment to an office in which the public is interested. The following are the examples of agreements that are void; since they are tantamount to sale of public offices.

(1) An agreement to pay money to a public servant in order to induce him to retire from his office so that another person may secure the appointment is void.

(2) An agreement to procure a public recognition like Padma Vibhushan for reward is void.

Example 48: Harish paid Rs. 15000 to the officer to give his son the job in the Forest department of India. On failure by officer he couldn't recover the amount as such contract amounts to trafficking in public office which is opposed to public policy.

5. **Agreements tending to create monopolies**: Agreements having for their object the establishment of monopolies are opposed to public policy and therefore void.

Example 49: XYZ and ABC were only the manufactures of oxygen cylinders in West Bengal. They both entered into contract of supplying the same at very high rates and enjoy the monopoly rates during the covid period in the country. Such contract is opposed to public policy as they intended to create monopolies.

6. **Marriage brokerage agreements**: An agreement to negotiate marriage for reward, which is known as a marriage brokerage contract, is void, as it is opposed to public policy. For instance, an agreement to pay money to a person hired to procure a wife is opposed to public policy and therefore void.

   Note: Marriage bureau only provides information and doesn't negotiate marriage for reward, therefore, it is not covered under this point.

7. **Interference with the course of justice**: An agreement whose object is to induce any judicial officer of the State to act partially or corruptly is void, as it is opposed to public policy; so also is an agreement by A to reward B, who is an intended witness in a suit against A in consideration of B's absenting himself from the trial. For the same reasons, an agreement which contemplates the use of under-hand means to influence legislation is void.

8. **Interest against obligation**: The following are examples of agreement that are void as they tend to create an interest against obligation. The object of such agreements is opposed to public policy.

   (1) An agreement by an agent to receive without his principal's consent compensation from another for the performance of his agency is invalid.

   (2) A, who is the manager of a firm, agrees to pass a contract to X if X pays to A Rs.200,000 privately; the agreement is void.

9. **Consideration Unlawful in Part**: By virtue of Section 24, if any part of a single consideration for one or more objects, or any one or any part of any one of several considerations for a single object, is unlawful, the agreement is void."

   This section is an obvious consequence of the general principle of Section 23. There is no promise for a lawful consideration if there is anything illegal in a consideration which must be taken as a whole. The general rule is that where the legal part of a contract can be severed from the illegal part, the bad part may be rejected and the good one can be retained. But where the illegal part cannot be severed, the contract is altogether void.

VOID AGREEMENTS

Expressly declared Void Agreements

- ✓ Made by incompetent parties (Section 11)
- ✓ Agreements made under Bilateral mistake of fact (Section 20)
- ✓ Agreements the consideration or object of which is unlawful (Section 23)
- ✓ Agreement the consideration or object of which is unlawful in parts (Section 24)
- ✓ Agreements made without consideration (Section 25)
- ✓ Agreement in restraint of marriage (Section 26)
- ✓ Agreements in restraint of trade (Section 27)
- ✓ Agreement in restraint of legal proceedings (Section 28)
- ✓ Agreement the meaning of which is uncertain (Section 29)
- ✓ Wagering Agreement (Section 30)
- ✓ Agreements to do impossible Acts (Section 56)

1. **Agreement in restraint of marriage (Section 26)**: Every agreement in restraint of marriage of any person other than a minor, is void. So, if a person, being a major, agrees for good consideration not to marry, the promise is not binding and considered as void agreement.

2. **Agreement in restraint of trade (Section 27)**: An agreement by which any person is restrained from exercising a lawful profession, trade or business of any kind, is to that extent void. But this rule is subject to the following exceptions, namely, where a person sells the goodwill of a business and agrees with the buyer to refrain from carrying on a similar business, within specified local limits, so long as the buyer or his successor in interest carries on a like business therein, such an agreement is valid (goodwill is the advantage enjoyed by a business on account of public patronage and encouragement from habitual customers). The local limits within which the seller of the goodwill agrees not to carry on similar business must be reasonable. Under Section 36 of the Indian Partnership Act, 1932 if an outgoing partner makes an agreement with the continuing partners that he will not carry on any business similar to that of the firm within a specified period or within specified local limits, such an

agreement, thought in restraint of trade, will be valid, if the restrictions imposed are reasonable. Similarly, under Section 11 of that Act an agreement between partners not to carry on competing business during the continuance of partnership is valid.

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

Example 50: B, a physician and surgeon, employs A as an assistant for a term of three years and A agrees not to practice as a surgeon and physician during these three years. The agreement is valid and A can be restrained by an injunction if he starts independent practice during this period.

Example 51: An agreement by a manufacturer to sell during a certain period his entire production to a wholesale merchant is not in restraint of trade.

Example 52: Agreement among the sellers of a particular commodity not to sell the commodity for less than a fixed price is not an agreement in restraint of trade.

Exception to Rule that an Agreement in Restraint of Trade is Void

- Statutory Provision
  - sale of Goodwill
  - Indian Partnership Act, 1932
  - LLP Act, 2008
- Judicial Interpretations
  - Trade Combinations
  - Service Agreements
  - Sole or Exclusive Dealing Agreements and Franchise

3. **Agreement in restraint of legal proceedings (Section 28)**: An agreement in restraint of legal proceeding is the one by which any party thereto is restricted absolutely from enforcing his rights under a contract through a Court or which abridges the usual period for starting legal proceedings. A contract of this nature is void.

However, there are certain exceptions to the above rule:

(i) A contract by which the parties agree that any dispute between them in respect of any subject shall be referred to arbitration and that only the amount awarded in such arbitration shall be recoverable is a valid contract.

(ii) Similarly, a contract by which the parties agree to refer to arbitration any question between them which has already arisen or which may arise in future, is valid; but such a contract must be in writing.

4. **Agreement -** the meaning of which is uncertain (Section 29): An agreement, the meaning of which is not certain, is void, but where the meaning thereof is capable of being made certain, the agreement is valid.

Example 53: A agrees to sell B "a hundred tons of oil". There is nothing whatever to show what kind of oil was intended. The agreement is void for uncertainty. But the agreement would be valid if A was dealer only in coconut oil; because in such a case its meaning would be capable of being made certain.

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

Example 54: A agrees to pay Rs. 50,000 to B if it rains, and B promises to pay a like amount to A if it does not rain, the agreement will be by way of wager. But if one of the parties has control over the event, agreement is not a wager.

Essentials of a Wager

(1) There must be a promise to pay money or money's worth.

(2) Promise must be conditional on an event happening or not happening.

(3) There must be uncertainty of event.

(4) There must be two parties, each party must stand to win or lose.

(5) There must be common intention to bet at the timing of making such agreement.

(6) Parties should have no interest in the event except for stake.

Transactions similar to Wager (Gambling)

(i) **Lottery transactions**: A lottery is a game of chance and not of skill or knowledge. Where the prime motive of participant is gambling, the transaction amounts to a wager. Even if the lottery is sanctioned by the Government of India it is a wagering transaction. The only effect of such sanction is that the person responsible for running the lottery will not be punished under the Indian Penal Code. Lotteries are illegal and even collateral transactions to it are tainted with illegality (Section 294A of Indian Penal Code).

(ii) **Crossword Puzzles and Competitions**: Crossword puzzles in which prizes depend upon the correspondence of the competitor's solution with a previously prepared solution kept with the editor of a newspaper is a lottery and therefore, a wagering transaction.

Case Law: State of Bombay vs. R.M.D. Chamarbangwala AIR (1957)

Facts: A crossword puzzle was given in magazine. Abovementioned clause was stated in the magazine. A solved his crossword puzzle and his solution corresponded with previously prepared solution kept with the editor. Held, this was a game of chance and therefore a lottery (wagering transaction).

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 competitions are valid. According to the Prize Competition Act, 1955 prize competitions in games of skill are not wagers provided the prize money does not exceed Rs. 1,000.

(iii) **Speculative transactions**: an agreement or a share market transaction where the parties intend to settle the difference between the contract price and the market price of certain goods or shares on a specified day, is a gambling and hence void.

(iv) **Horse Race Transactions**: A horse race competition where prize payable to the bet winner is less than Rs. 500, is a wager.

Example 55: A and B enter into an agreement in which A promises to pay Rs. 2,00,000 provided 'Chetak' wins the horse race competition. This is not a wagering transaction.

However, Section 30 is not applicable in an agreement to contribute toward plate, prize or sum of money of the value of Rs. 500 or above to be awarded to the winner of a horse race.

Transactions resembling with wagering transaction but are not void

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

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

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

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

Distinction between Contract of Insurance and Wagering Agreement

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	There is no consideration between the two parties. There is just

	and compensation amount).	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 of Indemnity	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.

UNIT 4

PERFORMANCE OF CONTRACT

OBLIGATIONS OF PARTIES TO CONTRACTS (SECTION 37)

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

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

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

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

Actual Performance: Where a party to a contract has done what he had undertaken to do or either of the parties have fulfilled their obligations under the contract within the time and in the manner prescribed.

Example 3: X borrows Rs. 5,00,000 from Y with a promise to be paid after 1 month. X repays the amount on the due date. This is actual performance.

Offer to perform or attempted performance or tender of performance: It may happen sometimes, when the performance becomes due, the promisor offers to perform his obligation but the promisee refuses to accept the performance.

EFFECT OF REFUSAL TO ACCEPT OFFER OF PERFORMANCE (SECTION 38)

According to Section 38 of the Act - where a promisor has made an offer of performance to the promisee, and the offer has not been accepted, then the promisor is not responsible for non performance, nor does he thereby lose his rights under the contract.

Every such offer must fulfill certain conditions which are as follows, namely:

(i) it must be unconditional;

(ii) it must be made at a proper time and place, and under such circumstances that the person to whom it is made may have a reasonable opportunity of ascertaining that the person by whom it is made is able and willing there and then to do the whole of what he is bound by his promise to do;

(iii) if the offer is an offer to deliver anything to the promisee, then the promisee must have a reasonable opportunity of seeing that the thing offered is the thing which the promisor is bound by his promise to deliver.

An offer to one of several joint promisees has the same legal consequences as an offer to all of them.

Example 4: P promises to deliver certain goods to R. P takes the goods to the appointed place during business hours but R refuses to take the delivery of goods. This is an attempted performance as P the promisor has done what he was required to do under the contract.

EFFECT OF REFUSAL OF PARTY TO PERFORM WHOLLY (SECTION 39)

Section 39 provides that when a party to a contract has refused to perform or disabled himself from performing his promise in its entirety the promisee may put an end to the contract unless he had signified, by words or conduct his acquiescence in its continuance.

Example 5: X, a singer enters into a contract with Y, the manager of a theatre to sing at his theatres two nights in every week during the next two months, and Y engaged to pay her Rs. 10,000 for each night's performance. On the sixth night, X willfully absents herself from the theatre. Y is at liberty to put an end to the contract.

BY WHOM A CONTRACT MAY BE PERFORMED (SECTION 40, 41 AND 42)

Person by whom promise is to be performed- Section 40

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. In other cases, the promisor or his representatives may employ a competent person to perform it.

Example 6: A promises to pay B a sum of money. A may perform this promise, either by personally paying the money to B, or by causing it to be paid to B by another; and if A dies before the time appointed for payment, his representatives must perform the promise, or employ some proper person to do so.

Example 7: A promises to paint a picture for B and this must be performed by the promisor himself.

DISTINCTION BETWEEN SUCCESSION AND ASSIGNMENT

Distinction between two legal concepts, viz, succession and assignment may be noted carefully. When the benefits of a contract are succeeded to by process of law, then both burden and benefits attaching to the contract, may sometimes devolve on the legal heir. Suppose, a son succeeds to the estate of his father after his death, he will be liable to pay the debts and liabilities of his father owed during his life-time. But if the debts owed by his father exceed the value of the estate inherited by the son then he would not be called upon to pay the excess. In other words, the liability of the son will be limited to the extent of the property inherited by him. In the matter of assignment, however the benefit of a contract can only be assigned but not the liabilities thereunder. This is because when liability is assigned, a third party gets involved therein. Thus, a debtor cannot relieve himself of his liability to creditor by assigning to someone else his obligation to repay the debt.

On the other hand, if a creditor assigns the benefit of a promise, he thereby entitles the assignee to realise the debt from the debtor but where the benefit is coupled with a liability or when a personal consideration has entered into the making of the contract then the benefit cannot be assigned.

LIABILITY OF JOINT PROMISOR & PROMISEE

Devolution of joint liabilities (Section 42)

When two or more persons have made a joint promise, then, unless a contrary intention appears by the contract, all such persons, during their joint lives, and, after the death of any of them, his representative jointly with the survivor or survivors, and, after the death of last survivor, the representatives of all jointly, must fulfil the promise.

Example 13: X, Y and Z who had jointly borrowed money must, during their life-time jointly repay the debt. Upon the death of X his representative, say, S along with Y and Z should jointly repay the debt and so on. If in an accident all the borrowers X, Y and Z dies then their legal representatives must fulfil the promise and repay the borrowed amount. This rule is applicable only if the contract reveals no contrary intention.

We have seen that Section 42 deals with voluntary discharge of obligations by joint promisors. But if they do not discharge their obligation on their own volition, what will happen? This is what Section 43 resolves.

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

When two or more persons make a joint promise, the promisee may, in the absence of express agreement to the contrary, compel any one or more of such joint promisors to perform the whole of the promise.

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

In other words, if one of the joint promisors is made to perform the whole contract, he can call for a contribution from others.

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

Explanation to Section 43

Nothing in this section shall prevent a surety from recovering, from his principal, payments made

by the surety on behalf of the principal, or entitle the principal to recover anything from the surety on account of payment made by the principal.

Example 14: A, B and C jointly promise to pay D Rs. 3,00,000. D may compel either A or B or C to pay him Rs. 3,00,000.

Example 15: A, B and C are under a joint promise to pay D Rs. 3,00,000. C is unable to pay anything A is compelled to pay the whole. A is entitled to receive Rs. 1,50,000 from B.

Example 16: X, Y and Z jointly promise to pay Rs. 6,000 to A. A may compel either X or Y or Z to pay the amount. If Z is compelled to pay the whole amount; X is insolvent but his assets are sufficient to pay one-half of his debts. Z is entitled to receive Rs. 1,000 from X's estate and Rs. 2,500 from Y.We thus observe that the effect of Section 43 is to make the liability in the event of a joint contract, both joint & several, in so far as the promisee may, in the absence of a contract to the contrary, compel anyone or more of the joint promisors to perform the whole of the promise.

Effect of release of one joint promisor- Section 44

The effect of release of one of the joint promisors is dealt with in Section 44 which is stated below:

Where two or more persons have made a joint promise, a release of one of such joint promisors by the promisee does not discharge the other joint promisor or joint promisors, neither does it free the joint promisors so released from responsibility to the other joint promisor or promisors.

Example 17: 'A', 'B' and 'C' jointly promised to pay Rs. 9,00,000 to 'D'. 'D' released 'A' from liability. In this case, the release of 'A' does not discharge 'B' and 'C' from their liability. They remain liable to pay the entire amount of Rs. 9,00,000 to 'D'. And though 'A' is not liable to pay to 'D', but he remains liable to pay to 'B' and 'C' i.e. he is liable to make the contribution to the other joint promisors.

Rights of Joint Promisees

The law relating to Devolution of joint rights is contained in Section 45 which is reproduced below:

"When a person has made a promise to two or more persons jointly, then unless a contrary

intention appears from the contract, the right to claim performance rests, as between him and them, with them during their joint lives, and after the death of any of them, with the representative of such deceased person jointly with the survivor or survivors, and after the death of the last survivor, with the representatives of all jointly".

Example 18: A, in consideration of Rs. 5,00,000 rupees lent to him by B and C, promises B and C jointly to repay them that sum with interest on a specified day but B dies. In such a case right to demand payment shall rest with B's legal representatives, jointly with C during C's life-time, and after the death of C, with the legal representatives of B and C jointly.

TIME AND PLACE FOR PERFORMANCE OF THE PROMISE

The law on the subject is contained in Sections 46 to 50 explained below:

(i) **Time for performance of promise, where no application is to be made and no time is specified - Section 46**

Where, by the contract, a promisor is to perform his promise without application by the promisee, and no time for performance is specified, the engagement must be performed within a reasonable time.

Explanation to Section 46 - The expression reasonable time is to be interpreted having regard to the facts and circumstances of a particular case.

(ii) **Time and place for performance of promise, where time is specified and no application to be made - Section 47**

When a promise is to be performed on a certain day, and the promisor has undertaken to perform it without application by the promise, the promisor may perform it at any time during the usual hours of business, on such day and the place at which the promise ought to be performed.

Example 19: If the delivery of goods is offered say after 8.30 pm, the promisee may refuse to accept delivery, for the usual business hours are over. Moreover, the delivery must be made at the usual place of business.

(iii) **Application for performance on certain day to be at proper time and place - Section 48**

When a promise is to be performed on a certain day, and the promisor has not undertaken to perform it without application by the promisee, it is the duty of the promisee to apply for performance at a proper place and within the usual hours of business.

Explanation to Section 48 states that the question "what is a proper time and place" is, in each particular case, a question of fact.

(iv) **Place for the performance of promise, where no application to be made and no place fixed for performance - Section 49**

When a promise is to be performed without application by the promisee, and no place is fixed for the performance of it, it is the duty of the promisor to apply to the promisee to appoint a reasonable place for the performance of the promise, and to perform it at such a place.

Example 20: A undertakes to deliver a thousand maunds of jute to B on a fixed day. A must apply to B to appoint a reasonable place for the purpose of receiving it, and must deliver it to him at such place.

(v) **Performance in manner or at time prescribed or sanctioned by promisee - Section 50**

The performance of any promise may be made in any such manner, or at any time which the promisee prescribes or sanctions.

PERFORMANCE OF RECIPROCAL PROMISE

The law on the subject is contained in Sections 51 to 58. The provisions thereof are summarized below:

(i) **Promisor not bound to perform, unless reciprocal promise ready and willing to perform- Section 51**

When a contract consists of reciprocal promises to be simultaneously performed, no promisor needs to perform his promise unless the promisee is ready and willing to perform his reciprocal promise.

Example 21: A and B contract that A shall deliver the goods to B to be paid for by B on

delivery. A need not deliver the goods, unless B is ready and willing to pay for the goods on delivery.

(ii) Order of performance of reciprocal promises- Section 52

When the order of performance of the reciprocal promises is expressly fixed by the contract, they shall be performed in that order; and where the order is not expressly fixed by the contract, they shall be performed in that order which the nature of the transaction requires.

Example 22: A and B contract that A shall build a house for B at a fixed price. A's promise to build the house must be performed before B's promise to pay for it.

(iii) Liability of party preventing event on which the contract is to take effect - Section 53

When a contract contains reciprocal promises, and one party to the contract prevents the other from performing his promise, the contract becomes voidable at the option of the party so prevented; and he is entitled to compensation from the other party for any loss he may sustain in consequence of the non- performance of the contract.

Example 23: A and B contract that B shall execute some work for A for a thousand rupees. B is ready and willing to execute the work accordingly, but A prevents him from doing so. The contract is 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.

Example 24: In a contract for the sale of standing timber, the seller is to cut and cord it, whereupon buyer is to take it away and pay for it. The seller cords only a part of the timber and neglects to cord the rest. In that event the buyer may avoid the contract and claim compensation from the seller for any loss which he may have sustained for the non-performance of the contract.

(iv) Effect of default as to that promise which should be first performed, in contract consisting of reciprocal promises (Section 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.

(v) Effects of Failure to Perform at a Time Fixed in a Contract in which Time is Essential (Section 55)

The law on the subject is contained in Section 55 which is reproduced below:

"When a party to a contract promises to do certain thing at or before the specified time, and fails to do any such thing at or before the specified time, the contract, or so much of it as has not been performed, becomes voidable at the option of the promisee, if the intention of the parties was that time should be of essence of the contract".

Effect of such failure when time is not essential

If it was not the intention of the parties that time should be of essence of the contract, the contract does not become voidable by the failure to do such thing at or before the specified time; but the promisee is entitled to compensation from the promisor for any loss occasioned to him by such failure.

Effect of acceptance of performance at time other than agreed upon -

If, in case of a contract voidable on account of the promisor's failure to perform his promise at the time agreed, the promisee accepts performance of such promise at any time other than agreed, the promisee cannot claim compensation for any loss occasioned by the non-performance of the promise at the time agreed, unless, at the time of acceptance, he gives notice to the promisor of his intention to do so.

(vi) Agreement to do Impossible Act

Section 56 contemplates various circumstances under which agreement may be void, since it is impossible to carry it out. The Section is reproduced below:

"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.

Example 27: A agrees with B to discover treasure by magic. The agreement is void.

(vii) Reciprocal promise to do certain things that are legal, and also some other things that are illegal- Section 57-

Where persons reciprocally promise, first to do certain things which are legal and secondly, under specified circumstances, to do certain other things which are illegal, the first set of promises is a valid contract, but the second is a void agreement.

Example 32: A and B agree that A will sell a house to B for Rs. 500,000 and also that if B uses it as a gambling house, he will pay a further sum of Rs. 750,000. The first set of reciprocal promises, i.e. to sell the house and to pay Rs. 500,000 for it, constitutes a valid contract. But the object of the second, being unlawful, is void.

(viii) 'Alternative promise' one branch being illegal- Section 58

The law on this point is contained in Section 58 which says that "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 33: A and B agree that A shall pay B Rs. 1,00,000, for which B shall afterwards deliver to A either rice or smuggled opium.

This is a valid contract to deliver rice, and a void agreement as to the opium.

APPROPRIATION OF PAYMENTS

Sometimes, a debtor owes several debts to the same creditor and makes payment, which is not sufficient to discharge all the debts. In such cases, the payment is appropriated (i.e. adjusted against the debts) as per Section 59 to 61 of the Indian Contract Act.

(i) **Application of payment where debt to be discharged is indicated (Section 59):** Where a debtor, owing several distinct debts to one person, makes a payment to him either with express intimation or under circumstances implying that the payment is to be applied to the discharge of some particular debt, the payment, if accepted, must be applied accordingly.

(ii) **Application of payment where debt to be discharged is not indicated (Section 60):** Where the debtor has omitted to intimate and there are no other circumstances indicating to which debt the payment is to be applied the creditor may apply it at his discretion to any lawful debt actually due and payable to him from the debtor, where its recovery is or is not barred by the law in force for the time being as to the limitation of suits. However he cannot apply the payment to the disputed debt.

(iii) **Application of payment where neither party appropriates (Section 61):** Where neither party makes any appropriation, the payment shall be applied in discharge of the debts in order of time, whether they are or are not barred by the law in force for the time being as to the limitation of suits. If the debts are of equal standing, the payments shall be applied in discharge of each proportionately.

CONTRACTS, WHICH NEED NOT BE PERFORMED –
WITH THE CONSENT OF BOTH THE PARTIES

Under this heading, we shall discuss the principles of Novation, Rescission and Alteration. The law is contained in Sections 62 to 67 of the Contract Act.

(i) Effect of novation, rescission, and alteration of contract (Section 62)

"If the parties to a contract agree to substitute a new contract for it, or to rescind or alter it, the original contract need not be performed"

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

Example 35: A owes B Rs.5,00,000. A pays to B, and B accepts, in satisfaction of the whole debt,Rs. 2,00,000 paid at the time and place at which the Rs. 5,00,000 were payable. The whole debt is discharged.

(iii) Restoration of Benefit under a Voidable Contract (Section 64)

The law on the subject is "When a person at whose option a contract is voidable rescinds it, the other party thereto need not perform any promise therein contained in which he is the promisor. The party rescinding avoidable contract shall, if he has received any benefit thereunder from another party to such contract, restore such benefit, so far as may be, to the person from whom it was received".

Example 36: An insurance company may rescind a policy on the ground that material fact has not been disclosed. When it does so, the premium collected by it in respect of the policy reduced by the amount of expenses incurred by it in this connection must be repaid to the policy holder.

(iv) Obligations of Person who has Received Advantage under Void Agreement or contract that becomes void (Section 65)

"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."

Example 37: A pays B Rs. 1,00,000, in consideration of B's promising to marry C, A's daughter. C is dead at the time of the promise. The agreement is void, but B must repay A Rs. 1,00,000.

In a case, the plaintiff hired a godown from the defendant for twelve months and paid the whole of the rent in advance. After about seven months the godown was destroyed by fire, without any fault or negligence on the part of the plaintiff and the plaintiff claimed a refund

of a proportionate amount of the rent. Held, the plaintiff was entitled to recover the rent for the unexpired term, of the contract.

The Act requires that a party must give back whatever he has received under the contract. The benefit to be restored under this section must be benefit received under the contract (and not any other amount). A agrees to sell land to B for Rs. 400,000. B pays to A Rs. 40,000 as a deposit at the time of the contract, the amount to be forfeited by A if B does not complete the sale within a specified period. B fails to complete the sale within the specified period, nor is he ready and willing to complete the sale within a reasonable time after the expiry of that period. A is entitled to rescind the contract and to retain the deposit. The deposit is not a benefit received under the contract, it is a security that the purchaser would fulfil his contract and is ancillary to the contract for the sale of the land.

(v) **Communication of rescission (Section 66)**: You have noticed that a contract voidable at the option of one of the parties can be rescinded; but rescission must be communicated to the other party in the same manner as a proposal is communicated under Section 4 of the Contract Act. Similarly, a rescission may be revoked in the same manner as a proposal is revoked.

(vi) Effects of neglect of promisee to afford promisor reasonable facilities for performance (Section 67): If any promisee neglects or refuses to afford the promisor reasonable facilities for the performance of his promise, the promisor is excused by such neglect or refusal as to any non-performance caused thereby.

Example 38: If an apprentice refuses to learn, the teacher cannot be held liable for not teaching.

Example 39: A contracts with B to repair B's house. B neglects or refuses to appoint out to A the places in which his house requires repair. A is excused for the non-performance of the contract, if it is caused by such neglect or refusal.

DISCHARGE OF A CONTRACT

A contract is discharged when the obligations created by it come to an end. A contract may be discharged in any one of the following ways:

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

(1) Actual performance; or

(2) Attempted performance.

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

Example 40: A contracts to sell his car to B on the agreed price. As soon as the car is delivered to B and B pays the agreed price for it, the contract comes to an end by performance.

Example 41: A contracted to supply certain quantity of timber to B. B made the supply of timber at appointed time and place but A refused to accept the delivery. This is called as attempted performance.

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

Example 42: A owes B Rs. 1,00,000. A enters into an agreement with B and mortgage his (A's), estates for Rs. 50,000 in place of the debt of Rs. 1,00,000. This is a new contract and extinguishes the old.

Example 43: A owes B Rs. 5,00,000. A pays to B Rs. 3,00,000 who accepts it in full satisfaction of the debt. The whole is discharged.

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

(a) an unforeseen change in law;

(b) the destruction of the subject-matter essential to that performance;

(c) the non-existence or non-occurrence of particular state of things, which was naturally contemplated for performing the contract, as a result of some personal incapacity like dangerous malady;

(d) the declaration of a war (Section 56).

Example 44: A agrees with B to discover a treasure by magic. The agreement is void due to initial impossibility.

Example 45: A and B contract to marry each other. Before the time fixed for the marriage, A goes mad. The contract becomes void.

Example 46: A contracts to act at a theatre for six months in consideration of a sum paid in advance by B. On several occasions A is too ill to act. The contract to act on those occasions becomes void.

Example 47: X agrees to sell his horse to Y for Rs. 5,000 but the horse died in an accident. Here, it become impossible to perform the contract due to destruction of the subject. Thus, a valid contract changes into void contract because of impossibility of performance.

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

Example 48: If a creditor does not file a suit against the buyer for recovery of the price within three years, the debt becomes time-barred and hence irrecoverable.

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

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

Example 49: A contracted with B to supply 100 kgs of rice on 1st June. But A failed to deliver the same on said date. This is actual breach of contract. If time is not essential essence of contract B can give him another date for supply of goods and he will not be liable to claim for any damages if prior notice for the same is not given to A while giving another date.

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

Example 50: A owes B Rs. 5,00,000. C pays to B Rs.1,00,000 and B accepts them, in satisfaction of his claim on A. This payment is a discharge of the whole claim.

(viii) **Effects of neglect of promisee to afford promisor reasonable facilities for performance**: If any promisee neglects or refuses to afford the promisor reasonable facilities for the performance of his promise, the promisor is excused by such neglect or refusal as to any non-performance caused thereby. (Section 67)

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

Example 51: A took a land on lease from B. Subsequently, A purchases that very land. Now, A becomes the owner of the land and the ownership rights being superior to rights of a lessee, the earlier contract of lease stands terminated.

UNIT 5

BREACH OF CONTRACT AND ITS REMEDIES

ANTICIPATORY BREACH OF CONTRACT

An anticipatory breach of contract is a breach of contract occurring before the time fixed for performance has arrived. When the promisor refuses altogether to perform his promise and signifies his unwillingness even before the time for performance has arrived, it is called Anticipatory Breach.

Anticipatory breach of a contract may take either of the following two ways:

(a) Expressly by words spoken or written, and

(b) Impliedly by the conduct of one of the parties.

Example 1: Where A contracts with B on 15th July, 2020 to supply 10 bales of cotton for a specified sum on 14th August, 2020 and on 30th July informs B, that he will not be able to supply the said cotton on 14th August, 2020, there is an express rejection of the contract.

Example 2: Where A agrees to sell his white horse to B for Rs. 50,000/- on 10th of August, 2020, but he sells this horse to C on 1st of August, 2020, the anticipatory breach has occurred by the conduct of the promisor.

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

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

(1) To either treat the contract as "rescinded and sue the other party for damages from breach of contract immediately without waiting until the due date of performance;

or

(2) He may elect not to rescind but to treat the contract as still operative, and wait for the time of performance and then hold the other party responsible for the consequences of non-performance. But in this case, he will keep the contract alive for the benefit of the other

party as well as his own, and the guilty party, if he so decides on re-consideration, may still perform his part of the contract and can also take advantage of any supervening impossibility which may have the effect of discharging the contract.

ACTUAL BREACH OF CONTRACT

In contrast to anticipatory breach, it is a case of refusal to perform the promise on the scheduled date. The parties to a lawful contract are bound to perform their respective promises. But when one of the parties breaks the contract by refusing to perform his promise, he is said to have committed a breach. In that case, the other party to the contract obtains a right of action against the one who has refused to perform his promise.

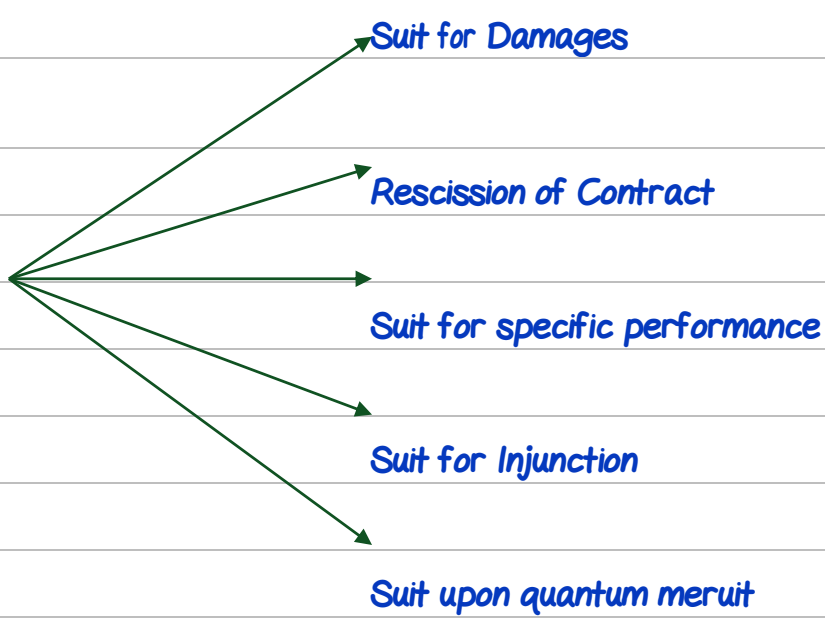
Actual breach of contract may be committed-

(a) **At the time when the performance of the contract is due.**

Example 3: A agrees to deliver 100 bags of sugar to B on 1st February 2020. On the said day, he failed to supply 100 bags of sugar to B. This is actual breach of contract. The breach has been committed by A at the time when the performance becomes due.

(b) **During the performance of the contract**: Actual breach of contract also occurs when during the performance of the contract, one party fails or refuses to perform his obligation under it by express or implied act.

Remedies for Breach of Contract



SUIT FOR DAMAGES

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

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

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

Compensation for failure to discharge obligation resembling those created by contract: When an obligation resembling those created by contract has been incurred and has not been discharged, any person injured by the failure to discharge it is entitled to receive the same compensation from the party in default, as if such person had contracted to discharge it and had broken his contract.

Explanation to Section 73

In estimating the loss or damage arising from a breach of contract, the means which existed of remedying the inconvenience caused by the non-performance of the contract must be taken into account.

Remedy by way of Damages or Kind of Damages

Remedy by way of damages is the most common remedy available to the injured party. This entitles the injured party to recover compensation for the loss suffered by it due to the breach of contract, from the party who causes the breach. Section 73 to 75 of the Contract Act incorporate the provisions in this regard. The damages which may be awarded to the injured party may be of the following kinds:

Damages

- General / Ordinary
- Special
- Vindictive or Exemplary
- Nominal
- Damages for deterioration caused by delay
- Pre-fixed damages

(i) **Ordinary damages**: When a contract has been broken, the party who suffers by such breach is entitled to receive, from the party who has broken the contract, compensation for any loss or damage cause to him thereby, which naturally arose in the usual course of things from such breach, or which the parties know, when they made the contract, to be likely to result from the breach of it:

Such compensation is not to be given for any remote and indirect loss or damage sustained by reasons of the breach. (Section 73 of the Contract Act and the rule in Hadley vs. Baxendale).

HADLEY vs. BAXENDALE- Facts

The crankshaft of P's flour mill had broken. He gives it to D, a common carrier who promised to deliver it to the foundry in 2 days where the new shaft was to be made. The mill stopped working, D delayed the delivery of the crankshaft so the mill remained idle for another 5 days. P received the repaired crankshaft 7 days later than he would have otherwise received. Consequently, P sued D for damages not only for the delay in the delivering the broken part but also for loss of profits suffered by the mill for not having been worked. The count held that P was entitled only to ordinary damages and D was not liable for the loss of profits because the only information given by P to D was that the article to be carried was the broken shaft of a mill and it was not made known to them that the delay would result in loss of profits.

Example 4: A agrees to sell to B bags of rice at Rs. 5,000 per bag, delivery to be given after two months. On the date of delivery, the price of rice goes up to Rs. 5,500 per bag. A refuse to deliver the bags to B. B can claim from A Rs. 500 as ordinary damages arising directly from the breach.

(ii) **Special damages**: Where a party to a contract receives a notice of special circumstances affecting the contract, he will be liable not only for damages arising naturally and directly from the breach but also for special damages.

Example 5: 'A' delivered a machine to 'B', a common carrier, to be conveyed to 'A's mill without delay. 'A' also informed 'B' that his mill was stopped for want of the machine. 'B' unreasonably delayed the delivery of the machine, and in consequence 'A' lost a profitable contract with the

Government. In this case, 'A' is entitled to receive from 'B', by way of compensation, the average amount of profit, which would have been made by running the mill during the period of delay. But he cannot recover the loss sustained due to the loss of the Government contract, as 'A's contract with the Government was not brought to the notice of 'B'.

(iii) **Vindictive or Exemplary damages**

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; and

(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. A business man whose credit has suffered will get exemplary damages even if he has sustained no pecuniary loss. But a non-trader cannot get heavy damages in the like circumstances, unless the damages are alleged and proved as special damages. (Gibbons v West Minister Bank)

(iv) **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.

(v) **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.

(vi) **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).

Example 6: If the penalty provided by the contract is Rs. 1,00,000 and the actual loss because of breach is Rs. 70,000, only Rs. 70,000 shall be available as damages, i.e., the amount of actual loss and not the amount stipulated. But if the loss is, say, Rs. 1,50,000, then only, Rs.1,00,000 shall be recoverable.

Example 7: X promised Y, a priest, to pay Rs. 10,000 as charity. The priest on X's promise incurred certain liabilities towards the repairing of the temple to the extent of Rs. 7,500. Y, the priest, can recover from X Rs. 7,500.

PENALTY AND LIQUIDATED DAMAGES (SECTION 74)

The parties to a contract may provide before hand, the amount of compensation payable in case of failure to perform the contract. In such cases, the question arises whether the courts will accept this figure as the measure of damage.

English Law: According to English law, the sum so fixed in the contract may be interpreted either as liquidated damages or as a penalty.

If the sum fixed in the contract represents a genuine pre-estimate by the parties of the

Indian Law: Indian law makes no distinction between 'penalty 'and liquidated damages'. The Courts in India award only a reasonable compensation not exceeding the sum so mentioned in the contract. Section 74 of the Contract Act lays down if the parties have fixed what the damages will be, the courts will never allow more. But the court may allow less. A decree is to be passed only for reasonable compensation not exceeding the sum named by the parties. Thus, Section 74 entitles a person complaining of breach of contract to get reasonable compensation and does not entitle him to realise anything by way of penalty.

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.

Example 8: A contracts with B, that if A practices as a surgeon in Kolkata, he will pay B Rs. 50,000. A practice as a surgeon at Kolkata, B is entitled to such compensation not exceeding Rs. 50,000 as the court considers reasonable.

Example 9: A borrows Rs. 10,000 from B and gives him a bond for Rs. 20,000 payable by five yearly instalments of Rs. 4,000 with a stipulation that in default of payment, the whole shall become due. This is a stipulation by way of penalty.

Example 10: A undertakes to repay B, a loan of Rs. 10,000 by five equal monthly instalments with a stipulation that in default of payment of any instalment, the whole shall become due. This stipulation is not by way of penalty and the contract may be enforced according to its terms.

Distinction between liquidated damages and penalty

Penalty and liquidated damages have one thing in common that both are payable on the occurrence of a breach of contract. It is very difficult to draw a clear line of distinction between the two but certain principles as laid down below may be helpful.

1. If the sum payable is so large as to be far in excess of the probable damage on breach, it is certainly a penalty.
2. Where a sum is expressed to be payable on a certain date and a further sum in the event of default being made, the latter sum is a penalty because mere delay in payment is unlikely to cause damage.
3. The expression used by the parties is not final. The court must find out whether the sum fixed in the contract is in truth a penalty or liquidated damages. If the sum fixed is extravagant or exorbitant, the court will regard it is as a penalty even if, it is termed as liquidated damages in the contract.
4. The essence of a penalty is payment of money stipulated as a terrorem of the offending party. The essence of liquidated damages is a genuine pre-estimate of the damage.
5. English law makes a distinction between liquidated damages and penalty, but no such distinction is followed in India. The courts in India must ascertain the actual loss and award the same which amount must not, however exceed the sum so fixed in the contract. The courts have not to bother about the distinction but to award reasonable compensation not exceeding the sum so fixed.

Besides claiming damages as a remedy for the breach of contract, the following remedies are also available:

(i) **Rescission of contract**: When a contract is broken by one party, the other party may treat the contract as rescinded. In such a case he is absolved of all his obligations under the contract and is entitled to compensation for any damages that he might have suffered.

Example 11: A promises B to deliver 50 bags of cement on a certain day. B agrees to pay the amount on receipt of the goods. A failed to deliver the cement on the appointed day. B is discharged from his liability to pay the price.

(ii) **Quantum Meruit**: 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. Quantum Meruit i.e. as much as the party doing the service has deserved. 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. Damages are compensatory in nature while quantum merit is restitutory. It is but reasonable compensation awarded on implication of a contract to remunerate. Where a person orders only 12 bottles of a whiskey from a wine merchant but also receives 2 bottles of brandy, and the purchaser accepts them, the purchaser must pay a reasonable price for the brandy.

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) Where there is an express or implied contract to render services but there is no agreement as to remuneration.

(d) When one party abandons or refuses to perform the contract.

(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.

Example 12: X wrongfully revoked Y's (his agent) authority before Y could complete his duties. Held, Y could recover, as a quantum meruit, for the work he had done and the expenses he had incurred in the course of his duties as an agent.

Example 13: A agrees to deliver 100 bales of cottons to B at a price of Rs.1000 per bale. The cotton bales were to be delivered in two instalments of 50 each. A delivered the first instalment but failed to supply the second. B must pay for 50 bags.

(iii) **Suit for specific performance**: Where damages are not an adequate remedy in the case of breach of contract, the court may in its discretion on a suit for specific performance direct party in breach, to carry out his promise according to the terms of the contract.

(iv) **Suit for injunction**: Where a party to a contract is negating the terms of a contract, the court may by issuing an 'injunction orders', restrain him from doing what he promised not to do.

Example 14: N, a film star, agreed to act exclusively for a particular producer, for one year. During the year she contracted to act for some other producer. Held, she could be restrained by an injunction.

Example 15: A, a singer, agreed with B to perform at his theatre for two months, on a condition that during that period, he would not perform anywhere. In this case, B could move to the Court for grant of injunction restraining A from performing in other places.

Party rightfully rescinding contract, entitled to compensation (Section 75)

A person who rightfully rescinds a contract is entitled to compensation for any damage which he has sustained through non-fulfilment of the contract.

Example 16: A, a singer, contracts with B, the manager of a theatre, to sing at his theatre for two nights in every week during the next two months, and B engages to pay her Rs. 100 for each night's performance. On the sixth night, A wilfully absents herself from the theatre, and B, in consequence, rescinds the contract. B is entitled to claim compensation for the damage which he has sustained through the non- fulfilment of the contract.

UNIT – 6

CONTINGENT AND QUASI CONTRACTS

CONTINGENT CONTRACTS

In this unit, we shall briefly examine what is called a 'contingent contract', its essentials and the rules regarding enforcement of this type of contracts. The Contract Act recognises certain cases in which an obligation is created without a contract. Such obligations arise out of certain relations which cannot be called as contracts in the strict sense. There is no offer, no acceptance, no consensus ad idem and in fact neither agreement nor promise and yet the law imposes an obligation on one party and confers a right in favour of the other. We shall have a look on these cases of 'Quasi-contracts'.

A contract may be absolute or a contingent. An Absolute contract is one where the promisor undertakes to perform the contract in any event without any condition.

Definition of 'Contingent Contract' (Section 31)

"A contract to do or not to do something, if some event, collateral to such contract, does or does not happen".

Contracts of Insurance, indemnity and guarantee fall under this category.

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

Example 2: A makes a contract with B to buy his house for Rs. 5,00,000 if he is able to secure to bank loan for that amount. The contract is contingent contract.

Meaning of collateral Event: Pollock and Mulla defined collateral event as "an event which is neither a performance directly promised as part of the contract, nor the whole of the consideration for a promise".

Example 3: A contracts to pay B Rs. 100,000 if B's house is burnt. This is a contingent contract. Here the burning of the B's house is neither a performance promised as part of the contract nor it is the consideration obtained from B. The liability of A arises only on the happening of the collateral event.

Example 4: A agrees to transfer his property to B if her wife C dies. This is a contingent contract because the property can be transferred only when C dies.

Essentials of a contingent contract

(a) The performance of a contingent contract would depend upon the happening or non-happening of some event or condition. The condition may be precedent or subsequent.

Example 5: 'A' promises to pay Rs. 50,000 to 'B' if it rains on first of the next month.

(b) The event referred to as collateral to the contract. The event is not part of the contract. The event should be neither performance promised nor a consideration for a promise.

Thus (i) where A agrees to deliver 100 bags of wheat and B agrees to pay the price only afterwards, the contract is a conditional contract and not contingent; because the event on which B's obligation is made to depend is part of the promise itself and not a collateral event. (ii) Similarly, where A promises to pay B Rs. 1,00,000 if he marries C, it is not a contingent contract. (iii) 'A' agreed to construct a swimming pool for 'B' for Rs. 200,000. And 'B' agreed to make the payment only on the completion of the swimming pool. It is not a contingent contract as the event (i.e. construction of the swimming pool) is directly connected with the contract.

(c) The contingent event should not be a mere 'will' of the promisor. The event should be contingent in addition to being the will of the promisor.

Example 6: If A promises to pay B Rs. 100,000, if he so chooses, it is not a contingent contract. (In fact, it is not a contract at all). However, where the event is within the promisor's will but not merely his will, it may be contingent contract.

Example 7: If A promises to pay B Rs.100,000 if it rains on 1st April and A leave Delhi for Mumbai on a particular day, it is a contingent contract, because going to Mumbai is an event no doubt within A's will, but raining is not merely his will.

(d) The event must be uncertain. Where the event is certain or bound to happen, the contract is due to be performed, then it is a not contingent contract.

Example 8: 'A' agreed to sell his agricultural land to 'B' after obtaining the necessary permission from the collector. As a matter of course, the permission was generally granted on the fulfilment of certain formalities. It was held that the contract was not a contingent contract as the grant of permission by the collector was almost a certainty.

RULES RELATING TO ENFORCEMENT

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

(a) **Enforcement of contracts contingent on an event happening**: Where a contract identifies happening of a future contingent event, the contract cannot be enforced until and unless the event 'happens'. If the happening of the event becomes impossible, then the contingent contract is void.

Section 32 says that "where a contingent contract is made to do or not to do anything if an uncertain future event happens, it cannot be enforced by law unless and until that event has happened. If the event becomes impossible, such contracts become void".

Example 9: A contracts to pay B a sum of money when B marries C. C dies without being married to B. The Contract becomes void.

(b) **Enforcement of contracts contingent on an event not happening**: Where a contingent contract is made contingent on a non-happening of an event, it can be enforced only when it's happening becomes impossible. Section 33 says that "Where a contingent contract is made to do or not do anything if an uncertain future event does not happen, it can be enforced only when the happening of that event becomes impossible and not before".

Example 10: Where 'P' agrees to pay 'Q' a sum of money if a particular ship does not return, the contract becomes enforceable only if the ship sinks so that it cannot return.

Where A agrees to pay sum of money to B if certain ship does not return however the ship returns back. Here the contract becomes void.

(c) **A contract would cease to be enforceable** if it is contingent upon the conduct of a living person when that living person does something to make the 'event' or 'conduct' as impossible of happening.

Section 34 says that "if a contract is contingent upon as to how a person will act at an unspecified time, the event shall be considered to have become impossible when such person does anything which renders it impossible that he should so act within any definite time or otherwise than under further contingencies".

Example 11: Where 'A' agrees to pay 'B' a sum of money if 'B' marries 'C'. 'C' marries 'D'. This act of 'C' has rendered the event of 'B' marrying 'C' as impossible; it is though possible if there is divorce between 'C' and 'D'.

In Frost V. Knight, the defendant promised to marry the plaintiff on the death of his father. While the father was still alive, he married another woman. It was held that it had become impossible that he should marry the plaintiff and she was entitled to sue him for the breach of the contract.

(d) **Contingent on happening of specified event within the fixed time**: Section 35 says that Contingent contracts to do or not to do anything, if a specified uncertain event happens within a fixed time, becomes void if, at the expiration of time fixed, such event has not happened, or if, before the time fixed, such event becomes impossible.

Example 12: A promises to pay B a sum of money if certain ship returns within a year. The contract may be enforced if the ship returns within the year, and becomes void if the ship is burnt within the year.

(e) **Contingent on specified event not happening within fixed time**: Section 35 also says that - "Contingent contracts to do or not to do anything, if a specified uncertain event does not happen within a fixed time, may be enforced by law when the time fixed has expired, and such event has not happened or before the time fixed has expired, if it becomes certain that such event will not happen".

Example 13: A promises to pay B a sum of money if a certain ship does not return within a year. The contract may be enforced if the ship does not return within the year, or is burnt within the year.

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

Example 14: 'A' agrees to pay 'B' Rs.one lakh if sun rises in the west next morning. This is an impossible event and hence void.

Example 15: X agrees to pay Y Rs.1,00,000 if two straight lines should enclose a space. The agreement is void.

Difference between a contingent contract and a wagering contract

Basis of difference	Contingent contract	Wagering contract
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.
Doctrine of mutuality of lose and gain	Contingent contract is not based on doctrine of mutuality of lose and gain.	A wagering contract is a game, losing and gaining alone matters.
Effect of contract	Contingent contract is valid.	A wagering agreement is void.

QUASI CONTRACTS

A valid contract must contain certain essential elements, such as offer and acceptance, capacity to contract, consideration and free consent. But sometimes the law implies a promise imposing obligations on one party and conferring right in favour of the other even when there is no offer, no acceptance, no genuine consent, lawful consideration, etc. and in fact neither agreement nor promise. Such cases are not contract in the strict sense, but the Court recognises them as relations resembling those of contracts and enforces them as if they were contracts. Hence the term Quasi –contracts (i.e. resembling a contract). Even in the absence of a contract, certain social relationships give rise to certain specific obligations to be performed by certain persons. These are known as quasi contracts as they create same obligations as in the case of regular contract.

Quasi contracts are based on principles of equity, justice and good conscience.

A quasi or constructive contract rest upon the maxims, "No man must grow rich out of another person's loss".

Example 16: T, a tradesman, leaves goods at C's house by mistake. C treats the goods as his own. C is bound to pay for the goods.

Example 17: A pays some money to B by mistake. It is really due to C. B must refund the money to A.

Example 18: A fruit parcel is delivered under a mistake to R who consumes the fruits thinking them as birthday present. R must return the parcel or pay for the fruits. Although there is no agreement between R and the true owner, yet he is bound to pay as the law regards it a Quasi-contract.

These relations are called as quasi-contractual obligations. In India it is also called as 'certain relation resembling those created by contracts.

Salient features of quasi contracts:

(a) In the first place, such a right is always a right to money and generally, though not always, to a liquidated sum of money.

(b) Secondly, it does not arise from any agreement of the parties concerned, but is imposed by the law; and

(c) Thirdly, it is a right which is available not against all the world, but against a particular person or persons only, so that in this respect it resembles a contractual right.

Cases Deemed as Quasi – Contracts

Claims for necessaries supplied [Section 68]	Payment by an interested person [Section 69]	Obligation of a person enjoying benefit of non gratuitous act [Section 70]	Responsibility of finder of goods [Section 71]	Money paid by mistake or under coercion [Section 72]

Under the provisions of the Indian Contract Act, the relationship of quasi contract is deemed to have come to exist in five different circumstances which we shall presently dilate upon. But it may be noted that in none of these cases there comes into existence any contract between the parties in the real sense. Due to peculiar circumstances in which they are placed, the law imposes in each of these cases the contractual liability.

(a) **Claim for necessaries supplied to persons incapable of contracting (Section 68)**: If a person, incapable of entering into a contract, or anyone 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.

Example 19: A supplies B, a lunatic, or a minor, with necessaries suitable to his condition in life. A is entitled to be reimbursed from B's property.

To establish his claim, the supplier must prove not only that the goods were supplied to the person who was minor or a lunatic but also that they were suitable to his actual requirements at the time of the sale and delivery.

(b) **Payment by an interested person (Section 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.

Example 20: B holds land in Bengal, on a lease granted by A, the zamindar. The revenue payable by A to the Government being in arrear, his land is advertised for sale by the Government. Under the revenue law, the consequence of the sale will be the annulment of B's

lease. B, to prevent the sale and the consequent annulment of his own lease, pays to the government the sum due from A. A is bound to make good to B the amount so paid.

(c) **Obligation of person enjoying benefits of non-gratuitous act (Section 70)**: In term of section 70 of the Act "where a person lawfully does anything for another person, or delivers anything to him not intending to do so gratuitously and such other person enjoys the benefit thereof, the latter is bound to pay compensation to the former in respect of, or to restore, the thing so done or delivered".

It thus follows that for a suit to succeed, the plaintiff must prove:

(i) that he had done the act or had delivered the thing lawfully;

(ii) that he did not do so gratuitously; and

(iii) that the other person enjoyed the benefit.

The above can be illustrated by a case law where 'K' a government servant was compulsorily retired by the government. He filed a writ petition and obtained an injunction against the order. He was reinstated and was paid salary but was given no work and in the meantime government went on appeal. The appeal was decided in favour of the government and 'K' was directed to return the salary paid to him during the period of reinstatement. [Shyam Lal vs. State of U.P. A.I.R (1968) 130]

Example 21: A, a tradesman, leaves goods at B's house by mistake. B treats the goods as his own. He is bound to pay A for them.

(d) **Responsibility of finder of goods (Section 71)**: 'A person who finds goods belonging to another and takes them into his custody is subject to same responsibility as if he were a bailee'.

Thus, a finder of lost goods has:

(i) to take proper care of the property as man of ordinary prudence would take

(ii) no right to appropriate the goods and

(iii) to restore the goods if the owner is found.

In Hollins vs. Howler L. R. & H. L., 'H' picked up a diamond on the floor of 'F's shop and handed over the same to 'F' to keep till the owner was found. In spite of the best efforts, the true owner could not be traced. After the lapse of some weeks, 'H' tendered to 'F' the lawful expenses incurred by him and requested to return the diamond to him. 'F' refused to do so.

Held, 'F' must return the diamond to 'H' as he was entitled to retain the goods found against everybody except the true owner.

Example 22: 'P' a customer in 'D's shop puts down a brooch worn on her coat and forgets to pick it up and one of 'D's assistants finds it and puts it in a drawer over the weekend. On Monday, it was discovered to be missing. 'D' was held to be liable in the absence of ordinary care which a prudent man would have taken.

(e) **Money paid by mistake or under coercion (Section 72)**: "A person to whom money has been paid or anything delivered by mistake or under coercion, must repay or return it".

Every kind of payment of money or delivery of goods for every type of 'mistake' is recoverable. [Shivprasad Vs Sirish Chandra A.I.R. 1949 P.C. 297]

Example 23: A payment of municipal tax made under mistaken belief or because of mis-understanding of the terms of lease can be recovered from municipal authorities. The above law was affirmed by Supreme Court in cases of Sales tax officer vs. Kanhaiyalal A. I. R. 1959 S. C. 835

Similarly, any money paid by coercion is also recoverable. The word coercion is not necessarily governed by section 15 of the Act. The word is interpreted to mean and include oppression, extortion, or such other means [Seth Khanjelek vs National Bank of India].

In a case where 'T' was traveling without ticket in a tram car and on checking he was asked to pay Rs.5/- as penalty to compound transaction. T filed a suit against the corporation for recovery on the ground that it was extorted from him. The suit was decreed in his favour. [Trikamdas vs. Bombay Municipal Corporation A. I. R.1954]

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

Difference between quasi contracts and contingent contracts

Basis of distinction	Quasi- Contract	Contingent- 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

UNIT – I

FORMATION OF THE CONTRACT OF SALE

Q1. Define contract of sale?

Ans. **According to section 4(1),**

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

Wider scope: The term "Contract of Sale" broader than the term Sale. It includes "Sale" and "an Agreement to Sell". A contract of sale may be absolute or conditional. [Section 4(2]

➢ Where under a contract of sale	➢ where the transfer of
➢ the property in the goods	➢ the property in the goods
➢ is transferred from the seller to the buyer,	➢ is to take place at a future time or subject to some condition thereafter to be fulfilled,
➢ the contract is called a sale [Section 4(3)]	➢ the contract is called an agreement to sell. [Section 4(3)]
	➢ An agreement to sell becomes a sale when the time elapses or the conditions are fulfilled subject to which the property in the goods is to be transferred. [Section 4(4)]

Q2. What are the elements of a contract of sale?

Ans. **The essential elements of a contract of sale are** :

(i) There must be at least two parties, the seller and the buyer.

(ii) The subject matter of the contract must necessarily be goods covering only movable property. It may be either existing goods or future goods

(iii) A price in money (not in kind) should be paid or promised But the consideration can be partly in money and partly in kind.

(iv) A transfer of property in goods from seller to the buyer must take place.

(v) A contract of sale may be absolute or conditional.

(vi) 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.

Q3. Define the following terms :

Ans.

Goods

"Good means" —

- every kind of movable property
- other than actionable claims and money; and
- includes stock and shares, growing crops, grass, and things attached to or forming part of the land,
- which are agreed to be severed before sale or under the contract of sale. [Section 2(7)]

Buyer and Seller

- Buyer means a person who buys or agrees to buy goods [Section 2(1)].
- Seller means a person who sells or agrees to sell goods [Section2(13)].

Document of title to goods

Document of title to goods" includes

- bill of lading,
- dock-warrant,
- warehouse keeper's certificate,
- wharfingers' certificate,
- railway receipt,
- multimodal transport document,
- warrant or order for the delivery of goods and
- any other document 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. [Section 2(4)]

  A document amounts to a document of title only where it shows an unconditional undertaking to deliver the goods to the holder of the document.

  However, 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 id 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.

Property [Section 2(11)]

'Property' here means 'ownership' or general property. In every contract of sale, the ownership of goods must be transferred by the seller to the buyer, or there should be an agreement by the seller to transfer the ownership to the buyer. It means the general property (right of owner-ship-in goods) and not merely a special property.

The general property in a thing may be transferred, subject to the special property continuing to remain with another person i.e., the pledgee who has a right to retain the goods pledged till payment of the stipulated dues.

Example: When "A" owns certain Goods, he has general property in the Goods. If it is pledged with "B", "B" has mere possession or limited interest, i.e. special property and A continues to have a general property

Mercantile Agent [Section 2(9)]

It means an agent having in the customary course of business as such agent authority either to sell goods or to consign goods for the purpose of sale or to buy goods or to raise money on the security of the goods.

Price[Section 2(10)]

Price means the money consideration for a sale of goods.

Q4. Define Delivery and its various types?

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

TYPES OF DELIVERY

Actual Delivery	Constructive Delivery	Symbolic delivery
When the goods are physically delivered to the buyer	When it is effected without any change in the custody or actual possession of the thing as in the case of delivery by attornment (acknowledgement) **Ex.** : where a warehouseman holding the goods of A agrees to hold them on behalf of B, at A's request.	(i) When there is a delivery of a thing (ii) in token of a transfer of something else, (iii) **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.

Q5. Distinction between sale and an agreement to sell?

Ans.

Basis	Sale	Agreement to Sale
Transfer of property	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.
Nature of contract	It is an executed contract. i.e. contract for which	It is an executory contract. i.e. contract for which

	consideration has been paid.	consideration is to be paid at a future date.
Remedies for breach	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.
Liability of parties	A subsequent loss or destruction of the goods is the liability of the buyer.	Such loss or destruction is the liability of the seller.
Burden of risk	Risk of loss is that of buyer since risk follows ownership.	Risk of loss is that of seller.
Nature of rights	It creates Jus in rem	It creates Jus in personam
Right of resale	The seller cannot resell the goods.	The seller may sell the goods since ownership is with the seller.

Q6. The Subject matter of a contract of sale is Good- Comment.

Or

What are the types of goods?

Ans. The subject matter of a contract of sale is always goods.

- 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. (Section 6)
- 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.
- 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 goods are classified into following types:

Existing Goods	Future Goods	Contingent Goods
Existing goods are such goods as are in existence at the time of the contract of sale, i.e., those owned or possessed by the seller at the time of contract of sale (Section 6).	Future goods means goods to be manufactured or produced or acquired by the seller after making the contract of sale [Section 2 (6)]. A contract for the sale of future goods is always an agreement to sell. It is never actual sale	The acquisition of which by the seller depends upon an uncertain contingency (uncertain event) are called 'contingent goods' [Section 6(2)]. Contingent goods also operate as 'an agreement to sell' and not a 'sale'

Q7. What are the types of existing goods?

Ans. Existing goods are further classified into:

Specific Goods	Ascertained Goods	Unascertained Goods
Specific goods means goods identified and agreed upon at the time a contract of sale is made [Section 2(14)].	Ascertained Goods are those goods which are identified in accordance with the agreement after the contract of sale is made. In actual practice the term 'ascertained goods' is used in the same sense as 'specific goods.'	Unascertained goods are the goods which are not specifically identified or ascertained at the time of making of the contract. They are indicated or defined only by description or sample.

Q8. Distinguish between

(a) Sale and Hire purchase

(b) Sale and Bailment

(c) Sale and contract for work and labour

Ans.

Sale and Hire purchase

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

Sale and Bailment

Basis	Sale	Bailment
Transfer of property	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 .
Return of goods	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.
Consideration	The consideration is the price in terms of money.	The consideration may be gratuitous or non-gratuitous.

Sale and contract for work and labour

- A contract of sale of goods is one in which some goods are sold or are to be sold for a price.
- But where not goods are sold, and there is only the doing or rendering of some work of labour, then the contract is only of work and labour and not of sale of goods

Q9. How contract of sale is made ?

Ans. A contract of sale may be made in any of the following modes:

- Contract of sale is made by an offer to buy or sell goods for a price and acceptance of such offer.
- There may be immediate delivery of the goods; or
- There may be immediate payment of price, but it may be agreed that the delivery is to be made at some future date; or
- There may be immediate delivery of the goods and an immediate payment of price; or
- It may be agreed that the delivery or payment or both are to be made in installments; or
- It may be agree that the delivery or payment or both are to be made at some future date

Q10. What are the consequences of "destruction of goods" under the Sale of Goods Act, 1930, where the goods have been destroyed after the agreement to sell but before the sale is affected?

Ans. **Consequences of destruction of goods —**

(a) Goods perishing before making of contract (Section 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 perished or become so damaged as no longer to answer to their description contract, at the time when the contract was made.

(b) Goods perishing before sale but after agreement to sell (Section 8):

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

Q11. What are the rules relating to ascertainment of price in a contract of sale ?

Ans. **'Price' means the monetary consideration for sale of goods [Section 2 (10)].**

By virtue of Section 9, the price in the contract of sale may be

(1) fixed by the contract, or

(2) agreed to be fixed in a manner provided by the contract, e.g., by a valuer, or

(3) determined by the course of dealings between the parties.

Where the price is not determined in accordance with the above provisions, the buyer shall pay the seller a reasonable price

Agreement to sell at valuation (Section 10):

(1) Where there is an agreement to sell goods on the terms that the price is to be fixed by the valuation of third party cannot or does not make such valuation, the agreements is thereby avoided:

Provided that, if the goods or any part thereof have been delivered to, and appropriated by, the buyer, he shall pay a reasonable price therefore.

(2) Where such third party is prevented from making the valuation by the fault of the seller or buyer, the party not in fault may maintain a suit for damages against the party in default

UNIT – 2

CONDITIONS & WARRANTIES

Q1. Define Condition and Warranty?

Ans. At the time of selling the goods, a seller usually makes certain statements or representations with a view to induce the intending buyer to purchase the goods. A representation which forms a part of the contract of sale and affects the con- tract, is called a stipulation.

- **Sec. 12(1)** : Condition and warranty (Section 12): A stipulation in a contract of sale with reference to goods which are the subject thereof may be a condition or a warranty.
- **Sec. 12(2)** : "A condition is a stipulation essential to the main purpose of the contract, the breach of which gives rise to a right to treat the contract as repudiated".
- **Sec. 12(3)** : "A warranty is a stipulation collateral to the main purpose of the contract, the breach of which gives rise to a claim for damages but not to a right to reject the goods and treat the contract as repudiated".
- **Sec. 12(4)** : 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.

Q2. Difference between condition and warranty?

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.

Q3. When a condition can be treated as warranty?

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

In the following cases, a contract is NOT avoided even on ac- count of a breach of a condition:

(i) Where the buyer altogether waives the performance of the condition. A party may for his own benefit waive a condition.

(ii) Where the buyer elects to treat the breach of the conditions, as one of warranty. That is to say, he may claim only dam- ages instead of repudiating the contract.

(iii) Where the contract is non-severable and the buyer has accepted either the whole goods or any part thereof. Acceptance means acceptance as envisaged in Section 72 of the Indian Contract Act, 1872.

(iv) Where the fulfillment of any condition or warranty is excused by law by reason of impossibility or otherwise.

Q4. Define Express condition and warranty?

Ans. 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 are those which are presumed by law to be present in the contract. It should be noted that an im- plied condition may be negated or waived by an express agreement.

Q5. Which conditions are implied in a contract of a sale unless a different intention appears .

Ans. Condition as to title [Section 14(a)]. In every contract of sale, unless there is an agreement to the contrary, the first implied condition on the part of the seller is that

(a) in case of a sale, he has a right to sell the goods, and

(b) in the case of an agreement to sell, he will have right to sell the goods at the time when the property is to pass.

Sale by description [Section 15]:

- Where there is a contract of sale of goods by description, there is an implied condition that the goods shall correspond with the description.

- This rule is based on the principle that " if you contract to sell peas, you cannot compel the buyer to take beans."
- The buyer is not bound to accept and pay for the goods which are not in accordance with the description of goods

A sale has been deemed to be by the description

(i) where the class or kind to which the goods belong has been specified, e.g. ,'Egyptian cotton', " java sugar", " Shfield crockery" etc., and

(ii) 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.

Sale by sample [Section 17]:

In a contract of sale by sample, there is an implied condition that

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

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

(c) The goods shall be free from any defect rendering them un- merchantable which would not be apparent on reasonable examination of the sample.

This condition is applicable only with regard to defects, which could not be discovered by an ordinary examination of the goods. But if the defects are latent, then the buyer can avoid the contract.

Sale by sample as well as by description [Section 15]:

- Where the goods are sold by sample as well as by description
- the implied condition is that the bulk of the goods supplied shall correspond both with the sample and the description.
- In case the goods correspond with the sample but do not tally with description or vice versa or
- both, the buyer can repudiate the contract.

Condition as to quality or fitness [Section 16(1)]:

Ordinarily, there is no implied condition as to the quality or fitness of the goods sold for any

However, the condition as to the reasonable fitness of goods for a particular purpose may be implied if:

- the buyer had made known to the seller the purpose of his purchase and
- relied upon the skill and judgment of the seller to select the best goods and
- the seller has ordinarily been dealing in those goods.

As a general rule, it is the duty of the buyer to examine the goods thoroughly before he buys them in order to satisfy himself that the goods will be suitable for his purpose for which he is buying them

Condition as to Merchantability [Section 16(2)]:

Where goods are bought by description from a seller who deals in goods of that description (whether he is the manufacturer or producer or not), there is an implied condition that the goods shall be of merchantable quality.

Provided that, if the buyer has examined the goods, there shall be no implied condition as regards defects which such examination ought to have revealed.

Goods should be of "Merchantable Quality" if they are in such condition as a man of ordinary prudence would accept them as Goods of that description. It applies to Goods whether or not the Goods are sold under a patent or trade name.

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

Q6. Which implied warranties are presumed in a con- tract of sale of goods ?

Ans. It is a warranty which the law implies into the contract of sale. These may also be excluded by the course of dealings be- tween the parties or by usage of trade (Section 62).

Warranty as to undisturbed possession [Section 14(b)]:

- An implied warranty that the buyer shall have and enjoy quiet possession of the goods.
- That is to say, if the buyer having got possession of the goods, is later on disturbed in his possession, he is entitled to sue the seller for the breach of the warranty.

Warranty as to non-existence of encumbrances [Section 14(c)]:

- An implied warranty that the goods shall be free from any charge or encumbrance in favourof

of any third party

- not declared or known to the buyer before or at the time the contract is entered into.

Warranty as to quality or fitness by usage of trade [Section 16(3)]:

An implied warranty as to quality or fitness for a particular purpose may be annexed or attached by the usage of trade.

Disclosure of dangerous nature of goods:

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

Q7. Define Caveat Emptor. What are the exceptions to the rule " Caveat Emptor " ?

Ans. Caveat emptor' means "let the buyer beware", i.e. in sale of goods the seller is under no duty to reveal unflattering truths about the goods sold. Therefore, when a person buys some goods, he must examine them thoroughly.

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.

The rule of Caveat emptor is laid down in the Section 16, which 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".

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

(i) Fitness for buyer's purpose:

Following are the conditions to be satisfied:

- if the buyer had made known to the seller the purpose of his purchase, and
- the buyer relied on the seller's skill and judgement, and
- seller's business is to supply goods of that description

the seller must supply the goods which shall be fit for the buyer's purpose. (Section16(1)

Case laws : { Priest vs. last } or { Bombay Burma Trading Corporation ltd. vs. Aga Muhammad }

(ii) **Sale under a patent or trade name**: In the case of a con- tract for the sale of a specified article under its patent or other trade name, there is no implied condition that the goods shall be reasonably fit for any particular purpose (Section 16(1))

(iii) **Merchantable quality**: Where goods are bought by description from a seller who deals in goods of that description (whether he is in the manufacturer or producer or not), there is an implied condition that the goods shall be of merchantable quality. But if the buyer has examined the goods, there is no implied condition as regards defects which such examination ought to have revealed. (Section 16(2))

(iv) **Usage of trade**: An implied warranty or condition as to qualify or fitness for a particular purpose may be annexed by the usage of trade. (Section 16(3)).

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

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

(vii) **Consent by fraud**: Where the consent of the buyer, in a contract of sale, is obtained by the seller by fraud or where the seller knowingly conceals a defect which could not be discovered on a reasonable examination, the doctrine of caveat emptor does not apply.

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

UNIT – 3

TRANSFER OF OWNERSHIP AND DELIVERY OF GOODS

Q1. What are the rules relating to the transfer of ownership of specific goods or ascertained goods ?

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

General rule (Sec. 19)

Sec. 19(1): Where there is a contract for the sale of specific or ascertained goods the property in them is transferred to the buyer at such time as the parties to the contract intend it to be transferred.

Sec. 19(2): For the purpose of ascertaining the 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.

Sec. 19(3): Unless a different intention appears, the following rules applies.

Specific goods in a deliverable state (Sec. 20)

- where there is an unconditional contract for the sale of specific goods in a deliverable state,
- the property in the goods passes to the buyer when 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, is postponed.

Specific goods to be put into a deliverable state (Sec. 21)

- Where there is a contract for the sale of specific goods and
- the seller is bound to do something to the goods for the purpose of putting them into a deliverable state,
- the property does not pass until such thing is done and the buyer has notice thereof.

Specific goods in a deliverable state, when the seller has to do anything there to in order to ascertain price (Sec. 22)

- Where there is a contract for the sale of specific goods in a deliverable state,
- but the seller is bound to weigh, measure, test or do some other act or thing with reference to

the goods

- for the purpose of ascertaining the price,
- the property does not pass until such act or thing is done and the buyer has notice thereof.

Q.2. What are the rules relating to the transfer of ownership of Unascertained good and future goods?

Ans. **Sec.18 —** Where there is a contract for the sale of unascertained goods, no property in the goods is transferred to the buyer unless and until the goods are ascertained.

Sale of unascertained goods and Appropriation:

Appropriation of goods involves selection of goods with the intention of using them in performance of the contract and with the mutual consent of the seller and the buyer.

The essentials are:

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

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

(c) The goods must be in a deliverable state.

(d) 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.

(e) The appropriation must be made by:

- the seller with the assent of the buyer; or
- the buyer with the assent of the seller.

(f) The assent may be expressed or implied.

(g) The assent may be given either before appropriation or after appropriation.

Q3. What are the rules relating to the transfer of ownership in case of goods sent on approval or on "sale or return" ?

Ans. When goods are delivered to the buyer on approval or "on sale or return" or other similar terms, the property therein passes to the buyer-

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

(b) if he does not signify his approval or acceptance to the seller but retains the goods without giving notice of rejection, then,

- If a time has been fixed for the return of the goods, on the expiration of such time and
- if no time has been fixed, on the expiration of a reasonable time; or

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

- 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.

Q4. Can a seller reserve the right of disposal of the goods ?

Ans. **Sec. 25(1)** — Where there is a contract for the sale of specific goods or where goods are subsequently appropriated to the contract, the seller may reserve the right of disposal of the goods by the terms of the contract or appropriation.

In such case, the property in the goods does not pass to the buyer until the conditions imposed by the seller are fulfilled even if the goods have already been delivered to a buyer, or to a carrier or other bailee for the purpose of transmission to the buyer,

Q5. What are the modes of Reservation of right of disposal of goods?

Ans. **Sec. 25(2)** —

- Where goods are shipped, or delivered to a railway administration for carriage by railway and
- by the bill of lading or railway receipts, the goods are deliverable to the order of the seller or his agent,
- the seller is prima facie deemed to reserve the right of disposal.

Sec. 25(3) —

- Where the seller of goods
- draws on the buyer for the price and transmits to the buyer the bill of exchange together

with the bill of lading or the railway receipt,

- to secure acceptance or payment of the bill of exchange,
- the ownership of goods will not be transferred to the buyer until the buyer honors the bill of exchange.

The buyer is bound to return the bill of lading or the railway receipt if he does not honour the bill of exchange and if he wrongfully retains the bill of lading or the railway receipt, the property in the goods does not pass to him

Q6. Risk prima facie passes with the property. Comment. ?

Ans. The general rule is that the risk follows ownership. It is the owner of the goods who has to bear the loss.

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".

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

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.

Q7. "Nemo Dat Quod Non Habet" – "None can give or transfer goods what he does not himself own." Explain the rule and state the cases in which the rule does not apply under the provisions of the Sale of Goods Act, 1930 ?

Ans. The term "Nemo Dat Quod Non Habet" means "none can give or transfer goods what he does not himself own".

The seller cannot give a better title to the buyer than he him self has .

Exception to the Rule and the cases in which the Rule does not apply under the provisions of the Sale of Goods Act, 1930 are enumerated below:

Sale by a Mercantile Agent:

A sale made by a mercantile agent of the goods or document of title to goods would pass a good title to the buyer in the following circumstances, namely;

(a) if he was in possession of the goods or documents with the consent of the owner;

(b) if the sale was made by him when acting in the ordinary course of business as a mercantile agent; and

(c) if the buyer had acted in good faith and has at the time of the contract of sale, no notice of the fact that the seller had no authority to sell. (Proviso to Sec. 27).

Sale by one of the joint owners (Sec. 28):

- If one of the several joint owners of goods has the sole possession of them with the permission of the others
- the property in the goods may be transferred to any person who buys them from such a joint owner in good faith and does not at the time of the contract of sale have notice that the seller has no authority to sell.

Sale by a person in possession under voidable contract:

- A buyer would acquire a good title to the goods sold to him
- by seller who had obtained possession of the goods under a contract voidable on the ground of coercion, fraud, misrepresentation or undue influence
- provided that the contract had not been rescinded until the time of the sale (Sec. 29).

Sale by one who has already sold the goods but continues in possession thereof:

- If a person has sold goods
- but continues to be in possession of them or of the documents of title to them,
- he may sell them to a third person, and
- if such person obtains the delivery thereof in good faith without notice of the previous sale, he would have good title to them, although the property in the goods had passed to the first buyer earlier.

A pledge or other deposition of the goods or documents of title by the seller in possession are equally valid. [Sec. 30(1)]

Sale by buyer obtaining possession before the property in the goods has vested in him :

- Where a buyer with the consent of seller
- obtains possession of the goods before the property in them has passed to him,
- he may sell, pledge or otherwise dispose of the goods to a third person, and
- if such person obtains delivery of the goods in good faith and without notice of the lien or other right of the original seller, he would get a good title to them. [Sec. 30 (2)]

Sale by an unpaid seller:

- Where an unpaid seller who had exercised his right of lien or stoppage in transit resells the goods,
- the buyer acquires a good title to the goods as against the original buyer [Sec. 54(3)]

Sale under the provisions of other Act:

- Sale by an official Receiver or liquidator of the company will give the purchaser a valid title.
- Purchase of goods from a finder of goods will get a valid title under circumstances.

Sale by a pawnee under default of pawnor will give valid title to the purchaser

Q8. Define delivery? What are the rules as to delivery ?

Ans. **Definition of Delivery [Sec. 2(2)]:** Delivery means voluntary transfer of possession from one person to another.

Payment and delivery are concurrent conditions (Sec. 32)

- Unless otherwise agreed, delivery of the goods and payment of the price are concurrent conditions,
- that is to say, the seller shall be ready and willing to give possession of the goods to the buyer in exchange for the price, and the buyer shall be ready and willing to pay the price in exchange for possession of the goods.

Mode of delivery (Sec. 33)

Delivery must have the effect of putting the goods into the buyer's on his authorized agent's possession.

Effect of part delivery (Sec. 34)

- A delivery of part of goods,
- with an intention of giving the delivery of the whole ,
- amounts to the delivery of the whole for the purpose of transfer of ownership of goods.

But

- a delivery of part of the goods,
- with an intention of severing it from the whole,
- does not operate as a delivery of the remainder.

Buyer to apply for delivery (Sec. 35)

Unless otherwise agreed , the seller of goods is not bound to deliver them until the buyer applies for delivery.

Place of delivery [Sec. 36(1)]

- Where there is a contract as to the place of delivery , the goods are to be delivered at the agreed place.
- Where there is no contract as to the place of delivery
  (a) goods sold are to be delivered at the place at which they are at the time of the sale,
  (b) goods agreed to be sold are to be delivered at the place at which they are at the time of the agreement to sell
  (c) in case of future goods , at the place at which they are manufactured or produced.

Time of delivery [Sec. 36(2)]

- Where under the contract of sale
- the seller is bound to send the goods to the buyer within agreed time ,
- but no time for sending them is fixed, the seller is bound to send them within a reasonable time.

Goods in possession of a third party [Sec. 36(3)]

- Where the goods at the time of sale are in possession of a third person,
- there is no delivery unless and until such third person acknowledges to the buyer that he holds the goods on his behalf.
- Provided that nothing in this Sec. shall affect the operation of the issue or transfer of any document of title to goods.

Time for tender of delivery [Sec. 36(4)]

- Demand or tender of delivery may be treated as ineffectual unless made at a reasonable hour. What is reasonable hour is a question of fact.

Expenses for delivery [Sec. 36(5)]

- The expenses of and incidental to putting the goods into a deliverable state must be borne by the seller
- in the absence of a contract to the contrary

Instalment deliveries (Sec. 38)

Unless otherwise agreed, the buyer is not bound to accept delivery in instalments.

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.

Deterioration during transit (Sec. 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.

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.
- Unless otherwise agreed, the seller is bound, on request, to auord the buyer a reasonable opportunity of examining the goods.

Q9. What are the rules as to delivery of wrong quantity ?

Ans. Delivery of wrong quantity [Section 37]

Sec. 37 (1) — Where the seller delivers to the buyer a quality of goods less than he contracted to sell,

- the buyer may reject them,
- but if the buyer accepts the goods so delivered he shall pay for them at the contract rate.

Sec. 37 (2) — Where the seller delivers to the buyer a quantity of goods larger than he contracted to sell,

- the buyer may accept the goods included in the contract and reject the rest, or
- he may reject the whole. If the buyer accepts the whole of the goods so delivered, he shall pay for them at the contract rate

Sec. 37 (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.

Sec. 37 (4) — The provisions of this section are subject to any usage of trade, special agreement or course of dealing between the parties.

Q10. What are the rules as to acceptance of delivery?

Ans. **Section 42 :** Acceptance is deemed to take place when the buyer-

(a) intimates to the seller that he had accepted the goods; or

(b) does any act to the goods, which is inconsistent with the ownership of the seller; or

(c) retains the goods after the lapse of a reasonable time, without intimating to the seller that he has rejected them.

Q11. What are the duties and liabilities of buyer in case of refusing to accept the goods ?

Ans. **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,
- he is not bound to return them to the seller,
- but it is sufIcient if he intimates to the seller that he refus- es to accept them.

Liability of buyer for neglecting or refusing delivery of goods (Section 44):

- When the seller is ready and willing to deliver the goods and requests the buyer to take delivery, and
- the buyer does not within a reasonable time take delivery of the goods,
- he is liable to the seller for any loss occasioned by his ne- glect or refusal to take delivery and
- also for a reasonable charge for the care and custody of the goods.

The above section does not affects seller's right to repudiate the contract where the buyer neglect or refuses to take delivery.

UNIT – 4

UNPAID SELLER

Q1. Define Unpaid Seller?

Ans. **According to Section 45(1) of the Sale of Goods Act, 1930 the seller of goods is deemed to be an 'Unpaid Seller' when-**

(a) The whole of the price has not been paid or tendered 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 dishonour of the instrument or otherwise.

The term 'seller ' here includes any person who is in the posi- tion 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)].

Q2. What are the unpaid sellers right against the goods and the buyer ?

Ans. **Rights of an unpaid seller [Sec. 46]:** The unpaid seller has by implication of law the following rights

Rights of an Unpaid Seller

Against the Goods	Against the Buyer
When Property in Goods has passed to the Buyer -	
• Right of Lien on the Goods in his possession, • Right of stoppage of Goods in transit if the Buyer becomes insolvent, • Right of Resale.	• Right to file a suit for price, • Right to file a suit for damages, and • Right to file a suit for interest.
When property in Goods has NOT passed to the Buyer-	
• In addition to the above 3 remedies, the right of withholding delivery.	

Q3. When right of lien can be used by the unpaid seller against the goods?

Ans. **Seller's lien (Section 47)**: According to sub-section (1), subject to the provisions of this Act, the unpaid seller of goods who is in possession of them is entitled to retain possession of them until payment or tender of the price in the following cases, namely:-

(a) where the goods have been sold without any stipulation as to credit;

(b) where the goods have been sold on credit, but the term of credit has expired;

(c) where the buyer becomes insolvent

According to sub-section (2), the seller may exercise his right of lien notwithstanding that he in possession of the goods as agent or bailee for 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.

Q4. When right of lien comes to an end?

Or

When right of lien is terminated?

Ans. **Termination of lien (Section 49)**: According to sub-section (1), the unpaid seller of goods loses his lien in the following circumstances :

(a) when he delivers the goods to a carrier or other bailee for the purpose of transmission to the buyer without reserving the right of disposal of the goods;

(b) when the buyer or his agent lawfully obtains possession of the goods;

(c) by waiver thereof.

(d) By Estoppel i.e., where the seller so conducts himself that he leads third parties to believe that the lien does not exist.

Exceptions

The unpaid seller of goods, having a lien thereon, does not lose his lien by reason only that he has obtained a decree for the price of the goods. [Sub-section (2)]

Q5. When right of stoppage in transit can be exercised?

Ans. The right of stoppage in transit means the right of stop- ping the goods while they are in transit, to regain the posses- sion and to retain them till the full price is paid.

When the unpaid seller has parted with the goods to a carrier and the buyer has become insolvent, he can exercise this right of asking the carrier to return the goods back, or not to deliver the goods to the buyer.

This right is the 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.

However, the right of stoppage in transit is exercised only when the following conditions are fulfilled: (Sec 50)

(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]

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.

Q6. When goods are deemed to be in Transit? When transit comes to an end?

Or

When right of stoppage of an unpaid seller comes to an end ?

Ans. **Duration of Transit (Sec 51)**

- Goods are deemed to be in the 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 in that behalf takes delivery of them from such carrier or other bailee.

The right of stoppage in transit is lost when transit comes to an end. Transit comes to an end in the following cases:

- When the buyer or other bailee obtains delivery.
- Buyer obtains delivery before the arrival of goods at destination.
- Where the carrier or other bailee acknowledges to the buyer or his agent that he holds the goods as soon as the goods are loaded on the ship, unless the seller has reserved the right of disposal of the goods.
- If the carrier wrongfully refuses to deliver the goods to the buyer.
- Where goods are delivered to the carrier hired by the buyer, the transit comes to an end.
- Where the part delivery of the goods has been made to the buyer, there the transit will come to an end for the remaining goods which are yet in the course of transmission.
- Where the goods are delivered to a ship chartered by the buyer, the transit comes to an end. [section 51]

Q7. How stoppage in transit is executed?

Ans. There are two modes of stoppage in transit-

(a) By taking actual possession of goods

(b) By giving notice to the carrier not to deliver the goods

Where the notice of stoppage in transit is given by the seller to the carrier or other bailee in possession of the goods, he shall re-deliver the goods to, or according to the directions of, the seller. The expenses of such re-delivery shall be borne by the seller.

Q8. Difference between Right of lien and Right of stoppage in transit?

Ans.

Right of lien	Right of stoppage in transit
The essence of a right of lien is to retain possession.	The right of stoppage in transit is right to regain possession.
Seller should be in possession of goods under lien.	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.
Right of lien can be exercised even when the buyer is not insolvent.	It is not the case with right of stoppage in x buyer is not insolvent.
The end of the right of lien is the starting point of the right of stoppage in transit.	Right of stoppage in transit begins when the right of lien ends.

Q9. When a right of re- sale can be exercised?

Ans. **Right of re-sale [Section 54]**: 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 con- tract price.

(iii) **A re-sale by the seller where a right of re-sale is expressly reserved in a contract of sale**: Sometimes, it is expressly reserved in a contract of sale: Sometimes, it is expressly agreed between the seller and the buyer that in case the buyer makes default in payment of the price, the seller will resell the goods to some other person. In such cases, the seller is said to have reserved his right of resale, and he may resell the goods on buyer's default.

It may be noted that in such cases, the seller is not required to give notice of resale. He is entitled to recover damages from the original buyer even if no notice of resale is given.

Q10. When a right of withholding can be exercised?

Ans. Where the property in goods has not passed to the buyer , the unpaid seller has in addition to his remedies a right of with- holding delivery of the goods. This right is similar to lien and is called "quasi-lien".

Q11. Explain the rights of an unpaid seller against a buyer?

Ans. **Suit for price (Section 55)**

Section 55(1) —

- 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(2) —

- 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.

Suit for damages for non- acceptance (Section 56)

- Where the buyer wrongfully neglects or refuses to accept and pay for the goods,
- the seller may sue him for damages for non-acceptance.
- As regards measure of damages, Section 73 of the Indian Contract Act, 1872 applies.

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 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.

Q12. Write note on Auction Sale.

AUCTION SALE (SECTION 64)

An 'Auction Sale' is a mode of selling property by inviting bids publicly and the property is sold to the highest bidder. An auctioneer is an agent governed by the Law of Agency. 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.

Legal Rules of Auction sale: Section 64 of the Sale of Goods Act, 1930 provides following rules to regulate the sale by auction:

(a) **Where goods are sold in lots**: Where goods are put up for sale in lots, each lot is prima facie deemed to be subject of a separate contract of sale.

(b) **Completion of the contract of sale**: The sale is complete when the auctioneer announces its completion by the fall of hammer or in any other customary manner and until such announcement is made, any bidder may retract from his bid.

(c) **Right to bid may be reserved**: Right to bid may be reserved expressly by or on behalf of the seller and where such a right is expressly reserved, but not otherwise, the seller or any one person on his behalf may bid at the auction.

(d) **Where the sale is not notified by the seller**: Where the sale is not notified to be subject to a right to bid on behalf of the seller, it shall not be lawful for the seller to bid himself or to employ any person to bid at such sale, or for the auctioneer knowingly to take any bid from the seller or any such person; and any sale contravening this rule may be treated as fraudulent by the buyer

(e) **Reserved price**: The sale may be notified to be subject to a reserve or upset price; and

(f) **Pretended bidding**: If the seller makes use of pretended bidding to raise the price, the sale is voidable at the option of the buyer.

INCLUSION OF INCREASED OR DECREASED TAXES IN CONTRACT OF SALE (SECTION 64A)

Where after a contract has been made but before it has been performed, tax revision takes place. Where tax is being imposed, increased, decreased or remitted in respect of any goods without any stipulations to the payment of tax, the parties would become entitled to read just the price of the goods accordingly. Following taxes are applied on the sale or purchase of goods:

- Any duty of customs or excise on goods,
- Any tax on the sale or purchase of goods

UNIT – I

GENERAL NATURE OF PARTNERSHIP

Q. 1 Define partnership, partner and firm?

Ans. **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'.

Q. 2 What are the essential elements of partnership?

or

What do you mean by mutual agency?

Ans. The following are the essential elements of partnership :

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

Partnership is an association of two or more persons.

Again, only persons recognized by law can enter into an agreement of partnership. Therefore, a firm, since it is not a person recognized in the eyes of law cannot be a partner. Again, a minor cannot be a partner in a firm, but with the consent of all the partners, may be admitted to the benefits of partnership.

The partnership Act is silent about the maximum number of partners but section 464 of the Companies Act, 2013 has now put a limit of 50 partners in any association/partnership firm.

2. **Agreement**:

Partnership must be the result of an agreement between two or more persons. There must be an agreement, either express or implied , entered into by all the persons concerned. Thus, the nature of the partnership is voluntary and contractual.

3. **Business**:

There must exist a business. For the purpose, the term 'business' includes every trade, occupation and profession. The motive of the business is the "acquisition of gains".

4. **Agreement to share profits:**

The sharing of profits is an essential feature of partnership. Partners must agree to share the profits in any manner they choose. But an agreement to share losses is not an essential element.

5. **Business carried on by all or any of them acting for all:**

- The business must be carried on by all the partners or by anyone or more of the partners acting for all. This is the cardinal principle of the partnership Law. In other words, there should be a binding contract of mutual agency between the partners.
- An act of one partner in the course of the business of the firm is in fact an act of all partners
- He is an agent in so far as he can bind the other partners by his acts and he is a principal to the extent that he is bound by the act of other partners.
- It may be noted that the true test of partnership is mutual agency rather than sharing of
- profits. If the element of mutual agency is absent, then there will be no partnership.

Q. 3 What is the true test of partnership?

or

What is the mode of existence of partnership?

Ans. **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.

1. **Agreement:**

- Partnership is created by agreement and by status (Section 5).

- The relation of partnership arises from contract and not from status
- So the members of a Hindu Undivided family carrying on a family business as such, or a Burmese Buddhist husband and wife carrying on business as such are not partners in such business.

2. **Sharing of Profit**:

Sharing of profit is an essential element to constitute a partnership. But, it is only a prima facie evidence and not conclusive evidence, in that regard.

Although the right to participate in profits is a strong test of partnership, and there may be cases where, upon a simple participation in profits, there is a partnership, yet whether the relation does or does not exist must depend upon the whole con- tract between the parties.

According to Section 6, regard must be had to the real relation between the parties as shown by all relevant facts taken together.

3. **Agency**:

- Existence of Mutual Agency which is the cardinal principal of partnership law, is very much helpful in reaching a conclusion in this regard.
- Each partner carrying on the business is the principal as well as an agent of other partners. So, the act of one partner done on behalf of firm, binds all the partners.
- If the elements of mutual agency relationship exist between the parties constituting a group formed with a view to earn profits by running a business, a partnership may be deemed to exist.

Q. 4 Difference between

(a) Partnership Vs. Joint Stock company

(b) Partnership Vs. Club

(c) Partnership vs. Hindu Undivided Family

(d) Partnership vs. Co-ownership

(e) Partnership vs. Association

Ans. **(a) Partnership Vs. Joint Stock company**

Basis	Partnership	Joint Stock Company
Legal status	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 (Salomon v. Salomon).
Agency	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
Distribution of profits	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 become distributable among the shareholders only when dividends are declared.
Extent of liability	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. 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.

Property	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.
Transfer of shares	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.
Management	In the absence of an express agreement to the contrary, all the partners are entitled to participate in the management.	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.
Registration	Registration is not compulsory in the case of partnership.	A company cannot come into existence unless it is registered under the Companies Act, 2013.

Winding up	A partnership firm can be dissolved at any time if all the partners agree.	A company, being a legal person is either wind up by the National Company Law Tribunal or its name is struck of by the Registrar of Companies.
Number of membership	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 restrict 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.
Duration of existence	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.

(b) Partnership Vs. club

Basis	Partnership	Club
Definition	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, etc.
Relationship	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.
Interest in the property	Partner has interest in the property of the firm.	A member of a club has no interest in the property of the club.
Dissolution	A change in the partners of the firm affect its existence.	A change in the membership of a club does not affect its existence.

(c) Partnership Vs. Joint Hindu Family

Basis	Partnership	Joint Hindu family
Mode of creation	Partnership is created necessarily by an agreement.	The right in the joint family is created by status means its creation by birth in the family.
Death of a member	Death of a partner ordinarily leads to the dissolution of partnership.	The death of a member in the Hindu undivided family does not give rise to dissolution of the family business.
Management	All the partners are equally entitled to take part in the partnership business.	The right of management of joint family business generally

		vests in the Karta, the governing male member or female member of the family.
Authority to bind	Every partner can, by his act, bind the firm.	The Karta or the manager, has the authority to contract for the family business and the other members in the family.
Liability	In a partnership, the liability of a partner is unlimited.	In a Hindu undivided family, only the liability of the Karta is unlimited, and the other coparcener are liable only to the extent of their share in the profits of the family business.
Calling for accounts on closure	A partner can bring a suit against the firm 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.
Governing Law	A partnership is governed by the Indian Partnership Act, 1932.	A Joint Hindu Family business is governed by the Hindu Law.
Minor's capacity	In a partnership, a minor cannot become a partner, though he can be admitted to the benefits of partnership, only with the consent of all the partners.	In HUF business, a minor becomes a member of the ancestral business by the incidence of birth. He does not have to wait for attaining majority.

Continuity	A firm subject to a contract between the partners gets dissolved by death or insolvency of a partner.	A Joint Hindu family has the continuity till it is divided. The status of Joint Hindu family is not thereby affected by the death of a member.
Number of Members	In case of Partnership number of members should not exceed 50.	Members of HUF who carry on a business may be unlimited in number
Share in the business	In a partnership each partner has a defined share by virtue of an agreement between the partners.	In a HUF, no coparceners has a definite share. His interest is a fluctuating one. It is capable of being enlarged by deaths in the family diminished by births in the family.

(d) Partnership vs. Co ownership

Basis	Partnership	Co-ownership
Formation	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.
Implied agency	A partner is the agent of the other partners.	A co-owner is not the agent of other co- owners.
Nature of interest	There is community of interest which means that profits and losses must	Co-ownership does not necessarily involve sharing of

	have to be shared.	profits and losses.
Transfer of interest	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.

(e) Partnership vs. Association

Basis	Partnership	Association
Meaning	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.
Examples	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.

Q. 5 What are the various types of partnership ?

Ans. The various types of partnerships are :

Partnership at will (Section 7):

- Partnership at will is a partnership when:
  - no fixed period has been agreed upon for the duration of the partnership; and
  - there is no provision made as to the determination of the partnership.

- But where there is an agreement between the partners either for the duration of the partnership or for the determination of the partnership, the partnership is not partnership at will.
- Where a partnership entered into for a fixed term is continued after the expiry of such term, it is to be treated as having become a partnership at will.
- It may be dissolved by any partner by giving notice in writing to all the other partners of his intention to dissolve the same.

Partnership for a 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'.
- It is a partnership created for a particular period of time. Such a partnership comes to an end on the expiry of the fixed period.

Particular partnership:

- A partnership may be organized for the prosecution of a single adventure as well as for the conduct of a continuous business.
- Where a person becomes a partner with another person in any particular adventure or undertaking the partnership is called 'particular partnership'.

A partnership, constituted for a single adventure or undertaking is, subject to any agreement, dissolved by the completion of the adventure or undertaking.

General partnership:

- Where a partnership is constituted with respect to the business in general, it is called a general partnership.
- A general partnership is different from a particular partnership.

In the case of a particular partnership the liability of the partners extends only to that particular adventure or undertaking, but it is not so in the case of general partnership.

Q. 6 What are the various types of partners ?

Ans. The various types of partners are:

Active or Actual or Ostensible partner

It is a person

- Who has become a partner by agreement, and
- Who actively participates in the conduct of the partnership.
- He acts as an agent of other partners for all acts done in the ordinary course of business.
- In the event of his retirement, he must give a public notice in order to absolve himself of liabilities for acts of other partners done after his retirement.

Sleeping or Dormant Partner

It is a person

- Who is a partner by agreement, and
- Who does not actively take part in the conduct of the partnership business.
- They are called as 'sleeping' or 'dormant' partners.
- They share profits and losses and are liable to the third parties for all acts of the firm. They are, however not required to give public notice of their retirement from the firm.

Nominal Partner

- A person who lends his name to the firm, without having any real interest in it, is called a nominal partner.
- He is not entitled to share the profits of the firm. Neither he invest in the firm nor takes part in the conduct of the business. He is, however liable to third parties for all acts of the firm

Partner in profits only

A partner who is entitled to share the profits only without being liable for the losses is known as the partner for profits only and also liable to the third parties for all acts of the profits only .

Incoming partners

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

Outgoing partner

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

Partner by holding out (Sec. 28)

- Partnership by holding out is also known as partnership by estoppel.
- Where a man holds himself out as a partner, or allows others to do it, he is then stopped from denying the character he has assumed and upon the faith of which creditors may be presumed to have acted.
- A person may himself, by his words or conduct have induced others to believe that he is a partner or he may have allowed others to represent him as a partner. The result in both the cases is identical.
- It is only the person to whom the representation has been made and who has acted thereon that has right to enforce liability arising out of 'holding out'.
- The rule given in Section 28 is also applicable to a former partner who has retired from the firm without giving proper public notice of his retirement. In such cases a person who, even subsequent to the retirement, give credit to the firm on the belief that he was a partner, will be entitled to hold him liable.

Q. 7 Write a short note on Partnership deed?

Ans. **Partnership Deed**

- Partnership is the result of an agreement. No particular formalities are required for an agreement of partnership.
- It may be in writing or formed verbally. But it is desirable to have the partnership agreement in writing to avoid future disputes.
- The document in writing containing the various terms and conditions as to the relationship of the partners to each other is called the 'partnership deed'.
- It should be drafted with care and be stamped according to the provisions of the Stamp Act, 1899.
- Where the partnership comprises immovable property, the instrument of partnership must be in writing, stamped and registered under the Registration Act.

Partnership deed may contain the following information:-

1. Name of the partnership form.
2. Names of all the partners.
3. Nature and place of the business of the firm.
4. Date of commencement of partnership.
5. Duration of the partnership firm.
6. Capital contribution of each partner
7. Profit Sharing ratio of the partners.
8. Admission and Retirement of a partner.
9. Rates of interest on Capital, Drawings and loans.
10. Provisions for settlement of accounts in the case of dissolution of the firm.
11. Provisions for Salaries or commissions, payable to the partners, if any.
12. Provisions for expulsion of a partner in case of gross breach of duty or fraud.

UNIT — 2

RELATION OF PARTNERS

Q. 1 Whether a minor may be admitted in the business of a partnership firm? Explain the rights and liabilities of a minor during minority in the partnership firm.

Ans. A minor cannot be bound by a contract because a minor's contract is void and not merely voidable. Therefore, a minor cannot become a partner in a firm because partnership is founded on a contract.

Though a minor cannot be a partner in a firm, he can none the- less be admitted to the benefits of partnership under Section 30 of the Act. When this has been done and it can be done with the consent of all the partners then the rights and liabilities of such a partner will be governed under Section 30 as follows :

Rights —

(i) A minor partner has a right to his agreed share of the profits and of the firm.

(ii) He can have access to, inspect and copy the accounts of the firm.

(iii) He can sue the partners for accounts or for payment of his share BUT only when severing his connection with the firm, and not otherwise.

(iv) On attaining majority he may within 6 months elect to become a partner or not to become a partner.

- If he elects to become a partner, then he is entitled to the share to which he WAS ENTITLED as a minor.
- If he does not, then his share is NOT liable for any acts of the firm after the date of the public notice served to that effect.

Liabilities Before attaining majority —

(a) The liability of the minor is confined only to the EXTENT of his share in the profits and the property of the firm.

(b) Minor has NO personal liability for the debts of the firm incurred during his minority.

(c) Minor CANNOT BE declared insolvent, but if the firm is declared insolvent his share in the firm vests in the Official Receiver/Assignee.

Q. 2 What are the liabilities of a minor after attaining majority ?

Ans. The liabilities of a minor after attaining majority are as follows :

Liabilities After attaining majority

- Within 6 months of his attaining majority or
- on his obtaining KNOWLEDGE that he had been admitted to the benefits of partnership,
- whichever date is LATER ,
- the minor partner has to DECIDE whether he shall remain a partner or leave the firm.

When he elects not to become a 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.

(i) His rights and liabilities continue to be those of a minor up to the date of giving public notice.

(ii) His share shall not be liable for any acts of the firm done after the date of the notice.

(iii) He shall be entitled to sue the partners for his share of the property and profits. It may be noted that such minor shall give notice to the Registrar that he has or has not become a partner.

When he becomes partner:

If he fails to give such notice he shall become a partner in the firm on the EXPIRY of the said six months.

If the minor becomes a partner 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:

(i) He becomes personally LIABLE to third parties for all acts of the firm done SINCE he was admitted to the benefits of partnership.

(ii) His share in the property and the profits of the firm REMAINS THE SAME to which he was entitled as a minor

Q. 3 Explain the duties of a partner of a partnership firm?

Ans. The duties of a partner can be divided into two parts

(a) **Mandatory duties** : these are provided in Section 9 & 10 of the Indian Partnership Act , 1932 which cannot be changed by mutual agreement amongst partners :

Section 9 — The partners should carry business of the firm to the greatest common advantages and

- to be just and faithful to each other i.e. a partner must observe the utmost good faith in his dealings with the other partners and
- to render true accounts and full information of all things affecting the firm to any partner or his legal representative.

SECTION 10 — Duty to indemnify for loss caused by fraud :

- Every partner shall indemnify (compensate or to make good) the firm
- for any loss caused to it
- by his fraud in the conduct of the business of the firm.

(b) **General duties**: The general duties as provided in the Act are subject to the agreement by partners. These can be changed by an agreement amongst the partners. Unless other- wise provided , every partner has the following duties :

To attend diligently [Sec 12 (b)] —

Every partner is bound to attend diligently (carefully) to his duties in the conduct of the business

Not to claim remuneration for taking part [Sec. 13(a)]

A partner is not entitled to receive remuneration for taking part in the conduct of the business;

To contribute equally to the losses [Sec. 13(b)]

The partners are entitled to share equally in the profits earned, and shall contribute equally to the losses sustained by the firm;

To indemnify the firm[Sec. 13(f)]

A partner shall indemnify the firm for any loss caused to it by his wilfull neglect in the conduct of business of the firm.

To hold and use firm's property for business purpose [Sec 15]

- Subject to contract between the partners,
- the property of the firm shall be held and used by the partners exclusively for the purposes of the business.

To account for and pay the personal profits from transactions of firm [Sec 16(a)]

If a partner derives any profit for himself from

- any transaction of the firm, or
- from the use of the property or
- business connection of the firm or
- the firm name,

he shall account for that profit and pay it to the firm;

To account for and pay the personal profits from competing business [Sec 16(b)]

If a partner carries on any business of the same nature as and competing with that of the firm, he shall account for and pay to the firm all profits made by him in that business.

Q. 4 What are the various rights of the partners?

Ans. Unless otherwise agreed , every partner has the following rights :

Right to take part [Sec.12 (a)]

Every partner has a right to take part in the conduct of the business;

Right to express opinion [Sec. 12 (c)]

Every partner shall have the right to express his opinion before the matter is decided. Any difference arising as to ordinary matters connected with the business may be decided by MAJORITY of the partners, but no change may be made in the nature of the business without the consent of ALL partners;

Right to have access to books [Sec. 12 (d)]

Every partner ,whether active or sleeping ,has a right to have access to and to inspect and copy any of the books of the firm.

The right must, however, be exercised bona fide.

Right to share profits equally [Sec. 13 (b)]

The partners are entitled to share equally in the profits earned, and shall contribute equally to the losses sustained by the firm

Right to receive interest on capital [Sec. 13 (c)]

The following elements must be there before a partner can be entitled to interest on moneys brought by him in the partnership business:

(i) an express agreement to that effect, or practice of the particular partnership or

(ii) any trade custom to that effect; or

(iii) a statutory provision which entitles him to such interest.

Where a partner is entitled to interest on the capital subscribed by him such interest shall be payable only out of profits.

Right to claim interest on advances [Sec. 13 (d)]

A partner making, any payment or advance beyond the amount of capital he has agreed to subscribe, is entitled to interest thereon at the rate of six percent per annum;

Right to be indemnified [Section 13 (e)]

Every partner has the right to be indemnified by the firm in respect of payments made and liabilities incurred by him

(i) in the ordinary and proper conduct of the business of the firm

(ii) in performing an act in an emergency for protecting the firm from any loss, he has acted in a manner as a person of ordinary prudence would have acted in similar circumstances in his own

Right to prevent introduction of a new partner[Sec. 31]

- Subject to contract between the partners and to the provisions of section 30,
- no person shall be introduced as a partner into a firm without the consent of all the existing partners.

Other Rights

- Right to retire [Sec. 32]
- Right not to be expelled [Sec 33]
- Right to carry on competing business [Sec. 36(1)]
- Right to share subsequent profits [Sec. 37]
- Right to dissolve the partnership [Sec 40]

Q. 5 How a partner can retire from the firm ? what are his rights and duties at/ after retirement ?

Ans. **Retirement of partners [Sec. 31(1)]**

A partner may retire:

(a) with the consent of all the other partners;

(b) in accordance with an express agreement by the partners; or

(c) where the partnership is at will, by giving notice in writing to all the other partners of his intention to retire.

Liabilities of an outgoing partner Sec. 31(3)

- A retiring partner CONTINUES to be liable to third party for acts of the firm after his retirement
- until public notice of his retirement has been given
- But the retired partner will NOT be liable to any third party if the latter deals with the firm without knowing that the former was partner.

Sec. 31(2) —As regards the liability for acts of the firm done BEFORE his retirement,

- the retiring partner remains liable for the same,
- UNLESS there is an agreement made by him with the third party concerned and the partners of the reconstituted firm.
- Such an agreement may be implied by a course of dealings between the third party and the reconstituted firm after he had knowledge of the retirement.
- Notices under sub-section (3) may be given by the retired partner or by any partner of the reconstituted firm.

Rights of an outgoing partner

Sec. 36 : Right to carry on competing business

- An outgoing partner may carry on business competing with that of the firm and he may advertise such business, but unless otherwise agreed , he cannot,

  (a) use the firm name,

  (b) represent himself as carrying on the business of the firm or

  (c) solicit the custom of persons who were dealing with the firm before he ceased to be a partner.

EXCEPTION —

- However, the partner may agree with his partners that on his ceasing to be so,
- he will not carry on a business similar to that of the firm within a specified period or within specified local limits.
- Such an agreement will not be in restraint of trade if the restraint is reasonable [Section 36(2)].
- A similar rule applies to such an agreement of sale of the firm's goodwill [Section 53(3)].

Sec. 37 : Right to share subsequent profits :

- Section 37 deals with rights of outgoing partners and a liability of the surviving or continuing partner,

- who without a settlement of accounts with legal representatives of the deceased partner utilizes the assets of partnership for continuing the business.
- A retiring partner at his option ,is entitled to claim either of the following :
  (a) such share of the profits made since he ceased to be a partner as may be attributable to the use of his share of the property of the firm or
  (b) to interest at the rate of six per cent per annum on the amount of his share in the property of the firm.
- However if the surviving or continuing partners purchases the interest of a deceased or outgoing partner , then the outgoing partner or his estate, is not entitled to any further or other share of profit.

Q. 6 The relation of partners with third parties are governed by the mutual agency relationship existing among the partners. Comment

Is the firm liable for all the acts of a partner due to mutual agency relationship. Comment.

Ans. A partnership is the relationship between the partners who have agreed to share the profits of the business carried on by all or any of them acting for all (Section 4). This definition suggests that any of the partners can be the agent of the others. Section 18 clarifies this position by providing that, subject to the provisions of the Act, a partner is the agent of the firm for the purpose of the business of the firm.

The partner indeed virtually embraces the character of BOTH a principal and an agent.

So far as he acts for himself and in his own interest in the common concern of the partnership, he may properly be deemed a principal and so far as he acts for his partners, he may properly be deemed as an agent.

The rule that a partner is the agent of the firm for the purpose of the business of the firm CANNOT be applied to all transactions and dealings between the partners themselves.

It is applicable only to the act done by partners for the purpose of the business of the firm.

Q. 7 Define implied authority ?

Ans. **Implied authority of partner as agent of the firm (section 19):**

Subject to the provisions of section 22, the act of a partner which is done to carry on, business

of the kind carried on by the firm, in the usual way , binds the firm.

The authority of a partner to bind the firm conferred by this section is called his "implied authority".

Sections 19(1) and 22 deal with the implied authority of a partner. The impact of these Sections is that

- the act of a partner which is done to carry on, in the usual way,
- in the usual way,
- business of the kind carried on by the firm
- binds the firm,
- provided that the act is done in the firm name, or any manner expressing or implying an intention to bind the firm.
- Such an authority of a partner to bind the firm is called his implied authority.

It is however subject to the following restrictions:

1. The act done must relate to the usual business of the firm, that is, within the scope of his authority and related to the normal business of the firm.
2. The act is such as is done for normal conduct of business of the firm. [Section 19(1)].
3. The act to be done in the FIRM'S NAME or in any other manner expressing or implying an intention to bind the firm (Section 22).

Q.8 What are the restrictions on the implied authority of a partner ?

Ans. In the absence of any usage or custom of trade to the contrary, the implied authority of a Partner does not empower him to-

(a) Submit a dispute relating to the business of the firm to arbitration;

(b) Open a banking account on behalf of the firm in his own name;

(c) Compromise or relinquish any claim or portion of a claim by the firm;

(d) Withdraw a suit or proceedings filed on behalf of the firm;

(e) Admit any liability in a suit or proceedings against the firm;

(f) Acquire immovable property on behalf of the firm

(g) Transfer immovable property belonging to the firm; and

(h) Enter into partnership on behalf of the firm.

Q. 9 Can the authority of a partner be restricted or ex- tended ? What is the effect on third parties of such restriction or extension ?

Ans. **Extension and restriction of partners' implied authority (section 20):**

The implied authority of a partner may be extended or restricted by contract between the partners.

Under the following conditions, the restrictions imposed on the implied authority of a partner by agreement shall be EFFECTIVE AGAINST a third party:

1. The third party knows about the restrictions, and
2. The third party does not know that he is dealing with a partner in a firm.

However, this restriction or extension is only possible with the consent of all the partners.

Any one partner, or even a majority of the partners, cannot restrict or extend the implied authority.

Q. 10 All partners are liable to third parties for all acts of a partner which fall within the scope of his implied authority. Explain the effect of implied authority and liability of the firm towards third parties in various cases ?

Ans.

Sec. 20 —Extension and restriction of partners' implied authority

Sec. 23 — Effect of admissions by a partner

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.

An admission or representation by a partner will NOT BIND the firm if his authority on the point is limited and the other party knows of the restriction

Sec. 24 — Effect of notice to acting partner

- Notice to a partner
- who habitually acts in the business of the firm (working partner and not sleeping partner)
- of any matter relating to the AFFAIRS of the firm operates as notice to the firm,
- except in the case of a fraud on the firm committed by or with the consent of that partner.

Sec. 25 — Liability of a partner for acts of the firm

- Every partner is liable,
- jointly with all the other partners and also severally,
- for all acts of the firm done
- while he is a partner

Sec. 26 — Liability of the firm for wrongful acts of a partner

The firm is liable to the same extent as the partner for any loss or injury caused to a third party by the wrongful acts of a partner, if they are done by the partner while acting.

(a) in the ordinary course of the business of the firm

(b) with the authority of the partners.

Sec. 27 — Liability Of Firm For Misapplication By Partners

The firm is liable to the third parties in the following two cases of misappropriation by a partner

(a) a partner acting within his APPARENT AUTHORITY receives money or property from a third

(b) 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.

Q. 11 State the modes by which a partner may transfer his interest in the firm in favour of another person under the Indian Partnership Act, 1932. What are the rights of such a transferee?

Ans. Section 29 of the Indian Partnership Act, 1932 provides that a share in a partnership is transferable like any other property, but as the partnership relationship is based on mutual confidence, the assignee of a partner's interest by sale, mort- gage or otherwise CANNOT ENJOY the same rights and privileges as the original partner.

The rights of such a transferee are as follows:

Rights during continuance —

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.

Rights after dissolution —

On the dissolution of the firm or on the retirement of the transferring partner, the transferee will be ENTITLED , against the remaining partners:

(a) to receive the share of the assets of the firm to which the transferring partner was entitled, and

(b) for the purpose of ascertaining the share,

he is entitled to AN ACCOUNT as from the date of the dissolution.

By virtue of Section 31, —

- no person can be introduced as a partner in a firm without the consent of all the partners.
- A partner cannot by transferring his own interest, make anybody else a partner in his place, unless the other partners agree to accept that person as a partner.
- At the same time, a partner is not debarred from transfer- ring his interest. A partner's interest in the partnership can be regarded as an existing interest and tangible property which can be assigned.

Q. 12 Can majority of partners expel any one partner? When an expulsion is valid?

Ans. **Sec. 33(1) —** A partner may not be expelled from a firm by any MAJORITY of the partners, unless the following conditions are satisfied :

(i) the power of expulsion must have existed in a contract between the partners;

(ii) the power has been exercised by a majority of the partners; and

(iii) it has been exercised in good faith.

If all these conditions are not present, the expulsion is not deemed to be in bona fide interest of the business of the firm.

The test of good faith as required under Section 33(1) includes

(i) The expulsion must be in the interest of the partnership.

(ii) The partner to be expelled is served with a notice.

(iii) He is given an opportunity of being heard.

If a partner is otherwise expelled, the expulsion is null and void.

Sec. 33(2) — The provisions of sub-section (2), (3) and (4) of section 32 shall apply to an expelled partner as if he were a retired partner.

Q. 13 What are the effects of Insolvency of a partner?

Ans. **Effects of insolvency of a partner (section 34)**

Sec. 34(1) — 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

Sec. 34(2) — The estate of the insolvent partner is not liable for the acts of the firm done after the date of order of adjudication.

- The firm is also not liable for any act of the insolvent partner after the date of the order of adjudication.
- Ordinarily but not necessarily , 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.

Sec 45 — No public notice is required on the insolvency of a partner.

Q. 14 What are the effects of death of a partner?

Ans. **Unless otherwise agreed by the partner, a firm is dissolved on the death of a partner [Sec. 42 (c)]**

Where under a contract between the partners, the firm is not dissolved by the death of a partner, the estate of a deceased partner is not liable for any act of the firm done after his death. (Sec. 35)

Q. 15 What are the effects of introduction of a partner?

Ans. **Introduction of a partner (section 31)**

31(1) — Admission of a partner

- Subject to contract between the partners and to the provisions of section 30(regarding minor partner) ,
- no person shall be introduced as a partner into a firm without the consent of all the existing partners.

31(2) — Rights and liabilities of new partner

- Subject to the provisions of section 30,
- a person who is introduced as a partner into a firm does not thereby become liable for any acts of the firm done before he became a partner.

This rule has following exceptions :

(a) An incoming partner is liable for the acts done before his admission if

(i) The new firm, including the new partner who joins it, may agree to assume liability for the existing debts of the old firm and

(ii) creditors may agree to accept the new firm as their debtor and discharge the old partners. A minor on attaining majority decides to become a partner ,is liable for all acts of the firm SINCE he was admitted to the benefits of partnership (Sec 30)

Q. 16 How a change in the constitution takes place?

Ans. The change in constitution of a firm takes place in the following cases :

- Where a new partner or partners come in
- Where some partner or partners go out, i.e., by death or retirement
- Where the partnership concerned carries on business other than the business for which it was originally formed
- Where the partnership business is carried on after the expiry of the term fixed for the purpose.

Q. 17 What are the rights and duties of a partner after a change in the constitution in the firm?

Ans. **Subject to the contract between the partners, —**

the mutual rights and duties of the partners in the reconstituted firm remain the same as they were immediately before the change in the firm. Section 17 provides for the following 3 types of changes :

- after a change in the firm Sec 17 (a)
- after the expiry of the term of the firm Sec 17 (b)
- where additional undertakings are carried out Sec 17 (c)

Q. 18 Can a partner exceed his authority in an emergency? what are his rights in an emergency ?

Ans. **Partner's authority in an emergency (section 21)**

- A partner has authority, 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,
- acting under similar circumstances, and such acts bind the firm.

Q. 19 Define partnership property and property of a partner?

Ans. **The Property Of The Firm (Section 14)**

The expression 'property of the firm', also referred to as 'partnership property', 'partnership assets', 'joint stock', 'common stock' or joint estate', denotes all property, rights and interests to which the firm i.e. all partners collectively, may be entitled.

The property which is deemed as belonging to the firm, in the absence of any agreement between the partners showing contrary intention, is comprised of the following items:

(i) all property, rights and interests which partners may have brought into the common stock–as their contribution to the common business;

(ii) all the property, rights and interest acquired or purchased by or for the firm, or for the purposes and in the course of the business of the firm; and

(iii) Goodwill of the business.

Property of a partner: Where the property is exclusively belonging to a person, it does not become a property of the partner- ship merely because it is used for the business of the partner-ship, such property will become property of the partnership if there is an agreement

Q. 20 What is the effect on continuing guarantee on change in constitution of partnership?

Ans. According to section 38, in the absence of an agreement to the contrary,

- a continuing guarantee given to a firm or to third party
- in respect of the transaction of a firm is,
- revoked as to future transactions
- from the date of any change in the constitution of the firm

UNIT – 3

REGISTRATION AND DISSOLUTION OF FIRM

Q. 1 How an application of registration of firm is to be made?

OR

What is the procedure for registration of firm?

Ans. **Application for registration (section 58):**

1. The registration of a firm may be effected at any time by sending by post or delivering to the REGISTRAR of the area in which any place of business of the firm is situated or proposed to be situated, a statement in the prescribed form and accompanied by the prescribed fee, stating-
   (a) The firm's name
   (b) The place or principal place of business of the firm,
   (c) The names of any other places where the firm carries on business,
   (d) the date when each partner joined the firm,
   (e) the names in full and permanent addresses of the partners, and
   (f) the duration of the firm.

The statement shall be signed by all the partners, or by their agents specially authorised in this behalf.

2. Each person signing the statement shall also verify it in the manner prescribed.

3. 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 State Government signifies its consent to the use of such words as part of the firm-name by order in writing.

Q. 2 When Registrar shall issue a registration certificate?

Ans. **Registration (section 59):**

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, and shall file the statement.

However, registration is deemed to be completed as soon as an application in the prescribed form with the prescribed fee and necessary details concerning the particulars of partnership is delivered to the Registrar. The recording of an entry in the register of firms is a routine duty of Registrar.

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 first and get the firm registered and then file a fresh suit.

Q. 3 Is it necessary to get the firm registered? what are the consequences of non registration ?

OR

The non registration of a firm attracts certain disabilities. Comment.

Ans. The Indian Partnership Act does not make the registration of firms compulsory nor does it impose any penalty for non-registration. However, under Section 69, non-registration of partnership gives rise to a number of disabilities which are as follows:

No suit in a civil court by firm or other co-partners against third party —

- The firm or any other person on its behalf
- cannot bring an action against the third party
- for breach of contract entered into by the firm,
- unless the firm is registered and
- the persons suing are or have been shown in the register of firms as partners in the firm.

No relief to partners for set- off of claim —

- If an action is brought against the firm by a third party,
- then neither the firm nor the partner can claim any set-off,
- if the suit be valued for more than Rs. 100 or
- pursue other proceedings to enforce the rights arising from any contract.

Aggrieved partner cannot bring legal action against other partner or the firm —

- A partner of an unregistered firm (or any other person on his behalf)
- is precluded from bringing legal action
- against the firm or any person alleged to be or to have been a partner in the firm.
- But, such a person may sue for
- dissolution of the firm or for accounts and realization of his share in the firm's property where the firm is dissolved.

Third party can sue the firm —

- In case of an unregistered firm,
- an action can be brought against the firm by a third party.

Q. 4 Even if the firm is unregistered, it does not affects certain rights ?

OR

The non registration of a firm attracts some disability. What are the exceptions to these disabilities?

Ans. **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 Assignees, Receiver of Court to release the property of the insolvent partner and to bring an action.
4. The right to sue or claim a set-off if the value of suit does not exceed Rs. 100 in value.

Q. 5 Distinguish between Dissolution of firm and Dissolution of Partnership?

Ans. According to Section 39 of the Indian Partnership Act, 1932, the dissolution of partnership between all partners of a firm is called the 'dissolution of the firm'.

In the case of dissolution of the firm, the whole firm is dissolved. The partnership terminates as between each and every partner of the firm.

But when only one or more partners retires or becomes incapacitated from acting as a partner

due to death, insolvency or insanity, the partnership, i.e. the relationship between such a partner and other is dissolved, but the other partner decides to continues the business .

Basis	Dissolution of Firm	Dissolution of Partnership
Continuation of business	It involves discontinuation of business in partnership.	It doesnot affect continuation of business. It involves only reconstitution of the firm.
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.
Order of court	A firm may be dissolved by the order of the court.	Dissolution of partnership is NOT ordered by the court.
Scope	It necessarily involves dissolution of partnership.	It may or may not involve Dissolution of firm.
Final closure of books	It involves final closure of books of the firm.	It does NOT involve final closure of the books.

Q. 6 What are the modes of dissolution of firm?

Ans. The following are the modes of dissolution of firm ?

I. Dissolution without the order of court.

II. Dissolution by the order of the court .

I. **Dissolution without the order of court or Voluntary dissolution : It consists of following four types:**

Dissolution by agreement (Section 40) —

- Section 40 gives rights to the partners to dissolve the firm with the consent of all the partners or
- in accordance with a contract between the partners.
- Contract between the partners' means a contract already made.

Compulsory dissolution (Section 41) —

- A firm is compulsorily dissolved
- by the happening of any event
- which makes it unlawful for the business of the firm
- to be carried on or for the partners to carry it on in partnership:

Provided that,

- when more than one separate adventure or undertaking is carried on by the firm,
- the illegality of one or more shall not of itself
- cause the dissolution of the firm in respect of its lawful adventures and undertakings.

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 :

- where the firm is constituted for a fixed term, on the expiry of that term
- where the firm is constituted to carry out one or more adventures or undertaking, then by completion thereof
- by the death of a partner, and
- by the adjudication of a partner as an insolvent

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.

Q.. 7 What are the modes of dissolution of firm by the order of Court?

Or

In which circumstances, the court will order for dissolution of firm ?

Ans. **Dissolution by the court (section 44)**

The Court may, at the suit of the partner, dissolve a firm on any of the following ground:

Insanity/ unsound mind —

- Where a partner (not a sleeping partner)
- has become of unsound mind,
- the court may dissolve the firm
- on a suit of the other partners or by the next friend of the insane partner.
- Temporary sickness is no ground for dissolution of firm.

Permanent incapacity —

- When a partner, other than the partner suing,
- has become in any way permanently incapable
- of performing his duties as partner,
- then the court may dissolve the firm.
- Such permanent incapacity may result from physical disability or illness etc.

Misconduct —

- Where a partner, other than the partner suing,
- is guilty of conduct which is likely to affect
- prejudicially the carrying on of business,
- the court may order for dissolution of the firm, by giving regard to the nature of business. .
- It is not necessary that misconduct must relate to the conduct of the business.
- The important point is the adverse effect of misconduct on the business. In each case nature of business will decide whether an act is misconduct or not.

Persistent breach of agreement —

- Where a partner other than the partner suing,
- 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,

Transfer of interest —

- Where a partner other than the partner suing,
- has transferred the whole of his interest in the firm to a third party or
- has allowed his share to be charged or sold by the court, in the recovery of arrears of land revenue,
- the court may dissolve the firm at the instance of any other partner.

Continuous/ Perpetual losses —

- Where the business of the firm cannot be carried on
- EXCEPT at a loss in future also,
- the court may order for its dissolution.

Just and equitable grounds —

- Where the court considers any other ground
- to be just and equitable for the dissolution of the firm,
- it may dissolve a firm. The following are the cases for the just and equitable grounds :

  (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 On a stock exchange

Q. 8 What are the rights and liabilities consequent to dissolution of firm?

Ans. **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,
- Untill public notice is given of the dissolution.

Therefore Section 45 has two fold objectives-

1. It seeks to protect third parties dealing with the firm who had no notice of prior dissolution and
2. It also seeks to protect partners of a dissolved firm from liability towards third parties

However, there are exceptions to the Section 45 i.e. where notice of dissolution has NOT been given, there will be NO liability for subsequent acts in the case of:

(a) the estate of a deceased partner,

(b) an insolvent partner, or

(c) a dormant partner, i.e., a partner, who was not known as a partner to the person dealing with the firm.

(2) Notices under sub-section (1) may be given by any partner.

Right of partners to have business wound up after dissolution (Section 46) —

- On the dissolution 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 (Section 47) —

- EVEN after the dissolution of a firm
- the authority of each partner to bind the firm, and the other mutual rights and obligations of the partners, CONTINUES ,
- so far as may be necessary to wind up the affairs of the firm and to complete transactions begun but unfinished at the time of the dissolution, but not otherwise:

Provided that the firm is in no case bound by the acts of a partner who has been adjudicated insolvent;

However this proviso does not affect the liability of any person who has after the adjudication represented himself or knowingly permitted himself to be represented as a partner of the insolvent.

Q. 9 How accounts of partnership firm is settled after dissolution?

Ans. Settlement of partnership accounts (Section 48): In settling the accounts of a firm after dissolution, prima facie, ac- counts between the partners shall be settled in the manner prescribed by partnership agreement.

However the following rules shall, subject to agreement by the partners, be observed:-

(i) Losses, including deficiencies of capital, shall be paid first out of PROFITS, next out of CAPITAL , and lastly, if necessary, by the partners individually in the proportions in which they were entitled to share profits.

(ii) The assets of the firm, including any sums contributed by the partners to make up deficiencies of capital, must be applied in the following manner and order:

(a) in paying the debts of the firm to third parties;

(b) in paying to each partner rateably what is due to him from capital;

(c) in paying to each partner rateably what is due to him on account of capital; and

(d) the residue, if any, shall be divided among the partners in the proportions in which they were entitled to share profits.

Q. 10 How the firm's property and separate property of a partner shall be applied for the payments of the debts of the firm and debts of each partner?

Ans. **Payment of firm debts and of separate debts (Section 49):**

Where there JOINT DEBTS due from the firm and also SEPA- RATE debts due from any partner:

(i) the property of the firm shall be applied

- Firstly in payment of the debts of the firm, and
- if there is any surplus, then the share of each partner shall be applied to the payment of his separate debts or paid to him;

be applied to the payment of his separate debts or paid to him;

(ii) 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.

CHAPTER 4 THE LIMITED LIABILITY PARTNERSHIP ACT, 2008

Q.1 Give a brief introduction of LLP Act, 2008?

Ans. The Parliament passed the Limited Liability Partnership Bill on 12th December, 2008 and the President of India has as sented the Bill on 7th January, 2009 and called as the Limited Liability Partnership Act, 2008.

This Act have been enacted to make provisions for the formation and regulation of Limited Liability Partnerships and for matters connected there with or incidental thereto.

The LLP Act, 2008 has 81 sections and 4 schedules.

The First Schedule deals with mutual rights and duties of partners, as well limited liability partnership and its partners where there is absence of a 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.

Q.2 Define LLP?

Ans. **A LLP is a new form of legal business entity with limited liability.**

It is an alternative corporate business vehicle that not only gives the benefits of limited liability at low compliance cost but allows its partners the flexibility of organising their internal structure as a traditional partnership.

The LLP is a separate legal entity and while the LLP itself will be liable for the full extent of its assets, the liability of the partners will be limited.

LLP is an alternative corporate business form that gives the benefits of limited liability of a company and the flexibility of a partnership.

Since LLP contains elements of both 'a corporate structure' as well as 'a partnership firm structure' LLP is called a hybrid between a company and a partnership.

Non-applicability of the Indian Partnership Act, 1932 (Section 4): Save as otherwise provided, the provisions of the Indian Partnership Act, 1932 shall not apply to a LLP.

Q. 3 Define the following :

Ans. **Body Corporate [(Section 2(d)]:**

It means a company as defined in **clause (20) of section 2 of the Companies Act, 2013** and includes:

(i) a limited liability partnership registered under this Act;

(ii) a limited liability partnership 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 clause (20) of section 2 of the Companies Act, 2013** or a limited liability partnership as defined in this Act), which the Central Government may, by notification in the Official Gazette, specify in this behalf.

Business [Section 2(e)]:

"Business" includes **every trade, profession, service and occupation except any activity which the Central Government may, by notification, exclude**

"Small limited liability partnership [Section 2(ta)]: It means a limited liability partnership—

(i) the contribution of which, does not exceed twenty-five lakh rupees or such higher amount, not exceeding five 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 forty lakh rupees or such higher amount, not exceeding fifty 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;

Financial Year [Section 2(f)]

- " 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.

Limited liability partnership [Section 2(n)]

Limited Liability Partnership means a partnership formed and registered under this Act.

Limited Liability partnership agreement [Section 2(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.

Partner [Section 2(q)]

Partner, in relation to a LLP, means any person who becomes a partner in the LLP in accordance with the LLP agreement.

Designated Partner [Section 2(j)]

" Designated partner" means any partner designated as such pursuant to section 7.

Entity [Section 2(k)]

"Entity" means any body corporate and includes, for the purposes of sections 18, 46, 47, 48, 49, 50, 52 and 53, a firm setup under the Indian Partnership Act, 1932.

Foreign LLP [section 2(m)]

It means a LLP formed, incorporated or registered outside India which establishes a place of business within India.

Q. 4 Who is eligible to be a partner in a LLP?

Ans. **Partners (Section 5):**

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.

Q. 5 How many persons should be there to form a LLP?

Ans. **Minimum number of partners (Section 6):**

(i) Every LLP shall have at least two partners.

(ii) What if no of partners reduced below two ;

- If at any time the number of partners of a LLP is reduced below two and
- the LLP carries on business for more than six months while the number is so reduced,
- the person, who is the only partner of the LLP during the time carries on business after those six 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 the period.

Q. 6 Write a short note on designated partners?

Ans. **Designated partners (Section 7):**

1. Every limited liability partnership shall have at least two designated partners who are individuals and at least one of them shall be a resident in India:

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

Explanation - For the purposes of this section, the term resident in India means a person who has stayed in India for a period of not less than one hundred and **twenty days during the financial year**.

2. Subject to the provisions of sub-section (1),

(i) if the incorporation document

(a) specifies who are to be designated partners, such persons shall be designated partners on incorporation; or

(b) states that each of the partners from time to time of limited liability partnership is to be designated partner, every partner shall be a designated partner;

(ii) any partner may become a designated partner by and in accordance with the limited liability

partnership agreement and a partner may cease to be a designated partner in accordance with limited liability partnership agreement.

3. An individual shall not become a designated partner in any limited liability partnership unless he has given his prior consent to act as such to the limited liability partnership in such form and manner as may be prescribed.
4. Every limited liability partnership shall file with the Registrar the particulars of every individual who has given his consent to act as designated partner in such form and manner as may be prescribed within thirty days of his appointment.
5. An individual eligible to be a designated partner shall satisfy such conditions and requirements as may be prescribed.
6. Every designated partner of a limited liability partnership shall obtain a Designated Partners Identification Number (DPIN) from the Central Government and the provisions of **sections 153 to 159 (both inclusive) of the Companies Act, 2013** shall apply mutatis mutandis for the said purpose.

Q. 7 What are the salient features of a LLP?

Ans. The salient features of a LLP are

LLP is a body corporate —

- Section 2(1)(d) of the LLP Act, 2008 provides that a LLP is a body corporate formed and incorporated under this Act and
- is a legal entity separate from that of its partners and shall have perpetual succession.
- Therefore, any change in the partners of a LLP shall not affect the existence, rights or liabilities of the LLP.
- Section 3 of LLP Act provides that a LLP is a body corporate formed and incorporated under this Act and is a legal entity separate from that of its

Perpetual Succession —

- The LLP can continue its existence irrespective of changes in partners.
- Death, insanity, retirement or insolvency of partners has no impact on the existence of LLP.
- It is capable of entering into contracts and holding property in its own name.

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.
- In other words, creditors of LLP shall be the creditors of LLP alone.

Mutual Agency —

- No partner is liable on account of the independent or un- authorized actions of other partners, thus individual partners are shielded from joint liability created by another partner's wrongful business decisions or misconduct.
- In other words, all partners will be the agents of the LLP alone. No one partner can bind the other partner by his acts.

Artificial Legal Person —

- A LLP is an artificial legal person because it is created by a legal process and is clothed with all rights of an individual.
- It can do everything which any natural person can do, except it cannot be sent to jail, cannot take an oath, cannot marry or get divorce nor can it practice a learned profession like CA or Medicine.
- A LLP is invisible, intangible, immortal (it can be dissolved by law alone) but not fictitious because it really exists.

Common Seal —

- A LLP being an artificial person can act through its partners and designated partners.
- LLP may have a common seal, if it decides to have one [Section 14(c)].
- Thus, it is not mandatory for a LLP to have a common seal.
- It shall remain under the custody of some responsible official and it shall be affixed in the presence of at least 2 designated partners of the LLP.

Limited Liability —

- Every partner of a LLP is, for the purpose of the business of LLP, the agent of the LLP, but not of other partners (Section 26).
- The liability of the partners will be limited to their agreed contribution in the LLP. Such contribution may be of tangible or intangible nature or both.

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.

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.

LLP Agreement —

- Mutual rights and duties of the partners within a LLP are governed by an agreement between the partners.
- The LLP Act, 2008 provides flexibility to partner to devise the agreement as per their choice.
- In the absence of any such agreement, the mutual rights and duties shall be governed by the provisions of the LLP Act, 2008.

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.

Q. 8 What are the advantages of LLP form?

Ans. **The advantages of LLP form are**

(a) Easy to dissolve

(b) Flexible capital structure

(c) All partners enjoy limited liability

(d) Easy to form

(e) provides flexibility without imposing detailed legal and procedural requirements.

(f) is organized and operates on the basis of an agreement.

Q. 9 What is the procedure to incorporate LLP ?

Ans. **For a LLP to be incorporated:**

- Two or more persons associated
- for carrying on a lawful business
- with a view to profit shall subscribe their names to an incorporation document;

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

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 Company Secretary or a Chartered Accountant or a Cost Accountant, who is engaged in the formation of the LLP and
- by anyone 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.

The incorporation document shall—

(a) be in a form as may be prescribed;

(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;

The incorporation document shall—

(a) be in a form as may be prescribed;

(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 the 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.

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.

Q. 10 What are the effects of Registration of LLP?

Ans. When the requirements imposed by clauses (b) and (c) of sub-section (1) of section 11 have been complied with, the Registrar shall retain the incorporation document and, unless the requirement imposed by clause (a) of that sub-section has not been complied with,

he shall, within a period of 14 days—

(a) register the incorporation document; and

(b) give a certificate that the LLP is incorporated by the name specified therein.

The certificate issued under clause (b) of sub-section (1) shall be signed by the Registrar and authenticated by his official seal. The certificate shall be conclusive evidence that the LLP is incorporated by the name specified therein.

On registration a LLP shall ,by its name, be capable of

suing and being sued	acquiring, owning, holding and developing or disposing of property, whether movable or immovable, tangible or intangible	doing and suffering such other acts and things as bodies corporate may lawfully do and suffer.	Having common seal, if it decides to have one.

Q 11 Write Short Note on Registered office of LLP and How it can be change?

Registered office of LLP and change therein (Section 13):

1. Every limited liability partnership 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 limited liability partnership or a partner or designated partner thereof by sending it by post under a certificate of posting or by registered post or by any other manner, as may be prescribed, at the registered office and any other address specifically declared by the limited liability partnership for the purpose in such form and manner as may be prescribed.
3. A limited liability partnership may change the place of its registered office and file the notice of such change with the Registrar in such form and manner and subject to such conditions as may be prescribed and any such change shall take effect only upon such filing.
4. If any default is made in complying with the requirements of this section, the limited liability partnership and its every partner shall be liable to a penalty of five hundred rupees for each day during which the default continues, subject to a maximum of fifty thousand rupees for the limited liability partnership and its every partner.

Q. 12 Explain the provisions relating to Name of LLP?

Ans. **Name (Section 15):**

1. Every limited liability partnership shall have either the words limited liability partnership or the acronym LLP as the last words of its name.
2. No limited liability partnership shall be registered by a name which, in the opinion of the Central Government is

(a) undesirable; or

(b) identical or too nearly resembles to that of any other limited liability partnership or a company or a registered trade mark of any other person under the Trade Marks Act, 1999.

Reservation of name (Section 16):

(a) 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;

(b) the name to which a LLP proposes to change its name.

(b) 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 Central Government 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

Change of name of LLP (Section 17):

1. Notwithstanding anything contained in sections 15 and 16, if through inadvertence or otherwise, a limited liability partnership, on its first registration or on its registration by a new body corporate, its registered name;"name, is registered by a name which is identical with or too nearly resembles to —

(a) that of any other limited liability partnership or a company; or

(b) a registered trade mark of a proprietor under the Trade Marks Act, 1999, as is likely to be mistaken for it, then on an application of such limited liability partnership or proprietor referred to in clauses (a) and (b) respectively or a company, the Central Government may direct that such limited liability partnership to change its name or new name within a period of three months from the date of issue of such direction:

Provided that an application of the proprietor of the registered trade marks shall be maintainable within a period of three years from the date of incorporation or registration or change of name of the limited liability partnership under this Act.

2. Where a limited liability partnership changes its name or obtains a new name under sub-section (1), it shall within a period of fifteen days from the date of such change, give notice of the change to Registrar along with the order of the Central Government, who shall carry out necessary changes in the certificate of incorporation and within thirty days of such change in the certificate of incorporation, such limited liability partnership shall change its name in the limited liability partnership agreement.

3. If the limited liability partnership is in default in complying with any direction given under sub-section (1), the Central Government shall allot a new name to the limited liability partnership in such manner as may be prescribed and the Registrar shall enter the new name in the register of limited liability partnerships in place of the old name and issue a fresh certificate of incorporation with new name, which the limited liability partnership shall use thereafter:

Provided that nothing contained in this sub-section shall prevent a limited liability partnership from subsequently changing its name in accordance with the provisions of section 16.

Q. 13 Explain the steps to incorporate the LLP?

Ans. **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.

Incorporate LLP —

- file e form 2 for incorporating a new LLP

- E form 2 contains the details of LLP proposed to be incorporated, partners/designated partners, details and consent of the partners and designated partners to act as partners and designated partners

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

Q. 14 How mutual rights and duties of partners and LLP will be decided?

OR

How is the relationship of partners mutually and with LLP decided?

Ans. **Section 22:**

- On the incorporation of a LLP,
- the persons who subscribed their names to the incorporation document shall be its partners and
- any other person may become a partner of the LLP by and in accordance with the LLP agreement.

Section 23 : Relationship of partners

- Save as otherwise provided by this Act,
- the mutual rights and duties of the partners of a LLP, and
- the mutual rights and duties of a LLP and its partners,
- shall be governed by the LLP agreement between the partners, or between the LLP and its partners. **Sec. 23 (1)**
- An agreement in writing made before the incorporation of a LLP
- between the persons who subscribe their names to the incorporation document
- may impose obligations on the LLP,
- provided such agreement is ratified by all the partners after the incorporation of the LLP.

Sec. 23 (3)

- In the absence of agreement as to any matter,
- the mutual rights and duties of the partners and
- the mutual rights and duties of the LLP and the partners

Q. 15 Cessation of Partnership Interest Section 24

Ans. **How a person may cease to be a partner from a LLP?**

Voluntarily :

A person may cease to be a partner of a LLP

- in accordance with an agreement with the other partners or,
- in the absence of agreement with the other partners as to cessation of being a partner, by giving a notice in writing of not less than 30 days to the other partners of his intention to resign as partner. **Sec. 24 (1)**

Compulsorily :

A person shall cease to be a partner of a LLP—

- on his death or dissolution of the LLP; or
- if he is declared to be of unsound mind by a competent court; or
- if he has applied to be adjudged as an insolvent or declared as an insolvent. **Sec. 24 (2)**

After cessation, can he still be deemed to be a partner? Sec. 24 (3)

Where a person has ceased to be a partner of a LLP (here in after referred to as "former partner"),

the former partner is to be regarded (in relation to any person dealing with the LLP) as still being a partner of the LLP unless—

(a) the person has notice that the former partner has ceased to be a partner of the LLP; or

(b) notice that the former partner has ceased to be a partner of the LLP has been delivered to the Registrar.

What are his obligations after cessation?

The cessation of a partner from the LLP does not by itself discharge the partner from any obligation to the LLP or to the other partners or to any other person which he incurred while being a partner. **Sec. 24 (4)**

A former partner or a person entitled to his share in consequence of the death or insolvency of the former partner shall not have any right to interfere in the management of the LLP. **Sec. 24 (6)**

What will be his rights or his legal heirs rights after cessation? Sec. 24 (5)

- Unless otherwise provided in the LLP agreement,
- where a partner of a LLP ceases to be a partner,
- the former partner or a person entitled to his share in consequence of the death or insolvency of the former partner, shall be entitled to receive from the LLP—

(a) an amount equal to the capital contribution of the former partner actually made to the LLP; and

(b) his right to share in the accumulated profits of the LLP, after the deduction of accumulated losses of the LLP, determined as at the date the former partner ceased to be a partner.

Q. 16 What are the rules relating to registration of changes in partners?

Ans. **Section 25** : The following provisions are to be complied with –

1. Every partner shall inform the limited liability partnership of any change in his name or address within a period of fifteen days of such change.
2. A limited liability partnership shall
   (a) where a person becomes or ceases to be a partner, file a notice with the Registrar within thirty days from the date he becomes or ceases to be a partner; and
   (b) where there is any change in the name or address of a partner, file a notice with the Registrar within thirty days of such change.
3. A notice filed with the Registrar under sub-section (2)

(a) shall be in such form and accompanied by such fees as may be prescribed;

(b) shall be signed by the designated partner of the limited liability partnership and authenticated in a manner as may be prescribed; and

(c) if it relates to an incoming partner, shall contain a statement by such partner that he consents to becoming a partner, signed by him and authenticated in the manner as may be prescribed.

4. **If the limited liability partnership contravenes the provisions of sub- section (2), the limited liability partnership and its every designated partner shall be liable to a penalty of ten thousand rupees.**

5. **If the contravention referred to in sub- section (1) is made by any partner of the limited liability partnership, such partner shall be liable to a penalty of ten thousand rupees.**

6. Any person who ceases to be a partner of a limited liability partnership may himself file with the Registrar the notice referred to in sub-section (3) if he has reasonable cause to believe that the limited liability partnership may not file the notice with the Registrar and in case of any such notice filed by a partner, the Registrar shall obtain a confirmation to this effect from the limited liability partnership unless the limited liability partnership has also filed such notice: Provided that where no confirmation is given by the limited liability partnership within fifteen days, the Registrar shall register the notice made by a person ceasing to be a partner under this section.

Q. 17 What are the rules relating to extent of liability of a partner and that of LLP under LLP Act, 2008?

Ans. The following provisions are to be complied with –

Partner as agent

Every partner of a LLP is, for the purpose of the business of the LLP, the agent of the LLP, but not of other partners. **(Section 26)**

Extent of liability of LLP (Section 27)

1. A LLP is not bound by anything done by a partner in dealing with a person if—

(a) the partner in fact has no authority to act for the LLP in doing a particular act; and

(b) the person knows that he has no authority or does not know or believe him to be a partner of the LLP.

2. The LLP is liable if a partner of a LLP is liable to any person as a result of a wrongful act or omission on his part in the course of the business of the LLP or with its authority.
3. An obligation of the LLP whether arising in contract or otherwise, shall be solely the obligation of the LLP.
4. The liabilities of the LLP shall be met out of the property of the LLP.

Extent of liability partner (Section 28)

1. A partner is not personally liable, directly or indirectly for an obligation referred to in section 27(3) solely by reason of being a partner of the LLP.
2. The provisions of Section 27(3) and Section 28 (1) shall not affect the personal liability of a partner for his own wrongful act or omission, but a partner shall not be personally liable for the wrongful act or omission of any other partner of the LLP.

Q. 18 What do you mean by Partner by Holding Out?

Ans. **Holding out (Section 29):**

1. **Any person,**
   - who by words spoken or written or by conduct,
   - represents himself, or knowingly permits himself to be represented to be a partner in a LLP
   - is liable to any person
   - who has on the faith of any such representation
   - given credit to the LLP, whether the person representing himself or represented to be a partner
   - does or does not know that the representation has reached the person so giving credit.

However,

- where any credit is received by the LLP as a result of such representation,
- the LLP shall,

- without prejudice to the liability of the person so representing himself or represented to be a partner,
- be liable to the extent of credit received by it or any financial benefit derived thereon.

2. Where

- after a partner's death the business is continued in the same LLP name,
- the continued use of that name or of the deceased part- ner's name as a part thereof
- shall not of itself make his legal representative or his estate liable
- for any act of the LLP done after his death.

Q. 19 How a LLP can be wound up?

Ans. **Winding up and dissolution (Section 63):** The winding up of a LLP may be either voluntary or by the Tribunal and LLP, so wound up may be dissolved.

Circumstances in which LLP may be wound up by Tribunal (Section 64): A LLP may be wound up by the Tribunal:

(a) if the LLP decides that LLP be wound up by the Tribunal;

(b) if, for a period of more than six months, the number of partners of the LLP is reduced below two;

(c) if the LLP is unable to pay its debts;

(d) if the LLP has acted against the interests of the sovereignty and integrity of India, the security of the State or public order;

(e) if the LLP has made a default in filing with the Registrar the Statement of Account and Solvency or annual return for any five consecutive financial years; or

(f) if the Tribunal is of the opinion that it is just and equitable that the LLP be wound up.

Q. 20 Difference between

(a) LLP and Partnership firm

(b) LLP and Limited Liability company

Ans. **(a) LLP and PARTNERSHIP FIRM —**

BASIS	LLP	PARTNERSHIP FIRM
Regulating Act	It is regulated by The Limited Liability Partnership Act, 2008.	It is regulated by The Indian Partnership Act, 1932.
Body corporate	It is a body corporate.	It is not a body corporate,
Separate legal entity	It is a legal entity separate from its members.	It is a group of persons with no separate legal entity.
Creation	It is created by a legal process called registration under the LLP Act, 2008.	It is created by an agreement between the partners.
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.
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.
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.

Liability	Liability of each partner limited to the extent to agreed contribution except in case of will ful fraud.	Liability of each partner is unlimited. It can be extended upto the personal assets of the partners.
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.
Designated partners	At least two designated partners and atleast one of them shall be resident in India.	There is no provision for such partners under the partnership Act, 1932.
Common seal	It may have its common seal as its official signatures.	There is no such concept in partnership
Legal compliances	Only designated partners are responsible for all the compliances and penalties under this Act.	All partners are responsible for all the compliances and penalties under the Act.
Foreign partnership	Foreign nationals can become a partner in a LLP.	Foreign nationals cannot become a partner in a partnership firm.
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.

Annual Filing of documents	LLP is required to file: (i) Annual statement of accounts (ii) Statement of solvency (iii) Annual return with the registration of LLP every year.	Partnership firm is not required to file any annual document with the registrar of firms

(b) LLP and Limited liability company —

Basis	LLP	Limited Liability Company
Regulating Act	The LLP Act, 2008.	The Companies Act, 2013.
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.
Internal governance structure	The internal governance structure of a LLP is governed by contract agreement between the partners.	The internal governance structure of a company is regulated by statute (i.e., Companies Act, 2013).
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 Pvt. Co. to contain the word "Private limited" as suffix.
No. of members/partners	Minimum – 2 members Maximum – No such limit on the members in the Act.	**Private company**: Minimum – 2 members Maximum 200 members **Public company**:

	The members of the LLP can corporate through the nominees.	Minimum – 7 members Maximum – No such limit on the members. Members can be organizations, trusts, another business form or individuals.
Liability of members/ partners	Liability of a partners is limited to the extent of agreed contribution in case of intention is fraud.	Liability of a member is limited to the amount unpaid on the shares held by them.
Management	The business of the company managed by the partners including the designated partners authorized in the agreement.	The affairs of the company are managed by board of directors elected by the shareholders.
Minimum number of directors/ designated partners	Minimum 2 designated partners.	Pvt. Co. – 2 directors Public co. – 3 directors

Q. 2.1 What is the liability of partners and LLP in case of fraud?

Ans. Unlimited liability in case of fraud (Section 30):

1. In the event of an act carried out by a limited liability partnership, or any of its partners, with intent to defraud creditors of the limited liability partnership or any other person, or for any fraudulent purpose, the liability of the limited liability partnership and partners who acted with intent to defraud creditors or for any fraudulent purpose shall be unlimited for all or any of the debts or other liabilities of the limited liability partnership:

Provided that in case any such act is carried out by a partner, the limited liability partnership is liable to the same extent as the partner unless it is established by the limited liability partnership that such act was without the knowledge or the authority of the limited

liability partnership.

2. Where any business is carried on with such intent or for such purpose as mentioned in sub-section (1), every person who was knowingly a party to the carrying on of the business in the manner aforesaid shall be punishable with imprisonment for a term which may extend to five years and with fine which shall not be less than fifty thousand rupees but which may extend to five lakh rupees.
3. Where a limited liability partnership or any partner or designated partner or employee of such limited liability partnership has conducted the affairs of the limited liability partnership in a fraudulent manner, then without prejudice to any criminal proceedings which may arise under any law for the time being in force, the limited liability partnership and any such partner or designated partner or employee shall be liable to pay compensation to any person who has suffered any loss or damage by reason of such conduct:

Provided that such limited liability partnership shall not be liable if any such partner or designated partner or employee has acted fraudulently without knowledge of the limited liability partnership.

Q. 2.2 What are the provisions relating to maintenance of books of accounts under LLP Act 2008?

Ans. **Maintenance of books of account, other records and audit, etc. (Section 34):**

1. The limited liability partnership shall maintain such proper books of account as may be prescribed relating to its affairs for each year of its existence on cash basis or accrual basis and according to double entry system of accounting and shall maintain the same at its registered office for such period as may be prescribed.
2. Every limited liability partnership shall, within a period of six months from the end of each financial year, prepare a Statement of Account and Solvency for the said financial year as at the last day of the said financial year in such form as may be prescribed, and such statement shall be signed by the designated partners of the limited liability partnership.
3. Every limited liability partnership shall file within the prescribed time, the Statement of Account and Solvency prepared pursuant to sub-section (2) with the Registrar every year in such form and manner and accompanied by such fees as may be prescribed.
4. The accounts of limited liability partnerships shall be audited in accordance with such rules as

may be prescribed:

Provided that the Central Government may, by notification in the Official Gazette, exempt any class or classes of limited liability partnerships from the requirements of this sub-section.

5. Any limited liability partnership which fails to comply with the provisions of sub-section (3), such limited liability partnership and its designated partners shall be liable to a penalty of one hundred rupees for each day during which such failure continues, subject to a maximum of one lakh rupees for the limited liability partnership and fifty thousand rupees for every designated partner.

6. Any limited liability partnership which fails to comply with the provisions of sub-section (1), sub-section (2) and sub-section (4), such limited liability partnership shall be punishable with fine which shall not be less than twenty-five thousand rupees, but may extend to five lakh rupees and every designated partner of such limited liability partnership shall be punishable with fine which shall not be less than ten thousand rupees, but may extend to one lakh rupees.

[34A. Accounting and auditing standards. The Central Government may, in consultation with the National Financial Reporting Authority constituted under section 132 of the Companies Act, 2013 —

(a) prescribe the standards of accounting; and

(b) prescribe the standards of auditing, as recommended by the Institute of Chartered Accountants of India constituted under section 3 of the Chartered Accountants Act, 1949, for a class or classes of limited liability partnerships.]

Q. 23 What are the provisions relating to filing of annual returns under LLP Act 2008?

Ans. **Annual return (Section 35):**

1. Every limited liability partnership shall file an annual return duly authenticated with the Registrar within sixty days of closure of its financial year in such form and manner and accompanied by such fee as may be prescribed.

2. If any limited liability partnership fails to file its annual return under sub- section (1) before the expiry of the period specified therein, such limited liability partnership and its designated partners shall be liable to a penalty of one hundred rupees for each day during which such

failure continues, subject to a maximum of one lakh rupees for the limited liability partnership and fifty thousand rupees for designated partners.

Q. 24 What are the provisions relating to conversion of a firm, private company, unlisted public company into a LLP?

Ans.

Conversion from firm into LLP (Section 55):	Conversion from private company into LLP (Section 56):	Conversion from unlisted public company into LLP (Section 57):
• A firm may convert into a LLP • in accordance with the provisions of this Chapter and • the Second Schedule	• A private company may convert into a LLP • in accordance with the provisions of this Chapter and • the third schedule	• An unlisted public company may convert into a LLP • in accordance with the provisions of this chapter and • the fourth schedule

Registration of conversion (Section 58)

- The Registrar, on satisfying that a firm, private company or an unlisted public company, as the case may be, has complied with the provisions of the various Schedules, provisions of this Act and the rules made thereunder,
- register the documents and issue a certificate of registration in such form as the Registrar may determine
- stating that the LLP is, on and from the date specified in the certificate, registered under this Act.
- The LLP shall, within 15 days of the date of registration,
- inform the concerned Registrar of Firms or Registrar of Companies, as the case may be,
- about the conversion and of the particulars of the LLP in such form and manner

Effect of Registration: Notwithstanding anything contained in any other law for the time being in force, on and from the date of registration specified in the certificate of registration issued under the various Schedule, as the case may be,—

- there shall be a LLP by the name specified in the certificate of registration registered under this Act;
- all tangible (movable or immovable) and intangible property vested in the firm or the company,

as the case may be, all assets, interests, rights, privileges, liabilities, obligations relating to the firm or the company, as the case may be, and the whole

- all tangible (movable or immovable) and intangible property vested in the firm or the company, as the case may be, all assets, interests, rights, privileges, liabilities, obligations relating to the firm or the company, as the case may be, and the whole of the undertaking of the firm or the company, as the case may be,

shall be transferred to and shall vest in the limited liability partnership without further assurance, act or deed; and

the firm or the company, as the case may be, shall be deemed to be dissolved and removed from the records of the Registrar of Firms or Registrar of Companies, as the case may be.

Q. 25 Write Short Note on Special Courts in Section LLP Act, 2008?

67A. Establishment of Special Courts.—

1. The Central Government may, for the purpose of providing speedy trial of offences under this Act, by notification, establish or designate as many Special Courts as may be necessary for such area or areas, as may be specified in the notification.

2. The Special Court shall consist of—

(a) a single Judge holding office as Sessions Judge or Additional Sessions Judge, in case of offences punishable under this Act with imprisonment of three years or more; and

(b) a Metropolitan Magistrate or a Judicial Magistrate of the first class, in the case of other offences, who shall be appointed by the Central Government with the concurrence of the Chief Justice of the High Court:

Provided that until Special Courts are designated or established under sub- section (1), the Courts designated as Special Courts in terms of section 435 of the Companies Act, 2013 shall be deemed to be Special Courts for the purpose of trial of offences punishable under this Act:

Provided further that notwithstanding anything contained in the Code of Criminal Procedure, 1973, any offence committed under this Act, which is triable by a Special Court shall, until a Special Court is established under this Act or the Companies Act, 2013, be tried by a Court of Sessions or the Court of Metropolitan Magistrate or a Judicial Magistrate of the first class, as the case may be, exercising jurisdiction over the area.]

67B. Procedure and powers of Special Court—

1. Notwithstanding anything contained in the Code of Criminal Procedure, 1973, all offences specified under sub- section (1) of section 67A shall be triable only by the Special Court established or designated for the area in which the registered office of the limited liability partnership is situated in relation to which the offence is committed or where there are more than one Special Courts for such area, by such one of them as may be specified in this behalf by the High Court concerned.
2. While trying an offence under this Act, a Special Court may also try an offence other than an offence under this Act with which the accused may, under the Code of Criminal Procedure, 1973 be charged at the same trial.
3. Notwithstanding anything contained in the Code of Criminal Procedure, 1973, the Special Court may, if it thinks fit, try in a summary way any offence under this Act which is punishable with imprisonment for a term not exceeding three years:

   Provided that in the case of any conviction in a summary trial, no sentence of imprisonment for a term exceeding one year shall be passed:

   Provided further that, when at the commencement of or in the course of a summary trial, it appears to the Special Court that the nature of the case is such that the sentence of imprisonment for a term exceeding one year may have to be passed or that it is, for any other reason, undesirable to try the case summarily, the Special Court shall, after hearing the parties, record an order to that effect and thereafter recall any witnesses who may have been examined and proceed to hear or re- hear the case in accordance with the procedure for the regular trial.

67C. Appeal and revision—

The High Court may exercise, so far as may be applicable, all the powers conferred by Chapters XXIX and XXX of the Code of Criminal Procedure, 1973 on a High Court, as if a Special Court within the local limits of the jurisdiction of the High Court were a Court of Sessions trying cases within the local limits of the jurisdiction of the High Court.]

Q. 26 Write Short Note on —

(A) Registration offices. 68A —

1. For the purpose of exercising such powers and discharging such functions as are conferred on the Central Government by or under this Act or under rules made thereunder and for the purpose of registration of limited liability partnerships under this Act, the Central Government shall, by notification, establish such number of registration offices at such places as it thinks fit, specifying their jurisdiction.
2. The Central Government may appoint such Registrars, Additional Registrars, Joint Registrars, Deputy Registrars and Assistant Registrars as it considers necessary, for the registration of limited liability partnerships and discharge of various functions under this Act.
3. The powers and duties of the Registrars referred to in sub-section (2) and the terms and conditions of their service shall be such as may be prescribed.
4. The Central Government may direct the Registrar to prepare a seal or seals for the authentication of documents required for, or connected with the registration of limited liability partnerships.]

(B) Payment of additional fee (Section 69) —

Any document or return required to be registered or filed under this Act with Registrar, if, is not registered or filed in time provided therein, may be registered or filed after that time, on payment of such additional fee as may be prescribed in addition to any fee as is payable for filing of such document or return:

Provided that such document or return shall be filed after the due date of filing, without prejudice to any other action or liability under this Act:

Provided further that a different fee or additional fee may be prescribed for different classes of limited liability partnerships or for different documents or returns required to be filed under this Act or rules made thereunder.

CHAPTER 5 THE COMPANIES ACT, 2013

Q.1 To whom Companies Act is applicable?

Ans. **Applicability of the Companies Act, 2013:**

The provisions of the Act shall apply to-

- Companies incorporated under this Act or under any previous company law.
- Insurance companies (except where the provision of the said Act are inconsistent with the provisions of the Insurance Act, 1938 or the IRDA Act, 1999)
- Banking companies (except where the provisions of the said Act are inconsistent with the provisions of the Banking Regulation Act, 1949)
- Companies engaged in the generation or supply of electricity (except where the provisions of the above Act are inconsistent with the provisions of the Electricity Act, 2003)
- Any other company governed by any special Act for the time being in force.
- Such body corporate which are incorporated by any Act for time being in force, and as the Central Government may by notification specify in this behalf.

Q. 2 Define Company?

Ans. **Section 2(20) of the Companies Act, 2013 defines** the term 'company'. "Company means a company incorporated under this by any Act for time being Act or under any previous law.

Q. 3 Explain the features of a Company?

Ans. The main features of a company are:

Separate legal Entity :

- The most striking feature of a company is it acquires a unique character of being a separate legal entity.
- When a company is registered, it is clothed with a legal personality.
- It comes to have almost the same rights and powers as a human being.
- Its existence is distinct and separate from that of its members.
- A company can own property, have bank account, raise loans, incur liabilities and enter into contracts. (Macaura v. Northern Assurance Co. Limited)

Perpetual Succession :

- Members may die or change, but the company goes on till it is wound up on the grounds specified by the Act.
- Since a company is an artificial person created by law, law alone can bring an end to its life. Its existence is not affected by the death or insolvency of its members

Limited Liability:

- The liability of a member depends upon the kind of company of which he is a member.
- In the case of a limited liability company The liability of the members of the company is limited to the extent of the nominal value of shares held by them
- In the case of a company limited by guarantee, the members are liable only to the extent of the amount guaranteed by them and that too only when the company goes into liquidation.
- In the case of an unlimited company, the liability of its members is unlimited as well.

Artificial Legal Person:

- A company is an artificial person a sit is created by a process other than natural birth.
- It is legal or judicial as it is created by law. It is a person since Company works through the agency of human beings Common seal is the official signature of a company, which is affixed by the officers and employees of the company on its every document. The common seal is a seal used by a corporation as the symbol of its incorporation.
- The Companies (Amendment) Act, 2015 has made the common seal optional.
- 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. it is clothed with all the rights of an individual.

Q. 4 Short note on:

Artificial Legal Person —

A company is an artificial person as it is created by a process other than natural birth. It is legal or judicial as it is created by law. It is a person since it is clothed with all the rights of an individual.

Further, the company being a separate legal entity can own property, have banking account, raise loans, incur liabilities and enter into contracts.

Even members can contract with company, acquire right against it or incur liability to it. It can sue and be sued in its own name.

It can do everything which any natural person can do except be sent to jail, take an oath, marry or practice a learned profession. Hence, it is a legal person in its own sense.

As the company is an artificial person, it can act only through some human agency, viz., directors. The directors can either on their own or through the common seal (of the company) can authenticate its formal acts.

Thus, a company is called an artificial legal person.

Separate Legal Entity -

The most striking feature in the company form of organization is that it acquires a unique character of being a separate legal entity.

When a company is registered, it is clothed with a legal personality. It comes to have almost the same rights and powers as a human being. Its existence is distinct and separate from that of its members. A company can own property, have bank account, raise loans, incur liabilities and enter into contracts.

1. It is at law, a person is different altogether from the subscribers to the memorandum of association. Its personality is distinct and separate from the personality of those who compose it.

2. Even members can contract with company, ac quire right against it or incur liability to it.

A company is capable of enjoying and disposing of property in its own name.

Although the capital and assets are contributed by the shareholders, the company becomes the owner of its capital and assets. The share holders are not the private or joint owners of

the company's property.

A member does not even have an insurable interest in the property of the company.

(Macaura v. Northern Assurance Co. Limited .)

Q. 5 Define corporate veil?

Ans. **Corporate Veil** refers to a legal concept whereby the company is identified separately from the members of the company.

The term Corporate Veil refers to the concept that members of a company are shielded from liability connected to the company's actions.

If the company incurs any debts or contravenes any laws, the corporate veil concept implies that members should not be liable for those errors. In other words, they enjoy corporate insulation.

Thus, the shareholders are protected from the acts of the company.

(Salomon Vs. Salomon and Co Ltd)

Q. 6 Explain the facts of the case "Salomon Vs. Salomon and Co Ltd"?

Ans. **The Salomon Vs. Salomon and Co Ltd** laid down the foundation of the concept of corporate veil or independent corporate personality. In Salomon vs. Salomon & Co. Ltd. the House of Lords laid down that a company is a person distinct and separate from its members.

Facts : In this case one Salomon incorporated a company named "Salomon & Co. Ltd.", with seven subscribers consisting of himself, his wife, four sons and one daughter.

This company took over the personal business assets of Salomon for €38,782 and inturn, Salomon took 20,000 shares of € 1 each, debentures worth € 10,000 of the company with charge on the company's assets and the balance in cash.

His wife, daughter and four sons took upon € 1 share each.

Subsequently, the company went into liquidation due to general trade depression.

The unsecured creditors to the tune of £ 7,000 contended that Salomon could not be treated as a secured creditor of the company, in respect of the debentures held by him, as he was the managing director of one-man company, which was not different from Salomon and the cloak of the company was a mere sham and fraud.

Decision: It was held by Lord Mac Naughten:

"The Company is at law a different person altogether from the subscribers to the memorandum, and though it may be that after incorporation the business is precisely the same as it was before and the same persons are managers, and the same hands receive the profits, the company is not in law the agent of the subscribers or trustees for them. Nor are the subscribers, as members, liable, in any shape or form, except to the extent and in the manner provided by the Act."

Reserved in a contract of sale: Sometimes, it is expressly agreed between the seller and the buyer that in case the buyer makes default in payment of the price, the seller will resell the goods to some other person. In such cases, the seller is said to have reserved his right of resale. And he may resell the goods on buyer's default

It may be noted that in such cases, the seller is not required to give notice of resale. He is entitled to recover damages from the original buyer even if no notice of resale is given.

Q. 7 Define lifting or piercing of corporate veil under which circumstances the veil can be lifted ?

Ans. **Meaning**:

"Lifting the veil" means looking behind the company as a legal person,

i.e., disregarding the corporate entity and paying regard, to the realities behind the legal façade. Where the Courts ignore the company and concern themselves directly with the members or managers, the corporate veil may be said to have been lifted.

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

1. **To determine the character of the company**

i.e. to findout whether co-enemy or friend: In the law relating to trading with the enemy where the test of control is adopted. A company may be characterised as an enemy company, if its affairs are under the control of people of an enemy country. For this purpose, the Court may examine the character of the persons who are really at the helm of affairs of the company.(Daimler Co. Ltd. vs. Continental Tyre & Rubber Co)

2. To protect revenue/tax:

In certain matters concerning the law of taxes, duties and stamps particularly where question of the controlling interest is in issue. [S. Berendsen Ltd. vs. Commissioner of Inland Revenue]

3. To avoid a legal obligation:

Where it was found that the sole purpose for the formation of the company was to use it as a device to reduce the amount to be paid by way of bonus to workmen, the Supreme Court upheld the piercing of the veil to look at the real transaction (The Workmen Employed in Associated Rubber Industries Limited, Bhavnagar vs. The Associated Rubber Industries Ltd., Bhavnagar and another).

4. Formation of subsidiaries to act as agents:

A company may sometimes be regarded as an agent or trustee of its members, or of another company, and may therefore be deemed to have lost its individuality in favour of its principal. (Merchandise Transport Limited vs. British Transport Commission)

5. Company formed for fraud/improper conduct or to defeat law:

Where the device of incorporation is adopted for some illegal or improper purpose, e.g., to defeat or circumvent law, to de- fraud creditors or to avoid legal obligations. [Gilford Motor Co. vs. Horne]

Q. 8 How companies are classified on the basis of liability?

Ans. **(a) Company limited by shares:**

Section 2(22) of the Companies Act, 2013, defines that when the liability of the members of a company is limited by its memorandum of association to the amount (if any) unpaid on the shares held by them, it is known as a company limited by shares.

(b) Company limited by guarantee:

Section 2(21) of the Companies Act, 2013 defines it as the company having the liability of its members 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.

(c) Unlimited company:

Section 2(92) of the Companies Act, 2013 defines unlimited company as a company not having any limit on the liability of its members. In such a company, the liability of a member ceases when he ceases to be a member.

The 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. The official liquidator may call the members for their contribution towards the liabilities and debts of the company, which can be unlimited.

Q. 9 Write a short note on One Person Company?

Ans. Section 2(62) of the Companies Act, 2013 defines one person company (OPC) as a company which has only one as a member. It encourages entrepreneurship and corporatization of business. According to section 3(1)(c) of the Companies Act, 2013, OPC is a private limited company with the minimum paid up share capital as may be prescribed and has at least one member.

OPC (One Person Company) - significant features

- Only one person as member.
- Minimum paid up capital no limit prescribed.

Eligibility :

(a) Only a natural person who is an Indian citizen and ~~resident in India~~ whether resident in India or otherwise and person who has stayed in India for a period of not less than ~~182~~ 120 days during the immediately preceding financial year.
    - Shall be eligible to incorporate a OPC;
    - Shall be a nominee for the sole member of a OPC.

(b) No minor shall become member of nominee of the OPC or can hold share with beneficial interest.

Restriction :

(i) Such Company cannot be incorporated or converted into a company under section 8 of the Act. Though it may be converted to private or public companies in certain cases.

(ii) Such Company cannot carry out Non-Banking Financial Investment activities including investment in securities of any- body corporate.

(iii) No person shall be eligible to incorporate more than one OPC or become nominee in more than one such company.

~~(iv) OPC cannot convert voluntarily into any kind of company unless two years have expired from the date of incorporation, except where the paid up share capital is increased beyond fifty lakh rupees or its average annual turnover during the relevant period exceeds two crore rupees.~~

Memorandum of OPC

(a) 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.

(b) The other person whose name is given in the memorandum shall give his prior written consent and the same shall be filed with Registrar of companies at the time of incorporation.

(c) Such other person may be given the right to withdraw his consent.

(d) 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.

(e) Any such change in the name of the person shall not be deemed to be an alteration of the memorandum.

Q.10 Define Private limited company?

Ans. **Private Company [Section 2(68)]:**

"Private company" means a company having a minimum paid-up share capital as may be prescribed, and which by its articles,—

(i) Restricts the rights to transfer its shares;

(ii) except in case of One Person Company, limits the number of its members to two hundred:

Provided that where two or more persons hold one or more shares in a company jointly, they shall be treated as a single member:

Provided further that—

(A) persons who are in the employment of the company; and

(B) persons who, having been formerly in the employment of the company, were members of

the company while in that employment and have continued to be members after the employment ceased,

Shall not be included in the number of members; and

(iii) prohibits any invitation to the public to subscribe for any securities of the company

Q.11 What are the features of a limited company?

Ans. **Private company - significant points**

- No minimum paid-up capital requirement.
- Minimum number of members – 2. (except if private company is an OPC, where it will be 1).
- Maximum number of members – 200, excluding present employee-cum- members and erstwhile employee-cum-members.
- Right to transfer shares restricted
- Prohibition on invitation to subscribe to securities of the company.
- Small company is a private company.
- OPC can be formed only as a private company

Q12. Define Small Company?

Ans. **Small Company**: Small company given under the section 2(85) of the Companies Act, 2013 which means a company, other than a public company -

(i) Paid-up share capital of which does not exceed four crore rupees or such higher amount as may be prescribed

(ii) Turnover of which as per its last profit and loss account does not exceed fourty crore rupees or such higher amount as may be prescribed.

Exceptions: This section shall not apply to:

(A) a holding company or a subsidiary company;

(B) a company registered under section 8; or

(C) a company or body corporate governed by any special Act.

Q.13 Define Public company and its features?

Ans. **Public company [Section 2(71)]:**

"Public company" means a company which—

(a) is not a private company; and

(b) has a minimum paid-up share capital, as may be prescribed:

Provided that a company which is a subsidiary of a company not being a private company shall be deemed to be public company for the purposes of this Act even where such subsidiary company continues to be a private company in its articles;

Public company – significant points

- It is not a private company (Articles do not have the restricting clauses).
- Shares are freely transferable.
- No minimum paid up capital requirement.
- Minimum number of members - 7.
- Maximum numbers of members - No limit.
- Subsidiary of a public company is deemed to be a public company.

According to section 3(1)(a), a company may be formed for any lawful purpose by seven or more persons, where the company to be formed is to be a public company.

Q.14 How company is classified on the basis of control?

Ans. **Holding and subsidiary companies —**

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

[Section 2(46)].

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

(i) controls the composition of the Board of Directors; or

(ii) exercises or controls more than one-half of the total share capital either at its own or together with one or more of its subsidiary companies:

For the purposes of this section —

(i) a company shall be deemed to be a subsidiary company of the holding company

even if the control referred to in sub- clause (i) or sub-clause (ii) is of another subsidiary company of the holding company;

(ii) The composition of a company's Board of Directors shall be deemed to be controlled by another company if that other company can appoint or remove all or a majority of the directors, by exercise of some power exercisable by it at its discretion

Associate company [Section 2(6)] —

- In relation to another company, means a company inwhich that other company has a significant influence,
- but which is not a subsidiary company of the company having such influence and includes a joint venture company.

Q.15 Define government company and foreign company?

Ans. **Government company [Section 2(45)] —**

Government Company means any company in which not less than 51%of the paid-up share capital is held by-

(i) the Central Government, or

(ii) by any State Government or Governments, or

(iii) partly by the Central Government and partly by one or more State Governments and the section includes a company which is a subsidiary company of such a Government company

Foreign Company [Section 2(42)] —

It means any company or body corporate incorporated outside India which -

(i) has a place of business in India whether by itself or through an agent, physically or through electronic mode; and

(ii) conducts any business activity in India in any other manner

Q.16 Write a short note on Section 8 company?

Ans. **Formation (section 8) —**

Section 8 companies are companies which are formed to promote the charitable objects of commerce, art, science, sports, education, research, social welfare, religion, charity, protection of environment etc.

Such company intends to apply its profit in

- promoting its objects and
- prohibiting the payment of any dividend to its members.

Examples of section 8 companies are FICCI, ASSOCHAM, National Sports Club of India, CII etc.

License —

(i) Section 8 allows the Central Government to register such person or association of persons as a company with limited liability without the addition of words 'Limited' or 'Private limited' to its name, by issuing licence.

(ii) On registration the company shall enjoy same privileges and obligations as of a limited company.

Revocation of license —

The Central Government may , after giving written notice and opportunity of being heard, by order revoke the licence of the company

- Where the company contravenes any of the requirements or the conditions of this sections or
- where the affairs of the company are conducted fraudulently, or
- violative of the objects of the company or
- prejudicial to public interest.

On revocation the Registrar shall put 'Limited' or 'Private Limited' against the company's name in the register.

Order of the government —

Where a licence is revoked, the Central Government may order that the company should be amalgamated with another Sec. 8 company or the company be woundup.

Penalty/ punishment in contravention —

For company : If a company makes any default in complying with any of the requirements laid down in this section, the company shall, without prejudice to any other action under the provisions of this section, be punishable with fine which shall not be less than ten lakh rupees but which may extend to one crore rupees

Directors and every officer of the company : who is in default shall be punishable with

- ~~imprisonment for a term which may extend to three years~~ or with fine varying from twenty-five thousand rupees to twenty-five lakh rupees, ~~or with both~~ and where it is proved that the affairs of the company were conducted fraudulently, every officer in default shall be liable for action under section 447 which deals with Fraud.

Q. 17 Explain the features of Sec. 8 company?

Ans. **Section 8 Company Significant Feature —**

- Formed for the promotion of commerce, art, science, religion, charity, protection environment, sports, etc.
- Requirement of minimum share capital does not apply.
- Uses its profits for the promotion of the objective for which formed.
- Does not declare dividend to members.
- Operates under a special licence from Central Government.
- Need not use the word Ltd./ Pvt. Ltd. in its name and adopt a more suitable name such as club, chambers of commerce etc.
- Licence revoked if condition contravened.
- On revocation, Central Government may direct it to.

  (a) Converts its status and change its name. (b) Wind – up

  (c) Amalgamate with another company having similar object.
- Can call its general meeting by giving a clear 14 days notice instead of 21 days.
- Requirement of minimum number of directors, independent directors etc. does not apply.
- Need not constitute Nomination and Remuneration Committee and Shareholders Relationship Committee.
- A partnership firm can be a member of Section 8 company.

Q.18 Explain the procedure to incorporate a company?

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

Filing of the documents and information with the registrar:

For the registration of the company following documents and information are required to be filed with the registrar within whose jurisdiction the registered office of the company is proposed to be situated-

(A) The memorandum and articles of the company duly signed by all the subscribers to the memorandum

(B) a declaration by person who is engaged in the formation of the company (an advocate, a chartered accountant, cost accountant or company secretary in practice), and by a person named in the articles (director, manager or secretary of the company), that all the requirements of this Act and the rules made there under in respect of registration and matters precedent or incidental thereto have been complied with.

(C) a declaration from each of the subscribers to the memorandum 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;

(D) the address for correspondence till its registered office is established;

(E) the particulars (names, including surnames or family names, residential address, nationality) of every subscriber to the memorandum along with proof of identity, and in the case of a subscriber being a body corporate, such particulars as may be prescribed.

(F) the particulars (names, including surnames or family names, the Director Identification Number, residential address, nationality) of the persons mentioned in the articles as the subscribers to the Memorandum and such other particulars including proof of identity as

may be prescribed; and

(G) the 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 in such form and manner as may be prescribed.

- The Registrar shall issue a certificate of Registration shall allot to the company a corporate identity number, which shall be a distinct identity for the company and which shall also be included in the certificate

Q.19 What is the effect of Registration of a company?

Ans. Section 9 of the Companies Act, 2013 provides for the effect of registration of a company which provides that,

- From the date of incorporation (mentioned in the certificate of incorporation), the subscribers to the memorandum and all other persons, who may from time to time become members of the company, shall be a body corporate by the name contained in the memorandum.

Such a registered company shall be capable of exercising all the functions of an incorporated company under this Act and having perpetual succession with power to acquire, hold and dispose of property, both movable and immovable, tangible and intangible, to contract and to sue and be sued, by the said name. [State Trading Corporation of India vs. Commercial Tax Officer]. [Spencer & Co. Ltd. Madras vs. CWT Madras]. [Hari Nagar Sugar Mills Ltd. vs. S.S. Jhunjhunwala]

Effect of memorandum and articles —

- As per section 10 of the Companies Act, 2013, where the memorandum and articles when registered,
- Shall bind the company and the members thereof to the same extent.
- As if they respectively had been signed by the company and by each member, and
- An agreement to observe all the provisions of the memorandum and of the articles.
- All monies payable by any member to the company under the memorandum or articles shall be a debt due from him to the company.

Q. 20 What are the types of capital?

Ans. (a) **Nominal or Authorised or Registered capital**: This form of capital has been defined in section 2(8) of the Companies Act, 2013. "Authorised capital" or "Nominal capital" means such capital as is authorised by the memorandum of a company to be the maximum amount of share capital of the company.

(b) **Issued capital**: Section 2(50) of the Companies Act, 2013 defines "issued capital" which means such capital as the company issues from time to time for subscription of authorised capital which is offered by the company for subscription and includes the shares allotted for consideration other than cash.

(c) **Subscribed capital**: Section 2(86) of the Companies Act, 2013 defines "subscribed capital" as such part of the capital which is for the time being subscribed by the members of a company.

(d) **Called-up capital**: Section 2(15) of the Companies Act, 2013 defines "calledup capital" as 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.

Q. 21 Write a short note on Memorandum of Association?

Ans. The Memorandum of Association of company is in fact its charter; it defines its constitution and the scope of the powers of the company with which it has been established under the Act. It is the very foundation on which the whole edifice of the company is built.

Object of registering a memorandum of association:

- It contains the object for which the company is formed and therefore identifies the possible scope of its operations beyond which its actions cannot go.
- It enables shareholders, creditors and all those who deal withcompany to know what its powers are and what activities it can engage in.
- A memorandum is a public document under Section 399 of the Companies Act, 2013. Consequently, every person entering into a contract with the company is presumed to have the knowledge of the conditions contained therein.

- The shareholders must know the purposes for which his money can be used by the company and what risks he is taking in making the investment.
- The memorandum must be printed, divided into paragraphs, numbered consecutively, and signed by at least seven persons (two in the case of a private company and one in the case of One Person Company) in the presence of at least one witness, who will attest the signatures. The particulars about the signatories to the memorandum as well as the witness, as to their address, description, occupation etc., must also be entered.

As per Section 4, Memorandum of a company shall be drawn up in such form as is given in Tables A, B, C, D and E in Schedule I of the Companies Act, 2013.

Table A is a form for memorandum of association of a company limited by shares.	Table B is a form for memorandum of association of a company limited by guarantee and not having a share capital.	Table C is a form for memorandum of association of a company limited by guarantee and having a share capital.	Table D is a form for memorandum of association of an unlimited company.	Table E is a form for memorandum of association of an unlimited company and having share capital.

Q. 22 What are the contents of Memorandum of Association?

Ans. **Content of the memorandum**:

(a) the name of the company (Name Clause)

- with the last word "Limited" in the case of a public limitedcompany, or
- the last words "Private Limited" in the case of a private limited company. This clause is not applicable on the companies formed under section 8 of the Act.
- a Government company's name must end with the word"Limited".
- In the case of One Person Company, the words "One Person Company", should be included below its name.

(b) the State in which the registered office of the company (Registered Office clause) is to be situated;

(c) the objects for which the company is proposed to be incorporated and any matter considered necessary in furtherance thereof (Object clause);

(d) the liability of members of the company (Liability clause), whether limited or unlimited, and also state, —

- **in the case of a company limited by shares,** that the liability of its members is limited to the amount unpaid, if any, on the shares held by them; and
- **in the case of a company limited by guarantee,** the amount up to which each member undertakes to contribute—
  (1) to the assets of the company in the event of its being wound-up while he is a member or within one year after he ceases to be a member, for payment of the debts and liabilities of the company
  (2) to the costs, charges and expenses of winding- up and for adjustment of the rights of the contributories among them-selves;
- the amount of authorized capital (Capital Clause)
- divided into share of fixed amounts and
- the number of shares with the subscribers to the memorandum have agreed to take, indicated opposite their names, which shall not be less than one share.
- A company having share capital need not have this clause.

(e) the desire of the subscribers to be formed into a company. The Memorandum shall conclude with the association clause. Every subscriber to the Memorandum shall take at least one share, and shall write against his name, the number of shares taken by him. The above clauses of the Memorandum are called compulsory clauses or "Conditions."

Q.23 Explain the doctrine of Ultra Vires

Ans. The meaning of the term ultra vires is simply " beyond (their) powers". The legal phrase "ultra vires" is applicable only to acts done in excess of the legal powers of the doers. This presupposes that the powers are in their nature limited. To an ordinary citizen, the law permits whatever does the law not expressly forbid.

It is a fundamental rule of Company Law that the objects of a company as stated in its memorandum can be departed from only to the extent permitted by the Act - thus far and no further [Ashbury Railway Company Ltd. vs. Riche].

Since the memorandum is a " public document", it is open to public inspection. Therefore, when

one deals with a company one is deemed to know about the powers of the company. If in spite of this you enter into a transaction which is ultra vires the company, you cannot enforce it against the company.

Effect of the Doctrine of Ultra Vires

(a) In consequence, any act done or a contract made by the company which is beyond the powers not only of the directors but also of the company is wholly void and inoperative in law and is therefore not binding on the company.

(b) An act which is ultra vires the company being void, cannot be ratified even by the unanimous consent of all the shareholders.

(c) Sometimes, act which is ultra vires regularized by ratifying it subsequently. For instance, if the act is ultra vires the power of the directors, the shareholders can ratify it; if it is ultra vires the articles of the company, it can be ratified by altering the articles by a special resolution at a general meeting ; if the act is within the power of the company but is done irregularly, shareholder can validate it.

(d) 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.

The impact of the doctrine of ultra vires is that a company can neither be sued on an ultra vires transaction, nor can it sue on it.

Q.2.4 Differentiate between Memorandum of Association and Articles of Association?

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

1. **Objectives**: Memorandum of Association defines and de- limits the objectives of the company whereas the Articles of association lays down the rules and regulations for the internal management of the company. Articles determine how the objectives of the company are to be achieved.
2. **Relationship**: Memorandum defines the relationship of the company with the outside world and Articles define the relationship between the company and its members.
3. **Alteration**: Memorandum of association can be altered only under certain circumstances and in

the manner provided for in the Act. In most cases permission of the Regional Director or the Tribunal is required. The articles can be altered simply by passing a special resolution.

4. **Ultra Vires**: Acts done by the company beyond the scope of the memorandum are ultra-vires and void. These cannot be ratified even by the unanimous consent of all the shareholders. The acts ultra-vires the articles can be ratified by a special resolution of the shareholders, provided they are not beyond the provisions of the memorandum.

Q.25 Write a short note on Articles of Association?

Ans. The articles of association of a company are its rules and regulations, which are framed to manage its internal affairs. The articles of association are in fact the byelaws of the company according to which director and other officers are required to perform their functions as regards the management of the company, its accounts and audit.

Just as the memorandum contains the fundamental conditions upon which the company is allowed to be incorporated, so also the articles are the internal regulations of the company **(Guiness vs. Land Corporation of Ireland)**.

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

1. **Contains regulations**: The articles of a company shall contain the regulations for management of the company.
2. **Inclusion of matters**: The articles shall also contain such matters, as are prescribed under the rules and may also include such additional matters as may be considered necessary for its management.
3. **Contain provisions for entrenchment**: Article of Association contains provisions for entrenchment for giving an effect that the specified provisions of AOA may be altered only if conditions or procedures as are more restrictive are met or complied with.
4. **Manner of inclusion of the entrenchment provision**: The provisions for entrenchment shall only be made
   - Either on formation of a company, or
   - By an amendment in the articles agreed to by all the members of the company in the case of a public company.

5. **Notice to the registrar of the entrenchment provision**:
   Where the articles contain provisions for entrenchment , the company shall give notice to the Registrar of such provisions.
6. **Forms of articles**: The articles of a company shall be in respective forms specified in Tables, F, G, H, I and J in Schedule I as may be applicable to such company.
7. **Model articles**: A company may adopt all or any of the regulations contained in the model articles applicable to such company.

Q.26 Write a short note on Doctrine of Constructive notice?

Ans. The Memorandum and Articles of association of a company when registered with Registrar of Companies, become public documents, and they are available for inspection to any person, on the payment of a nominal fees. Section 399 confers this right of inspection to all.
It is, therefore, the duty of every person dealing with a company to inspect its documents and make sure that his contract is in conformity with their provisions.
But whether a person reads them or not, it will be presumed that he knows the contents of the documents. This kind of presumed/implied notice is called constructive notice.

By constructive notice is meant:
Whether a person reads the documents or not, he is presumed not only to have read and obtain knowledge of the contents of the documents but also understood them in their true perspective, and
Every person dealing with the company not only has the constructive notice of the memorandum and articles, but also of all the other related documents, such as Special Resolutions etc., which are required to be registered with the Registrar.

Effect: Thus, if a person enters into a contract which is beyond the powers of the company as defined in the memorandum, or outside the authority of directors as per memorandum or articles, he cannot acquire any rights under the contract against the company.

Q. 27 Explain Doctrine of Indoor Management?

According to the "Doctrine of indoor management" the outsiders, dealing with the company though are supposed to have satisfied themselves regarding the competence of the company to enter into the proposed contracts are also entitled to assume that as far as the internal compliance to procedures and regulations by the company is concerned, everything has been done properly. They are bound to examine the registered documents of the company and ensure that the proposed dealing is not inconsistent therewith, but they are not bound to do more.

They are fully entitled to presume regularity and compliance by the company with the internal procedures as required by the Memorandum and the Articles.

This doctrine is a limitation of the doctrine of "constructive notice" and popularly known as the rule laid down in the celebrated case of Royal British Bank v. Turquand. Thus, the doctrine of indoor management aims to protect outsiders against the company.

Q. 28 Exception Doctrine of Indoor Management?

Ans. The doctrine of Indoor Management or Turquand Rule has limitations of its own. It is inapplicable to the following cases:

(a) **Actual or constructive knowledge of irregularity**: The rule does not protect any person when the person dealing with the whether actual or constructive, of the irregularity.

In Howard vs. Patent Ivory Manufacturing Co. where the directors could not defend the issue of debentures to themselves because they should have known that the extent to which they were lending money to the company required the assent of the general meeting which they had not obtained.

Likewise, in Morris v Kansseen, a director could not defend an allotment of shares to him as he participated in the meeting, which made the allotment. His appointment as a director also fell through because none of the directors appointed him was validly in office.

(b) **Suspicion of Irregularity**: The doctrine in no way, rewards those who behave negligently. Where the person dealing with the company is put upon an inquiry, for example, where the transaction is unusual or not in the ordinary course of business, It is the duty of the outsider to make the necessary enquiry.

The protection of the "Turquand Rule" is also not available where the circumstances

surrounding the contract are suspicious and therefore invite inquiry.

Suspicion should arise, for example, from the fact that an officer is purporting to act in matter, which is apparently outside the scope of the authority.

Where the plantiff accepted a transfer of a company's property from its accountant, the transfer was held void . The plaintiff could not have supposed, in absence of a power of attorney that the accountant had authority to effect transfer of the company's property. (Anand Bihari Lal Vs. Dinshaw & Co.)

(c) **Forgery**: The doctrine of indoor management applies only to irregularities which might otherwise affect a transaction but it cannot apply to forgery which must be regarded as nullity. Forgery may in circumstances exclude the 'Turquand Rule'.

The only clear illustration is found in the Ruben v Great Fingall Consolidated. In this case the plaintiff was the transferee of a share certificate issued under the seal of the defendant's company. The company's secretary, who had affixed the seal of the company and forged the signature of the two directors, issued the certificate.

The plaintiff contended that whether the signature were genuine or forged was a part of the internal management, and therefore, the company should be estopped from denying genuineness of the document. But it was held, that the rule has never been extended to cover such a complete forgery.

Q.29 Explain the case of Royal British Bank v. Turquand?

Ans. **Facts of the Case**:

Mr. Turquand was the official manager (liquidator) of the insolvent Cameron's Coalbrook Steam, Coal and Swansea and Loughor Railway Company. It was incorporated under the Joint Stock Companies Act, 1844. The company had given a bond for £ 2,000 to the Royal British Bank, which secured the company's drawings on its current account. The bond was under the company's seal, signed by two directors and the secretary. When the company was sued, it alleged that under its registered deed of settlement (the articles of association), directors only had power to borrow up to an amount authorized by a company resolution. A resolution had been passed but not specifying how much the directors could borrow.

Held, it was decided that the bond was valid, so the Royal British Bank could enforce the terms .

He said the bank was deemed to be aware that the directors could borrow only up to the amount resolutions allowed. Articles of association were registered with Companies House, so there was constructive notice. But the bank could not be deemed to know which ordinary resolutions passed, because these were not registrable. The bond was valid because there was no requirement to look into the company's internal workings. This is the indoor management rule, that the company's indoor affairs are the company's problem.

Q. 30 Define the following :

Ans. **Dormant Company Sec. 455 —**

Where a company is formed and registered under this Act for a future project or to hold an asset or intellectual property and has no significant accounting transaction, such a company or an inactive company may make an application to the Registrar in such manner as may be prescribed for obtaining the status of a dormant company.

"Inactive company" means a company which has not been carrying on any business or operation, or has not made any significant accounting transaction during the last two financial years, or has not filed financial statements and annual returns during the last two financial years.

Listed & Unlisted Company (on the basis of access to capital) —

Listed company: As per the definition given in the section 2(52) of the Companies Act, 2013, it is a company which has any of its securities listed on any recognized stock exchange.

Provided that such class of companies, which have listed or intend to list such class of securities, as may be prescribed in consultation with the Securities and Exchange Board, shall not be considered as listed companies.

Unlisted company means company other than listed company.

Nidhi Companies —

- Company which has been incorporated as a nidhi
- with the object of cultivating the habit of thrift (cost cutting) and savings amongst its members,
- receiving deposits from, and lending to, its members only for their mutual benefit and

- which complies with such rules as are prescribed by the Central Government for regulation of such class of companies. [Section 406 of the Companies Act, 2013

Public Financial Institution (PFI)—

By virtue of Section 2(72) of the Companies Act, 2013, the following institutions are to be regarded as public financial institutions:

(i) the Life Insurance Corporation of India, established under the Life Insurance Corporation Act, 1956;

(ii) the Infrastructure Development Finance Company Limited,

(iii) specified company referred to in the Unit Trust of India (Transfer of Undertaking and Repeal) Act, 2002;

(iv) institutions notified by the Central Government under section4A(2) of the Companies Act, 1956 so repealed under section 465 of this Act;

(v) such other institution as may be notified by the Central Governmentin consultation with the Reserve Bank of India:

Conditions for an institution to be notified as PFI: No institution shall be so notified unless —

(i) it has been established or constituted by or under any Central or State Act other than this Act or the previous Companies Law; or

(ii) not less than fifty-one per cent of the paid up share capital is held or controlled by

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

Equity share capital —

According to explanation to section 43:

"Equity share capital", with reference to any company limited by shares, means all share capital which is not preference share capital;

Preference Share capital —

"Preference share capital", with reference to any company limited by shares, means that part of the issued share capital of the company which carries or would carry a preferential right with respect to—

(a) payment of dividend,

either as a fixed amount or an amount calculated at a fixed rate,

which may either be free of or subject to income-tax; and

(b) in the case of a winding up or repayment of capital, repayment of the amount of the share capital paid-up or deemed to have been paid-up,

whether or not, there is a preferential right to the payment of any fixed premium or premium on any fixed scale, specified in the memorandum or articles of the company;

Capital shall be deemed to be preference capital, despite that it is entitled to either or both of the following rights, namely: —

(a) That in respect of dividends,

in addition to the preferential rights to the amounts specified as above,

it has a right to participate, whether fully or to a limited extent, with capital not entitled to the preferential right aforesaid;

(b) That in respect of capital,

in addition to the preferential right to the repayment, on a winding up, of the amounts specified above,

it has a right to participate, whether fully or to a limited extent, with capital not entitled to that preferential right in any surplus which may remain after the entire capital has been repaid.

Exception: In case of private company – Section 43 shall not apply where memorandum or articles of association of the private company so provides.