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MESSAGE TO STUDENTS

ABOUT THE BOOK

As you are aware, Business Law is a very vast subject and there are several books where different topics are covered.

At JKSC, our efforts are focused on simplifying the study process for our students, and giving them a comprehensive set of books that will help them prepare for the CA Foundation Business Law examination.

This book has been compiled to help students of CA Foundation prepare for their Business Law paper. To make studying the subject easier, the study material of this subject has been organized into two exhaustive volumes, ensuring students will not have to refer to any other books while preparing for the subject.

VOLUME I: BUSINESS LAW: Theory

This volume covers the theory notes and explanations of all chapters that have to be studied for the Business Law paper

Contents of the book

- Chapter wise distribution of marks of previous examinations from May 2018 onwards (1st attempt of CA Foundation).
- Comprehensive explanation of all concepts and topics to be covered based on the ICAI study material. (ICAI theory is fully covered here)
- Chapter summary at the end of each chapter, highlighting the key points in the topic.
- List of Case Laws, Legal terms, and Latin terms at the end of each chapter – provided for quick reference during study.

How to use this book

In the lecture, the faculty will follow this book during concept and topic explanation. Hence, it is mandatory for students to bring this book to class with them during the relevant lectures.

Also, this book is to be thoroughly read and revised at home for preparing the subject.

VOLUME II: BUSINESS LAW: Workbook

This volume is a workbook that has been compiled to assess your knowledge and understanding of the subject. The book has several Questions & Answers for you to attempt and assess your performance.

Contents of the book

- Questions & Answers of all chapters taken from all ICAI materials (ICAI Study Material, ICAI Revision Test Papers, ICAI Mock Test Papers)
- Homework questions at the end of each chapter for self practice and their respective answers
- Past exam papers (from May'18 onwards) and suggested answers as given by ICAI.

Note: The book does not cover Nov'23 & May'24 Question Papers and ICAI Suggested Answer, May' 2024 & Nov' 2023 ICAI Revision Test Papers and Mock Test Papers, as these materials are issued by the ICAI subsequent to the printing of this book. Students are advised to download such materials from the ICAI website www.icai.org as and when it becomes available.

How to use this book

Once the explanation is complete in class, the faculty will discuss the chapter based questions at length in class.

Students will be solving the question in the class and the faculty will also provide detailed inputs on how the questions must be answered as per the ICAI guidelines.

Once the chapter has been thoroughly discussed in class, students are expected to solve the Homework Questions provided at the end of each chapter, as part of their self study.

The answers for this section are provided at the end of the book to enable students to self evaluate. For a fair assessment, kindly check the answers only after writing your answers to those questions.

IMPORTANCE OF WRITING PRACTICE

You will hear your JKSC teachers repeat this regularly in the class, yet we must make this point here:

If you wish to score your best marks in this subject, you will have to invest time and effort in writing practice.

READING THE NOTES OR THE BOOKS TEN TIMES OVER IS NOT A REPLACEMENT FOR WRITING PRACTICE.

Let us explain: The law subject, when discussed and taught in class, is easy to understand and students enjoy the subject quite a bit. This gives them the false confidence that they will find the subject easy to prepare for the exam – all they have to do is read and they will remember everything.

The fact is each topic in this subject is vast and has to be attempted with certain parameters. The information that you have about the topic must fit a predefined framework to help the examiner realize that you know your subject well. You cannot merely string together whatever facts you can remember while writing, in some random order.

This knowledge and understanding of how the answers are to be presented, what ICAI is expecting of you from this paper, and how much of the topic you actually know can only come when you PHYSICALLY WRITE the practice papers. Additional questions under self study at the end of every chapter are given to help you assess yourself.

HOW TO STUDY EFFECTIVELY FOR THE EXAM?

- Once the chapter has been completed from Volume I and the faculty has discussed the Q&A in Volume II, it is time for you to study the theory, go through the notes and start attempting the question papers in writing.
- Do not make pointers or charts or short forms of the notes. These have already been provided in the book and the summary of the chapter is already provided at the end of every chapter. Practicing a chapter like this will not help you answer the questions in the final exam. Make sure you write the answers in the descriptive format just like you are expected to write in the finals. This will help you understand what you

are forgetting, how to organize your content and help you manage your time, while attempting the paper.

➢ How to learn the Legal & Latin Terms

- These terms are well highlighted in the content of the chapters and a list of such terms used in a given chapter is printed at the end of each chapter for your reference.
- Students are advised to write the page number where the term appears in the chapter alongside this quick reference list.
- This will make it easy to check the context of the technical term during revisions.

TYPES OF QUESTIONS ASKED IN EXAM & HOW TO ANSWER THEM?

- The questions in the exam can either be of theoretical or practical nature. While there are multiple ways / approaches in which both types of questions can be answered, the following approach is considered ideal:
  - For theory questions: Students must write the answer in point format to make it easy for the examiner to rapidly scan the answer.
  - For practical / case study questions: It is recommended that students write these answers in 3 paragraph formats. The flow of content in these answers should be as follows:
    - 1st paragraph: Write the relevant law and case law (if any)
    - 2nd paragraph: Write the situation in the question and how it is related to the legal provision.
    - 3rd paragraph: Write the final conclusion.
- Presenting your answers in these formats enables the examiner to understand how much you know and your clarity of thought, at a glance. A comprehensive answer that is well structured and presented can only be written in the final paper if you have practiced the same - in writing, regularly during your study time.
- What is expected in your answers
  1) Concept explanation of the topic with all relevant content
  2) You must quote Case Laws in the exam, use Legal and Latin Terms – this is imperative for scoring good marks.
- Students must note that endlessly repeating one point in different words is not going to help them get the desired marks. Only thorough preparation perfected by writing practice and self evaluation will help students in achieving the scores they want.

In conclusion, these books have everything you need to prepare for the CA Foundation Business Law paper. You do not need anything further in terms of reference material or additional paper samples. We hope you will make the best use of this carefully compiled study material and achieve success in your endeavours.

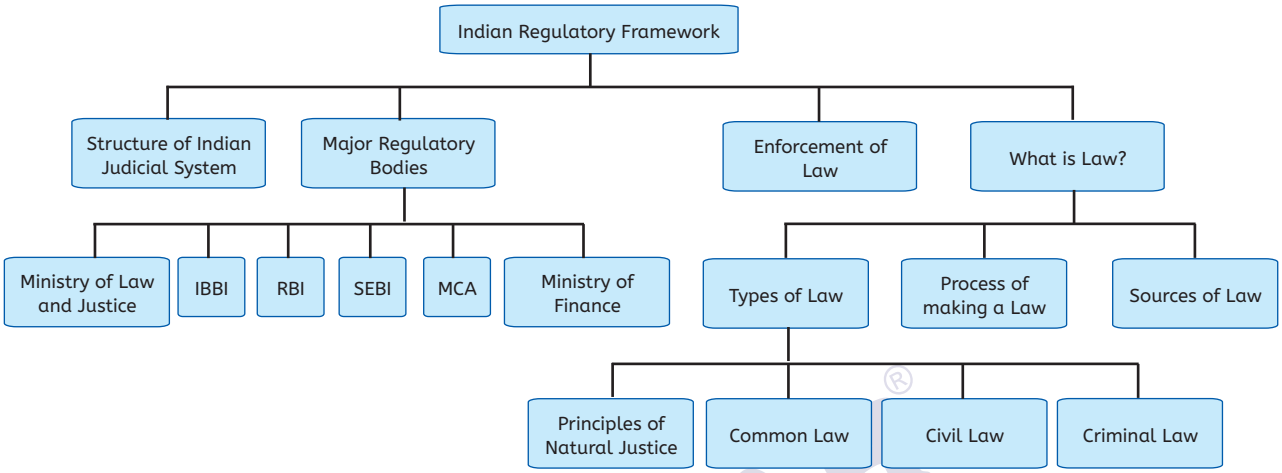
We wish you a very happy study time.
BEST OF LUCK!
JKSC

Chapter-wise marks distribution of previous Examination

Chp No.	Chapter Name	May' 2018	Nov' 2018	May' 2019	Nov' 2019	Nov' 2020	Jan' 2021	July' 2021	Dec' 2021	May' 2022	June' 2023
1.	Indian Regulatory Framework	0	0	0	0	0	0	0	0	0	0
2.	The Indian Contract Act,1872										
	Unit 1: Nature of Contract		8				13				9
	Unit 2: Consideration	5	3	4	7		5			7	7
	Unit 3: Other essential elements of valid Contract	9		12	5	11	4	4	6	6	2
	Unit 4: Performance of Contract	4			6			11	11	4	4
	Unit 5: Breach of Contract	6	4	6		6				5	
	Unit 6: Contingent & Quasi Contracts		7		4	5		7	5		
		24	22	22	22	22	22	22	22	22	22
3.	The Indian Contract Act, 1872 (Special Contract)	0	0	0	0	0	0	0	0	0	0
4.	The Sale of Goods Act, 1930										
	Unit 1: Formation of Contract of Sale	4	4						6	10	4
	Unit 2: Conditions & Warranties		6	10	6	4	6	6	7	6	
	Unit 3: Transfer of Ownership & Delivery of Goods	6	6	6	4	12	6	4			4
	Unit 4: Unpaid seller	6			6		4	6	3		8
		16	16	16	16	16	16	16	16	16	16
5.	Indian partnership Act, 1932										
	Unit 1: General Nature of Partnership	4				6	8		16	2	12
	Unit 2: Relations of Partners	6	14	14	14	12	10	12		10	4
	Unit 3: Registration of Firm & Dissolution of Firm	6	4	4	4			4		4	
		16	18	18	18	18	18	16	16	16	16
6.	The Limited Liability Partnership Act, 2008	5	5	5	5	5	5	5	5	5	5
7.	The Companies Act, 2013	13	13	13	13	13	13	13	13	13	13
8.	The Negotiable Instruments Act, 1881	0	0	0	0	0	0	0	0	0	0

1. INDIAN REGULATORY FRAMEWORK

OVERVIEW OF CHAPTER



INTRODUCTION

Have you ever wondered why you are studying this subject called law? Is it only because it has been prescribed in the syllabus or is it because you will need this knowledge as a member of the Institute of Chartered Accountants of India?

Awareness of law is essential to become a full-fledged Chartered Accountant. This is because a Chartered Accountant is the first level of contact on many legal matters. So, we should possess knowledge of law so that we can advise our management and clients on legal matters at a basic or threshold level.

Some of you may later wish to specialise in a subject called taxation. Remember tax laws are also laws. In order to become an expert in taxation you should possess a basic awareness of the legal and regulatory framework of our country. The purpose of a regulatory framework is to provide a set of uniform rules and regulations that will govern the conduct of people interacting with each other in personal as well as business relationships.

Down the ages, mankind has evolved from a hunter- gatherer society through agriculture and industrial revolution to a complex social framework. Throughout this journey, we have always needed laws and regulations to guide us on the right course of conduct as well as to identify violations and punish them.

If we talk about ancient law, on the basis of information available from different sources "Code of Hammurabi" is known for oldest law in written form. King Hammurabi ruled Babylon for the period from 1792 BC to 1758 BC. He carved the code on bulky stone slabs and ordered to place those stones on different places all over the city so that the public may have the knowledge of codes. He also appointed judges to check whether public is following the laws or not.

In 450 BC, a set of laws was engraved on 12 bronze tablets in Rome which is considered as first most detailed code of any of the civilisations and called Twelve Tables. The purpose of these tables was to protect the rights of public and to provide remedy for wrongs. All the citizens of Rome were supposed to have the knowledge of these tables. Over the time, many amendments were done in these laws as per the requirements.

In this subject, you will be introduced to many laws. Therefore, in this chapter we will first understand how these laws are made and how they are implemented.

WHAT IS LAW?

Law is a set of obligations and duties imposed by the government for securing welfare and providing justice to society. India's legal framework reflects the social, political, economic, and cultural aspects of our vast and diversified country.

SOURCES OF LAW

The main sources of law in India are the Constitution, the statutes or laws made by Parliament and State Assemblies, Precedents or the Judicial Decisions of various Courts and in some cases, established Customs and Usages.

You must be aware that India is a parliamentary democracy. We have a constitution which is the basis and source for all laws. We elect our representatives to the parliament as well as to the legislative assemblies of various States. These representatives of the people make laws in parliament or in their state assemblies as the case may be. So, Parliament is the ultimate law-making body. The laws passed by parliament may apply throughout all or a portion of India, whereas the laws passed by state legislatures apply only within the borders of the states concerned.

The Government of India Act, 1935, passed by the Parliament of the United Kingdom is the precursor for the Constitution of India. It defined the characteristics of the Government from "unitary" to "federal". Powers were distributed between Centre and State to avoid any disputes. In 1937, Federal Court was established and had the jurisdiction of appellate, original and advisory. The powers of Appellate Jurisdiction extended to civil and criminal cases whereas the Advisory Jurisdiction was extended with the powers to Federal Court to advise Governor-General in matters of public opinion. The Federal Court operated for 12 years and heard roughly 151 cases. The Federal Court was supplanted by India's current Apex Court, the Supreme Court of India.

The Constitution of India, 1950 is the foremost law that deals with the framework within which our democratic system works, and our laws are made for the people, by the people. The Constitution also provides for and protects certain Fundamental rights of citizens. It also lays down Fundamental duties as well as the powers and duties of Governments, both Central and State. The laws in India are interconnected with each other forming a hybrid legal system.

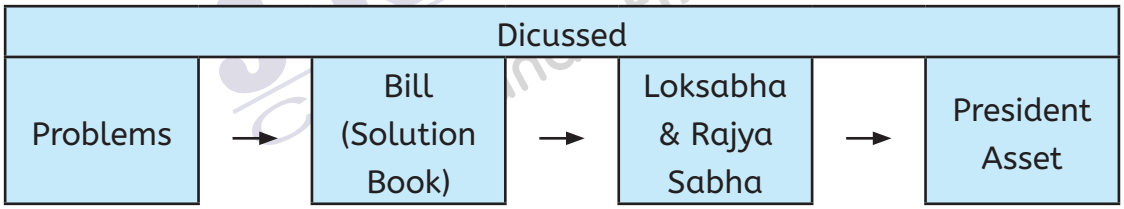
The people who wrote the Constitution decided to divide the law-making power between the Central Government and the various State Governments. So, the Indian Constitution has three lists Viz., Central List, State List and on current List.
Depending on the list in which it figures a matter would become the subject for Central law or a State law.

For example,

- Income Tax is a Central subject. So, throughout India we have only one law for Income Tax which is implemented by the Central Government through the Ministry of Finance.
- We also have matters for which both Central as well as State Governments can pass laws. Levy of stamp duty is such an example. Both Central Government and State Government have laws governing Levy of stamp duty.

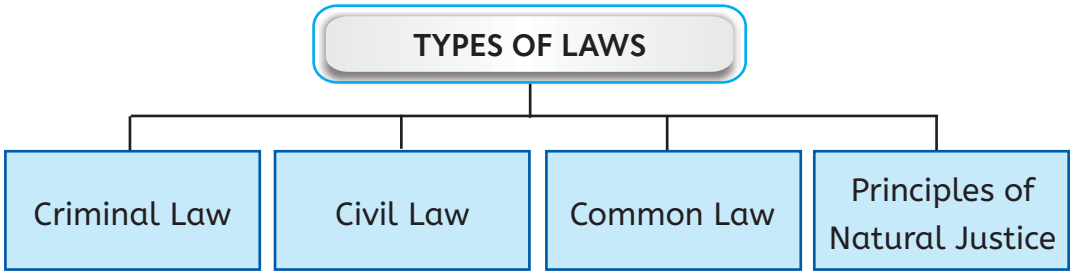
THE PROCESS OF MAKING A LAW

When a law is proposed in parliament it is called a Bill. After discussion and debate, the law is passed in Lok Sabha. Thereafter, it has to be passed in Rajya Sabha. It then has to obtain the assent of the President of India. Finally, the law will be notified by the Government in the publication called the Official Gazette of India. The law will become applicable from the date mentioned in the notification as the effective date. Once it is notified and effective, it is called an Act of Parliament.



TYPES OF LAWS IN THE INDIAN LEGAL SYSTEM

The laws in the Indian legal system could be broadly classified as follows



1. Criminal Law

- Criminal law is concerned with laws pertaining to violations of the rule of law or public wrongs and punishment of the same.
- Criminal Law is governed under the Indian Penal Code, 1860, and the Code of Criminal Procedure, 1973 (Crpc).

- The Indian Penal Code, 1860, defines the crime, its nature, and punishments whereas the Criminal Procedure Code, 1973, defines exhaustive procedure for executing the punishments of the crimes.
- For Example: Murder, rape, theft, fraud, cheating and assault are some examples of criminal offences under the law.

2. Civil Law

- Matters of disputes between individuals or organisations are dealt with under Civil Law.
- Civil courts enforce the violation of certain rights and obligations through the institution of a civil suit. Civil law primarily focuses on dispute resolution rather than punishment.
- The act of process and the administration of civil law are governed by the Code of Civil Procedure, 1908 (CPC). Civil law can be further classified into Law of Contract, Family Law, Property Law, and Law of Tort.
- For examples: are breach of contract, non-delivery of goods, non-payment of dues to lender or seller defamation, breach of contract, and disputes between landlord and tenant.

3. Common Law

- A judicial precedent or a case law is common law.
- A judgment delivered by the Supreme Court will be binding upon the courts within the territory of India under Article 141 of the Indian Constitution.
- The doctrine of Stare Decisis is the principle supporting common law.
- It is a Latin phrase that means “to stand by that which is decided.”
- The doctrine of Stare Decisis reinforces the obligation of courts to follow the same principle or judgement established by previous decisions while ruling a case where the facts are similar or “on all four legs” with the earlier decision.

4. Principles of Natural Justice

- Natural justice, often known as Jus Natural deals with certain fundamental principles of justice going beyond written law.
- Nemo judex in causa sua (Literally meaning “No one should be made a judge in his own cause, and it’s a Rule against Prejudice), audi alteram partem (Literally meaning “hear the other party or give the other party a fair hearing), and reasoned decision are the rules of Natural Justice.
- A judgement can override or alter a common law, but it cannot override or change the statute.

ENFORCING THE LAW

After a law is passed in parliament it has to be enforced. Somebody should monitor whether the law is being followed. This is the job of the executive. Depending on whether a law is a Central law or a State law the Central or State Government will be the enforcing authority.

For this purpose government functions are distributed to various ministries. Some of the popular Ministries are the Ministry of Finance, the Ministry of Corporate Affairs, the Ministry of Home Affairs, the Ministry of Law and Justice and so on. These Ministries are headed by a minister and run by officers of the Indian administrative and other services.

The Government of India exercises its executive authority through a number of Government Ministries or Departments of State. A Ministry is composed of employed officials, known as civil servants, and is politically accountable through a minister. Most major Ministries are headed by a Cabinet Minister, who sits in the Union Council of Ministers, and is typically supported by a team of junior ministers called the Ministers of State.

For example, the Income Tax Act is implemented and enforced by the Ministry of Finance through the Central Board for Direct Taxes coming under the Department of Revenue and is administered by the officers of the Indian Revenue Service. We will see some of the major Ministries and the laws which are enforced by them:

The Ministry of Finance (Vitta Mantralaya) is a Ministry within the Government of India concerned with the economy of India, serving as the Treasury of India. In particular, it concerns itself with taxation, financial legislation, financial institutions, capital markets, centre and state finances, and the Union Budget. This Ministry is so important that many ministers have preferred to hold the portfolio of Finance Minister also. One of the important functions of the Finance Ministry is the presentation of the Union Budget. This annual event is eagerly awaited by professionals and the common man as it provides for the rates of taxes and budget allocations for the ensuing year.

Who presented the 5 consecutive of Union Budgets as Finance Minister?

Arun Jaitley, P. Chidambaram, Yashwant Sinha, Dr. Manmohan Singh & Morarji Desai

CONSTITUTION OF THE MINISTRY OF FINANCE

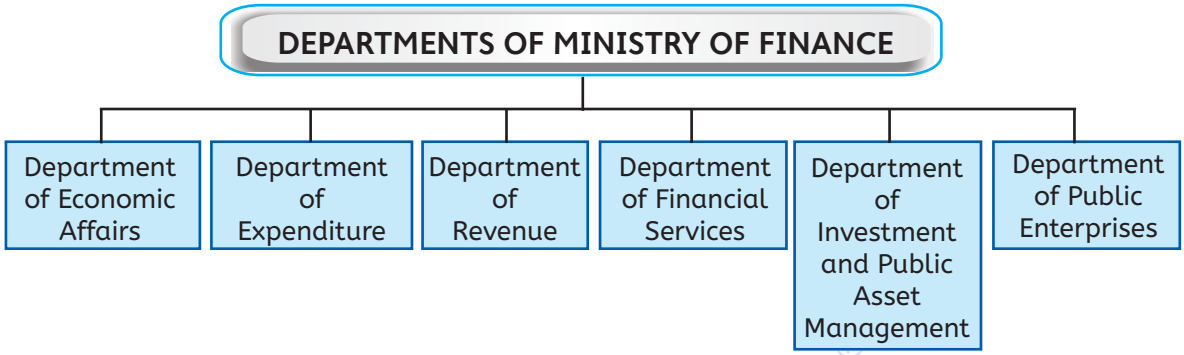
Ministry of Finance

- is the apex controlling authority
- of four Central Civil Services, namely:
  - Indian Revenue Service
  - Indian Audit and Accounts Service

- Indian Economic Service and
- Indian Civil Accounts Service.

➢ Also the apex controlling authority of one of the central commerce services namely
➢ Indian Cost and Management Accounts Service.

DEPARTMENTS UNDER THE MINISTRY OF FINANCE

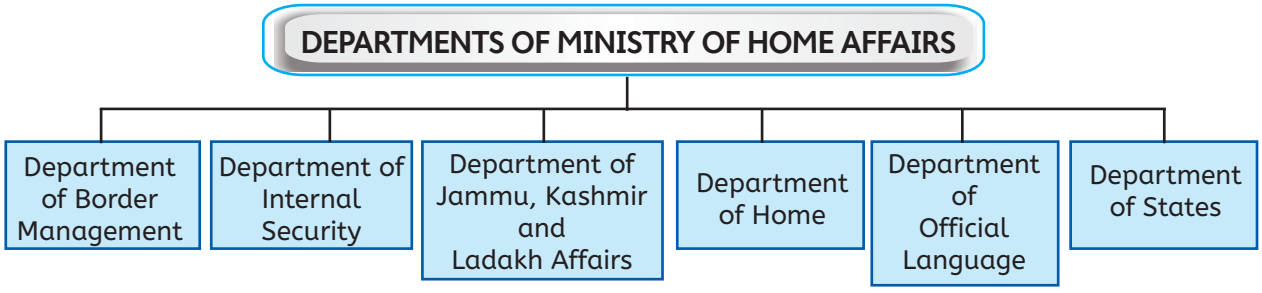


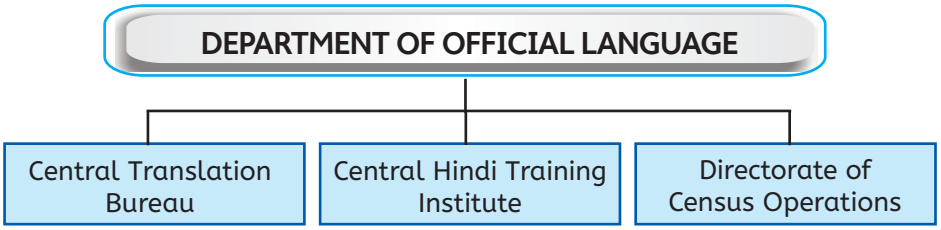
(i) Ministry of Corporate Affairs (MCA)

- is an Indian Government Ministry.
- primarily concerned with administration of the Companies Act 2013, the Companies Act 1956, the Limited Liability Partnership Act, 2008, and the Insolvency and Bankruptcy Code, 2016.
- responsible mainly for the regulation of Indian enterprises in the industrial and services sector.
- The Ministry is mostly run by civil servants of the ICLS cadre.
- These officers are elected through the Civil Services Examination conducted by Union Public Service Commission.
- The highest post, Director General of Corporate Affairs (DGCoA), is fixed at Apex Scale for the ICLS.

Ministry of Home Affairs (Grha Mantralaya):

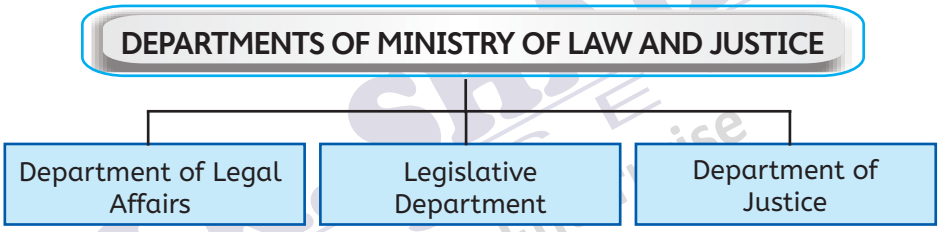
- is a ministry of the Government of India.
- As an interior ministry of India, it is mainly responsible for themaintenance of internal security and domestic policy.
- The Home Ministry is headed by Union Minister of Home Affairs.





Ministry of Law and Justice:

- in the Government of India is a Cabinet Ministry
- deals with the
  - ✓ management of the legal affairs, through the Legislative Department
  - ✓ legislative activities through the Department of Legal Affairs
  - ✓ administration of justice in India through the Department of Justice
- The Department of Legal Affairs is concerned with advising the various Ministries of the Central Government while the Legislative Department is concerned with drafting of principal legislation for the Central Government.



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

- is the regulatory body
- for securities and commodity market in India
- under the ownership of Ministry of Finance within the Government of India.
- It was established on 12 April, 1988 as an executive body and was given statutory powers on 30 January, 1992 through the SEBI Act, 1992.

(iii) Reserve Bank of India (RBI)

- is India's Central Bank and regulatory body responsible for regulation of the Indian banking system.
- It is under the ownership of Ministry of Finance, Government of India.
- It is responsible for the control, issue and maintaining supply of the Indian rupee.
- It also manages the country's main payment systems and works to promote its economic development.
- Bharatiya Reserve Bank Note Mudran (BRBNM) is a specialised division of RBI through which it prints and mints Indian currency notes (INR) in two of its currency printing presses located in Nashik (Western India) and Dewas (Central India).
- RBI established the National Payments Corporation of India as one of its specialised division to regulate the payment and settlement systems in India.

- Deposit Insurance and Credit Guarantee Corporation was established by RBI as one of its specialised division for the purpose of providing insurance of deposits and guaranteeing of credit facilities to all Indian banks.

(iv) Insolvency and Bankruptcy Board of India (IBBI)-

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

STRUCTURE OF THE INDIAN JUDICIAL SYSTEM

When there is a dispute between citizens or between citizens and the Government, these disputes are resolved by the judiciary.

The functions of judiciary system of India are:

- Regulation of the interpretation of the Acts and Codes,
- Dispute Resolution,
- Promotion of fairness among the citizens of the land.

In the hierarchy of courts, the Supreme Court is at the top, followed by the High Courts and District Courts. Decisions of a High Court are binding in the respective state but are only persuasive in other states. Decisions of the Supreme Court are binding on all High Courts under Article 141 of the Indian Constitution. In fact, a Supreme Court decision is the final word on the matter.

(i) Supreme Court

The Supreme Court is the apex body of the judiciary. It was established on 26th January, 1950. The Chief Justice of India is the highest authority appointed under Article 126. The principal bench of the Supreme Court consists of seven members including the Chief Justice of India. Presently, the number has increased to 34 including the Chief Justice of India due to the rise in the number of cases and workload. An individual can seek relief in the Supreme Court by filing a writ petition under Article 32.

What is writ?

A legal order to do not to someting, given by a court of law.

(ii) High Court

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

Which is the oldest High Court in India?

The oldest high court in the country is the Calcutta High Court, established on 2nd July, 1862.

(iii) District Court

Below the High Courts are the District Courts. The Courts of District Judge deal with Civil law matters i.e. contractual disputes and claims for damages etc., The Courts of Sessions deals with Criminal matters.

Under pecuniary jurisdiction, a civil judge can try suits valuing not more than Rupees two crore.

Jurisdiction means the power to control. Courts get territorial Jurisdiction based on the areas covered by them. Cases are decided based on the local limits within which the parties reside or the property under dispute is situated.

(iv) Metropolitan courts

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

2. THE INDIAN CONTRACT ACT, 1872

UNIT 1: NATURE OF CONTRACTS

DEFINITION OF CONTRACT :

The term 'contract' is defined in Section 2 (h) of Indian Contract Act, as under: "An agreement enforceable by law is a contract".

Contract = An Agreement + Enforceability by law

DEFINITION OF AGREEMENT:

The term 'agreement' is defined in Section 2 (e) of the Indian Contract Act, as under: "Every promise and every set of promises forming the consideration for each other is an agreement."

Agreement = Offer + Acceptance.

Example:

DEFINITION:

The term proposal/offer has been defined in Section 2 (a) as under:

"When one person signifies to another his willingness to do or to abstain (not to do) from doing anything, with a view to obtaining the assent of that another to such act or abstinence, he is said to make a proposal"

CHARACTERISTICS:

1. Offer must be capable of creating legal relationship:

Case law: Balfour v. Balfour

In, Balfour v. Balfour a husband promised to pay maintenance allowance every month to his wife. When he failed to perform this promise, she brought an action to enforce it. As it is an agreement of domestic nature, it was held that it does not contemplate to create any legal obligation.

2. The terms of the offer must be definite and certain:

The terms of the offer must be definite, unambiguous and certain and not vague.

3. Offer must be different from invitation to offer.*(Harvey v/s Facie)*

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 before making an offer. Acceptance of an invitation to an offer does not result in the contract and only an offer emerges in the process of negotiation.
- In 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.

  Example: 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.
- 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.

Difference between Offer & Invitation to offer

Offer	Invitation to Offer
(i) Person expresses his willingness to be bound by the terms of the offer if other party accepts.	(i) Person is inviting other people to make an offer
(ii) Offers leads to acceptance Example – application form filled up by students for taking admission in college	(ii) Invitation to offers leads to offer Example – Issue of prospectus by college

Case law: *Mac Pherson vs Appanna* [1951]: 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.

4. Offer should be communicated.

Unless an offer is properly communicated, there can be no acceptance of it.

Case law: *Lalman Shukla vs Gauri Dutt*, Gauri announced a reward for anyone who found his nephew. Lalman found the nephew in ignorance of reward. Held that, he is not entitled to reward as a person cannot accept an offer if he is unaware of its existence.

5. Offer can be express or implied.

An offer which is expressed by words, written or spoken, is called an express offer. The offer which is expressed by conduct is called an implied offer.

6. Offer can be conditional.

Such conditional offer should be accepted along with the condition.

7. Offer should not contain a term non-compliance of which would directly lead to acceptance.

Example: A offers to sell his house to B for ₹ 2 crores, The offer was for 10 days and if does not reply within 10 days, A will treat the offer as accepted. This is an invalid offer.

LAPSE OF OFFER/REVOCATION OF OFFER:

An offer should be accepted before it lapses (i.e. comes to an end). An offer may come to an end in any of the following ways stated in Section 6 of the Indian Contract Act:

1. By communication of notice of revocation by offeror:

An offer may come to an end by communication of notice of revocation by the offeror. An offeror can revoke his offer at any time before he becomes bound by it.

2. By lapse of time:

Where time is fixed for the acceptance of the offer, and it is not accepted within the fixed time, the offer comes to an end automatically on the expiry of fixed time. Where no time for acceptance is prescribed, the offer has to be accepted within reasonable time. The term 'reasonable time' will depend upon the facts and circumstances of each case.

3. By failure to accept condition in conditional offer:

Where, the offer requires that some condition must be fulfilled before the acceptance of the offer, the offer lapses, if it is accepted without fulfilling the condition.

4. By the death or insanity of the offeror/offeree:

Where, the offeror dies or becomes insane, the offer comes to an end if the fact of his death or insanity comes to the knowledge of the acceptor before he makes his acceptance. But if the offer is accepted in ignorance of the fact of death or insanity of the offeror, the acceptance is valid. This will result in a valid contract, and legal representatives, of the deceased offeror shall be bound by the contract. On the death of offeree before acceptance, the offer also comes to an end by operation of law.

5. By counter-offer by the offeree:

Where, a counter-offer is made by the offeree, then the original offer automatically comes to an end, as the counter-offer amounts to rejections of the original offer.

6. By rejection of offer by the offeree:

Where, the offeree rejects the offer, the offer comes to an end. Once the offeree rejects the offer, he cannot revive the offer by subsequently attempting to accept it. The rejection of offer may be express or implied.

DEFINITION OF ACCEPTANCE:

DEFINITION: The term acceptance has been defined in Section 2(b) as under: "When the person to whom the proposal is made signifies his assent thereto, the proposal is said to be accepted. A proposal when accepted becomes a promise".

CHARACTERISTICS OF ACCEPTANCE:

1. The acceptance must be communicated:

The acceptance is, completed only when it has been communicated to the offerer. Until the acceptance is communicated, it does not create any legal relations.

Case law: *Brogden vs. Metropolitan Railway Co.*

2. The acceptance must be communicated by a person who has the authority to accept.

Case law: *Boulton vs. 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)]

3. The acceptance must be absolute and unqualified:

As a conditional acceptance is counter offer.

4. Acceptance must be within a specific/reasonable time:

The acceptance must be made while the offer is still in force, i.e. before the offer lapses. If any time-limit is prescribed in the offer, it should be accepted within the prescribed time-limit. However, if not time is prescribed, it must be accepted within "a reasonable time".

5. Acceptance can be express or implied.

Case law: *Lilly White vs. Mannuswamy (1970)*

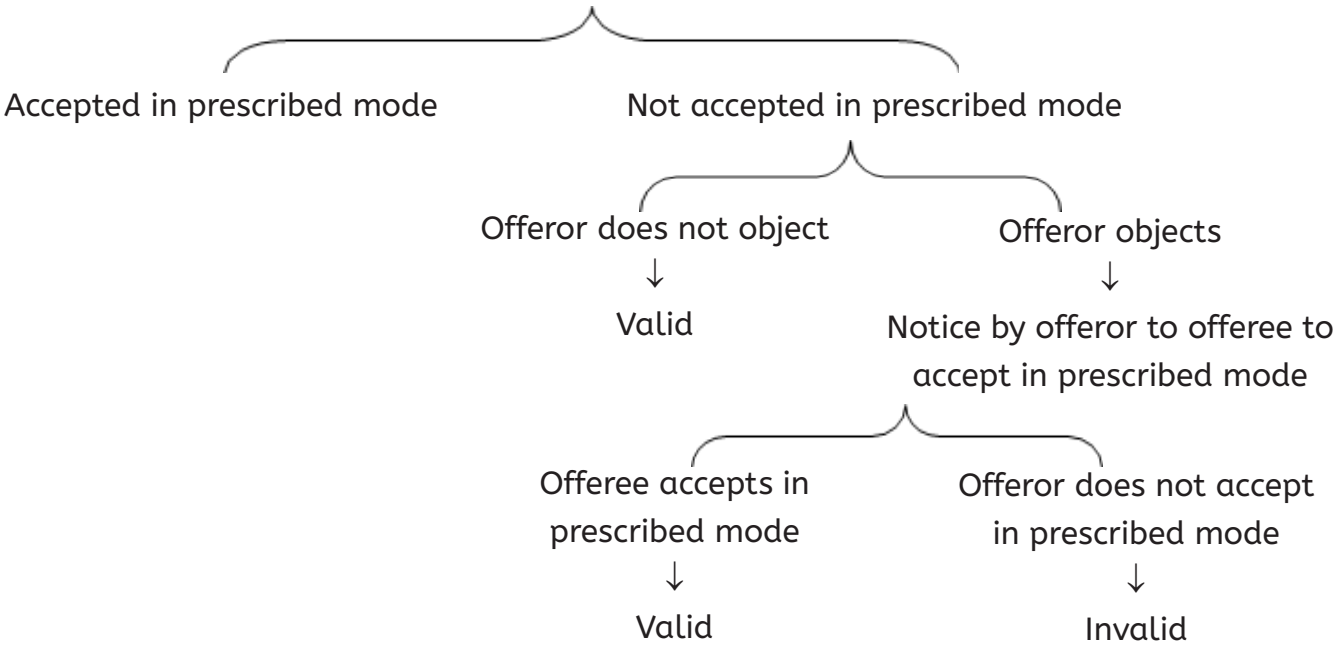
P delivered some clothes to drycleaner for which she received a laundry receipt containing a condition that in case of loss, customer would be entitled to claim 15% of the market price of value of the article, P lost her new saree. The terms were unreasonable and P was entitled to recover full value of the saree from the drycleaner. But, the court held that the respective documents have been accepted without a protest and hence amounted to implied acceptance. So she is entitled to recover only 15%

6. Mere silence does not amount to acceptance

Case law: *Felthouse vs. Bindley (1862)*

Facts: F (Uncle) offered to buy his nephew's horse for £30 saying "If I don't hear anything 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.

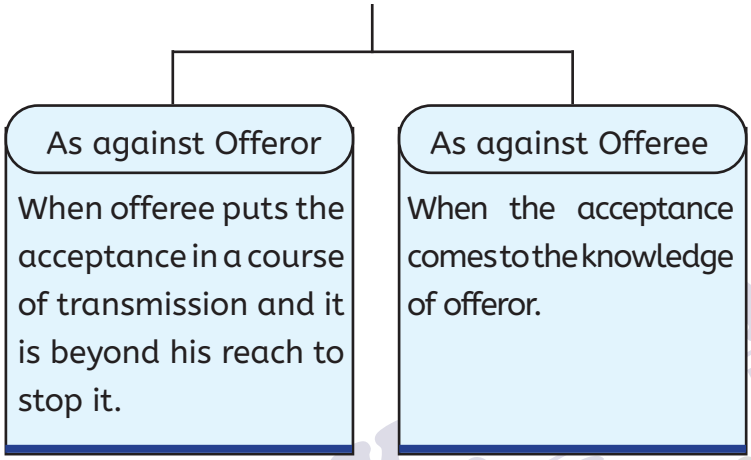
7. Acceptance should be via prescribed mode of communication.



COMMUNICATION OF OFFER AND ACCEPTANCE AND REVOCATION OF OFFER AND ACCEPTANCE:

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

2. Communication of acceptance is complete



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

4. Revocation of acceptance is valid before acceptance comes to the knowledge of offeror.
   - 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.

Diffierence Between

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

5. 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 ED1 - 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.

ESSENTIAL ELEMENTS OF A VALID CONTRACT

Essentials of a valid contract

As given by Section 10 of Indian Contract Act, 1872	Not given by Section 10 but are also considered essential
1. Agreements	1. Two parties
2. Free Consent	2. Intention to create legal relationship
3. Competency of the parties	3. Fulfillment of legal formalities
4. Lawful consideration	4. Certainty of meaning
5. legal object	5. Possibility of performance
6. Not expressly declared to be void	

UNIT 2: CONSIDERATION

DEFINITION:

The term 'consideration' is defined in section 2 (d) of the Indian Contract Act, as under: "When at the desire of the promisor, the promisee or any other person did or abstained from doing, or does or abstains from doing, or promises to do or abstain from doing something, such act or abstinence is called a consideration for the promise".

CHARACTERISTICS OF CONSIDERATION:

1. The consideration must move (i.e., must be done or promised to be done) at the desire of the promisor :

   An act or abstinence, which forms consideration for the promise, must be done or promised to be done according to the desire of the promisor

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

2. It may move from the promisee or any other person :

   Consideration may move from promisee or if the promisor has no objection from any other person.

   Case law: In Chinnayya v/s Ramayya, 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 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.

3. Consideration can be past, present or future:

   It can be executed or executory. But in England, past consideration is no consideration.

4. 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. It can be below market value.

5. It must be real and not illusory:

   The consideration to be valid must. be 'real' and 'valuable' and must not be 'imaginary'.

6. It must not be illegal, immoral, or opposed to public policy:
   The consideration given for an agreement must be a lawful one. Where the consideration to a contract is illegal, immoral or against public policy, the courts do not allow an action on such contract.

7. Consideration can be executed or executory.
   Example: A pays ₹ 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.

8. It can be negative or positive.

9. Consideration for an act which a person a legally bound to perform is not a valid consideration.
   Example: A promised to pay Rs. 5000 to B (a Police Officer) for investigating a crime, which B was already bound to investigate by law. Here A's promise to pay the amount is without valid consideration as B is already under a legal obligation to investigate the crime.

DOCTRINE OF PRIVITY OF CONTRACTS

Since a contract is a private relationship between parties who make it, the rights and obligations under such a contract are strictly confined to them. This is known as the doctrine of "privity of contract". It is a general rule of law that a person who is not a party to the contract cannot sue.

The rule is "Stranger to contract cannot sue. But a stranger to a consideration can sue".
Exception to Rule" A stranger to a contract cannot sue":
Under the Indian Law, the following are the exceptions to the rule that a stranger to a contract cannot sue.

(1) Beneficiaries in the case of trust:
   An agreement to create a trust can be enforced by the beneficiary, though he was not a party to the contract between the settlor and the trustees.
   Example:

(2) Written family settlements:

In the case of family settlement, if the terms of settlement are reduced in writing, members of the family who were not a party to the settlement can also enforce their claim.

Example: Two brothers X and Y agreed to pay an allowance of ₹ 20,000 to mother on partition of joint properties. But later they failed to pay. The mother, even though a stranger to contract can sue the sons

(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: 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) Assignment of contract:

Where there is an assignment of a contract, the assignee can enforce the contract for various benefits that would accrue to him on account of the assignment.

Example:

(5) Acknowledgement of Debts:

In case of part performance of a contractual obligations or where there is acknowledgment of liability on account of estoppel, a third party can sue for benefits. W here for example 'A' gives ₹ 25000/- to 'B' to be given to 'C' and 'B' informs 'C' that B is holding it on behalf of C, but subsequently refuses to pay 'C' then 'C' can sue and enforce his claim.

(6) Covenants with land:

Where a piece of land which is sold to buyer with certain covenants relating to land and the buyer is kept on notice of the covenants with certain duties, there the successors to the seller can enforce these covenants.

Example: One owner of the land having 2 land adjacent to each other. One was agricultural land. He sold other land containing a condition that it can never be used for industrial purpose so as to protect the other agriculture land from pollution. Such condition is a covenant attached to land. Even successor can enforce it

(7) Contracts made by the 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.

Example: A (Principal) instructed his agent B to sell goods to X for ₹ 1 lac. Hence, A sell goods to X. If X fails to pay ₹ 1 lac, apart from B, even A can sue X.

NO CONSIDERATION, NO CONTRACT

Every agreement must be supported by a consideration and agreement without consideration is void.

To this general rule there are certain exceptions which are mentioned in Section 25 of the Indian Contract Act.

(1) Out of Natural Love and Affection:

Where an agreement is expressed in writing and registered under law for the time being in force for the registration of documents and is made on account of natural love and affection between the parties standing in a near relation to each other is enforceable even if there is no consideration. Nearness of relationship, however, does not necessarily imply love and affection.

Example:

(2) Compensation paid for past voluntary services:

A promise to compensate wholly or in part for past voluntary services rendered by someone to promisor does not require consideration for being enforced. In order that a promise to pay for the past voluntary services is 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: P finds R's wallet give it to him. R promises to give P, ₹ 10,000. This is valid contract

(3) Promise to pay debts barred by limitation:

Where there is a promise in writing to pay a debt, which was barred by limitation, is valid without consideration.

Example: A is indebted to C for ₹ 60,000 but the debt is barred by limitation (Time Barred Debt). A gives a written promise to pay ₹ 50,000 in final settlement. It is a valid contract.

(4) Creation of Agency:

No consideration is necessary to create an agency

Example:

(5) In case of completed gifts, no consideration is necessary.

(6) Bailment:

Bailment is a contract where goods are delivered for a particular purpose and once the purpose is served, goods are to be returned back. There are 2 parties; bailor and bailee.

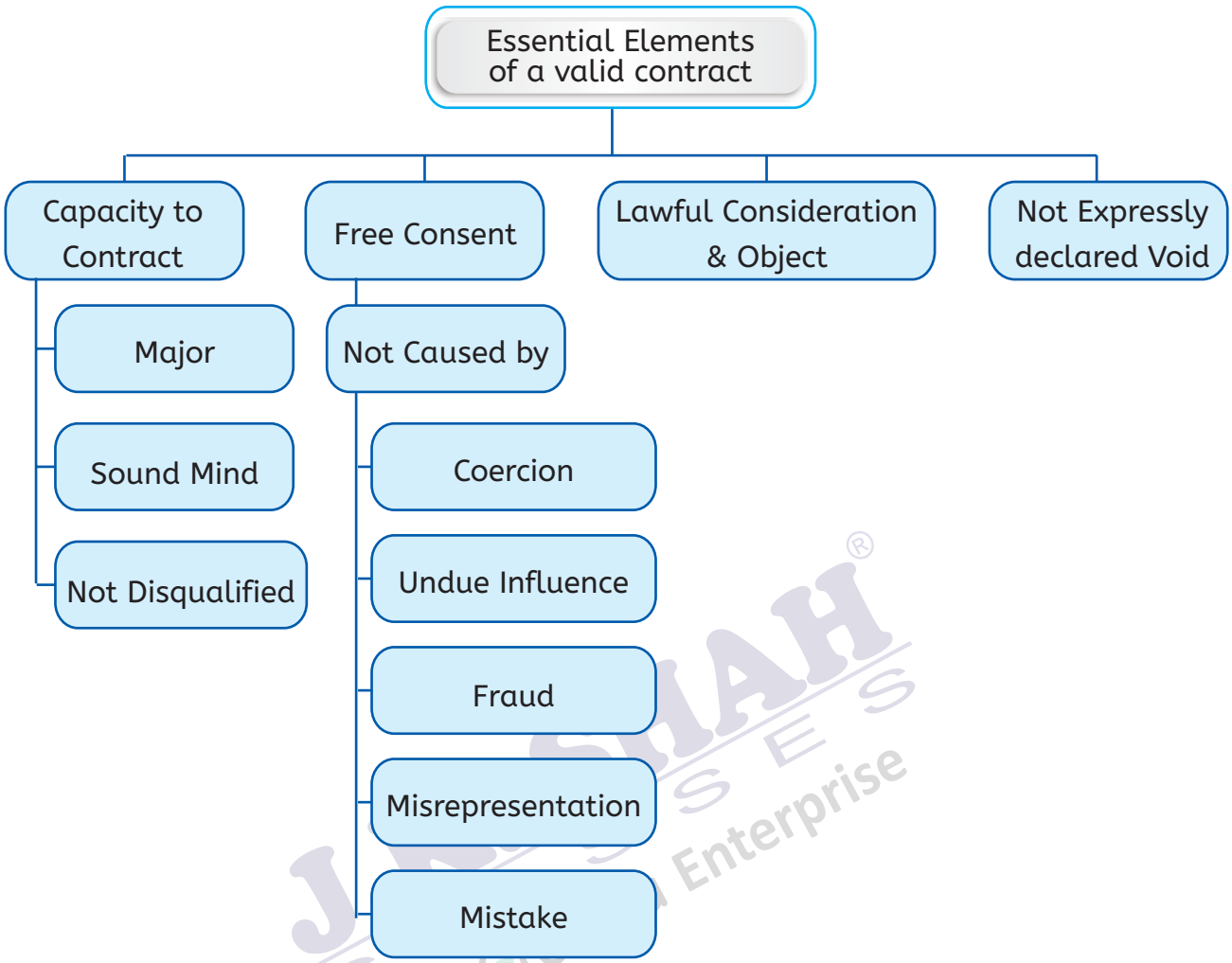
Bailment can be gratuitous. i.e. without consideration.

Example: A agreed to repair B's car for free. It is a valid contract even if it the contract of bailment is gratuitous

(7) Charity

If the promisee undertakes the liability on the promise of the person to contribute to charity, there the contract shall be valid.

UNIT 3: OTHER ESSENTIAL ELEMENTS OF A VALID CONTRACT



CAPACITY OF PARTIES

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".
Analysis of Section 11	This section deals with personal capacity of three types of individuals only. Every person is competent to contract who- (A) has attained the age of majority, (B) is of sound mind and (C) is not disqualified from contracting by any law.

(A) Minor	1. Every person in India shall attain the age of majority on the completion of 18 years of age 2. A agreement 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.. 3. Minor can be a beneficiary or can take benefit out of a contract: Though a minor is not competent to contract, he can be a beneficiary. Thus, a promissory note duly executed in favour of a minor (i.e minor is going to receive money) is valid. 4. Contract by guardian - how far enforceable: Though a minor's agreement is void, his guardian can enter into a valid contract on minor's behalf. Where the guardian makes a contract for the minor, which is for the benefit of the minor, there will be valid contract. 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. 5. Minor cannot bind his parents/guardians for his personal contracts. 6. 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. 7. 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-ab-initio agreement can never be ratified. 8. Liability for necessaries: If any necessaries of life are supplied to minor, then the person supplying the necessaries can claim it back from the property of minor. A claim for necessaries supplied to a minor is enforceable by law. But a minor is not personally liable for any amount 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 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. 9. No insolvency: A minor cannot be declared insolvent as he is incapable of contracting debts and dues are payable from the personal properties of minor and he is not personally liable. 10. 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. 11. Minor can be an agent: A minor can act as an agent. But he will not be liable to his principal for his acts. 12. Joint contract by minor and adult: In such a case, the adult will be liable on the contract and not the minor. 13. Minor as Shareholder: A minor, being incompetent to contract cannot be a shareholder of the company. If by mistake he becomes a member, the company can rescind the transaction and remove his name from register. But, a minor may, acting though his lawful guardian become a shareholder by transfer or transmission of fully paid shares to him. 14. Liability for torts: A tort is a civil wrong. A minor is liable for tort. Example: A boy aged 16 yrs cannot disrespect national flag. Case law: of *Mohori Bibi vs. Dharmo Das Ghose (1903),* "A, a minor borrowed ₹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.
(B) Person of unsound mind	As per Section 12, a person is of unsound mind if he is not capable of understanding the terms of contract and form a rational judgement as to its effect.

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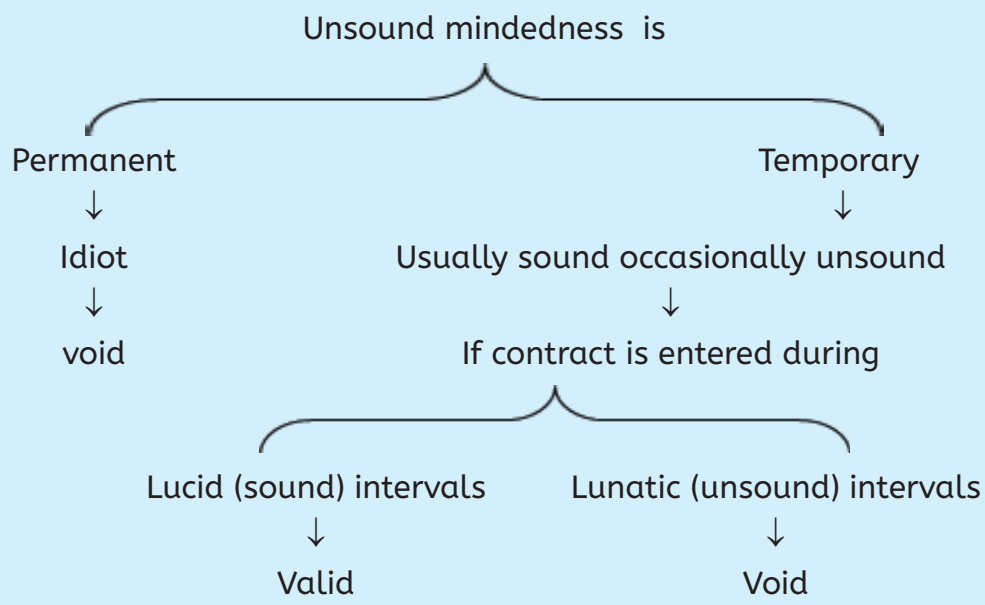
<tr><td></td><td> 
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<tr><td>(C) Persons disqualified by law</td><td>The following persons, who are disqualified by the law to which they are subject, are not competent to enter into a contract.
1. Alien enemies:
An ‘alien’ is a person who is a foreigner to the land. He may be either an ‘alien friend’ or an ‘alien enemy.’ If the country of the alien is at peace with the country of his stay, he is an alien friend. And if a war is declared between the two countries, he is termed as an alien enemy.
2. Insolvents:
When a person is declared as an insolvent, his property shall vest with the Receiver or ‘Official Assignee’. However, this disqualification of an insolvent is removed ‘when the court passes an order of discharge i.e when he is declared as solvent again.
3. Convicts:
A convict cannot enter into a contract while he is undergoing imprisonment. But when he is pardoned or the punishment gets over, he becomes capable of entering into a contract. Thus, the incapacity is only during the period of punishment.
4. Corporation and a company:
The contractual capacity of the corporation is expressly defined by the Special Act under which it is created. Whereas, the contractual capacity of a company, registered under the Companies Act 2013, is regulated by the terms of its ‘Memorandum of Association’ and the provisions of the Companies Act. If a company enters into a contract which is outside its object clause given in Memorandum of Association, it is void-ab-initio.</td></tr>
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	5. Foreign sovereigns, diplomatic staff, and accredited representatives of foreign states: Such persons can enter into valid contracts and can enforce them in Indian courts. However, a suit cannot be filed against them, in the Indian courts, without the prior sanction of the central government.

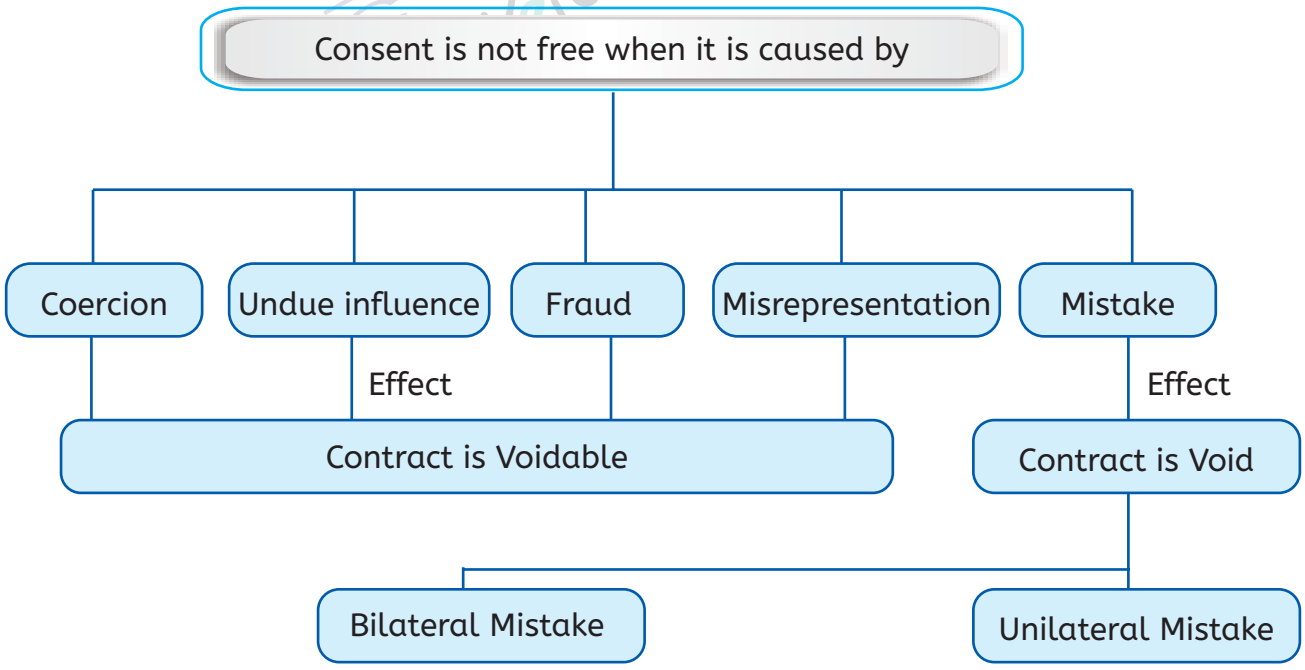
FREE CONSENT

The term 'consent' is defined in Section 13 of the Indian Contract Act, as under "Two or more persons are said to consent when they agree upon the same thing in the same sense. " It is also known as consensus-ad-idem (i.e. meetings of the minds). For the creation of contract, there must be consensus-ad-idem.

The term 'free consent' may be defined as the consent which is obtained by the free will of the parties, and neither party was forced or induced to give his consent. It is defined in Section 14 of the Indian Contract Act, as under:

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.



COERCION (Section 15)	➢ "Coercion is committing or threatening to commit, any act forbidden by the Indian Penal Code or unlawfully 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 agreements. ➢ Physical force is involved. ➢ Since no relationship is required for coercion, it can be exercised by 3rd party on 3rd party ➢ Suicide also amounts to coercion. ➢ Effects of coercion: (i) Contract induced by coercion is voidable at the option of the party whose consent was so obtained i.e aggrieved party (Section 19). In other words, either aggrieved party can rescind the contract or affirm the contract. (ii) If such voidable contract is rescinded by the aggrieved party, then if any benefit is derived should be returned back 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. ➢ Example: A threatens B that if he does not sell his house worth ₹ 5 crores for ₹ 5 lacs, A will kill B. Here, B's consent is obtained by coercion.
UNDUE INFLUENCE (Section 16)	➢ A contract is said to be induced by "undue influence" where the relations subsisting between the parties are such that one of the parties is in a position to dominate the will of the other and uses that position to obtain an unfair advantage of the other ➢ Analysis of Section 16 (1) Relation between the parties: A person can be influenced by the other when a near relation between the two exists. (2) Position to dominate the will: Relation between the parties exist in such a manner that one of them is in a position to dominate the will of the other. A person is deemed to be in such position in the following circumstances: (a) Real and apparent authority: Where a person holds a real authority over the other as in the case of master and servant, boss and employee and etc. (b) Fiduciary relationship: Where relation of trust and confidence exists between the parties to a contract. Such type of relationship exists between father and son, solicitor and client, doctor and patient etc.

	(c) Mental distress: An undue influence can be used against a person to get his consent on a contract where the mental capacity of the person is temporarily or permanently affected by the reason of mental or bodily distress, illness or of old age. (d) Unconscionable bargains: Where one of the parties to a contract is in a position to dominate the will of the other and the contract is apparently unconscionable i.e., unfair, it is presumed by law that consent must have been obtained by undue influence. Unconscionable bargains are witnessed mostly in money-lending transactions and in gifts. Case law: *Kirpa Ram vs. Sami-Ud-din Ad. Khan (1903* A youth of 18 years of age, spend thrift and a drunkard, borrowed ₹ 90,000 on a bond bearing compound interest at 2% per month (p.m.). It was held by the court that the transaction is unconscionable, the rate of interest charged being so exorbitant (3) The object must be to take undue advantage: Where the person is in a position to influence the will of the other in getting consent, must have the object to take advantage of the other. ➢ Mental force is involved ➢ Can be exercised between same parties only as relationship is required. ➢ The effect of undue influence is that it makes the contract voidable at the option of the party whose consent is obtained by undue influence, i.e., such party can put an end to the contract if he so chooses (Section 19) ➢ Any such contract may be set aside either absolutely or, if the party who was entitled to avoid it has received any benefit there under, upon such terms and conditions as to the Court may seem just. Example: A, a money lender advances ₹1,00,000 to B, an agriculturist, and by undue influence induces B to execute a bond for ₹2,00,000 with interest at 6 percent per month. The court may set aside the bond, ordering B to repay ₹1,00,000 with such interest as may seem just.
FRAUD (Section 17)	➢ The term 'fraud' may be defined as an intentional, deliberate or willful misstatement of facts, which are material for the formation of a contract. ➢ Fraud means and includes any of the following acts committed by a party to a contract with intent to deceive another party thereto or to induce him to enter into the contract : 1. The active concealment of a fact by one having knowledge or belief of the fact;

2. A promise made without any intention of performing it;
3. Any other act fitted to deceive(cheat);
4. Any such act or omission as the law specially declares to be fraudulent.
5. Person making the statement does not believe it as true

➢ Example: A, intending to cheat B, falsely represented that five tonnes of ice was manufactured daily in his factory. And thereby, induced B to buy the factor. In fact, the production was 3.5 tonnes per day. The contract is voidable at the option of B, as his consent is obtained by fraud.

➢ Mere silence does not amount to fraud.

If the defect in the goods is visible, then it is not the duty o seller to disclose such defect. 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. There is no duty to disclose facts which are within the knowledge of both the parties.

Silence is fraud:

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: 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.

   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 contract can be avoided.

      Example: In life Insurance contract, the person who takes such insurance has to disclose if he smokes cigarette or drinks alcohol.

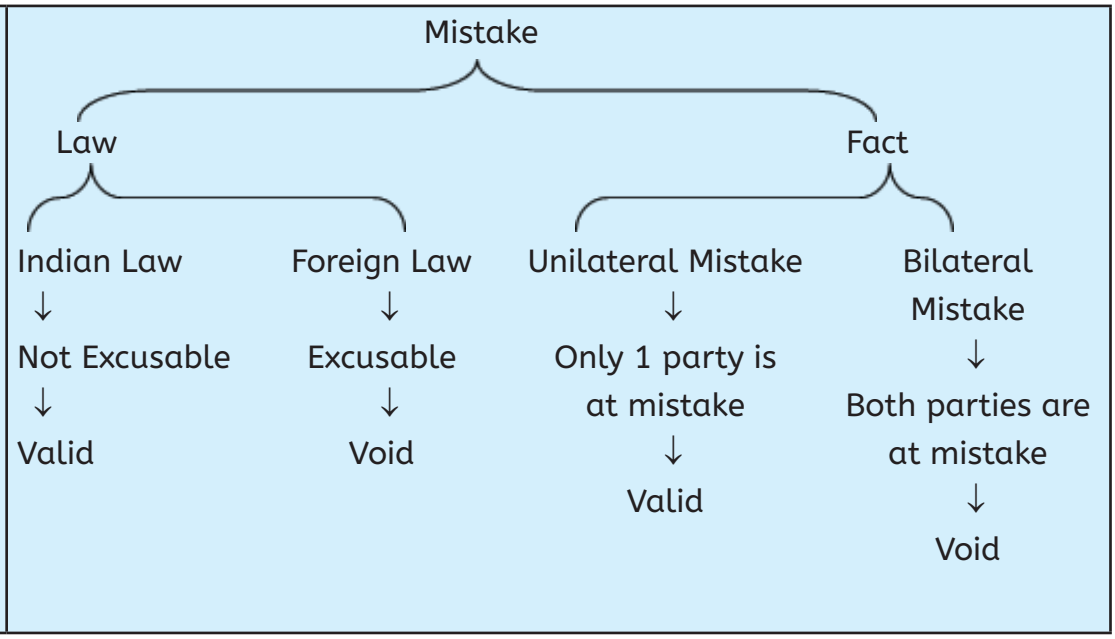
   c) Contracts of marriage: Every material fact must be disclosed by the parties to a contract of marriage.

      Example: If the grooms or brides have some health issues, that is to be disclosed.

	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. ➢ 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.
MISREPRESENTATION (Section 18)	➢ The term 'misrepresentation' may be defined as an innocent misstatement of facts which are material for the contract. In other words, misrepresentation is a false representation which is made innocently (i.e., without any intention to deceive the other party), ➢ A 'representation: means a statement of facts made by one party to the other with a view to induce the other party to enter into the contract. ➢ There is no intention to cheat, hence it is not forbidden by Indian Penal Code ➢ Person making the statement does believes it as true ➢ The effect of misrepresentation is that it makes the contract voidable at the option of the party whose consent was obtained by misrepresentation i.e., such party may put an end to the contract if he so chooses. Aggrieved party cannot claim damages (Section 19) ➢ Example: A, by misrepresentation, lead B erroneously to believe that five hundred T.V. sets were manufactured per month in his factory. Upon this representation, B bought the factory. The actual production was found to be only four hundred sets per month. Here, B's consent is caused by misrepresentation, and thus, the contract is voidable at his option.

EFFECT OF COERCION, UNDUE INFLUENCE, FRAUD, MISREPRESENTATION (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.

MISTAKE (Section 20 to 22)



UNLAWFUL OBJECT AND UNLAWFUL CONSIDERATION Section 23&24

1. Agreement forbidden by law: Acts forbidden by law means acts that are punishable under any Statute or Rules or Regulations made under any Statute.
   Example: A orders B to cut trees without permission of Municipality. Such agreement is void.

2. Agreement defeating the provisions of law or defeating any rule for the time being in force.
   Example: As per Payment of Bonus Act, minimum bonus to be paid to employees is 8.33 % of the salary. But A contracts with his employee B to pay him bonus of 5 % of salary. This agreement is defeating law and hence void.

3. Where object or consideration is unlawful because it involves or causing injury to a person or loss of property.
   Example: 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.

4. Where consideration is immoral.
   Example: A landlord cannot recover the rent of a house knowingly let to prostitute who carries on her business there. Here, the object being immoral, the agreement to pay rent is void.

5. Where object is fraudulent.
   Example: A, B, C agree to do fraud with public and the profits will be shared equally. This agreement is void.

6. An agreement which is against the general public, is said to be an agreement opposed to public policy.

a) Trading with an enemy:

Trading with an enemy is regarded as opposed to public policy. Thus, an agreement made with an alien enemy is unlawful on the ground of public policy, and is void.

b) Trafficking in public offices :

The agreements which affect the normal working of government offices are void as they are opposed to public policy e.g., appointment decisions in consideration of money are void. Similarly, the agreement for the procurement of a public recognition such as Param Veer Chakra or any other title, for monetary or other consideration, is void.

c) Interference with course of law and justice:

Any agreement with the object of inducing a judicial officer or administrative officer of the state to act corruptly or not impartially is void.

d) Stifling prosecution:

Any agreement to stifle or prevent illegally any prosecution is void as it would amount to abuse of justice.

Example: A offered ₹ 5 lacs to investigating officer to hide the evidences found during investigation.

e) Maintenance and Champerty:

Maintenance is promotion of litigation in which the litigant has no interest. Champerty is bargain whereby one party agrees to assist the other in recovering property with a view to sharing the profit of litigation.

Example:

f) Marriage brokerage contracts:

An agreement to procure the marriage of a person in consideration of a sum of money is called a 'marriage brokerage contract'. Such agreements being opposed to public policy are void.

g) Interest against obligation:

The following is example of agreement that are void as they tend to create an interest against obligation. The object of such agreements is opposed to public policy. A, who is the manager of a firm, agrees to pass a contract to X if X pay to A 20000 privately; the agreement is void.

h) Agreement for the creation of monopolies:

Agreements having for their object the establishment of monopolies are opposed to public policy and therefore void.

AGREEMENTS EXPRESSLY DECLARED AS VOID

1. Agreement in restraint of trade (Section 27):

Any agreement through which a person is restrained from exercising a lawful profession, trade or business of any kind is to that extent void. The object of this law is to protect trade. The restraint, even if it is partial, will make the agreement void.

However there are certain exceptions:

(i) Where a person sells his business along with the goodwill to another person, agrees not to carry on same line of business in certain reasonable local limits, such an agreement is valid.

(ii) An agreement through which an outgoing partner will not carry on the business of the firm for a reasonable time will be valid, though it is in restraint of trade.

(iii) An agreement of service through which an employee commits not to compete with his employer is not in restraint of trade.

Example: 'B' is a Doctor and he employs 'A' a junior Doctor as his assistant. 'A' agrees not to practice as Doctor during the period of his employment with 'B' as a Doctor independently. Such an agreement will be valid.

(iv) Trade Combinations are valid as long as they are not creating monopoly: An agreement between manufacturer and a wholesale merchant that the entire production during a period will be sold by the manufacturer to the wholesale merchant is not in restraint of trade. An agreement among sellers not to sell a particular product below a particular price is not an agreement in restraint of trade.

2. Agreement in restraint of legal proceedings (Section 28):

An agreement in restraint of legal proceedings resulting in restriction of one's right to enforce legal rights is void. Similarly any agreement which abridges the usual period for commencing the legal proceedings is also void.

In simple words, any agreement which restricts right to sue or waives right to sue or limits the time of justice is void.

However there are certain exceptions:

(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. Arbitration means settlement outside the court.

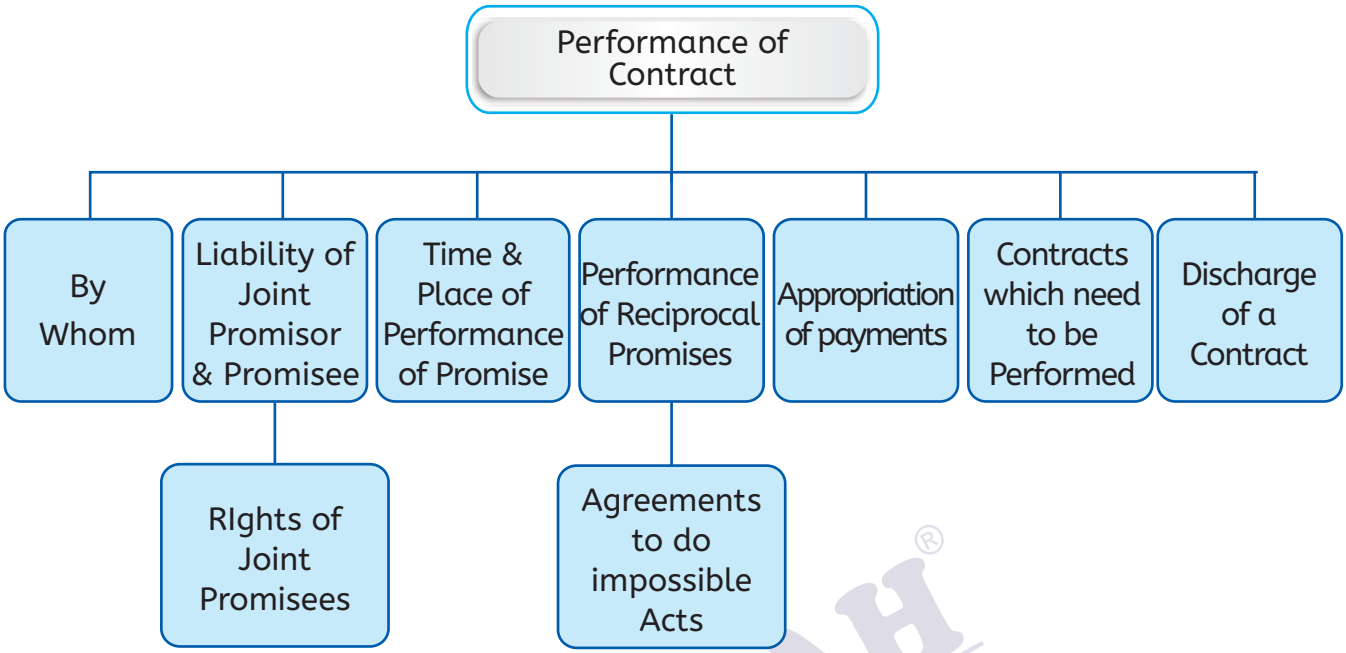
(ii) Contracts specifying the courts.

3. Wagering Agreements (Section 30):

Meaning	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.
Example	A agrees to pay ₹ 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.
Are wagering agreements Valid or Void?	The wagering agreements are void. But collateral to wagering are valid. Illegal agreements are void and collateral to illegal are also void.
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.
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.
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 (1957)* Facts: A crossword puzzle was given in magazine. Above mentioned 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).
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. ➢ In these transactions in which delivery of goods or shares is intended to be given or taken, do not amount to wagers.
Horse Race Transactions	A horse race competition where prize payable to the bet winner is less than ₹500 is a wager.
Chit Fund	Chit fund does not come within the scope of wagering. 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.
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. Contingent Contracts are covered in Unit 6. Distinction between Contract of Insurance and Wagering Agreement - covered in Unit 6
Promissory note given out of a wagering	A promissory note given out of a wagering contract is not enforceable by way of a suit. It is void.

UNIT 4: PERFORMANCE OF CONTRACT



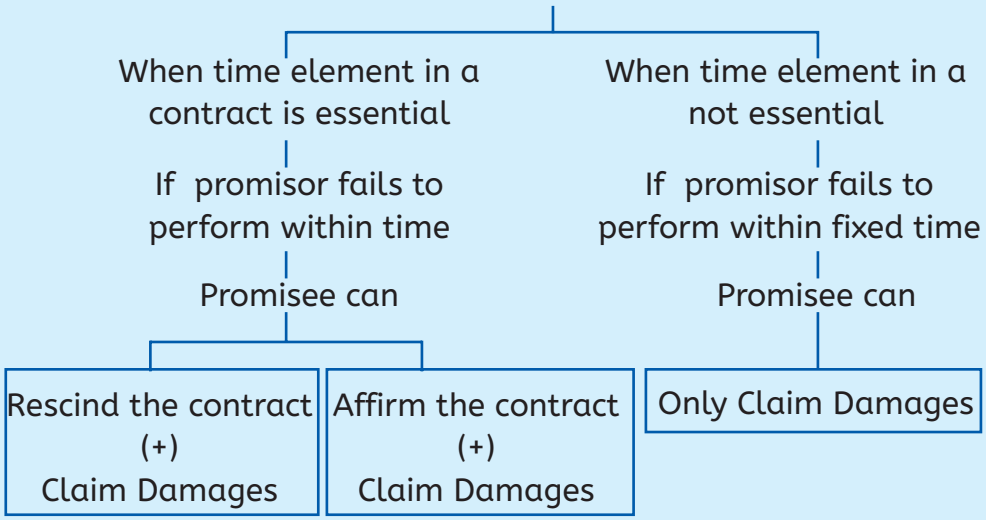
INTRODUCTION :

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. ➢ The contract must be performed by the Promisor. In case of his death, then his Legal Representative. ➢ But if the contract involves personal skills, if the promisor dies then the contract becomes void and legal representative cannot perform. ➢ Example 1: A promises to deliver goods to B on a certain day on payment of ₹1,00,000. A dies before that day. A's representatives are bound to deliver the goods to B, and B is bound to pay ₹1,00,000 to A's representatives. Example 2: A promises to paint a picture for B by a certain day, at a certain price. A dies before the day. The contract cannot be enforced either by A's representatives or by B because it involves use of personal skill. It is a contract of personal nature. ➢ It is the primary duty of each party to a contract to either perform or offer to perform his promise. Performance may be actual or offer to perform.

	➢ 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: X borrows ₹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. Example: 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.
BY WHOM A CONTRACT MAY BE PERFORMED (SECTION 37,40, 41 AND 42)	CONTRACT WILL BE PERFORMED BY: 1. Promisor himself: If there is something in the contract to show that it was the intention of the parties that the promise should be performed by the promisor himself, such promise must be performed by the promisor (Section 40). This means contracts which involve the exercise of personal skill or diligence, or which are founded on personal confidence between the parties must be performed by the promisor himself 2. Agent: W here personal consideration is not the foundation of a contract, the promisor or his representative may employ a competent person to perform it.(Section 40) 3. Representatives: A contract which involves the use of personal skill or is founded on personal consideration comes to an end on the death of the promisor. As regards any other contract the legal representatives of the decreased promisor are bound to perform it unless a contrary intention appears from the contract (Section 37). But their liability under a contract is limited to the value of the property they inherit from the deceased. 4. Third persons: W hen a promisee accepts performance of the promise from a third person, afterwards he cannot enforce it against the promisor. That is performance by a stranger, accepted by the promisee, produces the result of discharging the promisor, (Section 41)

	5. Joint promisors: When two or more persons have made a joint promise, then unless a contrary intention appears by the contract, all such persons must jointly fulfill the promise. If any of them dies, his legal representatives must, jointly with the surviving promisors, fulfill the promise. If all of them die, the legal representatives of all of them must fulfill the promise jointly (Section 42). Example: 'A', 'B' and 'C' jointly promised to pay ₹6,00,000 to 'D'. Here 'A', 'B' and 'C' must jointly perform the promise. If 'A' dies before performance, then his legal representatives must jointly with 'B' and 'C' perform the promise, and so on. And if all the three (i.e. 'A', 'B' and 'C') die before performance, and then the legal representatives of all must jointly perform the promise.
DISTINCTION BETWEEN SUCCESSION AND ASSIGNMENT	➢ Succession: When the benefits of a contract are succeeded by a process of law, both the burden and the benefit would sometimes devolve on the legal heir. For example 'B' is the son of 'A'. Upon A's death 'B' will inherit all the assets and liabilities of 'A' [These assets and liabilities are also referred to as debts and estates] Thus 'B' will be liable to all the debts of 'A', but if the liabilities inherited are more than the value of the estate [assets] inherited it will be possible to pay only to the extent of assets inherited. ➢ Assignment: Assignment is voluntary transfer of right. Unlike succession, the assignor can assign only the assets to the assignee and not the liabilities.
EFFECT OF REFUSAL TO ACCEPT OFFER OF PERFORMANCE (REQUIREMENTSOF A VALID PERFORMANCE) (Section 38)	➢ Where a promisor has made an offer of performance to the promisee, and the performance has not been accepted, then the promisor is not responsible for non performance. ➢ The attempted performance to be valid must fulfill the following conditions: (1) It must be unconditional: The performance must be in accordance with the terms of the contract (2) Performance must be at a proper time and place: What is proper place and time normally depends on facts and circumstances of the case. Performance must be within reasonable time.

	(3) Performance must give reasonable opportunity for inspection: If the offer is an offer to deliver anything to the promisee, the promisee must have a reasonable opportunity of inspecting the performance.
EFFECT OF A REFUSAL OF PARTY TO PERFORM PROMISE (Section 39)	➢ When a party to a contract has refused to perform or disabled himself from performing his promise in its entirety, the following two rights accrue to the aggrieved party namely: (i) To terminate the contract; OR (ii) Continue the contract. The aggrieved party can also claim damages. ➢ Example : A, a singer, enters into a contract with B, the manager of a theatre, to sing at his theatre two nights in every week during the next two months, and B agrees to pay her Rs. 100 for each night's performance. On the sixth night, A willfully absents herself from the theatre. B is at liberty to put an end to the contract.
LIABILITY OF JOINT PROMISOR (Section 42 to 44)	Where two or more persons enter into a joint agreement with one or more person, the promise is known as a joint promise. Example: A, B, and C jointly borrowed a sum of Rs.15000 from X, and jointly promised to repay the amount. It is a joint promise. 1. The joint promisors or their representatives must jointly perform the promise (Section 42): The joint promisors must jointly fulfill the promise during their joint life time. And if anyone of them dies, his legal representatives must jointly with the surviving promisors fulfill the promise. On the death of all the promisors, the representatives of all of them must jointly fulfill the promise 2. The promisee may compel anyone of the joint promisors to perform the promise (Section 43): Example: A, B and C are under a joint promise to pay D ₹3,00,000. C is unable to pay anything A is compelled to pay the whole. A is entitled to receive ₹1,50,000 from B. 3. The promisee may release one of the joint promisors (Section 44): 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: 'A', 'B' and 'C' jointly promised to pay ₹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 ₹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.
EFFECTS OF FAILURE TO PERFORM AT A TIME FIXED IN A CONTRACT IN WHICH TIME IS ESSENTIAL (Section 55)	Effects of failure to perform at a time fixed in a contract which time is essential  ➢ Effects of Failure to Perform at a Time Fixed in a Contract in which Time is Essential 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 i.e promisee can either rescind or affirm the contract, if the intention of the parties was that time should be of essence (important) 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.
IMPOSSIBILITY OF PERFORMANCE (Section 56)	(1) Impossibility existing at the time of contract: Even at the time of entering into the agreement, it may be impossible to perform certain contracts at the beginning or inception itself. The impossibility of performance may be known or may not be known to the parties (i) If the impossibility is known to the parties: A agreed with B to discover a treasure by magic. And B agreed to pay Rs. 500 to A for this act. This agreement is void (ii) If unknown to the parties: Even where both the promisor and the promisee are ignorant of the impossibility the agreement is void. Example: On 5th January, A entered into an agreement to send mangoes via ship to B. But unknown to both parties, ship had already sunk on 2nd January. It is void. (iii) If known only to the promisor: Where the promisor alone knows it is impossible to perform or even if he does not know but he should have known about the impossibility with reasonable diligence, the promisee is entitled to claim compensation for the loss suffered because of failure of the promisor to perform. Example:

(2) Supervening impossibility: When performance of a promise becomes impossible on account of subsequent developments of events or changes in circumstances, which are beyond the contemplation of parties, the contract becomes void. The idea of "supervening impossibility" is referred to as 'Doctrine of frustration' in English law. It is also called the post-contractual impossibility.

Supervening impossibility can arise due to a variety of circumstances as stated below.

(i) Accidental destruction of the subject matter of the contract:

Example: A entered into a contract to sell his house to B. But due to earthquake the house collapse. The contract becomes void

(ii) Non-existence or no -occurrence of a particular state of things:

Example: A booked movie tickets in advance. But the movie got banned & show got cancelled. Contract become void.

(iii) Incapacity to perform a contract of personal services: In case of contract of personal service, disability or incapacity to perform, caused by an Act of God e.g. illness, constitutes lawful excuse for non- performance of the contract. For example: A, a circus motor cyclist, contracted with B, the owner of a circus, to perform particular action on his motor cycle. -Before the performance, A died. In this case, the contract is discharged.

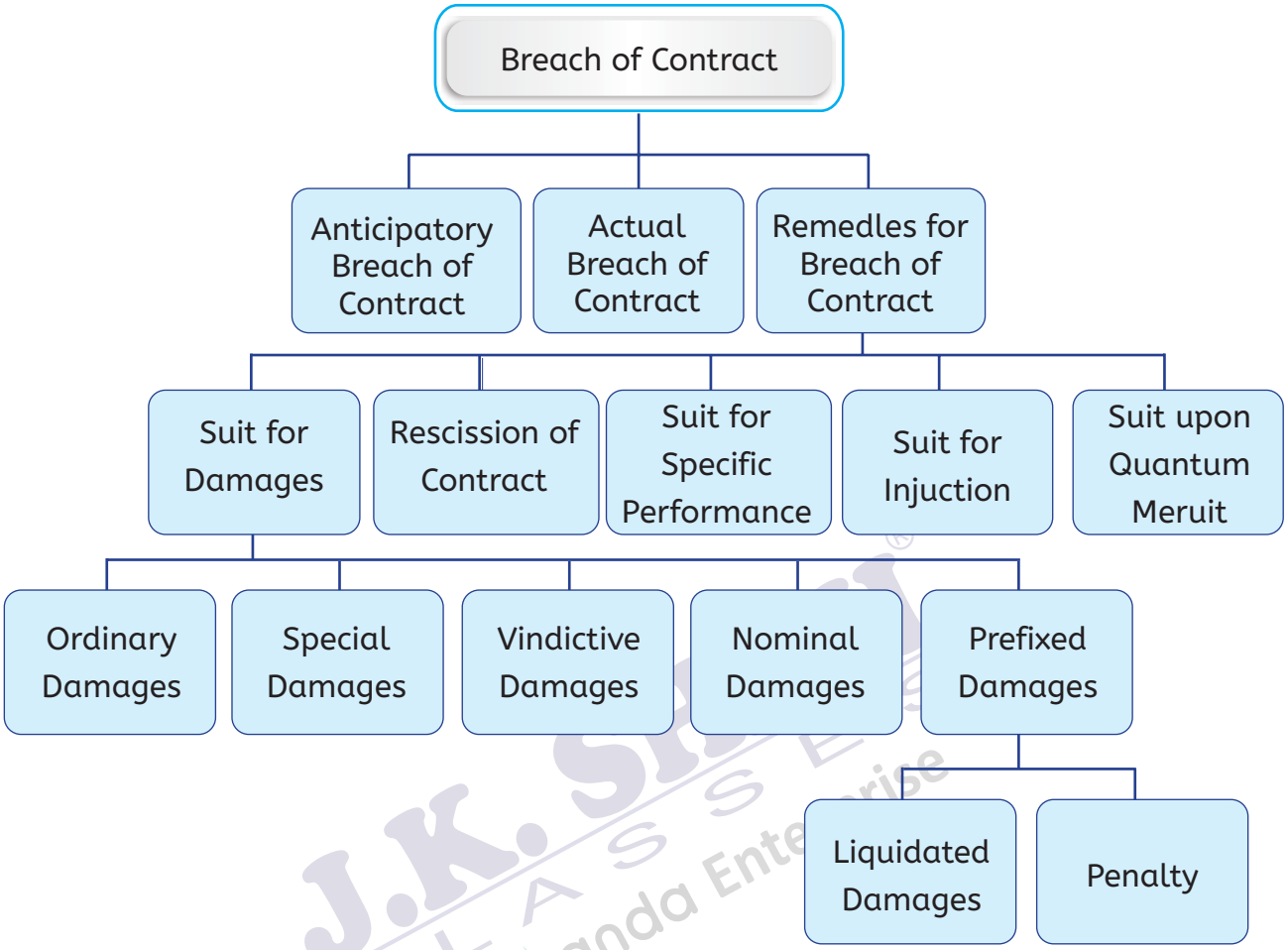
(iv) Change in law: Performance of a contract may also become impossible due to change in law subsequently. The law passed subsequently may prohibit the act which may form part as basis of contract. Here the parties are discharged from their obligations. For example 'A' and 'B' may agree to start a business for sale of lottery and contribute capital for the business. If the business of sale of lottery ticket is banned by a subsequent law, parties need not keep up their legal obligations.

(v) Outbreak of war: Outbreak of war will affect the enforceability of contracts in prohibiting or restraining transaction with alien enemy.

APPROPRIATION OF PAYMENTS (Section 59 to 61)	Sometimes, a debtor owes several debts to the same creditor and makes payment which is not enough to discharge all the debts. In such cases, the payment is appropriated (i.e., adjusted against the debts) as per Sections 59 to 61 of the Indian Contract Act. These sections contain the rules as to against which debt the payment is to be appropriated, and' may be discussed as under: 1. Where the debtor has stated that the payment made by him should be adjusted against a particular debt, the creditor must do so if he accepts the payment (Section 59). 2. Where the debtor makes payment without any indication about the appropriation of the payment, the creditor may adjust the payment according to his discretion. The creditor would like to adjust the payment against a debt which is not likely to be recovered. However, the creditor may also adjust the payment against the debts which are time barred (Section 60). 3. Where the debtor does not expressly intimate anything about the appropriation of the payment and the creditor also fails to make any appropriation, And if there is no express intimation, the law will gather his intention from the circumstances regarding the payment, e.g., if the amount paid by the debtor is the exact amount of one of the debts, it must be used to discharge that particular debt. the law prefers to wipe out the earlier debt in order of time irrespective of the fact that some of them are time barred (Section 61)., And if there are several debts of the same date, the payment shall be adjusted against each debt proportionately.
CONTRACTS, WHICH NEED NOT BE PERFORMED -WITH THE CONSENT OF BOTH THE PARTIES (Section 62, 63,66)	1. Novation : The term 'novation' means the substitution of existing contract for a new contract. In other words, when the parties to a contract agree to substitute the existing contract by a new contract, it is known as novation. The novation must be with the mutual consent of all the parties (Section 62). For example, A owes money to B under a contract. It is agreed between A, B and C that B shall thenceforth accept C as his debtor, instead of A. The old debt of A to B is at an end, and a new debt from C to B has been contracted. 2. Rescission: The term 'rescission' means the cancellation of the contract. A contract may be rescinded by mutual agreement between the parties at any time before it is discharged by performance or in some other way (Section 62)

	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. 3. Alteration: The term 'alteration' means change in one or more terms of the contract. The alteration is valid when it is made with the consent of all the parties. And the valid alteration discharges the original contract, and the parties become bound by the new contract (i.e., contract with altered terms).It is important to note here that in case of a written contract, the material alteration by one party without the consent of the other, also discharges the contract (Section 62). 4. Remission : The term 'remission' means the acceptance of lesser fulfillment of the terms of the promise, e.g., acceptance of a less sum of money where more is due. In other words, the remission is the lesser fulfillment of the promise made. The remission is the valid discharge of the whole of the liability under the contract (Section 63). For example, A owed Rs. 5,000 to B. A paid Rs. 2,000 to B, and B accepted it in full satisfaction. In this case, A is, discharged from his liability of Rs. 5,000.
RESTORATION OF BENEFIT UNDER A VOID CONTRACT (Section 64 & 65)	Quantum Meruit (as much as is earned): If any work is done, get paid for it and if any benefit is received then pay for it. 1. Any benefit received under voidable contract which is subsequently avoided is to be returned back (Section 64) Example: 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. 2. Any benefit received under void contract is to be returned back (Section 65) Example: A pays B ₹ 1,00,000, in consideration of B's promising to sell his horse. Horse was already dead at the time of the promise. The agreement is void, but B must repay A ₹ 1,00,000.

UNIT 5: BREACH OF CONTRACT



Introduction

In case of a valid contract, the parties are bound to perform their respective obligations. If any party fails to perform his obligations, there occurs a breach of the contract. The 'breach of contract' means the failure of a party to perform him obligations.

The party who fails to perform his obligations, is said to have committed a breach of contract. And a breach of a contract discharges the aggrieved party from performing his obligations. The breach of contract is of the following two types:

1. Anticipatory Breach 2. Actual Breach

1. Anticipatory Breach of Contract

It occurs when, prior to the due date of performance, the promisor absolutely refuses or disables himself from the performance of his obligations. In other words, it is a declaration by one party of his intention not to perform his obligations under the contract. Thus, the anticipatory breach is' the premature destruction of the contract, i.e., the repudiation of the contract before due date of performance.

Example:

A contracted to supply to B 100 pieces of denims on 15th December 2006. But before the due date of performance (i.e., 15th December, 2006), A informed B that he is not going to supply the denims at all. On A's refusal to supply the goods, the anticipatory breach of the contract occurs. And B may put an end to the contract.

The anticipatory breach may take place either by express refusal to perform the contract, or by some act of the promisor which makes the performance impossible.

In case of an anticipatory breach of the contract, the aggrieved party may exercise either of the following two options:

(i) He may treat the contract as discharged and bring an immediate action for damages.

(ii) He may treat the contract as operative and wait till the time of performance arrives.

2. Actual Breach of Contract

It occurs when, on the due date of performance or during the performance, a party fails to perform his obligations. Thus, the actual breach of contract may be discussed under the following two heads.

i. Actual breach of contract on the due date of performance:

Sometimes, on the due date of performance, one party fails to perform his obligations. In such cases, the other party is discharged from the performance of his obligations, and can hold the guilty party liable for the breach of contract.

Example:

A agreed to sell his car to B on 1st June. But on 1st June, A refused to sell the car to B. On A's refusal to sell the car, there occurred a breach of the contract. And B can hold A liable for the breach of contract.

ii. Actual breach of contract during its performance:

Sometimes, one party performs his obligations under the contract but the other party fails or refuses to perform his obligations. It is an actual breach of contract during its performance. And sometimes, one party, no doubt, performs his obligations but not strictly according to the contract. It is also an actual breach of contract. This type of breach of contract occurs when the party, performing the contract, commits a breach of the essential conditions to contract.

Example:

A contracted to sell 1000 goods to B to be delivered on 15th March. On the due date of delivery, A delivered the only 700 goods to B. In this case, the breach of contract is committed during the performance of the contract as A has not performed the contract according to its terms. And thus, B is not bound to take delivery of the goods and pay for them.

DAMAGES FOR BREACH OF CONTRACT (Section 73)

The term 'damages' may be defined as the monetary compensation payable by the defaulting party to the aggrieved party for the loss suffered by him. On the breach of the contract, the aggrieved party may file a suit for damages against the party who is guilty of the breach of the contract. And the guilty party is liable to pay damages to the aggrieved party.

Kinds of Damages

Following are the different kinds of damages:

1. Actual/Ordinary/ Usual damages:

   These are the damages which are payable for the loss arising naturally and directly, in the usual course, from the breach of contract. In other words, the ordinary damages are due to natural and probable consequence of the breach of the contract.

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

2. Liquidated/ Pre-fixed damages:

   Sometimes, the amount of compensation fixed for the breach of the contract is fair and genuine pre-estimate of the probable damages. Such an amount is known as liquidated damages.

   Example: On 1st January, A contracted with B to deliver goods on 15th January for ₹ 20,000. But on 1st Jan itself they had fixed damages as ₹ 6000 in the contract, in case any party breaches. Such damage are known as liquidated damages.

3. Special damages:

   These are the damages which are payable for the loss arising due to some special or unusual circumstances. In other words, the special damages are not due to the natural and probable consequences of the breach of the contract.

   The special damages are recoverable only if the parties knew about them and agree at the time of contract.

4. Exemplary/ vindictive/ punitive damages:

   The exemplary damages are claim with the intention of punishing the party in default. As a general rule, the exemplary damaged are not awarded for the breach of contract as they are punitive in nature. However, in following two cases, the court may award exemplary damages:

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

(ii) Where a banker wrongfully dishonors customers cheque, e.g., dishonor of customer's cheque when the banker has sufficient funds to the credit of the customer. In such cases, the damages are awarded taking into consideration the loss to the prestige and goodwill of the customer. The general rule, in this connection is, the smaller the amount of cheque the greater is the insult, and thus greater the amount of damages.

5. Nominal damages:

These are the damages which are very small in amount. Such damages are awarded simply to establish the right of the party to claim damages for the breach of contract even though the party has suffered no loss. Such damages are for nominal amounts like ten rupees or even ten paise.

Example:

6. Damages for deterioration caused by delay:

Compensation can be recovered even without notice for damages or 'deterioration' caused to goods on account of delay by carriers amounting to breach of contract. Here the word "deterioration" means not only physical damages but also loss of opportunity.

7. Remote or indirect damages:

These are the damages which are payable for the loss arising due to some remote or indirect causes. Generally, the remote damages are not recoverable.

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: 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 ₹ 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.

ADDITIONAL REMEDIES AVAILABLE IN CASE OF BREACH OF CONTRACT:

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

1. Suit for 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: 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: A agrees to deliver 100 bales of cottons to B at a price of ₹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.

2. Rescission of contract: When a contract is broken by one party, the other party may treat the contract as rescinded. In such a case the other party is discharged from performing his part of promise and is entitled to claim compensation for any loss that he might have suffered.

3. Suit for Specific Performance:

The term 'specific performance' may be defined as the actual carrying out the respective obligation by both the parties. Sometimes,

(i) the damages are not an adequate remedy for breach of the contract or
(ii) the damages cannot be estimated or
(iii) the subject matter of contract is unique in nature.

In such cases, the party aggrieved by the breach may bring an action for specific performance of the contract. And the court may direct the defaulting party to carry out his obligations according to the terms of the contract.

It may be noted that the specific performance of the contract cannot be claimed as a matter of right. The courts are always at discretion to grant the relief by specific performance. The courts may, at their discretion, order specific performance of contracts.

However, in following cases the specific performance cannot be ordered by court:

(i) If the performance involves personal skills
(ii) If the performance is continuous in nature

Example: 'A' agreed to sell a rare painting of Mughal period to 'B'. But on the due date of delivery, 'A'refused to sell the same. In this case, 'B' may file a suit against 'A' for obtaining an order from the Court to compel 'A' to perform the contract (i.e. to deliver the painting to 'B' at the agreed price).

4. Suit for Injunction:

The term 'injunction' may be defined as an order of the courts restraining a person from doing something which he promised not to do. In this case also, the courts are at discretion to issue an injunction order. It is, usually, issued in cases where the compensation in terms of money is not an adequate relief.

Sometimes, a party to a contract does something which he had promised not to do. In such cases, the aggrieved party may file a suit for injunction. And the courts may at their discretion, issue an order restraining such person from doing what he promised not to do.

Example: 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.

UNIT 6: CONTINGENT AND QUASI CONTRACTS

CONTINGENT CONTRACTS (Section 31 to 36)

DEFINITION

Definition of a Contingent Contract

The term 'contingent contract', in simple words, may be defined as a conditional contract. This term, in legal words, is defined in Section 31 of the Indian Contract Act, as under: contract, does or does not happen."

Example: A contracts to pay Rs.10,000 to B if his (B's) house is burnt. This is a contingent contract as its performance is dependent upon an uncertain event (i.e., burning of B's house).

ESSENTIALS OF A CONTINGENT CONTRACT

Following are the essential elements of a valid contingent contract :

1. There must be a valid contract:
   A contract to do or not to do something must be legally valid, i.e., it must fulfil the basic requirements of a valid contract.

2. The performance of the contract must be conditional:
   The performance of a contingent contract must depend upon the happening or non-happening of some future event.

3. The event must be uncertain:
   The future event, upon which the performance of a contract depends, must be an uncertain event. If the event is certain, i.e. the event is bound to happen, and then the contract is not a contingent contract.

4. The uncertain event must be collateral to the contract:
   The uncertain event, upon which the performance of the contract is dependent, must not form a part of the consideration of the contract. In other words, the event must be independent or ancillary to the contract.

RULES REGARDING ENFORCEMENT OF CONTINGENT CONTRACTS

The rules regarding the enforcement of contingent contracts are contained in Sections 32 to 36 of the Indian Contract Act, which may be discussed under the following heads:

1. Contingent Contracts Dependent on the 'Happening' of Future Uncertain Event
   A contingent contract dependent on the 'happening' of a future uncertain event can be enforced only when that uncertain event has happened [Section 32].
   Example:
   A offered to sell his horse to B for Rs. 4,000. Subsequently, A entered into a contract with C to sell the same horse to him for Rs. 3,500 if B refused to buy it. The contract between A and C is contingent and can be enforced by law only when B refuses to buy the horse from A.

However, if the event becomes impossible then such contract becomes void, and thus cannot be enforced by law.

2. Contingent Contracts Dependent on the 'Non-Happening' of Future Uncertain Event

A contingent contract dependent on the 'non-happening' of future uncertain event can be enforced only when the happening of that event becomes impossible as then that event cannot happen [Section 33].

Example:

A agreed to pay B Rs. 500 if a certain ship did not return. The ship was sunk. It is a contingent contract and can be enforced by law when the ship sinks. Because when the ship sinks, the event becomes impossible as the ship can never return.

3. Contingent Contracts dependent on future conduct of a living person (Section 34).

A contingent contract dependent on the future conduct of living person is valid if person acts accordingly otherwise it becomes void.

Case law: In *Frost V. Knight*, K promised to marry Miss.F 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 Miss.F and she was entitled to sue him for the breach of the contract.

4. Contingent Contracts Dependent on the Happening or Non- Happening of Specified Uncertain Event within Fixed Time

A contingent contract dependent on the 'happening' of a specified uncertain event within fixed time can be enforced if that event happens within the fixed time [Section 35].

Example:

A agreed to pay Rs. 1,000 to B if a certain ship returned within a year. It is a contingent contract and can be enforced by law if the ship returns within a year.

In this case also, if the event does not happen within the fixed time or if it becomes impossible before the expiry of the fixed time, then such contracts become void and cannot be enforced by law

5. Contingent Contracts Dependent on Impossible Events

A contingent contract dependent on the happening of impossible event is void and cannot be enforced by law [Section 36].

Example: A agreed to pay Rs. 500 to B if he proved that two straight lines can intersect. This is a void agreement as two straight lines can never' enclose a space.

QUASI CONTRACTS (Section 68 to 72)

DEFINITION

- 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 contracts 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 rests upon the maxims, "No man must grow rich out of another person's loss".

- It is based on the principle of "Prevention of unjust enrichment at the expense of other".

- Example: 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.

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 fixed 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 the entire world, but against a particular person or persons only, so that in this respect it resembles a contractual right.

CIRCUMSTANCES (OR CASES) OF QUASI CONTRACTS

Following are the circumstances in which the quasi contractual obligations arise. These are contained in Sections 68 to 72 of the Indian Contract Act :

1. Supply of necessaries to persons who are incompetent to contract (Section 68)
2. Payment by an interested person (Section 69)
3. Non-gratuitous acts (Section 70)
4. Finder of goods (Section 71)
5. Payment of money or deliver of goods by mistake or under coercion (Section 72)

1. **Supply of Necessaries to Persons Incompetent to Contract:**

Sometimes, a person supplies the necessaries to a person who is not competent to contract (i.e., minor, persons of unsound mind such as lunatics, etc.), or to another person to whom the incompetent person is bound to support. In such cases, the person supplying the necessaries is entitled to recover the cost of necessaries from the property of such incompetent person even if there is no valid contract between them.

Example:

A supplied necessaries of life to B, a minor, in this case, A is entitled to claim back from B's property.

2. **Payment by a Person Having Some Interest in Payment:**

Sometimes, a person makes the payment which is the legal duty of another person. In such cases, the person who has made the payment can recover such money from the person who is legally bound to pay.

Following conditions must be satisfied for the recovery of payment by an interested person:

(a) The person making the payment must have some interest in paying the amount.

(b) The person making the payment must not be bound by law to pay the amount.

(c) The other person from whom the money is to be recovered must be legally bound to pay the money.

Example:

A held land in Bengal on a lease granted by B, a Zamindar. The revenue payable by B fell in arrears. As such, his land was advertised for sale by the government. Under the Revenue Law, the consequences of such sale was the cancellation of A's lease. In order to prevent the consequent annulment of his lease, A paid to the government the amount due from B. In this case, A is entitled to recover the amount from B. And B is bound to pay the same to A.

3. **Non-Gratuitous Acts:**

The 'non-gratuitous- acts' means the acts which are not done free. A person, who does some non-gratuitous acts for another, is entitled to recover compensation for such acts if the other person enjoys the benefits of such acts.

Following conditions must be satisfied for recovery of compensation for non-gratuitous act:

(a) The person must lawfully do something for another person or deliver something to him.

(b) The person doing some act or delivering something must not intend to act gratuitously.

(c) The other person must voluntarily accept the acts or goods and he must have enjoyed their benefits.

Example:

A, a tradesman, gave certain goods to B to store at B's warehouse by paying rent. B sold A's goods to C for ₹ 100,000 without A's permission. A can claim 100,000 from B.

Case law: *Shyam Lal vs. State of U.P.*

Shyamlal, a government servant was compulsorily retired by the government due to his misconduct in job. He filed a petition and obtained a stay order against the order of government. He was reinstated and was paid salary but was given no work and in the mean time government went on appeal. The appeal was decided in favour of the government and Shyamlal was directed to return the salary paid to him during the period of reinstatement.

4. Finder of Goods:

Sometimes, a person finds certain goods, belonging to some other person. In such cases, the goods not become the property of the finder.

The law imposes certain obligations on the finder of goods. Under the law, the responsibility of finder of goods is the same as that of a bailee.

A 'bailee' is a person to whom the goods have been delivered for some specific purpose upon a condition that on the fulfillment of the purpose, the goods shall be returned to the actual owner.

Thus, it becomes the duty of the finder to keep the goods with care and take some steps to trace the true owner and return the goods to him. He is bound to take as much care of the goods as a man of ordinary prudence would take for his own goods under the similar circumstances.

He also gets some rights in respect of the goods in certain circumstances, when the true owner cannot be found, he can sell the goods which are of perishing nature.

Case law: *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 the lawful expenses to 'F' 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: '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.

5. Payment of Money or Delivery of Goods by Mistake or Under Coercion Sometimes, a certain amount of money is paid or something is delivered to a person by mistake or under coercion. In such cases, the person receiving the money or goods must repay or return the same to the person who has paid or delivered by a mistake or under coercion.

Example:

A and B jointly owed Rs. 1000 to C. A alone paid the amount to C. And B not knowing this fact, also paid Rs.1000 to C. In this case, C is bound to repay the amount to B who has paid it by mistake.

3. THE INDIAN CONTRACT ACT, 1872 (SPECIAL CONTRACT)

Introduction

In CPT/ CA Foundation you have studied Indian Contract Act, 1872, from Section 1 to 75. Sections 76 to 123 were sections related to Sale of Goods which were repealed from this Act and Sale of Goods Act, 1930 was formed. In this chapter we will study from Section 124 to Section 238 divided in following 3 units:

Unit 1: Contract of Indemnity and Guarantee

Unit 2: Bailment and Pledge

Unit 3: Agency

UNIT 1: CONTRACT OF INDEMNITY AND GUARANTEE

INDEMNITY

1.1: Meaning of Indemnity Contract (Section 124)

- As per Section 124, indemnity contract is a contract, by which one party promises to save the other from loss caused to him by the conduct of the promisor himself or by the conduct of any other person, is called a contract of indemnity.

- To indemnify means to compensate or make good the loss. The contract of indemnity is entered into with the object of protecting the promisee against anticipated losses.
- The person who promises to make good the loss is called 'indemnifier' and the person whose loss is to be made good is called the 'indemnified' or 'indemnity-holder.
- However, the above definition of indemnity restricts the scope of contracts of indemnity in as much as it covers only the loss caused:
  (i) By the conduct of the promisor himself, or
  (ii) By the conduct of any other person.
  Thus, loss occasioned by the conduct of the promisee, or accident, or an act of God is not covered.
- A contract of Fire Insurance or Marine Insurance is always a contract of indemnity. But there is no contract of indemnity in case of contract of Life Insurance.
- Indemnity Contract is a contingent contract. But it is like any other contract may be express or implied. A contract of indemnity is like any other contract and must,

therefore, fulfil all the essentials of a valid contract, e.g., consideration, free consent, competency of parties, lawful object, etc.

- Example 1: Akshay contracts with his company Aarav Ltd, who funded his further education, that after he returns India after completing his studies at University of Cambridge, he will serve the Company for a period of 5 years. If Akshay fails to return to India, he will have to reimburse the Company. It is a contract of indemnity.

  Example 2 : Vivek , a shareholder of a company lost his share certificate. He applied for the duplicate. The company agreed to issue the same on the term that Vivek will compensate the company against the loss where any holder produces the original certificate. Here, there is contract of indemnity between X and the company.
- Indemnifier cannot sue third person unless there is an assignment in his favour.

1.2 Rights of indemnity holder (Section 125)

- The promisee i.e., indemnity- holder acting within the scope of his authority is entitled to recover from the promisor i.e., indemnifier the following rights:
  (a) All damages which he may be compelled to pay in any suit
  (b) All costs which he may have been compelled to pay in bringing/ defending the suit and
  (c) All sums which he may have paid under the terms of any compromise of suit.
- It may be understood that the rights contemplated under section 125 are not exhaustive. The indemnity holder/ indemnified has other rights besides those mentioned above. If he has incurred a liability and that liability is absolute, he is entitled to call upon his indemnifier to save him from the liability and to pay it off.
- The Indian Contract Act, 1872, is silent on the time of commencement of liability of indemnifier, however, on the basis of judicial pronouncements it can be stated that the liability of an indemnifier commences as soon as the liability of the indemnity-holder becomes absolute and certain.
- Please note that the Indian Contract Act is silent about the rights which the Indemnifier has on carrying out his promise to indemnify. But they are similar to the rights of a surety under section 141 of the Indian Contract Act.

GUARANTEE

1.3 Meaning of Guarantee Contract (Section 126)

- 'A contract of guarantee' is a contract to perform the promise, or discharge the liability, of a third person in case of his default.
- The person who gives the guarantee is called the 'surety', the person in respect of whose default the guarantee is given is called 'principal debtor', and the person to whom the guarantee is given is called 'creditor'.

- From the above definition, it is clear that in a contract of guarantee there are, in effect three contracts:
  (i) A principal contract between the principal debtor and the creditor
  (ii) A secondary contract between the creditor and the surety.
  (iii) An implied contract between the surety and the principal debtor whereby principal debtor is under an obligation to indemnify the surety; if the surety is made to pay or perform.
- Example: Where C requests A to lend 5,000 to B and guarantee that C will repay the amount within the agreed and time and that on C failing to do so, he will himself pay A, there is a contract of guarantee.
- Essentials of a valid Guarantee:
  1. Existence of a principal debt.
  2. Benefit to principal debtor is sufficient consideration, but past consideration is no consideration for a contract of guarantee.
  3. Existence of a liability: There must be an existing liability or a promise whose performance is guaranteed. Such liability or promise must be enforceable by law. The liability must be legally enforceable and not time barred.
  4. Consent of surety should not be obtained by misrepresentation or concealment of a material fact.
  5. Can be oral or written.
  6. If the co-surety does not join, the contract of guarantee is not valid

1.4 Consideration for Guarantee (Section 127)

- As per Section 127 of the Act, no actual consideration is required for contract of guarantee. In other words, anything done, or any promise made, for the benefit of the principal debtor, may be a sufficient consideration to the surety for giving the guarantee.
- Example: B requests A to sell and deliver to him goods on credit. A agrees to do so, provided C will guarantee the payment of the price of the goods. C promises to guarantee the payment in consideration of A's promise to deliver the goods. This is a sufficient consideration for C's promise.

1.5 Nature of Surety's Liability (Section 128)

- The liability of the surety is co-extensive with that of the principal debtor unless it is otherwise provided by the contract.
- The term "co-extensive with that of principal debtor" means that the surety is liable

for what the principal debtor is liable. Where a debtor cannot be held liable on account of any defect in the document, the liability of the surety also ceases.

- Liability of surety is of secondary nature as he is liable only on default of principal debtor. His liability arises immediately on the default by the principal debtor.
- The Creditor has a right to sue the surety directly without first proceeding against principal debtor if the agreement specifies.

1.6 Types of Guarantee (Section 129 to 131)

Specific guarantee | Continuing guarantee

1. Specific guarantee

When a guarantee is given in respect of a single debt or specific transaction and is to come to an end when the guaranteed debt is paid or the promise is duly performed, it is called a specific guarantee.

A specific guarantee once given is irrevocable. Even the death of a surely does not result in revocation or termination of guarantee. Surety's legal successors shall continue to remain liable up to the value of the assets inherited by them.

2. Continuing guarantee (Section 129)

A guarantee which extends to a series of transactions is called a continuing guarantee.

Example: A guarantees payment to B, a spice dealer, to the amount Rs.25000 for any spice he may supply to C. B supplies C with spice the value of Rs.25000, and C pays B for it. Afterwards, B supplies spice to the value of Rs.5000. C fails to pay B. The guarantee given by A was a continuing guarantee and accordingly he is liable B to the extent of 5000.

A continuing guarantee can be revoked as to future transactions in the following manner:

(1) By Notice to the creditor (Section 130): A continuing guarantee may at any time be revoked by the surety, as to future transactions, by notice to the creditor.

Example: A guarantees payment to B, a trader, for goods sold to C up to 10,000 for one year. B supplies goods to C for 4000 in the first three months. A revokes his guarantee by sending a notice. Here A shall not be liable for any goods supplied to C after his revocation, but A is liable to B for 4,000 on default of C.

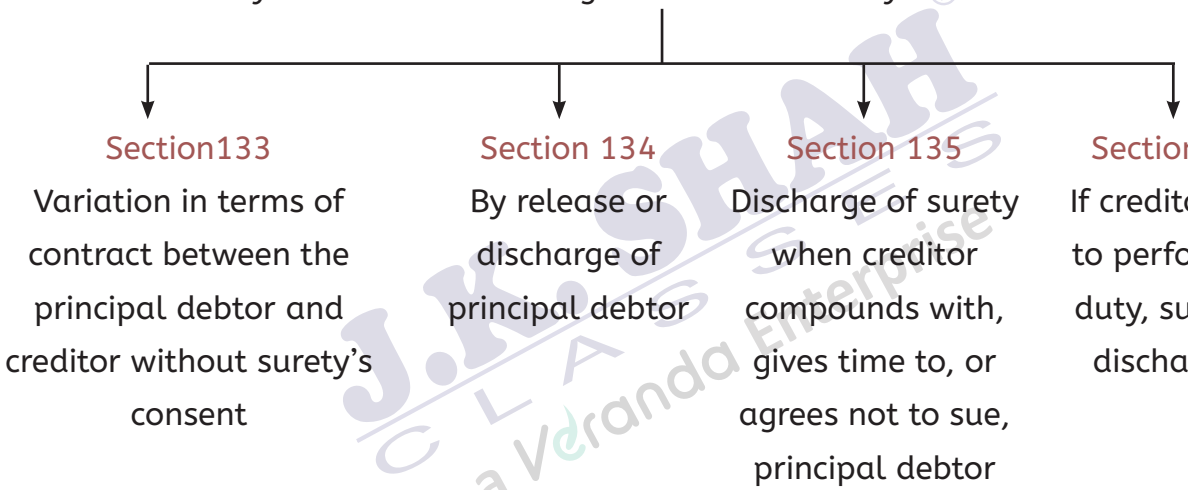
(2) By death of surety (Section 131): The death of the surety operates in the absence of any contract to the contrary, as to revocation of a continuing guarantee so for as regards future transactions.

The estate of deceased surety is, however, liable for those transactions which had already taken place during the lifetime of the deceased. Surety's estate will not be liable for the transactions taking place after the death of surety even if the creditor had no knowledge of surety's death

(3) By novation [Section 62]: The surety under original contract is discharged if a fresh contract is entered into either between the same parties or between the other parties, the consideration being the mutual discharge of the old contract.

1.7 Discharge of Surety

A surety is said to be discharged when his liability comes to an end.



1. Variation in terms of contract between the principal debtor and creditor without surety's consent (Section 133):
   - Where there is any variance in the terms of contract between the principal debtor and creditor without surety's consent, it would discharge the surety in respect of all transactions taking place subsequent to such variance.

     Example: Ajit becomes surety to Chintan for Bhairav's conduct as a manager in Chiintan's bank. Afterwards, Bhairav and Chintan contract, without Ajit's consent, that Bhairav's salary shall be raised, and that he shall become liable for one-fourth of the losses on overdrafts. Bhairav allows a customer to overdraw, and the bank loses a sum of money. Ajit is discharged from his surety ship by the variance made without his consent, and is not liable to make good this loss.
   - But if the variation is not substantial or material or which is beneficial to the surety will not discharge him of his liability.

Case law: *: M.S Anirudhan v Thomco's Bank Ltd.*, the surety guaranteed the repayment of loan provided by the bank to the principal debtor of only upto ₹25,000. Subsequently, since the bank was willing to provide loan only upto ₹20,000, the principal debtor reduced the amount to ₹20,000 in the guarantee form and without intimation to the surety gave it to the bank which was then accepted. On default by the principal debtor, the court held that the surety's liability was not discharged as the alteration was beneficial to him and not substantial.

2. By release or discharge of principal debtor (Section 134): The surety is discharged if the creditor:
   (i) Enters into a fresh/ new contract with principal debtor; by which the principal debtor is released, or
   (ii) Does any act or omission, the legal consequence of which is the discharge of the principal debtor.

3. Discharge of surety when creditor compounds with, gives time to, or agrees not to sue, principal debtor (Sector 135): A contract between the creditor and the principal debtor, by which the creditor makes a composition with, or promises to give time to, or promises not to sue, the principal debtor, discharges the surety, unless the surety assents to such contract.
   (i) Composition: If the creditor makes a composition with the principal debtor, without consulting the surety, the latter is discharged. Composition involves variation of the original contract, and, therefore, the surety is discharged.
   (ii) Promise to give time: It is one of the duties of the creditor towards the surety not to allow the principal debtor more time for payment.
   (iii) Promise not to sue: If the creditor under an agreement with the principal debtor promises not to sue him, the surety is discharged. But there is a difference between promise not to sue and "forbearance to sue." A promise not to sue is an engagement which ties the hand of the creditor. Forbearance to sue is explained in Section 137.

4. Creditor fails to perform his duty (Section 139): It is the plain duty of the creditor not to do anything inconsistent with the rights of the surety. A surety has a right to his indemnity from the principal debtor, after paying off the creditor. If the creditor's act or omission deprives the surety of the benefit of this right, the surety is discharged.

Example: Manoj contracts to build a bungalow for Nita for a given sum, to be paid by instalments as the work reaches certain stages. Pramila becomes surety to Nita for Manoj's due performance of the contract. Nita, without informing Pramila, prepays the last two instalments to Manoj. Pramila is discharged by this prepayment.

Case law: : *In State bank of Saurashtra Vs Chitranjan Rangnath Raja,* bank granted a loan on the security of the stock in the godown. The loan was also guaranteed by the surety. The goods were lost from the godown on account of the negligence of the bank officials. The surety was discharged to the extent of the value of the stock so lost.

1.8 Non-Discharge of Surety

The surety is not discharged in the following cases:

A surety is said to be discharged when his liability comes to an end.

Section136	Section 137	Section 138
Surety is not discharged when agreement made with third person to give time to principal debtor.	Mere forbearance on the part of the creditor to sue the principal debtor does not in the absence of any provision in the guarantee to the contrary, discharge the surety. Example: Bhavin owes to Chirag a debt guaranteed by Ayan. The debt becomes payable. Chirag does not sue Bhavin for a year after the debt has become payable. A is not discharged from his surety ship.	Where there are co-sureties, a release by the creditor of one of them does not discharge the other; neither does it free the surety so released from his responsibility to the other sureties.

1.9 Rights of Surety

- Rights against the Principal Debtor
- Rights against the Creditor

A. Rights against the Principal Debtor

(a) **Rights of subrogation (Section 140):** Where, a guaranteed debt has become due, or default of the principal debtor to perform a guaranteed duty has taken place, the surety, upon payment or performance of all that he is liable for, gets all the rights which the creditor had against the principal debtor. This right is known as right of subrogation. It means that on payment of the guaranteed debt, or performance of the guaranteed duty, the surety steps into the shoes of the creditor.

(b) **Implied promise to indemnify surety (Section 145):** In every contract of guarantee there is an implied promise by the principal debtor to indemnify the surety. The surety is entitled to recover from the principal debtor whatever sum he has rightfully paid under the guarantee, but no sums which he has paid wrongfully.

Example: Paras is indebted to Shashank, and Suneet is surety for the debt. Shashank demands payment from Suneet, and on his refusal sues him for the amount. Suneet defends the suit, having reasonable grounds for doing so, but is compelled to pay the amount of the debt with costs. He can recover from Paras the amount paid by him for costs, as well as the principal debt.

B. Rights against the Creditor

(a) **Surety's right to benefit of creditor's securities (Section 141):** A surety is entitled to the benefit of every security which the creditor has against the principal debtor at the time when the contract of surety ship is entered into, whether the surety knows of the existence of such security or not; and, if the creditor loses, or, without the consent of the surety, parts with such security, the surety is discharged to the extent of the value of the security.

Example: Chinmay gives ₹500,000 loan to Priyam, on the guarantee of Arvind. Chinmay has also a further security for the ₹500,000 by a mortgage of Priyam's furniture. Chinmay cancels the mortgage. Priyam becomes insolvent, and Chinmay sues Arvind on his guarantee. Arvind is discharged from liability to the amount of the value of the furniture.

(b) Right to set off: If the creditor sues the surety, for payment of principal debtor's liability, the surety may have the benefit of the set off, if any, that the principal debtor had against the creditor.

(c) Right to share reduction: The surety has right to claim proportionate reduction in his liability if the principal debtor becomes insolvent.

1.10 Invalid Guarantee (Section 142 To 144)

(a) Guarantee obtained by misrepresentation invalid (Section 142):

Any guarantee which has been obtained by means of misrepresentation made by the creditor, or with his knowledge and assent, concerning a material part of the transaction, is invalid.

(b) Guarantee obtained by concealment invalid (Section 143):

Any guarantee which the creditor has obtained by means of keeping silence as to material circumstances is invalid.

Example: John engages Tony as a clerk to collect money for him, Tony fails to account for some of his receipts, and John in consequence calls upon him to furnish security for his duly accounting. Anthony gives his guarantee for Tony's duly accounting. John does not inform Anthony about Tony's previous conduct. Tony afterwards makes default. The guarantee is invalid.

(c) Guarantee on contract that creditor shall not act on it until co¬-surety joins (Section 144): Where more than 1 surety is required, guarantee given by only 1 surety is invalid until others join.

1.11 Contribution of Co-Sureties

When a debt is guaranteed by two or more sureties they are called as to co-sureties. They are liable to contribute as agreed towards the payment of the guaranteed debt.

Rules for Co-Sureties: -

(1) Co- sureties liable to contribute equally (Section 146): Where there are two or more co-sureties for the same debt or duty and the Principal debtor makes a default, the co-sureties in absence of any contract to contrary are liable to contribute equally to the extent of default. This principle applies, whether the liability arises under the same or different contracts, with or without the knowledge of each other.

Example: S1, S2, S3 are co-sureties to C for a sum of Rs.3000 lent to P. P makes a default and S1, S2, S3 are liable amongst themselves to contribute Rs.1000 each.

(2) Liability of co-sureties, bound in different sums (Section 147): Where the co-sureties have agreed to guarantee different sums, they have to contribute in the agreed ratio.

(3) Sureties' liability towards other co-sureties (Section 138): Creditor may sue any one of the co-sureties or he may release any of the co-sureties from the liability. However, this does not free the surety so released from his liability towards the other co-sureties.

(4) Mutual agreement between co-sureties (Section 132): Any understanding/mutual agreement between co-sureties interse that one of them only shall be liable as a surety will not affected the rights of the creditor in any way even if the creditor knew the arrangement between the debtors.

1.12 Distinction between Indemnity and Guarantee

Point of distinction	Contract of Indemnity	Contract of Guarantee
Number of parties/ Parties to the contract	There are only two parties namely the indemnifier (promisor) and the indemnified (promisee).	There are three parties creditor, principal debtor and surety.
Nature of liability	The liability of the indemnifier is primary and independent	The liability of the surety is secondary as the primary liability is that of the principal debtor.
Time of liability	The liability of the indemnifier arises only on the happening of a contingency.	Liability is already in existence but specifically crystallizes when principal debtor fails.
Time to Act	The indemnifier need not necessarily act at the request of indemnified.	Surety must act by extending guarantee at the request of debtor.
Right to sue third party	Indemnifier cannot sue a third party for loss in his own name as there is no privity of contract. Such a right would arise only if there is an assignment in his favour.	Surety can proceed against principal debtor in his own right because he gets all the right of a creditor after discharging the debts.

Purpose	Reimbursement of loss	For the security of the creditor
Competency to contract	All parties must be competent to contract	In the case of a contract of guarantee, where a minor is a principal debtor, the contract is still valid.
Number of Contracts	Only one original and independent contract between indemnifier and indemnified.	There are 3 contracts made between- • Creditor and principal debtor • Creditor and Surety • Surety and Principal debtor

UNIT 2: BAILMENT AND PLEDGE

BAILMENT

1.13 Meaning of Bailment

The word "Bailment" has been derived from the French word "ballier" which means "to deliver".

- Definition under Section 148: Bailment is defined under Section 148 as "A contract whereby goods are delivered by one person to another for some purpose, that the goods shall, when the purpose is over be returned or disposed off according to directions of the person delivering the goods."
- The person delivering the goods is called the "bailor". The person to whom they are delivered is called the "bailee"

1.14 Essential elements of Bailment

The essential elements of a contract of bailment are–

(1) Contract: Bailment is based upon a contract. The contract may be express or implied. No consideration is necessary to create a valid contract of bailment. Bailment is an exception to Section 25 No Consideration-No contract.

(2) Delivery of goods: It involves the delivery of goods from one person to another for some purposes. Bailment is only for moveable goods and never for immovable goods or money. The delivery of the possession of goods is of the following kinds:

(i) Actual Delivery: When goods are physically handed over to the bailee by the bailor. Example: Delivery of a mixer grinder for repair to repair shop.

(ii) Symbolic Delivery: When there is a delivery of a thing in token of a transfer of something else. Example: Delivery of the key of a car to a workshop dealer for repair of the car

(iii) Constructive Delivery: Where delivery is made by doing anything that has the effect of putting goods in the possession of the bailee or of any person authorized to hold them on his behalf.

(3) Purpose: The goods are delivered for some purpose. The purpose may be express or implied.

(4) Possession:

- In bailment, possession of goods changes. Change of possession can happen by physical delivery or by any action which has the effect of placing the goods in the possession of bailee.
- The change of possession does not lead to change of ownership. In bailment, bailor continues to be the owner of goods as there is no change of ownership.
- Where a person is in custody without possession he does not became a bailee. For example, servants of a master who are in custody of goods of the master do not become bailees. Similarly, depositing ornaments in a bank locker is not bailment, because ornaments are kept in a locker whose key are still with the owner and not with the bank. The ornaments are in possession of the owner though kept in a locker at the bank.

(5) Return of goods:

- Bailee is obliged to return the goods physically to the bailor. The goods should be returned in the same form as given or may be altered as per bailor's direction.
- Exchange of goods is not allowed. The bailee cannot deliver some other goods, even not those of higher value.
- Deposit of money in a bank is not bailment since the money returned by the bank would not be identical currency notes.

1.15 Forms and Classification of Bailment

- Forms of Bailment

(1) Delivery of goods by one person to another to be held for the bailor's purpose.
(2) Gratuitous bailment: Where neither the bailor nor the bailee gets any remuneration. For example, A lends his book to his friend.
(3) Hiring of goods.
(4) Delivering goods to a creditor to serve as security for a loan.
(5) Delivering goods for repair with or without remuneration.
(6) Delivering goods for carriage.
(7) Finder of Goods.

- Classification of Bailment

Gratuitous Bailment

The word 'gratuitous' means free of charge. So a gratuitous bailment is one when the provider of service does it gratuitously i.e. free of charge. Such bailment would be either for the exclusive benefits of bailor or bailee.

Non-Gratuitous Bailment

Non gratuitous bailment means for consideration.
Where both the parties get some benefit i.e. bailment for the benefit of both bailor & bailee

1.16 Duties and Rights of Bailor

Duties of Bailor

1. To disclose the faults (Section 150)
2. Duty to pay necessary expenses (Section 158)
3. Duty to indemnify the Bailee for premature termination (Section 159)
4. Bailor's responsibility to bailee (Section 164)

Rights of Bailor

1. Right to terminate the bailment (Section 153)
2. Right to demand back the goods at any time (Section 159)
3. Right to file a suit against a wrong doer (Section 180 and section 181)
4. Right to sue the bailee

Duties of Bailor

1. Bailor's duty to disclose faults in goods bailed [Section 150]

In case of gratuitous Bailment.

The bailor is bound to disclose to the bailee faults in the goods bailed, of which the bailor is aware, and which materially interfere with the use of them, or expose the bailed to extraordinary risks; and if he does not disclose, he is responsible for damage arising to the bailee directly from such faults.

Example: A lends a horse, which he knows to be unsound but appears sound. The horse runs madly & B in thrown & injured, A is responsible to B for damages.

In case of non-gratuitous Bailment.

If the goods are bailed for hire, the bailor is responsible for such damages, whether he was or was not aware of the existence of such faults in the goods bailed.

Example: A hires a carriage of B. The carriage is unsafe, though B is not aware of it & A is injured. B is responsible to A for the injury.

Case law: *In Hyman & Wife v. Nye & Sons (1881)*, A hired from B a carriage along with a pair of horses and a driver for a specific journey. During the journey a bolt in the under-part of the carriage broke away. As a result of this, the carriage collapsed and A was injured. It was held that B was liable to pay damages to A for the injury sustained by him. The court observed that it was the bailor's duty to supply a carriage fit for the purpose for which it was hired.

2. Duty to pay necessary expenses [Section 158]:

If the bailment is gratuitous, the bailor shall repay to the bailee the necessary expenses incurred by him and any extraordinary expenses incurred by him for the purpose of the bailment.

However, in case of non-gratuitous bailment the bailor is liable to pay the extraordinary expenses.

Example: Ashwin hired a taxi from Rohan for the purpose of going to Pune from Mumbai, during the journey, a major defect occurred in the engine. A had to pay ₹10,000 as repair charges. These are the extraordinary expenses and it is the bailor's duty to bear such expenses. However, the usual and ordinary expenses for petrol, toll taxes etc are to be borne by the bailee itself.

3. Duty to indemnify the Bailee for premature termination (Section 159):

In case of gratuitous bailment, the bailor must compensate the bailee for the loss or damage suffered by the bailee that is in excess of the benefit received, if he decides to terminate the bailment before the expiry of the period of bailment.

4. Bailor's responsibility to bailee (Section 164):

The bailor is responsible to the bailee for the following:

(i) If there was any defective title in the goods, then bailor has to compensate the bailee.

(ii) It is the duty of the bailor to receive back the goods when the bailee returns them after the time of bailment has expired or the purpose of bailment has been accomplished. If the bailor refuses to take delivery of goods when it is offered at the proper time the bailee can claim compensation for all necessary expenses incurred for the safe custody.

Rights of Bailor

1. Right to terminate the bailment [Section 153]:

If bailee does any act with regards to the goods bailed, which is not permissible as per the contract of bailment, the contract becomes voidable at the option of the bailor

Example: Aditya gave his car to mechanic for repairs but mechanic takes his wife in the car for a long drive. The contract is voidable at the option of Aditya.

2. Right to demand back the goods at any time (Section 159):

When the goods are lent gratuitously, the bailor can demand back the goods at any time even before the expiry of the time fixed or the achievement of the object.

But due to the premature return of the goods, if the bailee suffers any loss, which is more than the benefit actually obtained by him from the use of the goods bailed, the bailor has to compensate the bailee.

3. Right to file a suit against a wrong doer (Section 180 and section 181):

- Suit by bailor & bailee against wrong doers (Section 180): If a third person wrongfully takes possession of the goods or disturbs the possession of goods, or does them any injury, then the bailee will get same rights as owner and either the bailor or the bailee may bring a suit against a third person for such deprivation or injury.
- Apportionment of relief or compensation obtained by such suits (Section181): Whatever is obtained by way of relief or compensation in any such suit shall, as between the bailor and the bailee, be dealt with according to their respective interests

4. Right to sue the bailee:

The bailor has a right to sue the bailee for enforcing all the liabilities and duties of him. It includes:

(i) Right to claim compensation for loss caused to the goods by the negligence of the bailee.
(ii) Right to claim compensation for unauthorized mixing of goods.
(iii) Right to claim damages for unauthorized use of the goods.
(iv) Right to demand back goods.
(v) Right to any accretion to the goods bailed.

1.17 Duties and Rights of Bailee

Duties of Bailee
1. Take reasonable Care of the goods (Section 151 & 152)
2. Not to make inconsistent use of goods (Section 153 & 154)
3. Not to mix the goods (Section 155, 156 and 157)
4. Return the goods (Section 160 & 161)
5. Return an accretion from the Goods (Section 163)
6. Not to setup Adverse Title

Rights of a Bailee
1. Right to Deliver the Goods to any one of the Joint Bailors (Section 165)
2. Right to indemnity (Section 166)
3. Right to claim compensation in case of faulty goods (Section 150)
4. Right to claim extraordinary expenses (Section 158)
5. Right to Apply to Court to Decide the Title to the Goods [Section 167)
6. Right of particular lien for payment of services (Section 170)
7. Right of general lien (Section 171)

Duties of Bailee

1. Take reasonable Care of the goods (Section 151 & 152)
   - In all cases of bailment, the bailee is bound to take as much care of the goods bailed to him as a man of ordinary prudence would, under similar circumstances, take of his own goods of the same bulk, quality and value as the goods bailed.
   - Bailee when not liable for loss, etc., of thing bailed [Section 152]: The bailee, in the absence of any special contract, is not responsible for the loss, destruction or deterioration of the thing bailed, if he has taken the amount of care of it described in section 151.
   - Example: Abhishek deposited his goods in Rahul's godown. On account of unexpected floods, a part of the goods were damaged. It was held that, Rahul is not liable for the loss

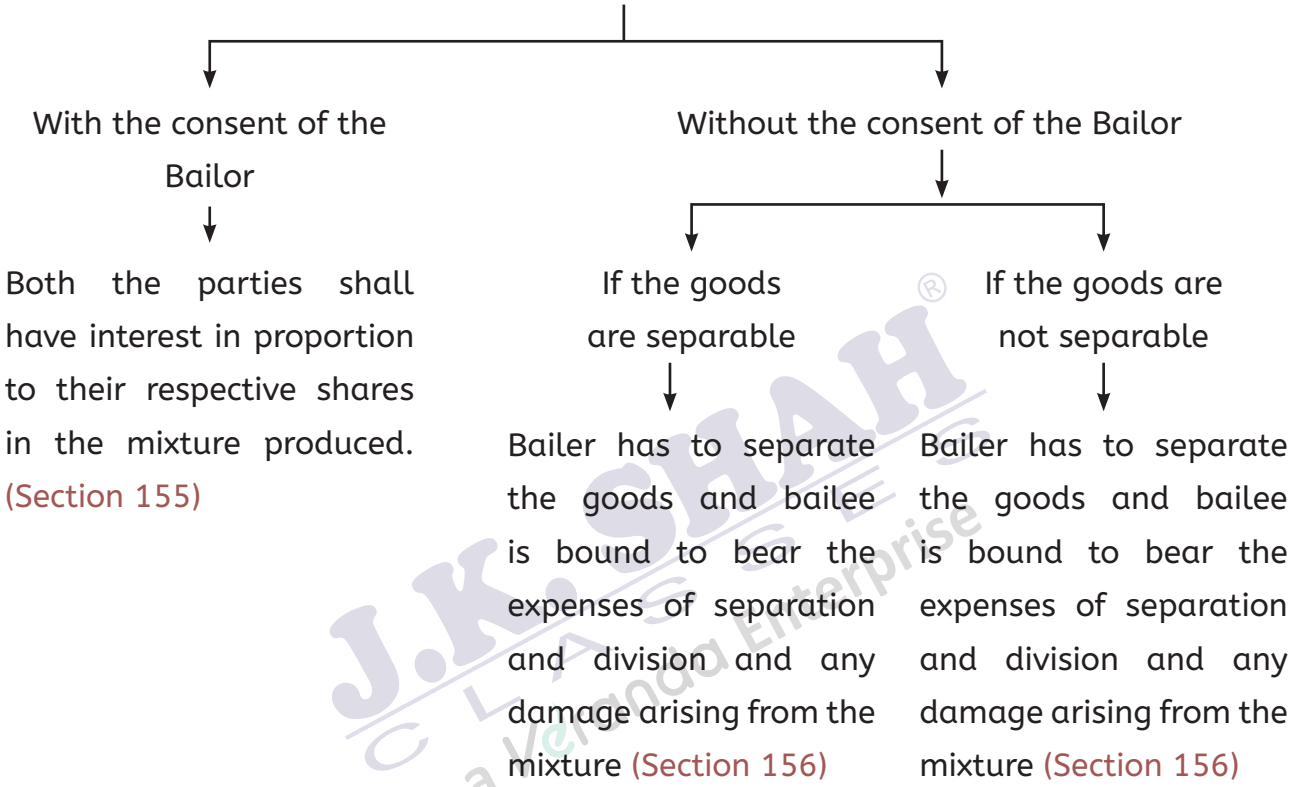
2. Not to make inconsistent use of goods (section 153 & 154): As per Section 154, if the bailee makes any use of the goods bailed, which is not according to the conditions of the bailment, he is liable to make compensation to the bailor for any damage arising to the goods from or during such use of them. If bailee does any act with regards to the goods bailed, which is not permissible as per the contract of

bailment, the contract becomes voidable at the option of the bailor

Example: Aditya gave his car to mechanic for repairs but mechanic takes his wife in the car for a long drive. The contract is voidable at the option of Aditya and Aditya can also claim damages.

3. Duty to not mix the goods (Sec. 155, 156 and 157)

If the Bailee mixes the goods bailed with this own goods:



4. Return the goods (Section 160 & 161):

- It is the duty of bailee to return, or deliver according to the bailor's directions, the goods bailed without demand, as soon as the time for which they were bailed, has expired, or the purpose for which they were bailed has been accomplished (Section 160)
- If, by the default of the bailee, the goods are not returned, delivered or tendered at the proper time, he is responsible to the bailor for any loss, destruction or deterioration of the goods from that time. (Section 161)

  Example: Vivek delivered car to Vikas to be bound. Vikas promised to return the car within a reasonable time. Vivek asked for the return of the car. But Vikas, failed to deliver car back even after the expiry of reasonable time. Subsequently the car was burnt in an accidental fire at the premises of Vikas. Here, Vikas is liable for the loss.

5. Return an accretion from the Goods (Section 163):

In the absence of any contract to the contrary, the bailee is bound to deliver to the bailor, or according to his directions, any increase or profit which may have accrued from the goods bailed.

Example: Sitaram leaves a cow in the custody of Baluram. The cow gives birth a calf. Baluram is bound to deliver the calf as well as the cow to Sitaram.

6. Not to setup Adverse Title:

Bailee must not set up a title adverse to that of the bailor. In other words, bailee should not sell the goods. He must hold the goods on behalf of and for the bailor.

Rights of a Bailee

1. Right to Deliver the Goods to any one of the Joint Bailors (Section 165):

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

Example: Ravi, Sunil, Hari are the joint owners of a car. They delivered it on hire to Shanaya for one month. After the expiry of one month, Shanaya may return the car to any one of the joint owners namely Ravi, Sunil or Hari.

2. Right to indemnity (Section 166):

Bailee is entitled to be indemnified by the bailor for any loss arising to him by reasons that the bailor's title to goods was defective. If the bailor has no title to the goods, and the bailee in good faith, delivers them back to, or according to the directions of the bailor, the bailee shall not be responsible to the owner in respect of such delivery. Bailee can also claim all the necessary expenses incurred by him for the purpose of gratuitous bailment.

3. Right to claim compensation in case of faulty goods (Section 150):

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

4. Right to claim extraordinary expenses (Section 158):

A bailee is expected to take reasonable care of the gods bailed. In case he is required to incur any extraordinary expenses, he can hold the bailor liable for such expenses.

5. Right to Apply to Court to decide the Title to the Goods (Section 167):

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

6. Right of particular lien for payment of services (Section 170):

Where the bailee has

(a) in accordance with the purpose of bailment,

(b) rendered any service involving the exercise of labour of skill,

(c) in respect of the goods, he shall have

(d) in the absence of a contract to the contrary, right to retain such goods, until he receives due remuneration for the services he has rendered in respect of them. Bailee has, however, only a right to retain the goods and not to sell it. The service must have entirely been formed within the time agreed or a reasonable time and the remuneration must have become due.

This right of particular lien shall be available only against the property in respect of which skill and labour has been used.

7. Right of general lien (Section 171): Bankers, factors, wharfingers, attorneys of a High Court and policy brokers will be entitled to retain, as a security for a general balance of amount, any goods bailed to them in the absence of a contract to the contrary. By agreement other types of bailees excepting the above given five (Bankers, factors, wharfingers, attorneys of a High Court and policy brokers) may also be given this right of general lien.

1.18 Termination of Bailment

On expiry of stipulated period:	• If the goods were given for a stipulated period, the contract of bailment shall terminate after the expiry of such period.
On fulfillment of the purpose:	• If the goods were delivered for a specific purpose, a bailment shall terminate on the fulfillment of that purpose
By Notice	• Where the bailee acts in a manner which is not permitted as per the terms of the bailment, the bailor can always terminate the contract of bailment by giving a notice to the bailee. • A gratuitous bailment can be terminated by the bailor at any time by giving a notice to the bailee. However, if the bailee suffers any loss then bailor must compensate (Section 159).
By death	• A gratuitous bailment terminates upon the death of either the bailor or the bailee.
Destruction of the subject matter	• If the original condition of the bailed goods does not exist or is destroyed, the contract of bailment is automatically terminated, because of impossibility of performance.

1.19 Finder of Goods

- The term 'finder of goods' means a person who has found some goods belonging to an¬other. When a person comes across some article he is under no duty to pick them up, but if he picks them up, he becomes a finder of goods and is subject to the same responsibil¬ity as a bailee.

- The obligations of a finder of goods:
  1) He must take reasonable care of the goods: By reasonable care we mean that much care as a man of ordinary prudence would take of his own goods under similar circumstances. If he takes that much care, the finder shall not be responsible for any loss, destruction or deterioration of the thing found.
  2) He must not use the goods for his own purpose.
  3) He must not mix them with his own goods.
  4) He must make appropriate efforts to find the true owner of the goods.

- Rights of finder of goods
  1) Right to retain goods: The finder can retain the goods against the true owner until he receives compensation for trouble and expenses incurred by him in preserving the goods and finding out the owner. This right is known as the finder's lien on the goods. But the finder cannot file a suit against the true owner for the recovery of such expense.
  2) Right to sue for reward (Section 168): If the owner has offered some reward for the return of goods and the finder has the knowledge of such reward, he can file a suit for the recovery of the award.
  3) Right to claim expenses incurred: If the finder of goods has incurred any expenses on the lost goods, he has a right to recover it from the real owner of goods.
  4) Right of sale: Section 169 permits the finder to sell the goods in the following cases:
     a) If the owner cannot be found after reasonable search; or
     b) If found, the owner refuses to pay the lawful charges to the finder; or
     c) If the thing is in danger of perishing or losing the greater part of their value; or
     d) If the lawful charges of the finder amount to two - thirds of their value.

     A finder of goods has a right to keep the goods with him against the whole world except the true owner.

1.20 Types of Lien

1) Particular Lien (Section 170):
   - If in accordance with the purpose of the bailment, any service requiring labour or skill is rendered by the bailee in respect of the goods bailed, he is entitled to remuneration. If the bailor refuses to pay for the service, the bailee has the

right to retain the goods bailed until he receives his remuneration. This right of the bailee to retain the goods is known as the particular lien of the bailee.

- In entitles the bailee to retain the goods but ordinarily he has no right to sell the goods to realize his dues. A right to sell may, however, will be given to the bailee by special agreement.
- Example: Archana delivers a rough diamond to Kapil, a jeweller, to be cut and polished, which is accordingly done. Kapil is entitled to retain the stone till he is paid for the services he has rendered.

2) General Lien (Section 171):

- A general lien is the right to retain the property of another for a general balance of account.
- Bankers, factors, wharfingers, attorney of a High Court and policy - brokers have general lien on goods coming into their possession in the course of their trade.
- No other persons have a right to retain, as a security for such balance, goods bailed to them, unless there is an express contract to the effect.
- Example: Uday borrows ₹50,000 from the bank and subsequently again borrows another ₹100,000 but with security of say certain jewellery. Here, even if Uday has returned ₹100,000 being the second loan, the banker can retain the jewellery given as security to the second loan towards the first loan which is yet to be repaid.

Difference between General lien and Particular lien

General lien	Particular lien
1. General lien means the right to keep possession of goods belonging to other against general balance of account.	1. Particular lien implies a right of the bailee to retain specific goods bailed for non-payment of amount.
2. A general lien is not automatic but is recognized through on agreement. It is exercised by the bailee only by name	2. It is automatic i.e. implied

3.	Only such persons as are specified under Section 171, example: Bankers, factors, wharfingers, policy brokers etc. are entitled to general lien.	3.	Bailee, finder of goods, pledgee, unpaid seller, agent, partner etc are entitled to particular lien
4.	It can be exercised against goods even without involvement of labour or skill.	4.	It comes into play only when some labour or skill is involved has been expended on the goods, resulting in an increase in value of goods.

PLEDGE

1.21 Meaning and Characteristics of Pledge

- Meaning: Pledge is defined under Section 172 as the bailment of goods as security for a payment of a debt or performance of a promise is called pledge/pawn.
- The person who makes such a bailment is called a pledger or pawnor and the bailee is known as pawnee/pledgee.
- Example: Pyarelal lends money to Ananya against the security of jewellery deposited by Ananya with him. This bailment of jewellery is a pledge as security for lending the money. Ananya is a pawnor and Pyarelal is a pawnee.
- Essentials of a valid pledge:
  1) Delivery of goods: Delivery of the goods may be actual or constructive or symbolic.
  2) Goods must be the subject matter of the contract of pledge. The goods pledged must be in existence
  3) Purpose of pledge is security for payment of debt.
  4) Pledge is specie of bailment.

1.22 Duties and Rights of Pawnee

Duties of Pawnee

1) Duty to take reasonable care of the pledged goods
2) Duty not to make unauthorized use of pledged goods.
3) Duty to return the goods when the debt has been repaid or the promise has been performed.
4) Duty not to mix his own goods with goods pledged.
5) Duty not to do any act which is inconsistent with the terms of the pledge.
6) Duty to return accretion to the goods, if any.

Rights of Pawnee

1) Right of retain the goods pledged (Section 173)
2) Right to retention of pledged goods for subsequent debts (Section 174)
3) Pawnee's right as to extraordinary expenses Incurred (Section 175)
4) Pawnee's right where pawnor makes default (Section 176): If the pawnor makes default in payment of the debt, or performance, pawnee may retain the goods or sell the goods.

   If the proceeds of such sale are less than the amount due, the pawnor is still liable to pay the balance.

   If the proceeds of the sale are greater than the amount so due, the pawnee shall pay over the surplus to the pawnor.

1.23 Duties and Rights of Pawnor

Duties of Pawnor

1) The pawnor is liable to pay the debt or perform the promise as the case may be.
2) It is the duty of the pawnor to compensate the pawnee for any extraordinary expenses incurred by him for preserving the goods pawned.
3) It is the duty of the pawnor to disclose all the faults which may put the pawnee under extraordinary risks.
4) If loss occurs to the pawnee due to defect in pawnor's title to the goods, the pawnor must indemnify the pawnee.
5) If the pawnee sells the good due to default by the pawnor, the pawnor must pay the deficit.

Rights of Pawnor

1) Right to redeem (Section 177): If a time is fixed for the payment of the debt, or performance of the promise, for which the pledge is made, and the pawnor makes default in payment of the debt or performance of the promise at the stipulated time, he may redeem the goods pledged at any subsequent time before the actual sale of them; but he must, in that case, pay, in addition, any expenses which have arisen from his default.

1.24 Pledge by Non-Owners

1) Pledge by mercantile agent [Section 178]:

Generally only an owner of goods can pledge, but the Act recognizes the right of certain mercantile agents to pledge it provided following conditions are satisfied:

(i) The person pledging the goods must be a mercantile agent,

(ii) Mercantile agent must be in possession either of the goods or the documents of title to goods,

(iii) Such possession must be with the consent of the owner. If possession has been obtained dishonestly or by a trick, a valid pledge cannot be effected.

(iv) Pledge must have been made by the mercantile agent, when acting in the ordinary course of business of a mercantile agent,

(v) The pledgee must act in good faith;

(vi) The pledgee should have no notice of the pledger's defect of title. If the pledgee knows that the pledger has a defective title, the pledge will not be valid.

(vii) In this section, the expressions 'mercantile agent and documents of title' shall have the meanings assigned to them in the Sale of Goods Act, 1930.

2) Pledge by person in possession under voidable contract (Section 178A): When the pawnor has obtained possession of the goods pledged by him under a contract voidable under section 19 or section 19A, but the contract has not been rescinded at the time of the pledge, the pawnee acquires a good title to the goods, provided he acts in good faith and without notice of the pawnor's defect of title.

3) Pledge where pawnor has only a limited interest [Section 179]: Where a person pledges goods in which he has only a limited interest, the pledge is valid to the extent of that interest.

Example : Mr. Ravi finds a defective mobile phone lying on the road. He picks it up, gets it repaired for 5000. He later pledges the mobile phone for 2000. The true owner can recover the mobile phone only on paying 5000.

4) Pledge by a co-owner in possession: Where the goods are owned by many persons and with the consent of other owners, the goods are left in the possession of one of the co-owners. Such a co-owner may make a valid pledge of the goods in his possession.

5) Pledge by seller or buyer in possession : A seller, in whose possession, the goods have been left after sale or a buyer who with the consent of the seller, obtains possession of the goods, before sale, can make a valid pledge, provided the pawnee acts in good faith and he has no knowledge of the defect in title of the pawnor.

Example : Taarak buys television from Jethalal but leaves it with Jethalal. Jethalal then pledges the TV with Babita, who does not know of sale to Taarak and acted in good faith. This is valid pledge.

1.25 Distinction between Bailment and Pledge

Aspects	Pledge	Bailment
Purpose	A pledge is made for a specific purpose as security for payment of debt or performance of a promise.	A bailment can be for any purpose.
Parties	The person who delivers the good as security is called the "Pawnor". The person to whom the goods are delivered as security is called the pawnee.	The person delivering the goods under a contract of bailment is called as "Bailor".

Use of Goods	A pawnee does not have the right to use the goods.	The bailee may use the goods bailed as per the terms of the contract.
Lien	Lien can be exercised even for non-payment of interest.	A bailee can exercise lien on the goods bailed only for his labour and skill employed
Sale of Goods	The pawnee can sell the goods after due notice to the pawnor.	The bailee has no right of sale.
Nature of Intrest in Property	The pledgee gets a special property in the goods. The general property remains with the pawnor.	The bailee has only right of possession of the goods bailed.

UNIT 3: AGENCY

1.26 Meaning of Agency

- Meaning: The Indian Contract Act does not define 'Agency' but it defines an agent as a person employed to do any act for another or to represent another in dealings with third person. The person for whom such act is done, or who is so represented is called the principal(Section 182).
- 'Agency' is a comprehensive word which is used to describe the relationship that arises where one person is employed by another in order to bring the latter into legal relations with a third person.
- The Rule of Agency is based on the maxim "Quit facit per alium, facitper se" i.e., he who acts through an agent is himself acting.
- Test of Agency:

  (a) Whether the person has the capacity to bind the principal and make him answerable to the third party.

  (b) Whether he can establish Privity of Contract between the principal and third parties.

  If the answer to these questions is yes, then there is a relationship of agency.

1.27 Essentials of Agency

1) Basis of the agreement:
   - According to the definition under Section 182, an agent never acts on his own, behalf but always on behalf on behalf of another.
   - He either represents his principal in any transactions or dealings with a third person, or performs an act for the principal. In either case the act of the agent will be deemed in law to be not his own but of the principal.

2) Consideration not necessary:
   - The peculiarity in the law of agency lies in the fact that unlike other forms of contract the existence of consideration in not at all necessary for its validity (Section 185).
   - Thus, a contract of agency constitutes an exception to the general rule contained in Section 25 that no contract can be valid unless it is entered into for consideration

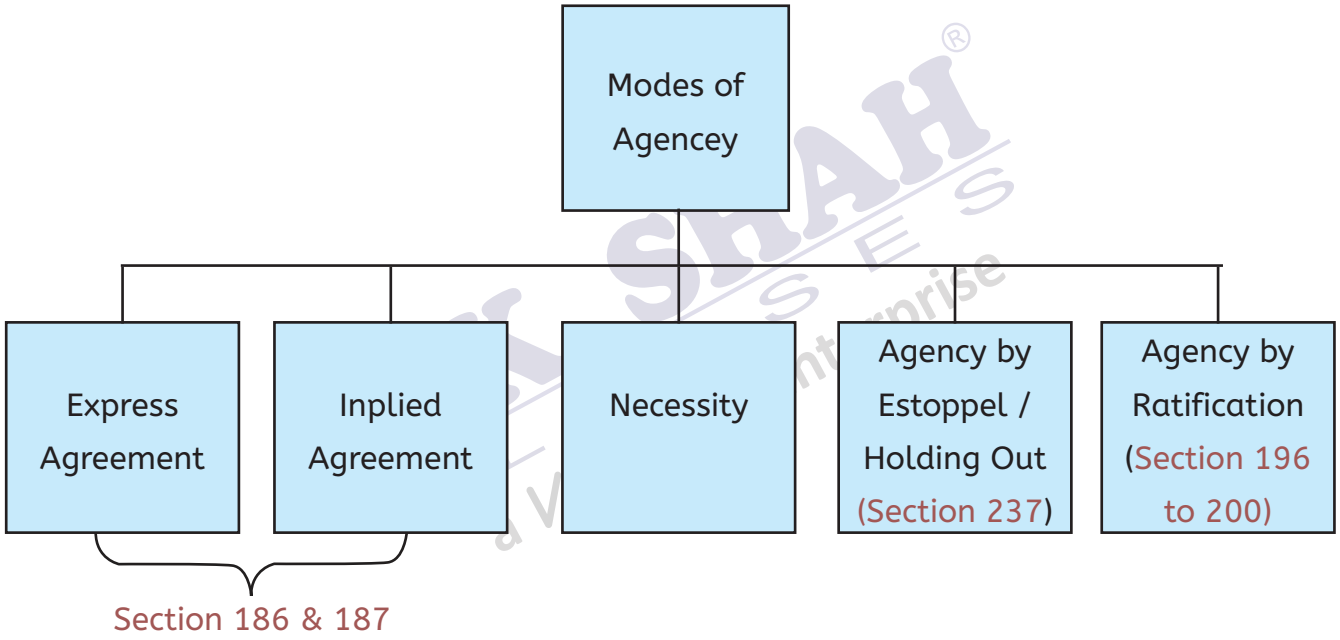
3) Capacity to employ agent:

   Only a person who has contractual capacity can lawfully employ an agent. Thus a minor or a person of unsound mind cannot appoint an agent (Section 183).

4) Capacity to be employed as agent:

- Between the principal and the third person, any person can become an agent, irrespective of whether he has contractual capacity or not. But a person who is not of the age of majority and of sound mind cannot be agent so as to be responsible to his principal.
- Even a minor can become an agent and the principal can be bound by his acts (Section 184).
- Thus, if the agent happens to be a person incapable of contracting, then the principal cannot hold the agent liable, in case of his misconduct or where the agent has been negligent in performance of his duties.

1.28 Modes of Agency



Definitions of express and implied authority (Section 186 &187)

(1) Express Authority:

- The authority of an agent may be expressed or implied (Section 186). An authority is said to be express when it is given by words, spoken or written (Section 187).

- Example: Anil is residing in Delhi and he has a house in Kolkata. Anil appoints Soham by a deed called the power of attorney, as a caretaker of his house. Agency is created by express agreement.

(2) Implied Authority:

- An authority is said to be implied when it is to be inferred from the circumstances of the case; and things spoken or written, or the ordinary course of dealing, may be accounted circumstances of the case.
  - Example: Abhijit owns a shop in Mumbai, living himself in Kolkata and visiting the shop occasionally. The shop is managed by Sudhir, and he is in the habit of ordering goods from Chirag in the name of Abhijit for the purposes of the shop, and of paying for them out of Abhijit's funds with Abhijit's knowledge. Sudhir has an implied authority from Abhijit to order goods from Chirag in the name of Abhijit for the purposes of the shop.

(3) Agency by Estoppel [Section 237]:

- An agency by estoppel is based on the principle of estoppel. According to section 237 of the Contract Act, an agency by estoppel may be created when following essentials are fulfilled:
  1. The principal must have made a representation;
  2. The representation may be express or implied;
  3. The representation must state that the agent has an authority to do certain act although really he has no authority;
  4. The principal must have induced the third person by such representation; and
  5. The third person must have believed the representation and made the contract on the belief of such representation.
- Example: If Varun (the principal) has for several moths permitted Arjun to buy goods on credit from Prasad and has paid for the goods bought by Arjun, Varun cannot later refuse to pay Prasad who had supplied goods on credit to Arjun in the belief that he was Varun's agent and was buying the goods on behalf of Varun. Varun is stopped from now asserting that Arjun is not his agent because on earlier occasions he permitted Prasad to believe that Arjun was his agent and Prasad had acted in that belief.

(4) Necessity:

- An agency of necessity arises due to some emergent circumstances. In emergency a person is authorised to do what he cannot do in ordinary circumstances. Thus, where an agent is authorised to do certain act, and while doing such an act, an emergency arises, he acquires an extra-ordinary or special authority to prevent his principal from loss.
- Example: Raman has a large farm on which Chaman is the caretaker. When Raman is in Canada, there is a huge fire on the farm. Chaman becomes an agent of necessity for Raman so as to save the property from being destroyed

by fire. Raman (the principal) will be liable for any expenses, Chaman (his agent of necessity) incurred to put out the fire and save the farm from destruction during Raman's absence from the country.

(5) Agency by Ratification

- Rights of person as to acts done for him without his authority, Effect of ratification (Section 196): Where acts are done by one person on behalf of another, but without his knowledge or authority, he may elect to ratify or to disown such acts. If he ratifies them, the same effects will follow as if they had been performed by his authority.

  Essentials of a valid Ratification

  1. Ratification may be expressed or Implied (Section 197): Ratification may be expressed or may be implied in the conduct of the person on whose behalf the acts are done.

     Example:

     A, without authority, buys goods for B. Afterwards B sells them to C on his own account; B's conduct implies a ratification of the purchase made for him by A.

  2. Knowledge requisite for valid ratification (Section 198): No valid ratification can be made by a person whose knowledge of the facts of the case is materially defective.

     Example: A has an authority from P to buy certain goods at the market rate. He buys at a higher rate but P accepts the purchase. Afterwards P comes to know that the goods purchased by A for P belonged to A himself. The ratification is not binding on P.

     If however the alleged principal is prepared to take the risk of what the purported agent has done, he can choose to ratify without full knowledge of facts.

  3. Effect of ratifying unauthorized act forming part of a transaction (Section 199): There can be ratification of an act in entirely or its rejection in entirely. The principal cannot ratify a part of the transaction which is beneficial to him and reject the rest.

  4. Ratification of unauthorized act cannot injure third person (Section 200): An act done by one person on behalf of another, without such other person's authority, which, if done with authority, would have the effect of subjecting a third person to damages, or of terminating any right or

interest of a third person, cannot, by ratification, be made to have such effect.

Example: A holds a lease from B, terminable on three days' notice. C, an unauthorized person, gives notice of termination to A. The notice cannot be ratified by B, so as to be binding on A.

5. Ratification within reasonable time: Ratification must be made within a reasonable period of time.
6. Communication of Ratification: Ratification must be communicated to the other party.
7. Act to be ratified must be valid: Act to be ratified should not be void or illegal, for e.g. payment of dividend out of capital is void and cannot be ratified.

1.29 Extent of Agent's Authority

- The authority of an agent means his capacity to bind the principal to third parties. The agent can bind the principal only if he acts within the scope of his authority.
- The extent of an agent's authority, whether expressed or implied is determined by:
  (a) The nature of the act or the business he is appointed to do
  (b) Things which are incidental to the business or are usually done in the course of such business,
  (c) The usage of trade or business.
- Whatever be the nature or extent of the agent's authority, it will always include the authority to do:
  (1) Every lawful thing necessary for the purpose of carrying it out,
  (2) Every lawful thing justified by various customs of trades,
  (3) In an emergency, all such acts for the purpose of protecting the principal from loss as will be done by a person of ordinary prudence in his own case under similar circumstances.

- The agent's authority is governed by two principles

(a) Agent's authority in normal circumstances (Section 188):

- An agent having an authority to do an act has authority to do every lawful thing which is necessary in order to do such act.
- Example: A is employed by B, residing in London, to recover at Mumbai a debt due to B. A may adopt any legal process necessary for the purpose of recovering the debt, and may give a valid discharge for the same.

(b) In case of emergency (Section 189):

- He has an authority in an emergency to do all such acts for the purpose of protecting his principal from loss as would be done by a prudent person, in his own case under similar circumstances.
- To constitute a valid agency in an emergency, following conditions must be satisfied.
  (a) Agent should not be a in a position or have any opportunity to communicate with his principal within the time available.
  (b) There should have been actual and definite commercial necessity for the agent to act promptly.
  (c) The agent should have acted bonafide and for the benefit of the principal.
  (d) The agent should have adopted the most reasonable and practicable course under the circumstances, and
  (e) The agent must have been in possession of the goods belonging to his principal and which are the subject of contract.
- Example: A consigns provisions to B at Kolkata, with directions to send them immediately to C at Cuttack. B may sell the provisions at Kolkata, if they will not bear the journey to Cuttack without spoiling.

1.30 Sub-Agent and Substituted Agent

Sub-Agent (Section 190 to 193)

- The term sub-agent is defined in Section 191 as, "a sub-agent is a person employed by and acting under the control of the original agent in the business of agency."
- Thus a sub-agent is an agent appointed by the agent. The relation of the sub-agent to the original agent is that of the agent and the principal.
- The general rule of law is that an agent cannot delegate his powers to another without the consent of the principal (Section 190). This general principal is based upon the Latin Maxim "delegatus non Protest delegate" which means a delegatee cannot further delegate.
- The contract of agency is of a fiduciary nature. It is based on the confidence reposed by the principal in the agent. Therefore, agent has no authority to further delegate his authority to another person.
- The agent is responsible to the principal for the acts of the sub-agents. The sub-agent is responsible for his acts to the agent and not the principal. The agent is responsible to the principal as well as to third parties for the acts of the sub-agents. The sub-agent is not responsible to the principal at all. He is answerable only to the agent (Section 193).
- However, in the following cases, however, the agent may appoint a sub-agent:
  a. Where the principal has expressly allowed the appointment of a sub-agent.
  b. Where the principal knows that the agent intends to appoint a sub-agent but he does not object to it.
  c. Where the custom of trade permits the appointment of a sub-agent.
  d. Where the act to be done is purely ministerial and does not involve exercise of discretion or any skill.
  e. Where unforeseen emergencies arise which makes the appointment of sub-agent necessary.

  Where a sub-agent is properly appointed (as mentioned in above cases), the prin¬cipal is bound and is liable to third parties for his act, as if he were an agent origi¬nally appointed by the principal (Section 192). Where sub-agent is not properly appointed, the principal is not bound by the acts of sub-agent.

Substituted Agent (Section 194 & 195)

- Substituted Agent is a person appointed by the agent to act for the principal, in the business of agency, with the knowledge and consent of the principal.
- Substituted agents are not sub agents. They are agents of the principal. Where the

principal appoints an agent and if that agent identifies another person to carry out the acts ordered by principal, than the second person is not to be treated as a sub agent but only as an agent of the original principal (Section 194).

- While selecting a "substituted agent" the agent is bound to exercise same amount of diligence as a man of ordinary prudence and if he does so he will not be responsible for acts or negligence of the substituted agent (Section 195).
- Example: X consigns goods to 'Y' a merchant for sale on auction. 'Y' in due course employs an auctioneer in goods to sell goods of X and also allows him to receive the proceeds of sale. The auctioneer becomes insolvent afterwards without handing over the proceeds. Here 'Y' will not be responsible to X as he has discharged his duties as a man of ordinary prudence and diligence.

Difference between Sub-Agent and Substituted Agent

	Sub-Agent	Substituted Agent
1.	A sub-agent works under, the control and directions of the agent.	A substituted agent works under the control and directions of the principal.
2.	The agent delegates to the sub-agent a part of his own duties.	The agent does not delegate any part of his duties to the substituted agent.
3.	There is no privity of contract between the principal and the sub-agent.	There is privity of contract between principal and substituted agent.
4.	The sub-agent is responsible to the agent alone.	The substituted agent is responsible to the principal
5.	The agent is responsible to the principal for the acts of the sub-agent.	The agent is not responsible to the principal for the acts of the substituted agent.
6.	The sub-agent has no right of action against the principal for remuneration due to him.	The substituted agent can sue the principal for remuneration due to him.
7.	Sub-agents may be improperly appointed	Substituted agents can never be improperly appointed.
8.	The agent remains liable for the acts of the sub-agent as long as the sub-agency continues.	The agent's duty ends once he has named the substituted agent

1.31 Duties and Rights of Agent

Duties of Agent	Rights of Agent
1. Duty to execute Mandate 2. Conduct business in accordance with the directions given by the principal (Section 211) 3. Duty of reasonable care and skill (Section 212) 4. Duty to communicate with the principal (Section 214) 5. Duty to avoid conflict of interest (Section 215 & 216) 6. Duty not to make secret profit 7. Duty to render proper accounts (Section 213) 8. Duty not to delegate 9. Agent's duty to pay sums received for principal (Section 218) 10. Duty not to use any confidential information received in the course of agency against the principal.	1. Right of retain out of sums received on principal's account (Section 217) 2. Right to remuneration (Section 219 & 220) 3. Agent's lien on principal's property (Section 221) 4. Right of indemnification (Section 222 to 224) 5. Right to compensation for injury caused by principal's neglect (Section 225)

Duties of Agent

1. Duty to execute mandate:

- He should perform the work which he has been appointed to do. Any failure in this respect would make the agent absolutely responsible for the principal's loss.

Case law: *In Pannalal Jankidas Vs Mohanlal*, a commission agent purchased goods for his principal and stored them in a godown pending their dispatch. The agent was under instruction to insure them. He actually charged the premium for insurance but failed to insure the goods. The goods were lost in an explosion in Bombay harbor. The agent was held liable to compensate the principal for his loss minus the amount received under the Bombay explosion (compensation) ordinance, 1944.

2. Duty to follow instructions or customs:

- According to Section 211 an agent is bound to conduct the business of his principal according to the direction given by the principal, or, in the absence of any such directions, according to the custom which prevails in doing business of the same kind at the place where the agent conducts such business.
- When the agent acts otherwise, if any loss be sustained, he must make it good to his principal, and, if any profit accrues, he must account for it.
- Example: A, an agent engaged in carrying on for B a business, in which it is the custom to invest from time to time, at interest, the moneys which may be in hand, omits to make such investment. A must make good to B the interest usually obtained by such investment.

3. Duty of Reasonable care and skill:

- According to Section 212, an agent is bound to conduct the business of the agency with as much skill as is generally possessed by persons engaged in similar business, unless the principal has notice of his want of skill.
- If the agent acts negligently, he has to compensate the principal in respect of the direct consequences of his own neglect, want of skill or misconduct, but not in respect of loss of damage which are indirectly or remotely caused by such neglect, want of skill or misconduct.
- Example : A, an agent for the sale of goods, having authority to sell on credit, sells to B on credit, without making the proper and usual enquiries as to the solvency of B. B, at the time of such sale is insolvent. A must make compensation to his principal in respect of any loss thereby sustained.

4. Agent' duty to communicate with principal [Section 214]: It is the duty of an agent, in cases of difficulty, to use all reasonable diligence in communicating with his principal, and in seeking to obtain his instructions.

5. Duty to Avoid Conflict of interest (Section 215 & 216)

- According to Section 215, If an agent deals on his own account in the business of the agency, without first obtaining the consent of his principal and informing him with all material circumstances which have come to his own knowledge on the subject, the principal may cancel the transaction, if the case shows either that any material fact has been dishonestly concealed from him by the agent, or that the dealings of the agent have been disadvantageous to him.

- According to section 216 if an agent, without the knowledge of his principal deals in the business of the agency on his own account instead of on account of his principal, the principal is entitled to claim from the agent any benefit which may have resulted to him from the transaction.
- Example: Arvind directs Balwant to sell Arvind's estate. Balwant, on looking over the estate before selling it, finds a mine on the estate which is unknown to Arvind. Balwant informs Arvind that he wishes to buy the estate for himself, but conceals the discovery of the mine. Arvind allows Balwant to buy, in ignorance of the existence of the mine. Arvind, on discovering that Balwant knew the mine at the time he bought the estate may either repudiate or adopt the sale at his option and can claim compensation.

6. Duty not to make secret profits:
   - It is the duty of an agent not to make any secret profit in the business of agency. His relationship with the principal is of fiduciary nature and this requires absolute good faith in the conduct of agency.
   - Secret Profit means any advantage obtained by the agent over and above his agreed remuneration and which he would not have been able to make but for his position as agent.

7. Duty to render proper accounts (Section 213): An agent is bound to render proper accounts to his principal on demand. Rendering accounts does not mean showing the accounts but the accounts supported by vouchers.

8. Duty not to Delegate: According to section 190, an agent cannot lawfully employ to perform acts which he has expressly or impliedly undertaken to perform personally, unless by the ordinary custom of trade a sub-agent may, or, from the nature of agency, a sub- agent must be employed.

9. Agent's duty to pay sums received for principal (Section 218): Subject to such deductions, the agent is bound to pay to his principal all sums received on his account.

10. Duty not to use any confidential information received in the course of agency against the principal.

Rights of Agent

1. Right of retain out of sums received on principal's account [Section 217]: The agent can retain, out of any sums received on account of the principal in the business of the agency for the following payments:
   (a) All moneys due to him in respect of advances made
   (b) In respect of expenses properly incurred by him in conducting such business
   (c) Such remuneration as may be payable to him for acting as agent.
   The right can be exercised on any sums received on account of the principal in the business of agency.

2. Right to remuneration [Section 219]:
   - The agent in the normal course is entitled for remuneration as per the contract.
   - In the absence of any agreed amount of remuneration, he is entitled for usual remuneration which is customary in the business.
   - However an agent who is guilty of misconduct in the business of the agency is not entitled to any remuneration in respect of that part of the business which he has committed misconduct (Section 220).

3. Agent's lien on principal's property [Section 221]:
   - The conditions of this right are:
     (i) The agent should be lawfully entitled to receive from the principal a sum of money by way of commission earned or disbursement made or services rendered in the proper execution of the business of agency.
     (ii) The property over which the lien is to be exercised should belong to the principal and it should have been received by the agent in his capacity and during the course of his ordinary duties as agent.
     (iii) The agent has only a particular lien.
   - However, the agent's right to lien is lost in the following cases:
     (i) When the possession of the property is lost.
     (ii) When the agent waives his right. Waiver may arise out of agreement express or implied.
     (iii) The agent's lien is subject to a contract to the contrary.

4. Right to indemnity (Section 222 to 224):

Right of indemnification for lawful acts (Section 222)

The principal is bound to indemnify the agent against all consequences of lawful acts done in exercise of his authority. The right to indemnity extends to all losses and expenses incurred by the agent in the conduct of the business.

Example: 'A' of Delhi appoints 'B' of Mumbai as agent to sell his merchandise. As a result 'B' contracts to deliver the merchandise to various parties. But A fails to send the merchandise to B and B faces litigations for non-performance. Here, A is bound to protect B against the litigations and all costs, expenses arising of that.

Right of indemnification against acts done in good faith (Section 223)

Where the agent acts in good faith on the instruction of principal, agent is entitled for indemnification of any loss or damage from the principal.

However, the agent cannot claim any reimbursement or indemnification for any loss etc. arising out of acts done by him in violation of any penal laws of the country.

Non-liability of employer of agent to do a criminal act (Section 224)

Where one person employs another to do an act which is criminal, the employer is not liable to the agent, either upon an express or an implied promise, to indemnify him against the consequences of that act.

Example: A employs B to beat C, and agrees to indemnify him against all consequences of the act. B thereupon beats C, and has to pay damages to C for so doing. A is not liable to indemnify B for those damages.

5. Right to compensation for injury caused by principal's neglect [Section 225]: The principal must make compensation to his agent in respect of injury caused to such agent by the principal's neglect or want of skill. Thus, every principal owes to his agent the duty of care not to expose him to unreasonable risks. Example: A employs B as a bricklayer in building a house, and puts up the scaffolding himself.

The scaffolding is unskilfully put up, and B is in consequence hurt. A must make compensation to B.

1.32 Liability to Third Parties

An agent does all acts on behalf of the principal but incurs no personal liability. The liability remains that of the principal. But in some cases agent is personally liable.

In following cases principal liable for agent's act:

1. Principal liable for the acts of agents which are within the scope of his authority (Section 226)
2. When agent exceeds authority and when the part of what he does, which is within his authority, can be separated from the part which is beyond his authority, then principal is liable only for the part which is within authority (Section 227)
   If the agent has exceeded his authority and principal has ratified it then principal is liable
3. Principal is bound by the notice given to agent provided notice is in course of business (Section 229)
4. Liability for Misrepresentation or fraud by an agent when agent is acting within his authority (Section 238).
5. When an agent has, without authority, done acts or incurred obligations to third persons on behalf of his principal, the principal is bound by such acts or obligations, if he has by his words or conduct induced such third persons to believe that such acts and obligations were within the scope of the agent's authority (Section 237).
   Example: A consigns goods to B for sale, and gives him instructions not to sell under a fixed price. C, being ignorant of B's instructions, enters into a contract with B to buy the goods at a price lower than the reserved price. A is bound by the contract.
6. When agent is incompetent to contract.
7. When agent acts in emergency and good faith.

In following cases agent is personally liable:

1. When agent exceeds authority and when the part of what he does, which is within his authority, cannot be separated from the part which is beyond his authority, then agent is liable (Section 228)
2. When he is working for a foreign principal (Section 230)
3. Where he is acting for a principal who cannot be sued on account of his being a foreign sovereign, ambassador etc. (Section 230)
4. Liability of pretended agent [Section 235]: A pretended agent is a person who represents himself to be an agent of another, when in fact he has no authority from

him, whatsoever if the principal ratifies his acts as agent, he has no liability. But if the principal refuses to ratify his acts, he becomes personally liable to third party for any loss or damage caused to him. It is to be noted that where agent is personally liable, the third party can sue the principal or the agent or both the principal and the agent, as the liability of the principal and agent is joint and several.

5. Person falsely contracting agent not entitled to performance [Section 236]: A person with whom a contract has been entered into in the character of agent, is not entitled to require the performance of it if he was in reality acting, not as agent, but on his own account.
6. Liability for Misrepresentation or fraud by an agent when agent is acting beyond his authority (Section 238)

1.33 Rights of third Party

1. Where the agent does not disclose the name of his principal or existence of principal.
   - If an agent makes a contract with a person who neither knows, nor has reason to suspect, that he is an agent, agent is personally liable
   - If the principal discloses himself before the contract is completed, the other contracting party may refuse to fulfil the contract, if he can show that, if he had known who was the principal in the contract, or if he had known that the agent was not a principal, he would not have entered into the contract (Section 231)
   - Where one man makes a contract with another, neither knowing nor having reasonable ground to suspect that the other is an agent, the principal, if he requires the performance of the contract, can only obtain such performance subject to the rights and obligations subsisting between the agent and the other party to the contract (Section 232)
   - Example: A, who owes ₹50,000 to B, sells ₹1,00,000 worth of rice to B. A is acting as agent for C in the transaction, but B has neither knowledge nor reasonable ground of suspicion that such is the case. C cannot compel B to take the rice without allowing him to set off A's debt.
2. In cases where the agent is personally liable, a person dealing with him may hold either him or his principal, or both of them, liable (Section 233).
   - Example: A enters into a contract with B to sell him 100 bales of cotton, and afterwards discovers that B was acting as agent for C. A may sue either B or C, or both, for the price of the cotton.
   - When a person who has made a contract with an agent induces the agent

to act upon the belief that the principal only will be held liable, or induces the principal to act upon the belief that the agent only will be held liable, he cannot afterwards hold liable the agent or principal respectively (Section 234).

1.34 Termination of Agency

(A) Act of the Parties:

1) Mutual agreement: The relationship between principal & agent may be terminated at any stage by a mutual agreement between them.

2) Revocation by Principal (Section 203 to 207):

- Principal may revoke the authority given to an agent at any point of time and the agency would come to an end. The only exception would be in case of IRREVOCABLE agency (Section 203 & 204).

3) Renunciation by Agent: Agency may also be terminated by expressed re¬nunciation of the agent, provided the agent gives the principal a reasonable notice.

- Compensation for revocation by principal, or renunciation by agent [Section 205]: Where there is an express or implied contract that the agency should be continued for any period of time, the principal must make compensation to the agent, or the agent to the principal, as the case may be, for any previous revocation or renunciation of the agency without sufficient cause.
- Notice of revocation or renunciation [Section 206]: Reasonable notice must be given of such revocation or renunciation; otherwise the damage thereby resulting to the principal or the agent, as the case may be, must be made good to the one by the other.
- Revocation and renunciation may be expressed or implied [Section 207]: Revocation and renunciation may be expressed or may be implied in the conduct of the principal or agent respectively.
- When termination of agent's authority takes effect as to agent, and as to third persons (Section 208): The termination of the authority of an agent does not, so far as regards the agent, take effect before it becomes known to him, or, so far as regards third persons, before it becomes known to them.

  Example: A directs B to sell goods for him, and agrees to give B five per cent commission on the price fetched by the goods. A afterwards, by letter, revokes B's authority. B, after the letter is sent, but before he

receives it sells the goods for ₹1,00,000. The sale is binding on A, and B is entitled to ₹5,000 as his commission.

(B) Operation of Law:

1) Performance of contract: The most obvious mode of putting on end of the agency is to do what the agent had undertaken to perform. Thus if the con¬tract is performed the agency gets terminated.
2) Expiry of time: When an agent is appointed for a fixed period the agency comes to an end after the expiry of time even if work is not complete.
3) Death / Insanity (Section 209): Death or Insanity of the Principal or the agent amounts to termination of agency if it is not coupled with interest.
4) Insolvency: Insolvency of the Principal puts an end to the relationship of agency there is nothing mentioned in the contract act regarding insolvency of agent. However courts have accepted that insolvency of agent also termi¬nates agency.
5) Destruction of subject matter: An agency created to deal with a subject matter comes to an end by destruction of that subject matter.
6) Parties becoming alien enemies: When the agent and principal become alien enemies of each other, both of them become incompetent to contract and agency is terminated.

1.35 Irrevocable Agency

As per Section 202, where the agency cannot be terminated, it is irrevocable agency. Where the agent has himself an interest in the property which forms the subject matter of the agency, the agency cannot in the absence of an express contract, be terminated.

Example : A (Principal) gives authority to B (agent) to sell A's land and to pay himself, out of the process, the debts due to him from A. A cannot revoke this authority, nor can it be terminated by his insanity or death.

SUMMARY

UNIT1: CONTRACT OF INDEMNITY AND GUARANTEE

INDEMNITY

1.1: Meaning of Indemnity Contract [Section 124]

- As per Section 124, indemnity contract is a contract, by which one party promises to save the other from loss caused to him by the conduct of the promisor himself or by the conduct of any other person, is called a contract of indemnity.
- The person who promises to make good the loss is called 'indemnifier' and the person whose loss is to be made good is called the 'indemnified' or 'indemnity-holder.

1.2 Rights of indemnity holder [Section 125]

- The promisee i.e., indemnity- holder acting within the scope of his authority is entitled to recover from the promisor i.e., indemnifier the following rights:
  (a) All damages which he may be compelled to pay in any suit
  (b) All costs which he may have been compelled to pay in bringing/ defending the suit and
  (c) All sums which he may have paid under the terms of any compromise of suit.

GUARANTEE

1.3 Meaning of Guarantee Contract (Section 126)

- 'A contract of guarantee' is a contract to perform the promise, or discharge the liability, of a third person in case of his default.
- The person who gives the guarantee is called the 'surety', the person in respect of whose default the guarantee is given is called 'principal debtor', and the person to whom the guarantee is given is called 'creditor'.

1.4 Consideration for Guarantee (Section 127)

- As per Section 127 of the Act, no actual consideration is required for contract of guarantee. In other words, anything done, or any promise made, for the benefit of the principal debtor, may be a sufficient consideration to the surety for giving the guarantee.

1.5 Nature of Surety's Liability (Section 128)

- The liability of the surety is co-extensive with that of the principal debtor unless it is otherwise provided by the contract.

1.6 Types of Guarantee (Section 129 to 131)

Specific guarantee | Continuing guarantee

3. Specific guarantee

When a guarantee is given in respect of a single debt or specific transaction and is to come to an end when the guaranteed debt is paid or the promise is duly performed, it is called a specific guarantee.

4. Continuing guarantee (Section 129)

A guarantee which extends to a series of transactions is called a continuing guarantee.

1.7 Discharge of Surety

A surety is said to be discharged when his liability comes to an end.

Section133	Section 134	Section 135	Section 139
Variation in terms of contract between the principal debtor and creditor without surety's consent	By release or discharge of principal debtor	Discharge of surety when creditor compounds with, gives time to, or agrees not to sue, principal debtor	If creditor fails to perform his duty, surety is discharged.

1.8 Non-Discharge of Surety

The surety is not discharged in the following cases:

A surety is said to be discharged when his liability comes to an end.

Section136	Section 137	Section 138
Surety is not discharged when agreement made with third person to give time to principal debtor.	Mere forbearance on the part of the creditor to sue the principal debtor does not in the absence of any provision in the guarantee to the contrary, discharge the surety.	Where there are co-sureties, a release by the creditor of one of them does not discharge the other; neither does it free the surety so released from his responsibility to the other sureties.

1.9 Rights of Surety

Rights against the Principal Debtor

1) Rights of subrogation (Section 140)
2) Implied promise to indemnify surety (Section 145)

Rights against the Creditor

1) Surety's right to benefit of creditor's securities (Section 141)
2) Right to set off
3) Right to share reduction

1.10 Invalid Guarantee (Section 142 to 144)

1) Guarantee obtained by misrepresentation invalid (Section 142)
2) Guarantee obtained by concealment invalid (Section 143)
3) Guarantee on contract that creditor shall not act on it until co¬-surety joins (Section 144)

1.11 Contribution of Co-Sureties

Rules for Co-Sureties:

1) Co- sureties liable to contribute equally (Section 146)
2) Liability of co-sureties, bound in different sums (Section 147)
3) Sureties' liability towards other co-sureties (Section 138)

4) Mutual agreement between co-sureties (Section 132)

1.12 Distinction between Indemnity and Guarantee

UNIT 2: BAILMENT AND PLEDGE

BAILMENT

1.13 Meaning of Bailment

- Definition under Section 148: Bailment is defined under Section 148 as "A contract whereby goods are delivered by one person to another for some purpose, that the goods shall, when the purpose is over be returned or disposed off according to directions of the person delivering the goods."
- The person delivering the goods is called the "bailor". The person to whom they are delivered is called the "bailee"

1.14 Essential elements of Bailment

1) Contract
2) Delivery of goods
3) Purpose
4) Possession
6) Return of goods

1.15 Forms and Classification of Bailment

- Forms of Bailment
  1) Delivery of goods by one person to another to be held for the bailor's purpose.
  2) Gratuitous bailment: Where neither the bailor nor the bailee gets any remuneration. For example A lends his book to his friend.
  3) Hiring of goods.
  4) Delivering goods to a creditor to serve as security for a loan.
  5) Delivering goods for repair with or without remuneration.
  6) Delivering goods for carriage.
  7) Finder of Goods.

1.16 Duties and Rights of Bailor

Duties of Bailor

1. To disclose the faults (Section 150)
2. Duty to pay necessary expenses (Section 158)
3. Duty to indemnify the Bailee for premature termination (Section 159)
4. Bailor's responsibility to bailee (Section 164)

Rights of Bailor

1. Right to terminate the bailment (Section 153)
2. Right to demand back the goods at any time (Section 159)
3. Right to file a suit against a wrong doer (Section 180 and section 181)
4. Right to sue the bailee

1.17 Duties and Rights of Bailee

Duties of Bailee

1. Take reasonable Care of the goods (Section 151 & 152)
2. Not to make inconsistent use of goods (Section 153 & 154)
3. Not to mix the goods (Section 155, 156 and 157)
4. Return the goods (Section 160 & 161)
5. Return an accretion from the Goods (Section 163)
6. Not to setup Adverse Title

Rights of a Bailee

1. Right to Deliver the Goods to any one of the Joint Bailors (Section 165)
2. Right to indemnity (Section 166)
3. Right to claim compensation in case of faulty goods (Section 150)
4. Right to claim extraordinary expenses (Section 158)
5. Right to Apply to Court to Decide the Title to the Goods (Section 167)
6. Right of particular lien for payment of services (Section 170)
7. Right of general lien (Section 171)

1.18 Termination of Bailment

1) On expiry of stipulated period
2) On fulfilment of the purpose:
3) By Notice
4) By death
5) Destruction of the subject matter

1.19 Finder of Goods

- The obligations of a finder of goods:
  1) He must take reasonable care of the goods
  2) He must not use the goods for his own purpose.
  3) He must not mix them with his own goods.
  4) He must make appropriate efforts to find the true owner of the goods.

- Rights of finder of goods
  1) Right to retain goods
  2) Right to sue for reward (Section 168)
  3) Right to claim expenses incurred
  4) Right of sale: Section 169 permits the finder to sell the goods in the certain cases

1.20 Types of Lien

1) Particular Lien (Section 170):

   If in accordance with the purpose of the bailment, any service requiring labour or skill is rendered by the bailee in respect of the goods bailed, he is entitled to remuneration. If the bailor refuses to pay for the service, the bailee has the right to retain the goods bailed until he receives his remuneration.

2) General Lien (Section 171):
   - A general lien is the right to retain the property of another for a general balance of account.
   - Bankers, factors, wharfingers, attorney of a High Court and policy - brokers have general lien on goods coming into their possession in the course of their trade.

PLEDGE

1.21 Meaning and Essentials of Pledge

- Meaning: Pledge is defined under Section 172 as the bailment of goods as security for a payment of a debt or performance of a promise is called pledge/pawn.
- Essentials of a valid pledge:
  1) Delivery of goods
  2) Goods must be the subject matter of the contract of pledge. The goods pledged must be in existence
  3) Purpose of pledge is security for payment of debt.
  4) Pledge is specie of bailment.

1.22 Duties and Rights of Pawnee

Duties of Pawnee

1) Duty to take reasonable care of the pledged goods
2) Duty not to make unauthorized use of pledged goods.
3) Duty to return the goods when the debt has been repaid or the promise has been performed.
4) Duty not to mix his own goods with goods pledged.
5) Duty not to do any act which is inconsistent with the terms of the pledge.
6) Duty to return accretion to the goods, if any.

Rights of Pawnee

1) Right of retain the goods pledged (Section 173)
2) Right to retention of pledged goods for subsequent debts (Section 174)
3) Pawnee's right as to extraordinary expenses Incurred (Section 175)
4) Pawnee's right where pawnor makes default (Section 176)

1.23 Duties and Rights of Pawnor

Duties of Pawnor

1) The pawnor is liable to pay the debt or perform the promise as the case may be.
2) It is the duty of the pawnor to compensate the pawnee for any extraordinary expenses incurred by him for preserving the goods pawned.
3) It is the duty of the pawnor to disclose all the faults which may put the pawnee under extraordinary risks.
4) If loss occurs to the pawnee due to defect in pawnor's title to the goods, the pawnor must indemnify the pawnee.
5) If the pawnee sells the good due to default by the pawnor, the pawnor must pay the deficit.

Rights of Pawnor

1) Right to redeem (Section 177)

1.24 Pledge by Non-Owners

1) Pledge by mercantile agent (Section 178)
2) Pledge by person in possession under voidable contract (Section 178A)
3) Pledge where pawnor has only a limited interest (Section 179)
4) Pledge by a co-owner in possession
5) Pledge by buyer and seller in possession

1.25 Distinction between Bailment and Pledge

UNIT 3: AGENCY

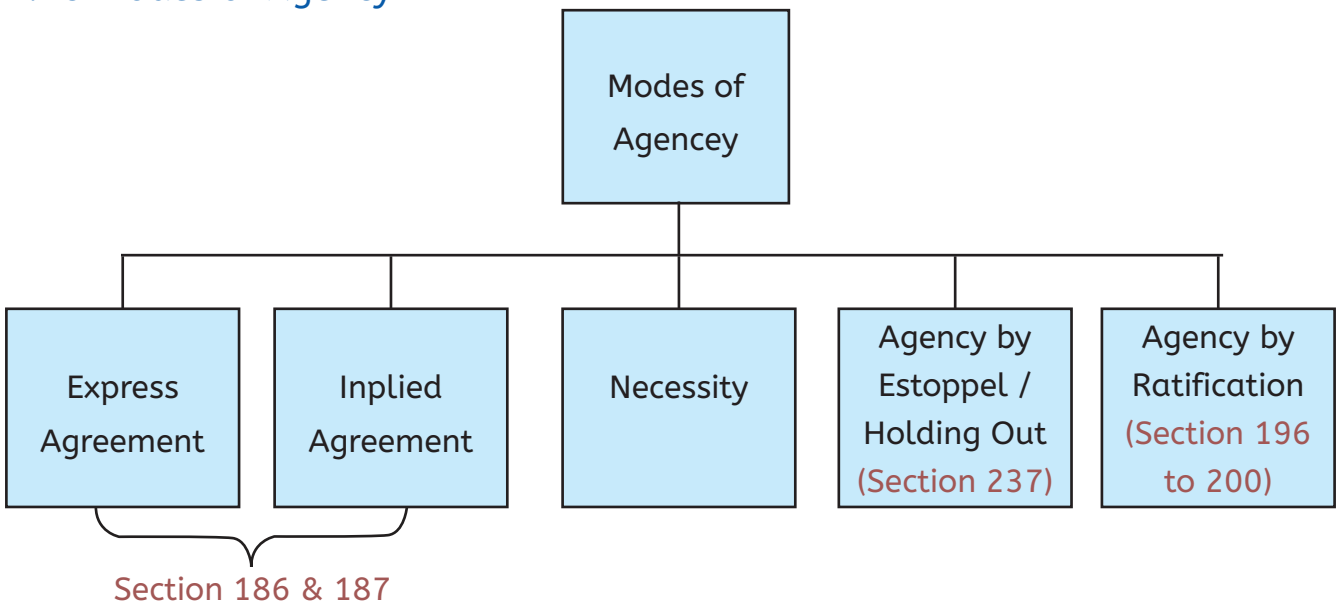
1.26 Meaning of Agency

- Meaning: The Indian Contract Act does not define 'Agency' but it defines an agent as a person employed to do any act for another or to represent another in dealings with third person. The person for whom such act is done, or who is so represented is called the principal (Section 182).
- The Rule of Agency is based on the maxim *"Quit facit per alium, facitper se"* i.e., he who acts through an agent is himself acting.

1.27 Essentials of Agency

1) Basis of the agreement
2) Consideration not necessary
3) Capacity to employ agent
4) Capacity to be employed as agent

1.28 Modes of Agency



1.29 Extent of Agent's Authority

The agent's authority is governed by two principles

(a) Agent's authority in normal circumstances (Section 188)

(b) In case of emergency (Section 189): He has an authority in an emergency to do all such acts for the purpose of protecting his principal from loss as would be done by a prudent person, in his own case under similar circumstances.

1.30 Sub-Agent and Substituted Agent

Sub-Agent (Section 190 to 193)

- The term sub-agent is defined in Section 191 as, "a sub-agent is a person employed by and acting under the control of the original agent in the business of agency."
- The general rule of law is that an agent cannot delegate his powers to another without the consent of the principal (Section 190). This general principal is based upon the Latin Maxim "delegatus non Protest delegate" which means a delegatee cannot further delegate.

Substituted Agent (Section 194 & 195)

- Substituted agents are not sub agents. They are agents of the principal. Where the principal appoints an agent and if that agent identifies another person to carry out the acts ordered by principal, than the second person is not to be treated as a sub agent but only as an agent of the original principal (Section 194).

1.31 Duties and Rights of Agent

Duties of Agent

1. Duty to execute Mandate
2. Conduct business in accordance with the directions given by the principal (Section 211)
3. Duty of reasonable care and skill (Section 212)
4. Duty to communicate with the principal (Section 214)
5. Duty to avoid conflict of interest (Section 215 & 216)
6. Duty not to make secret profit
7. Duty to render proper accounts (Section 213)
8. Duty not to delegate
9. Agent's duty to pay sums received for principal (Section 218)
10. Duty not to use any confidential information received in the course of agency against the principal.

Rights of Agent

1. Right of retain out of sums received on principal's account (Section 217)
2. Right to remuneration (Section 219 & 220)
3. Agent's lien on principal's property (Section 221)
4. Right of indemnification (Section 222 to 224)
5. Right to compensation for injury caused by principal's neglect (Section 225)

1.32 Liability to Third Parties

An agent does all acts on behalf of the principal but incurs no personal liability. The liability remains that of the principal. But in some cases agent is personally liable.

1.33 Rights of third Party

1. Where the agent does not disclose the name of his principal or existence of principal.
   - If an agent makes a contract with a person who neither knows, nor has reason to suspect, that he is an agent, agent is personally liable
   - If the principal discloses himself before the contract is completed, the other contracting party may refuse to fulfil the contract, if he can show that, if he had known who was the principal in the contract, or if he had known that the agent was not a principal, he would not have entered into the contract

(Section 231)

- Where one man makes a contract with another, neither knowing nor having reasonable ground to suspect that the other is an agent, the principal, if he requires the performance of the contract, can only obtain such performance subject to the rights and obligations subsisting between the agent and the other party to the contract (Section 232)
- Example: A, who owes ₹50,000 to B, sells ₹1,00,000 worth of rice to B. A is acting as agent for C in the transaction, but B has neither knowledge nor reasonable ground of suspicion that such is the case. C cannot compel B to take the rice without allowing him to set off A's debt.

2. In cases where the agent is personally liable, a person dealing with him may hold either him or his principal, or both of them, liable (Section 233).
   - Example: A enters into a contract with B to sell him 100 bales of cotton, and afterwards discovers that B was acting as agent for C. A may sue either B or C, or both, for the price of the cotton.
   - When a person who has made a contract with an agent induces the agent to act upon the belief that the principal only will be held liable, or induces the principal to act upon the belief that the agent only will be held liable, he cannot afterwards hold liable the agent or principal respectively (Section 234).

1.34 Termination of Agency

(A) Act of the Parties:

1) Mutual agreement
2) Revocation by Principal (Section 203 & 204)
3) Renunciation by Agent (Section 205 to 208)

(B) Operation of Law:

1) Performance of contract
2) Expiry of time
3) Death / Insanity (Section 209)
4) Insolvency
5) Destruction of subject matter
6) Parties becoming alien enemies

1.35 Irrevocable Agency

As per Section 202, where the agency cannot be terminated, it is irrevocable agency. An irrevocable agency may be in the following case:

Where the agent has himself an interest in the property which forms the subject matter of the agency.

LIST OF LEGAL TERMS

SR. NO.	LEGAL WORD	MEANING	PAGE NUMBER (This column is to be filled by students)
1.	Judicial pronouncements	Judgements by court	
2.	Forbearance	Here it means delay	
3.	Interse	Internally	
4.	Accretion	Addition	
5.	Man of ordinary prudence	Normal human being	

LIST OF LATIN TERMS

SR. NO.	LATIN TERM	MEANING	PAGE NUMBER (This column is to be filled by students)
1.	Quit facit per alium, facitper se	He who acts through an agent is himself acting	
2.	delegatus non Protest delegate	A delegatee cannot further delegate	

LIST OF CASE LAWS

SR. NO.	CASE LAW	PAGE NUMBER (This column is to be filled by students)
1.	M.S Anirudhan v Thomco's Bank Ltd	
2.	State bank of Saurashtra Vs Chitranjan Rangnath Raja	
3.	Hyman & Wife v. Nye & Sons (1881)	
4.	Pannalal Jankidas V Mohanlal	

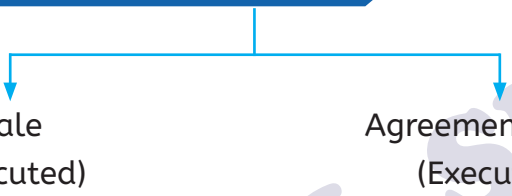
4. THE SALE OF GOODS ACT, 1930

UNIT 1: FORMATION OF CONTRACT OF SALE

INTRODUCTION :

- It came into force on the 1st of July, 1930.
- It is applicable to whole of India
- The Law relating to this statute was contained in the Chapter VII of the Indian Contract Act, 1872.
- Where the Sale of Goods Act is silent on any point, the general principles of the law of contract apply.

CONTRACT OF SALE



- The term 'contract of sale' is defined in Section 4(1) of the Sale of Goods Act, as under : "A contract of sale of goods is a contract whereby the seller transfers or agrees to transfer the property in the goods to the buyer for a price. "

- A contract of sale may be absolute or conditional. [Section 4(2)]

- Sale: In Sale, the property in goods is transferred from seller to the buyer immediately. The term sale is defined in the Section 4(3) of the Sale of Goods Act, 1930 as – "where under a contract of sale the property in the goods is transferred from the seller to the buyer, the contract is called a sale."

- Agreement to Sell: In an agreement to sell, the ownership of the goods is not transferred immediately.
  It is intending to transfer at a future date upon the completion of certain conditions thereon. The term is defined in Section 4(3) of the Sale of Goods Act, 1930, as – "where the transfer of the property in the goods is to take place at a future time or subject to some condition thereafter to be fulfilled, the contract is called an agreement to sell."
  Thus, whether a contract of sale of goods is an absolute sale or an agreement to sell, depends on the fact whether it contemplates immediate transfer from the seller to the buyer or the transfer is to take place at a future date.

- When agreement to sell becomes sale: 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.

DEFINITIONS

1) Buyer [Section 2(1)]:

"Buyer means a person who buys or agrees to buy goods."

2) Seller [Section 2(13)]:

"Seller means person who sells or agrees to sell goods."

3) Goods [Section 2(7)]:

"Goods" means every kind of movable asset
other than actionable claims and money; and
includes stocks and shares,
growing crops, grass and things attached to or forming part of the land which are agreed to the severed before sale or under the contract of sale.

- An actionable claim is a claim to any debt. For example: a money debt, book debts, etc.
- Money here means legal tender of money, i.e. the recognised circulation in the country; but not old rare coins.
- Things attached to the earth are not movables, but trees, growing crops which can be easily severed from the earth before sale. Fruits, vegetables and flowers which can be separated from the trees, are included in 'goods'.
- Livestock i.e. cows, buffaloes, cats etc are 'goods'.
- Patents, copyrights, goodwill, trade-marks, are all considered goods which can be the subject matter of a contract.
- A ship has also been considered to come within the definition of the word "goods". Similarly water, gas and electricity are included in the definition.
- As per English law, "shares and stock" are not treated as "goods".
- Even the Fixed Deposit Receipts (FDR) are considered as goods under the Sales of Goods Act.
- To conclude, everything movable is goods, except the following:-
  1. Money
  2. Actionable Claims
  3. Immovable assets
  4. Services

➢ Classification of Goods:

Existing Goods
Goods which are already in existence at the time of contract of sale

Future Goods
Goods which are yet to be manufactured in future.

Example: A contracts to sell to B all the apples which will be produced in his garden next year

Contingent Goods
Acquisition of such goods depends upon a contingency which may or may not happen.

Example: A agrees to sell to B a certain car provided he is able to purchase it from its present owner.

Specific/Ascertained Goods
Goods which are identified and agreed upon at the time of a contract

Example: A particular painting

Unascertained Goods
Goods which are not specifically identified but indicated by description at the time of the Contract

Example: Any 1 pen out of 50 pens

4) Delivery[Section 2(2)]:

"Delivery' means voluntary transfer of possession from one person to another" [Sec. 2 (2)].Therefore, in case of theft, there is no delivery, though there is a transfer of possession.

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

Symbolic delivery
When there is a delivery of a thing in token of a transfer of something else

Example: Handing over car keys, handing over documents of title

Constructive delivery:
When it is affected without any change in the custody or actual possession.

Example: Where a warehouseman holding the goods of A agrees to hold them on behalf of B, at A's request.

5) Documents showing Title to Goods/ Documents of Title to Goods[Section 2 (4)]

It is a document which shows the ownership of goods. If a person wants to transfer his ownership to other person, he cannot do it by endorsement or delivery, he has to follow procedure for transferring ownership It includes share certificate, RC book of car, etc	It is a document which is used as proof of the possession or control of goods. If a person wants to transfer his possession to other person, he can simply do it by endorsement or delivery. It includes a Bill of lading, Dock-warrant, Warehouse keeper's Certificate, Wharfinger Certificate, Railway Receipt

6) Price [Section 2 (10)]:

- ✓ "Price' means the money consideration for a sale of goods."
- ✓ No sale can take place without a price.
- ✓ Therefore,
  - a. Exchange of goods for goods will not be considered as sale
  - b. Gift of goods will not be considered as sale
  - c. Exchange of goods for goods along with price will be considered as sale
  - d. Distribution of goods as free samples will not be considered as sale.

7) Property[Section 2 (11)]:

General property (Ownership) | Special property (Interest)

But in Sale Of Goods Act, 'property' means the general property in goods and not merely a special property

Example: A who owns the goods pledges them to B, then A has the general property in the goods, while B has a special property or interest in them.

DISTINGUISH BETWEEN

1. SALE AND AGREEMENT TO SELL

SALE	AGREEMENT TO SELL
1. Transfer of property: the property in goods passes from the seller to the buyer immediately	1. Transfer of property: In agreement to sell, the ownership of the property will pass from the seller to the buyer at some future time or on fulfilment of some conditions.

2. Nature of contract: A sale is an executed contract	2. Nature of contract: An agreement to sell is an executory contract
3. Consequences of Breach by buyer : In a sale, if the buyer fails to pay for the goods, the seller can: i. Sue him for recovery of price ii. Claim damages	3. Consequences of Breach by buyer : In an agreement to sell, the seller can only sue for damages for breach of contract
4. Consequences of Breach by seller : In a sale, if the seller defaults, i.e. commits a breach, the buyer can: 1. Claim goods from third party 2. Sue for damages	4. Consequences of Breach by seller: In the case of an agreement to sell, if the seller commits a breach, the buyer can only claim damages.
5. Transfer of risk: In a sale, if the goods are destroyed, the loss falls on the buyer even though they are in the possession of the seller.	5. Transfer of risk: In an agreement to sell, if the goods are destroyed, the loss falls on the seller, even though they are in the possession of the buyer.
6. Subsequent destruction: A subsequent loss or destruction of the goods is the liability of the buyer.	6. Subsequent destruction: Such loss or destruction is the liability of the seller.
7. Nature of rights: Creates Jus in rem	7. Nature of rights: Creates Jus in personam

2. SALE AND HIRE- PURCHASE

Contract of sale resembles with contracts of hire purchase very closely, and indeed the real object of a contract of hire purchase is the sale of the goods ultimately.

Hire purchase agreements are governed by the Hire-purchase Act, 1972. Term "hire-purchase agreement" means an agreement under which goods are let on hire and under which the hirer has an option to purchase them in accordance with the terms of the agreement and includes an agreement under which–

a) Possession of goods is delivered by the owner thereof to a person on condition that such person pays the agreed amount in periodical instalments, and

b) The property in the goods is to pass to such person on the payment of the last of such instalments and

c) Such person has a right to terminate the agreement at any time before the property so passes;

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

SALE	HIRE-PURCHASE
1. Property in the goods is transferred to the buyer immediately at the time of Contract.	1. The property in goods passes to the hirer upon payment of the last instalment.

2. The position of the buyer is that of an Owner of the goods.	2. The position of the hirer is that of a bailee till he pays the last instalment.
3. The buyer cannot terminate the contract and is bound to pay the price of the goods.	3. The hirer may, if he so likes, terminate the contract by returning the goods to its owner without any liability to pay the remaining instalments.
4. The seller takes the risk of any loss resulting from the insolvency of the buyer.	4. The owner takes no such risk, for if the hirer fails to pay an instalment the owner has right to take back the goods.
5. The buyer can resell the goods.	5. The hirer cannot resell the goodstill the last instalment.
6. Tax is levied at the time of the contract.	6. Tax is not leviable until it eventually converts into a sale.

3. SALE AND BAILMENT

A 'bailment' is the delivery of goods for some specific purpose under a contract on the condition that the same goods are to be returned to the bailor or are to be disposed of according to the directions of the bailor.

SALE	BAILMENT
1. The property in goods is transferred from the seller to the buyer.	1. There is only transfer of possession of goods from the bailor to the bailee for any of the reasons like safe custody, carriage, etc.
2. The return of goods in contract of sale is not possible.	2. The bailee must return the goods to the bailor on the accomplishment of the purpose for which the bailment was made.
3. The consideration is the price in terms of money.	3. The consideration may be gratuitous or non-gratuitous.

EFFECT OF DESTRUCTION OF GOODS

Goods are destroyed before the contract of sale	Goods are destroyed after agreement to sell but before sale	Goods are destroyed after the contract of sale
↓	↓	↓
Agreement is void i.e void-ab-initio (Risk of goods is with the seller)	Contract becomes void (Risk if goods is with the seller) *Aggrieved party can claim damages	Contract is already executed (Risk if goods is with the buyer)

- Existing or future goods (section 6):
  a) The goods which form the subject of a contract of sale may be either existing goods or future goods.
  b) 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.

- Goods perishing before making of contract (Section 7):
  Where there is a contract for the sale of specific goods, the contract is void-ab-initio if the goods without the knowledge of the seller have, at the time when the contract was made, perished or become so damaged as no longer to answer to their description contract.
  Example: A agrees to sell B 50 bags of wheat stored in the A's godown. Due to water logging, all the goods stored in the godown were destroyed. At the time of agreement, neither parties were aware of the fact. The contract is void-ab-initio.

- 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 contract becomes void.

- Goods perishing after contract of sale: The contract is already executed

PRICE AND MODES OF FIXING THE PRICE

The price means the money consideration for the sale of goods. Price may be fixed in any of the following modes provided in Section 9:

1. The fixation of price by the contract of sale [Section 9 (1)]:
   The price may be expressly fixed the contract of sale. The parties may fix any price they like.
2. The fixation of price in a manner provided in the contract of sale [Section 9 (1)]:
   The contract of sale may provide for some manner in which 'price is to, be fixed. In such cases, the price may be fixed in a manner provided in the contract.
3. The fixation of price by course of dealings [Section 9 (1)]:
   Sometimes, the customs or usage of trade provides certain principles for the determination of the price. In such cases, the price may be determined from the course of dealings between the parties.
4. The fixation of a reasonable price [Section 9 (2)]:
   Sometimes, none of the above principles is applicable. In such cases, the buyer shall pay to the seller a reasonable price. The term 'reasonable' price is a question of fact which depends on the circumstances of each particular case.
5. The fixation of price by third party [Section 10]:
   - ✓ The parties may agree to sell and buy goods on the terms that the price shall be fixed by the valuation of a third party.
   - ✓ However, if such third party fails to make the valuation, the contract becomes void.

But if the buyer has received the goods and has appropriated them, he becomes bound to pay reasonable price to the seller.

- ✓ Sometime, the third party is influenced or prevented by the buyer or the seller from fixing the price. In such cases, the innocent party may recover damages from the defaulting party.

Example:

A agreed to sell his 100 bags of rice to B at a price to be fixed by C. But C failed to fix the price. In this case, the agreement becomes void on C's failure to fix the price.

UNIT 2: CONDITIONS AND WARRANTIES

INTRODUCTION :

In every contract of sale of goods there are certain stipulations made with reference to goods which are the subject-matter thereof. Such stipulations differ in character and importance. The clause divides stipulations into conditions and warranties.

Condition [Section 12]:

"A condition is a stipulation essential to the main purpose of the contract,that breach of which gives a right to treat the contract as repudiated."

Warranty [Section 12]:

"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 a right to reject the goods and treat the contract as repudiated".

CONDITION	WARRANTY
1. A condition is essential to the main purpose of the contract.	1. It is only collateral to the main purpose of the contract.
2. In case of breach of condition, aggrieved party can: a) Rescind the contract, return the goods and claim refund. b) Claim damages	2. In case of breach of warranty, aggrieved party can only claim damages.
3. A breach of condition may be treated as a breach of warranty	3. A breach of warranty cannot be treated as a breach of condition.
4. Example:	4. Example:

WHEN A CONDITION CAN BE TREATED AS A WARRANTY

[Section 13]: In following cases, Buyer can only claim damages

1. Voluntary waiver of condition: Where a contract of sale is subject to any condition to be fulfilled by the seller, the buyer may waive the condition or elect to treat the breach of the condition as a breach of warranty and not as a ground for treating the contract as repudiated.

2. Where the buyer elects to treat the breach of the conditions, as one of a warranty. That is to say, he may claim only damages instead of repudiating the contract
   Example: A agrees to supply B 10 bags of first quality sugar @ ₹625 per bag but supplies only second quality sugar, the price of which is ₹600 per bag. There is a breach of condition and the buyer can reject the goods. But if the buyer so elects, he may treat it as a breach of warranty, accept the second quality sugar and claim damages @ ₹25 per bag.

3. Compulsory waiver of a condition:
   Where a contract of a sale is not severable and the buyer has accepted the goods or part thereof, the breach of any condition to be fulfilled by the seller can only be treated as a breach of warranty and not as a ground for rejecting the goods and treating the contract as repudiated, unless there is a terms of the contract, express or implied, to that effect.
   Example: B agrees to buy from A 20 bales of cotton by sample. The cotton is delivered to B who makes payment of its price. B upon examination of cotton finds them not equal to sample but uses 2 bales and sells 3. At this point he cannot rescind the contract and recover the price. But A is bound to compensate for the loss caused to B by breach of warranty.

4. Impossibility:
   Nothing in this section shall affect the case of any condition or warranty, fulfilment of which is excused by reason of impossibility or otherwise.

CONDITIONS

Express conditions: Express conditions are those, which are agreed upon between the parties at the time of contract and are expressly provided in the contract.

Implied Conditions:

- ✓ It is a condition, which the law implies into the contract of sale. The law presumes that the parties have incorporated it into their contract.
- ✓ The implied conditions are read into every contract of sale unless they are expressly excluded by the parties.
- ✓ In case of conflict between the express and implied conditions, the express term shall prevail and the implied terms shall not be considered.
- ✓ Following are the implied conditions which are contained in the Sale of Goods Act :

1. Conditions as to title [Section 14]:

- ❖ According to this condition, it is presumed that the seller has a valid title to the goods, i.e., he has the right to sell the goods. If later on, the buyer comes to know that the seller had no valid right to sell the goods, then he may reject the goods and claim the refund of the price, if already paid.
- ❖ This implied condition may be analysed as under:
  - (i) In case of sale, the implied condition is that the seller has the right to sell the goods, and
  - (ii) In case of an agreement to sell, the implied condition is that the seller will have the right to sell the goods at the time when the ownership is to pass from the seller to the buyer.
- ❖ Example: A sold car to B for ₹ 5 lacs. But A had stolen the car from X. Subsequently X took car back from B. B can rescind the contract and claim refund of ₹5 lacs from B.

2. Condition as to description [Section 15]:

- ❖ Sometimes, the goods are sold by description. In such cases, the implied condition is that the goods shall correspond with the description.
- ❖ The term 'correspondence with description' means that the goods purchased by the buyer must be the same which were described by the seller.
- ❖ If subsequently, it is discovered that the goods do not correspond with the description, the buyer may reject the goods and claim the refund of the price, if already paid.
- ❖ Example: B ordered 1000 jeans, blue in colour and three-fouth in length. But seller delivered black jeans. B can reject the goods.

3. Condition as to sample [Section 17]:

- ❖ In case of sale of goods by showing the sample to the buyer, there are following three implied conditions,
  - (i) That the goods delivered shall correspond with the quality of the sample
  - (ii) That the buyer shall have a reasonable opportunity of comparing the bulk with the sample.

(iii) That the goods shall be free from latent defects (i.e., the defects which are not discoverable on reasonable examination of sample)

4. Condition as to sample as well as description [Section 15]:

- Sometimes, the seller shows sample of the goods to the buyer and also gives him their description. In such cases, the implied condition is that the goods shall correspond with both, the sample as well as description.

5. Condition as to quality or fitness for buyer's purpose [Section 16(1)]:

- Ordinarily, there is no implied condition that the goods shall be fit for the particular purpose of the buyer.
- Seller is not responsible:
  (i) To know the particular purpose of buyer.
  (ii) If buyer chooses the goods negligently.
- However in following exceptions, there is an implied condition that the goods shall be fit for the buyer's specific purpose.
  In following cases seller is responsible to the buyer:
  (i) If the buyer makes his purpose clear to the seller.
  (ii) If the buyer buys the goods 'relying upon his skill and judgment'.
- Example: B wanted to buy truck which can use in hilly, snow regions. He specified his purpose to seller and relied on his skill. But the seller delivered the truck which was not fit for the purpose. B can reject the truck.

6. Condition as to merchantability [Section 16(2)]:

The expression "merchantable quality", though not defined, but it means goods of such quality and in such a condition a man of ordinary prudence would accept them as goods of that description.

However, it has been interpreted by the courts, and basically it means the two things, namely:

If goods are purchased for:

Self Use	Resale
Then they should be reasonably fit for the purpose for which they are generally used. Example:	Then they should be immediately re-saleable in the market under their description. Example:

7. Condition as to wholesomeness:

This condition is a part of the condition as to merchantability. It is applicable in cases of eatables, i.e., foodstuffs and other goods which are used for human consumption. As per this condition, goods sold must be fit for human consumption.

Example:

WARRANTIES :

- EXPRESS WARRANTIES
- IMPLIED WARRANTIES

Implied Warranties:

- ✓ It is a warranty, which the law implies into the contract of sale. The law presumes that the parties have incorporated it into their contract.
- ✓ The implied warranties are read into every contract of sale unless they are expressly excluded by the parties.
- ✓ In case of conflict between the express and implied warranties, the express term shall prevail and the implied terms shall not be considered.
- ✓ Following are the implied warranties which are contained in the Sale of Goods Act :

1. Warranty as to undisturbed possession [Section 14(b)]:
   - ❖ Where the buyer has obtained the possession of the goods, he has a right to enjoy them in a way he likes, i.e., no one should interfere with the quiet enjoyment of the buyer.
   - ❖ If buyer's right of possession and enjoyment is disturbed by anyone, then the buyer can recover damages from the seller.
   - ❖ Example:

2. Warranty as to free from encumbrance [Section 14(c)]:
   - ❖ In every contract of sale there is an implied warranty that the goods sold shall be free from any charge.
   - ❖ If the possession of the buyer is disturbed due to such charge in favour of third party, he can claim damages from the seller.
   - ❖ Example:

3. Disclosure of dangerous nature of goods:
   - ❖ There is another implied warranty on the part of the seller that in case the goods are inherently dangerous or they are likely to be dangerous to the buyer and the buyer is ignorant of the danger, the seller must warn the buyer of the probable danger.
   - ❖ If there is breach of this warranty, the seller will be liable in damages.

4. Warranties quality or fitness by usage of trade [Section 16(3)]:
   - ❖ Like implied conditions, implied warranties are also attached by custom or usage of trade. This is so because the parties enter into an agreement subject to the known customs or usages of trade.

THE DOCTRINE OF CAVEAT EMPTOR(BUYER BEWARE) [SECTION 16]:

- ❖ 'Caveat Emptor' is a Latin expression which means "let the buyer beware".
- ❖ The Doctrine states generally seller is not responsible for bad goods.
- ❖ This Doctrine takes the side of the seller.
- ❖ As per the rule, seller is not responsible in following cases:-
  (i) To know the particular purpose of buyer.
  (ii) If buyer chooses the goods negligently
  (iii) If the goods are defective and the defect is patent (i.e. defect which can be discovered by mere inspection)
- ❖ When the goods are purchased under some brand name:
  If the buyer relying on the brand name, purchases the goods and unfortunately the goods turn out to be defective, then the buyer is responsible.

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

1. Where the buyer specifies the particular purpose for which the goods are required to the seller.
   Where the article can be used for only one particular purpose, the buyer need not tell the seller the purpose for which he required the goods. But where the article can be used for a number of purposes, the buyer should tell the seller the purpose for which he requires the goods, if he wants to make the seller responsible.

Case law: In *Bombay Burma Trading Corporation Ltd. vs. Aga Muhammad,* timber was purchased for the express purpose of using it as railways sleepers and when it was found to be unfit for the purpose, the Court
held that the contract could be avoided.

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

UNIT 3: TRANSFER OF OWNERSHIP AND DELIVERY OF GOODS

TRANSFER OF PROPERTY: (Section 18 to 30)	DELIVERY OF GOODS: (Section 31 to 41)	ACCEPTANCE OF GOODS (Section 42 to 44)
1. Meaning 2. Rules	1. Meaning 2. Rules	

TRANSFER OF PROPERTY (OWNERSHIP) (Section 18 to 30):

(1) Appropriation of goods (Section 23):

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.

It is a bilateral act of the seller and the buyer to identify and set apart the goods.

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 appropriated tothe contract either by delivery to the buyer or his agent or the carrier.
e) The appropriation must be made by:
   (i) The seller with the assent of the buyer; or
   (ii) The buyer with the assent of the seller.
f) The assent may be express or implied.
g) The assent may be given either before or after appropriation.

Example:

(2) Goods sent on approval or "on sale or return" (Section 24)

- The ownership of goods is with seller and the possession of goods is with buyer
- The buyer has an option to return the goods.
- The ownership is transferred to the buyer in any of the following three ways:

1) When the buyer accepts the goods:
The acceptance by the buyer may be express or implied.
2) When the buyer adopts the transaction:
The buyer may adopt the goods by doing some act which shows that he has accepted the goods e.g., where he further sells or pledges the goods.
Example: 'A' delivered some jewellery to 'B' on sale or return basis. 'B' pledged the jewellery with 'C'. It was held that the ownership of the jewellery had been transferred to 'B' as he had adopted the transaction by pledging the jewellery with 'C'. In this case, 'A' has no right against 'C'. He can only recover the price of the jewellery from 'B'.
3) Where the buyer fails to return the goods within fixed or reasonable time

➢ Sale for cash only or Return

It may be noted that where the goods have been delivered by a person on "sale or return" on the terms that the goods were to remain the property of the seller till they are paid for, the property therein does not pass to the buyer until the terms are complied with, i.e., cash is paid for.

Example: 'A' delivered his jewellery to 'B' on sale for cash only or return basis. It was expressly provided in the contract that the jewellery shall remain 'A's property until the price is paid. Before the payment of the price, 'B' pledged the jewellery with 'C'. It was held that at the time of pledge, the ownership was not transferred to'B'. Thus, the pledge was not valid and 'A' could recover the jewellery from 'C'.

(3) Transfer of title by non-owners (Section 27 to 30)

➢ "Nemo dat quod non-habet": This means that 'no one can transfer a better title than he himself has'. Thus, the buyer cannot get a better title than that of the seller. If the seller's own title is defective, the buyer's title will also be defective. If the seller is not the owner of goods, then the buyer also will not become the owner i.e. the title of the buyer shall be the same as that of the seller.

➢ Example:

➢ If this rule is strictly followed, then the innocent buyers may be put to loss in many cases. Therefore, to protect the innocent buyers, a number of exceptions have been provided to this rule.

Exceptions:

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

1. Sale by a mercantile agent (Section 27)

   Sale made by a mercantile agent of the goods for document of title to goods would pass a good title to the buyer in the following circumstances; namely;

   (a) If he was in possession of the goods or documents with the consent of the owner;

   (b) If the sale was made by him when acting in the ordinary course of business as a mercantile agent; and

   (c) If the buyer had acted in good faith and has at the time of the contract of sale, no notice of the fact that the seller had no authority to sell.

2. Sale by a joint owner (Section 28): When the joint owner is in the sole possession of the goods, and he sells them to a person who buys in a good faith, the buyer gets a valid title to the goods.

   Example: A, B, C jointly purchase a TV which is kept at A's house. In B&C's absence, A sold the TV to X, who buys in good faith. X will get a good title.

3. Sale by estoppel: When the owner of goods, by his conduct or by statement, wilfully leads the buyer to believe that the seller has the authority to sell, then he is estopped (i.e., prevented) from denying the seller's authority to sell

   Example: In A's presence, B sold A's phone to X. A does not deny it & X buy in good faith. A will get a good title.

4. Sale by unpaid seller: To be done in Unit 4

5. Sale by a seller in possession of goods after their sale [Section 30(1)]: If the seller continues to have the possession of the goods even after their sale and if he resells the same goods to a new buyer then in such cases, the second buyer gets a valid title to the goods if he buys them in a good faith.

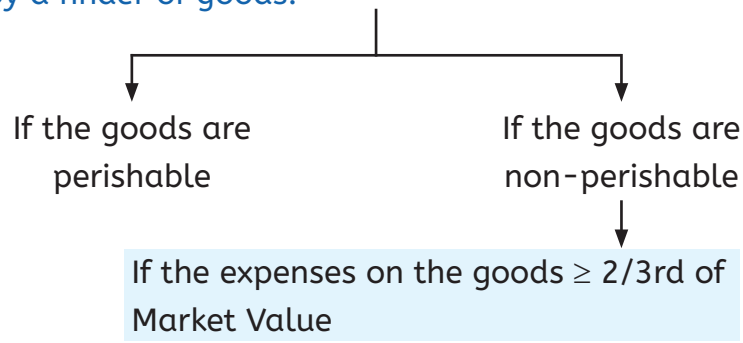
   Example: A sold TV to B. B got the ownership but the requested A to keep the TV with himself for few days. In B's absence, A sold the same TV to X, who buys in good faith. He will get a good title.

6. Sale by a buyer in possession of goods before the ownership is transferred. [Section 30(2)]: If the buyer obtains the possession of the goods which he has bought or agreed to buy from the seller and the seller still has some lien

or other rights over the goods. If the buyer resells the same goods to a new person. In such cases, the second buyer gets a valid title free.

Example: A gave the machine to B but reserved his ownership. B sold the machine to X, who buys in good faith. X will get a good title.

7. Sale by a finder of goods:



8. Sale by a person in possession under a voidable contract (Section 29):The buyer gets a valid title only if the following conditions are satisfied:-
   a. A person must obtain the possession of the goods by coercion, undue influence, fraud or misrepresentation.
   b. The seller must have obtained the possession of the goods under a voidable contract and not under a void contract.
   c. The contract must not have been rescinded (i.e., put to an end) at the time of sale
   d. The buyer must act in a good faith.

   Example: A obtained a diamond ring from B fraudulently. But before B could rescind the contract, A sold the ring to X who buys in good faith. He will get a good title.

9. Sale Under the Provision of Other Acts :
   a. Sale by an Official Receiver or Liquidator of the Company will give a valid title to the purchaser.
   b. Sale by a pawnee/pledgee under default of pawnor in repayment of debt will give valid title to the purchaser.

   ➢ In case of hire-purchase, hirer cannot pass a good title even to a bonafide buyer.

   Example: P, the hirer of vehicle under a hire purchase agreement, sells them to Q. Q, though a bona fide purchaser does not acquire the ownership in the vehicle.

   ➢ In theft, thief cannot pass a good title even to a bonafide buyer.

ACCEPTANCE OF DELIVERY OF GOODS

- Rule related to Acceptance of Delivery of Goods (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.

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

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

UNIT 4 : UNPAID SELLER

MEANING OF UNPAID SELLER [SECTION 45(1)]:

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

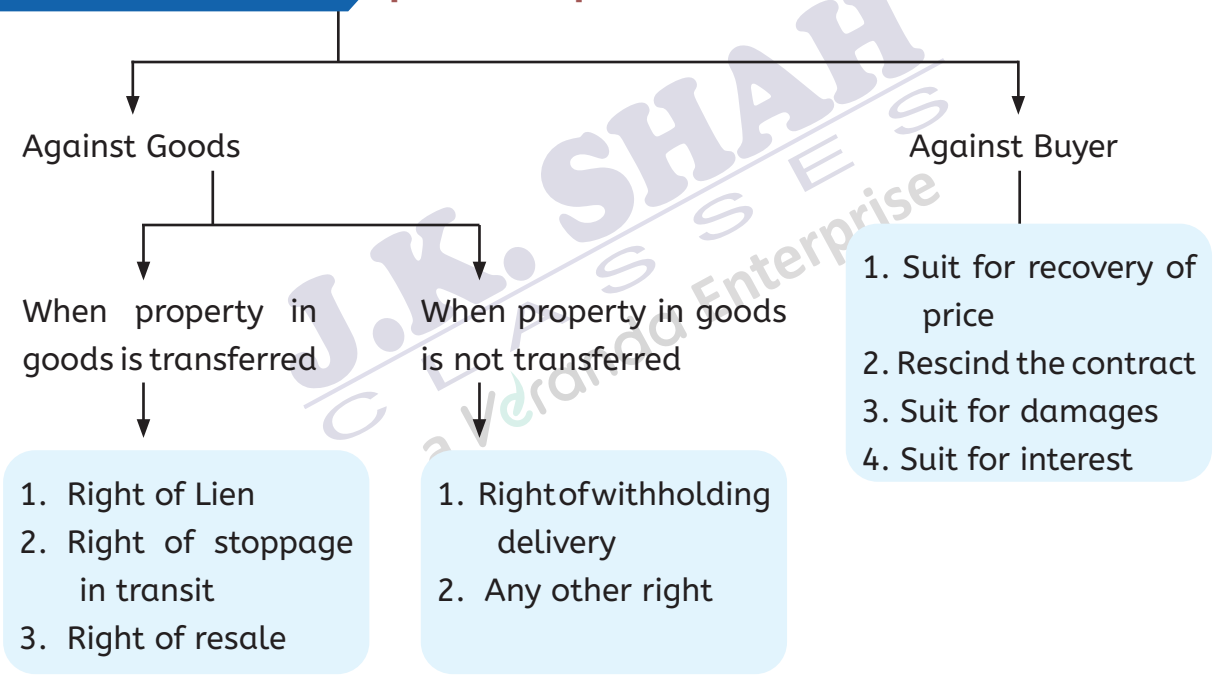
(1) The whole or part of the price has not been paid or tendered and that the seller has immediate right of action for the price.

Example: X sold certain goods to Y for 50,000. Y paid 40,000 but fails to pay the balance. X is an unpaid seller.

(2) A bill of exchange or other negotiable instrument has been received but the same has been dishonoured.

Example: P sold some goods to R for 60,000 and received a cheque for a full price. On presentment, the cheque was dishonoured by the bank. P is an unpaid seller.

RIGHTS OF UNPAID SELLER [SECTION 46]



(A) Rights against the Goods:

1. Where the ownership of the goods has transferred to the buyer:

In this case, the unpaid seller has the following rights:

(a) Right of Lien [section 47 to 49]

- The right of lien is the right to retain possession of the goods.
- This right can be exercised only when the possession of goods is with the seller.
- The unpaid seller of goods can retain his possession of goods until payment of the price in following cases[Section 47]:

a) Where the goods are not sold on credit.

b) Where the goods have been sold on credit, but the term of credit has expired

c) Where the buyer becomes insolvent.

- The unpaid seller can retain the goods only for the payment of the price of the goods: He cannot retain the goods for any other charges, e.g., maintenance, charges for storage of goods during the exercise of lien etc.
- 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
- The right of lien is indivisible in nature.
- Termination of Lien (Section 49):

a) By delivery of goods to the carrier/ buyer

b) By Estoppel i.e., where the seller by his conduct makes third parties believe that he has waived his right of lien.

c) By waiver of the lien

d) By payment of price by the buyer

- The unpaid seller of the goods, having a lien thereon, does not lose his lien by reason only that he has obtained a decree (order from court) for the price of the goods.
- Example: A sold 100 bottles of coconut oil to B. Bottles were still kept with A. B fails to pay price for the bottles. A can refuse the bottles and can exercise his right of lien.

(b) Right of stoppage in transit [Section 50 to 52]

- Meaning of right of stoppage in transit [Section 50]: The right of stoppage in transit means the right of stopping the goods while they are in transit, to regain the possession 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.
- Therefore, the right of stoppage in transit is exercised only when the following conditions are fulfilled:

(a) The seller must be unpaid.

(b) He must have parted with the possession of goods.

(c) The goods are in transit.

(d) The buyer has become insolvent.

➢ Duration of transit [Section 51]: The goods are deemed to be in course of transit from the time when they are delivered to a carrier or other bailee for the purpose of transmission to the buyer, until the buyer or his agent in that behalf takes delivery of them from such carrier or other bailee.

➢ When does the transit come to an end?

The right of stoppage in transit is lost when transit comes to an end. Transit comes to an end in the following cases:

1) When the buyer or other bailee obtains delivery.
2) Buyer obtains delivery before the arrival of goods at destination.
3) Where the carrier or other bailee acknowledges to the buyer or his agent that he holds the goods assoon as the goods are loaded on the ship, unless the seller has reserved the right of disposal of the goods.
4) If the carrier wrongfully refuses to deliver the goods to the buyer.
5) Where goods are delivered to the carrier hired by the buyer, the transit comes to an end.
6) 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.
7) Where the goods are delivered to a ship chartered by the buyer, the transit comes to an end.

➢ How stoppage in transit is effected (Section 52)

1) The unpaid seller may exercise his right of stoppage in transit either by taking actual possession of the goods, or by giving notice of his claim to the carrier or other bailee in whose possession the goods are. Such notice may be given either to the person in actual possession of the goods or to his principal.

   If the notice is sent to the principal then the notice is deemed to have reached when such principal communicates it to his servant or agent.

2) When 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.

(c) Right of Resale [Section 54]

The unpaid seller has the direct right to resell the goods in the following circumstances:

1. Where the goods are of perishable nature
2. Where the unpaid seller has expressly reserved his right of resale.

In any other case, the unpaid seller has the right to resell the goods by following the procedure:

1. Unpaid seller should give a notice to the buyer of his intention to resell the goods (+) Additional time for payment
2. If the buyer does not pay the price within a reasonable time, the seller may resell the goods
   - ❖ If the notice of resale is given then in case of loss on resale, it can be recovered and in case of profit on resale, it can be retained.
   - ❖ However the notice of resale is not given, the seller cannot recover the loss suffered on resale. Moreover, if there is any profit on resale he must return it to the original buyer

➢ Sale by unpaid seller: Where on 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 (It is an exception to the rule of "Nemo dat quod non-habet')

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

(a) Right of Withholding Delivery

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

(b) Any other right

Since ownership and possession of goods is with the seller, seller can use, gift, resell the goods without giving any notice, etc.

(B) Rights against the Buyer [Section 55, 56, 60,61]

1. Suit for recovery of price [Section 55]

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

2. Suit for damages [Section 56]

Where the seller is ready and willing to deliver the goods to the buyer, but the buyer wrongfully neglects or refuses to accept the goods and pay for them, then the seller may bring a legal action against the buyer for the recovery of damages suffered due to non-acceptance of the goods.

3. Repudiation (cancellation) of contract before due date [Section 60]: Where the buyer repudiates the contract before the date of delivery, the seller may treat the contract as rescinded and sue damages for the breach. This is known as the 'rule of anticipatory breach contract'.

4. Suit for interest [Section 61]

Where there is specific agreement between the seller and the buyer as to interest on the price of the goods from the date on which payment becomes due, the seller may recover interest from the buyer.

In the absence of a contract 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.

EFFECTS OF SUB-SALE OR PLEDGE BY BUYER [Section 53]

- The right of lien or stoppage in transit is not affected by the buyer selling or pledging the goods unless the seller has assented to it.

- Exceptions:

(a) When the seller has assented to the sale, mortgage or other disposition of the goods made by the buyer.

(b) When a document showing title to goods has been transferred to the buyer and the buyer transfers the documents to a person who has bought goods in good faith and for value.

- Example:

Case law: In *Mount D. F. Ltd. vs Jay & Jay (Provisions) Co. Ltd*

A entered into a contract to sell cartons in possession of a wharfinger to B and agreed with B that the price will be paid to A from the sale proceeds recovered from his customers. Now B sold goods to C and C duly paid to B. But anyhow B failed to make the payment to A. A wanted to exercise his right of lien and ordered the wharfinger not to make delivery to C. Held that the seller had assented to the resale of the goods by the buyer to the sub-buyers. As a result A's right to lien is defeated

RIGHTS OF PARTIES IN BREACH OF CONTRACT

Rights of Seller against Buyer [Section 55, 56, 60, 61]

1) Suit for recovery of price
2) Suit for damages
3) Repudiation (cancellation) of contract before due date
4) Suit for interest

(Already explained above)

Rights of Buyer against Seller (Section 57 to 60)

1) Damages for non-delivery
2) Suit for specific performance
3) Suit for breach of warranty
4) Repudiation (cancellation) of contract before due date
5) Suit for interest

AUCTION SALES [Section 64]

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

He acts as an agent of the seller till the article is 'knocked down' to the bidder.	He acts as an agent of the buyer after the article is 'knocked down' to the bidder.

- Rules regarding Auction Sales:

Section 64 of the Sale of Goods Act, 1930 provides following rules to regulate thesale 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.

5. THE INDIAN PARTNERSHIP ACT, 1932

UNIT 1:GENERAL NATURE OF PARTNERSHIP

INTRODUCTION :

- It came into force on 1st October, 1932.
- Prior to the passing of the Act, the law of partnership was included in Chapter XI of the Indian Contract Act.
- Where the Partnership Act is silent on any point, the general principles of the law of contract apply. The partnership is a specialized branch of the Contract Act.

DEFINITION OF PARTNERSHIP

Section 4 of the Partnership Act defines partnership as under:

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

PARTNER& FIRM

- 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".
- Crown', Emperor', 'Empress', 'Empire', 'Imperial', 'King', 'Queen', 'Royal', or words cannot be used in the name of the firm except when the State Government signifies its consent to the use of such words as part of the firm-name by order in writing.

  However, now such rule does not exist.

ESSENTIAL ELEMENTS OF PARTNERSHIP

Therefore, the essential elements of the relationship of partnership may be stated as follows:

(1) There must be an association of two or more persons.
(2) There must be an agreement.
(3) There must be a business
(4) There must be an agreement to share the profits of a business, and
(5) There must be an element of 'agency' i.e. the business must be carried on by all or any of them acting for all.

Thus, essential elements of relationship of partnership are:

(1) There must be two or more persons:

- There must be at least two persons to form a partnership. Maximum number of partners, partnership act is silent. But Section 464 0f The Companies Act 2013 specifies it as 50. If number of partners fall below it ceases to be partnership. If it goes beyond 50, it will become an illegal association.
- The persons can be natural or artificial. Hence 2 companies can be partners. But a firm cannot enter into a contract for partnership though their partners can become partners.
- All such persons must be competent to contract. According to Indian Contract Act every person except the following:
  (i) Minor
  (ii) Person of unsound mind
  (iii) Person disqualified by any law to which they are subject (alien, insolvents etc)

(2) There must be an agreement:

- A partnership arises only as a result of an agreement. Such an agreement may be express or implied. Implied in the sense that it may be a voluntary act by the persons. Agreement can be oral or in writing but partnership deed must be in writing
- Partnership is thus created by contract; it does not arise by operation of law or from status
- Agreement must be valid
  Partnership agreement is like any other contract, so it must satisfy all the essentials of a valid contract. In other words, the parties must be 'competent', i.e. capable of entering into an agreement, their consent must be free and there should be a lawful consideration and object.

(3) There must be a business:

- The existence of a business is essential in a partnership. "Business" includes every trade, occupation and profession carried on with an intention to make profits.
- If two or more persons join together to form a 'dramatic club' it is not a partnership because there is no business in this case. Similarly, if A and Bare co-owners of a building and let it to a tenant for rent and divide the net rents between themselves. A and B are not partners because letting a house is not a business. But if A and B agree to convert the building into a hotel and to share the profits equally, there is a "business" here and hence A and B are partners in respect of such business.
- The business must be lawful.
- Multiple business are allowed.

(4) Sharing of profits:

- The agreement to share profit is essential, but it should be noted that an agreement to share the losses is not essential. Where nothing is said as to the sharing of losses, it is implied in a partnership deed.
  It may, however, be agreed that as between the partners anyone or more of them shall not be liable for losses. But the reverse is not just possible. So where persons agree to share the profits of a money-lending business, they become partners, but where one of them, so called partner is not to receive profits, he is not a partner. E.g. A and B agree to work together as carpenters, but that A shall receive all profits and shall pay wages to B, A and B are not partners. When profit is made, it must be distributed (in absence of any agreement) equally, or in the agreed ratio.

- It is just a prima facia evidence but not a conclusive evidence of partnership.

- A person, who receives the profits of a business, is not necessarily a partner. The persons who receive the profits but are not the partners are referred as under:
  1. Retired partner
     After retirement if the settlement of accounts is not done then the retired partner may get share in profits. But he is not treated as partner.
  2. Money-lenders receiving profits:
     A money-lender is a person who lends money on interest. Sometimes, a money-lender receives, in addition to or in place of his interest, a portion of the profits of a business. In such cases, he cannot be said to be a partner only on the ground that he receives the profits of the business.
  3. Employee or agent receiving profits:
     Sometimes, an employee or an agent of a business agrees to receive, in addition to or in place of his regular remuneration, a portion of the profits of the business. In such cases, he cannot be said to be a partner only on the ground that he receives the profits of the business.
  4. Widow or child of a deceased partner:
     Sometimes, the widow or a child of deceased partner receives a portion of profits as annuity. In such cases, they cannot be said to be the partners of the firm only on the ground that they receive the profits of the business.
  5. Seller of goodwill:
     Sometimes, a person who sells his business along with its goodwill, is given a share in the profits of the business he has sold. In such cases, that person does not become a partner in the business only on the ground that he receives the profits of the business.
  6. Minor:
     Minor receives share in profits but is not considered as partner.
- Just because a person is sharing profits, he is not a partner. But if a person is a partner, he will definitely get share in profits.

(5) Business carried on by all or any of them acting for all:

- The business must be carried on by all the partners or by anyone or more of the partners acting for all. This is the cardinal principle of the partnership Law. In other words, there should be a binding contract of mutual agency between the partners.
- An act of one partner in the course of the business of the firm is in fact an act of all partners. Each partner carrying on the business is the principal as well as the agent for all the other partners. He is an agent in so far as he can bind the other partners by his acts and he is a principal to the extent that he is bound by the act of other partners.
- It means every partner is a

  Agent of the firm — Principal for other partners acts

- 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.

CLASSES OF PARTNERSHIP:

Partnership can be classified as under:

1. Partnership at will according to Section 7 of the Act, partnership at will is a partnership when:
   1. No fixed period has been agreed upon for the duration of the partnership; and
   2. There is no provision made as to the determination of the partnership.

   These two conditions must be satisfied before a partnership can be regarded as a partnership at will.

   Where a partnership entered into for a fixed term is continued after the expiry of such term, it is to be treated as having become a partnership at will.

   A partnership at will may be dissolved by any partner by giving notice in writing to all the other partners of his intention to dissolve the same.

2. 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 particular period of time. Such a partnership comes to an end on the expiry of the fixed period.

3. 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 business, subject to any agreement, dissolved by the completion of the business.

4. 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.

CLASSES OR TYPES OF PARTNERS :

Partners can be classified as shown below:

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

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

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

4. Partner for profits only :
   - ❖ Partners may agree that a particular partner shall get a share of the profits only but he will not be called upon to contribute towards the losses. Such a partner is known as 'partner for profits only'.
   - ❖ This is simply an, inter-se agreement binding the partners only. Hence, he continues to be liable to third parties for all acts of the firm.

5. Sub-Partner :
   - ❖ When a partner agrees to share his profits divided from the firm with a third person, that third person is known as 'sub-partner'. Such a sub-partner is in no way connected with the firm.

- He cannot represent the firm and bind the firm by his acts. He has no right against the firm nor is he liable for the acts of the firm.

6. Partner by Holding Out or by Estoppel (Section 28):

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

  X and Y are partners in a partnership firm. X introduced A, a manager, as his partner to Z. A remained silent. Z, a trader believing A as partner supplied 100 T.V sets to the firm on credit. After expiry of credit period, Z did not get amount of T.V sets sold to the partnership firm. Z filed a suit against X and A for the recovery of price. Here, in the given case, A, the Manager is also liable for the price because he becomes a partner by holding out (Section 28, Indian Partnership Act, 1932).
- 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.

  Example: A partnership firm consisting of P, Q, R and S. S retires from the firm without giving public notice and his name continues to be used on letterheads. Here, S is liable as a partner by holding out to creditors who have lent on the faith of his being a partner.

7. Incoming Partner:

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

8. Outgoing Partner:

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

REGISTRATION OF FIRM

- The registration of a firm is not compulsory. It is optional for the firm either to get itself registered or not. There is no penalty for non-registration of a firm. The registration can be done anytime, either in the beginning or during the continuance of business.

❖ Procedure (Section 58):

1. Step 1- Obtain a statement in the form from the office of the Registrar.

2. Step 2- State the following information:
   - Name of the firm
   - Principal place of the firm
   - Name of the other places where the firm carries its business
   - Date when each partner joined
   - Name in full and permanent address of each partner
   - Duration of the firm.

3. Step 3- Get the statement of duly verified and signed by all the partners or their agents.

4. Step4- File the statement along with prescribed fees

5. Step 5- Obtain a certificate or registration from the Registrar.

❖ 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. Then he shall issue a certificate of Registration. 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.

❖ Consequences of non-registration (Section 69):

1. The partners cannot file a suit against the firm or other partners:
   A partner of an unregistered firm cannot file a suit against the firm or his other present or past partners, for the enforcement of any right arising from a contract or conferred by the Indian Partnership Act. However, this disability may be removed by getting the firm registered before filing the suit.
2. The firm cannot file a suit against third parties:
   An unregistered firm cannot file a suit against any third party for the enforcement of any right arising from some contract.
   This disability of an unregistered firm can be removed by getting the firm registered before filing the suit.
3. The partner of the firm cannot claim a set-off:
   The term 'set-off' means the adjustment of debts by one party due to him from the other party who files a suit against him. The partners of an unregistered firm

or the firm itself cannot claim a set-off, in a suit filed against them or the firm. But the right of set-off is not affected if the claim for setoff does not exceed Rs 100 in value.

❖ Following rights are not affected by non-registration:

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 ₹ 100 in value.
5. The right to suit and proceeding instituted by legal representatives or heirs of the deceased partner of a firm for account s of the firm or to realise the property of the firm.

Example: A & Co. is registered as a partnership firm in 2017 with A, B and C partners. In 2018, A dies. In 2019, B and C sue X in the name and on behalf of A & Co. without fresh registration. Now the first question for our consideration is whether the suit is maintainable.

In the case of a registered firm (whose business was carried on after its dissolution by death of one of the partners), a suit can be filed by the remaining partners in respect of any subsequent dealings or transactions without notifying to the Registrar of Firms, the changes in the constitution of the firm, it was decided that the remaining partners should sue in respect of such subsequent dealings or transactions even though the firm was not registered again after such dissolution and no notice of the partner was given to the Registrar.

If in the above example, what difference would it make, if in 2019 B and C had taken a new partner, D, and then filed a suit against X without fresh registration?

Where a new partner is introduced, the fact is to be notified to Registrar who shall make a record of the notice in the entry relating to the firm in the Register of firms. Therefore, the firm cannot sue as D's (new partner's) name has not been entered in the register of firms. It was pointed out that in the second requirement, the phrase "person suing" means persons in the sense of individuals whose names appear in the register as partners and who must be all partners in the firm at the date of the suit.

UNIT 2: RELATION OF PARTNERS

DUTIES OF PARTNERS

1. Duty to account for personal profits (Section 16):

This duty is based on the principle of good faith, which requires that a partner shall not make personal profits at the expense of the firm. If a partner makes personal profits in any of the following ways, he must give account of those profits and pay back the same to the firm:

(a) Personal profits from any transaction of the firm.
(b) Personal profits from the use of the property of the firm.
(c) Personal profits from the business connection of the firm.
(d) Personal profits from the use of the name of the firm.

However, the above duty is subject to a contract between the partners i.e., by a contract, the partners may allow/all or any of them to earn personal profits by using firm name, property etc.

Example: A, B, C & D established partnership business for refining sugar. A, himself was a wholesale grocer, was entrusted with the work of selection and purchase of sugar. As a wholesale grocer, A was well aware of the variations in the sugar market and had the suitable sense of propriety as regards purchases of sugar. He had already in stock sugar purchased at a low price which he sold to the firm when it was in need of some, without informing the partners that the sugar sold had belonged to him. It was held that A was bound to account to the firm for the profit so made by him. This rule, however, is subject to a contract between partners. Where a partner carries on a competing business, he must account for and pay to the firm all profits made by him in that business.

Example: A, B, C and D started a business in partnership for importing salt from foreign ports and selling it at Chittagong. A struck certain transactions in salt on his own account, which were found to be of the same nature as the business carried on by the partnership. It was held that A was liable to account to the firm for profits of the business so made by him. This rule is also subject to a contract between the partners.

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, that is, 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 firm as their contribution to the common business;
(ii) All the property, rights and interest purchased by or for the firm, or for the purposes and in the course of the business of the firm;

(iii) All the property, rights and interest acquired by the firm in other way and

(iv) Goodwill of the business:

Goodwill may be defined as the value of the reputation of a business house in respect of profits expected in future over and above the normal level of profits earned by undertaking belonging to the same class of business.

When a partnership firm is dissolved every partner has a right, in the absence of any agreement, to have the goodwill of business sold for the benefit of all the partners. Goodwill is a part of the property of the firm. It can be sold separately or along with the other properties of the firm.

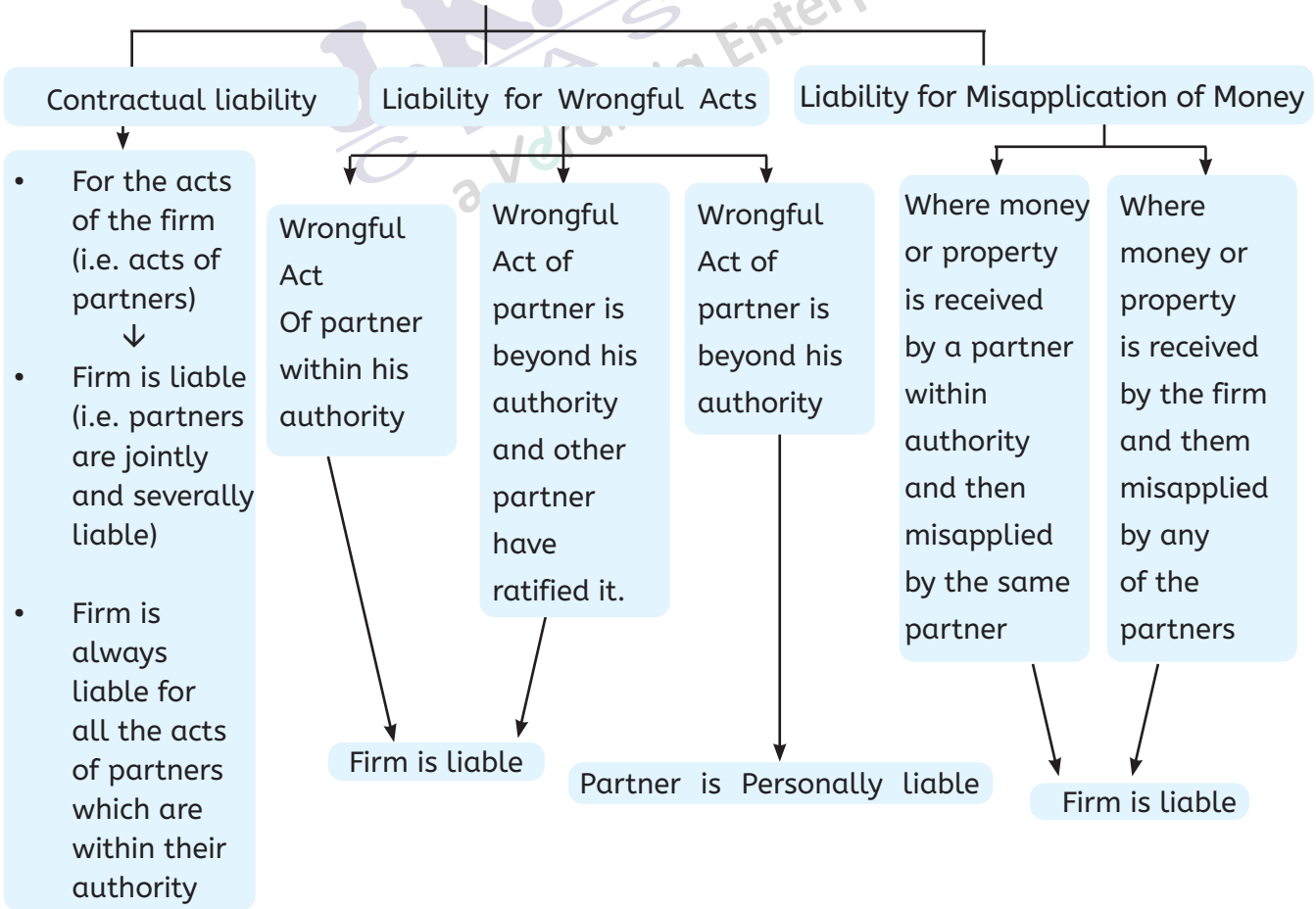
❖ Admission/Representation by a partner (Section 23):

An admission or representation made by a partner relating to affairs of the firm will make the whole firm liable, if it is made in the ordinary of course of business.

Example: X and Y are partners in a firm dealing in spare parts of different brands of motorcycle bikes. Z purchases a spare part for his Yamaha motorcycle after being told by X that the spare part is suitable for his motorcycle. Y is ignorant about this transaction. The spare part proves to be unsuitable for the motorcycle and it is damaged. X and Y both are responsible to Z for his loss.

❖ LIABILITY OF A FIRM AND ITS PARTNERS TO A THIRD PARTY (Section 25 to 27)

This liability may be discussed under the following heads:



1. Liability of a partner for acts of the firm- Contractual liability (Section 25): The partners are jointly and severally responsible to third parties for all acts which come under the scope of their express or implied authority. This is because that all the acts done within the scope of authority are the acts done towards the business of the firm.

   The expression 'act of firm' indicates any act or omission by all the partners or by any partner of the firm, which gives rise to a right enforceable by or against the firm.

2. Liability of the firm for wrongful acts of a partner (Section 26): 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.

   All the partners in a firm are liable to a third party for loss or injury caused to him by the negligent act of a partner acting in the ordinary course of the business.

3. Liability of firm for misapplication by partners (Section 27): Analysis of section 27:

   a) A partner acting within his apparent authority receives money or property from a third party and misapplies it, the firm is liable to make good the loss, or

   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, the firm is liable to make good the loss.

TRANSFER OF PARTNER'S INTEREST (Section 29):

A share in a partnership is transferable like any other property, but as the partnership relationship is based on mutual confidence, the transferee of a partner's interest by sale, or otherwise cannot enjoy the same rights and privileges as the original partner.

The rights of such a transferee are as follows:

1) During the continuance of partnership, such transferee is NOT entitled

   a) to interfere with the conduct of the business,

   b) to require accounts, or

   c) to inspect books of the firm.

   He is only entitled to receive the share of the profits of the transferring partner and he is bound to accept the profits as agreed to by the partners, i.e., he cannot challenge the accounts.

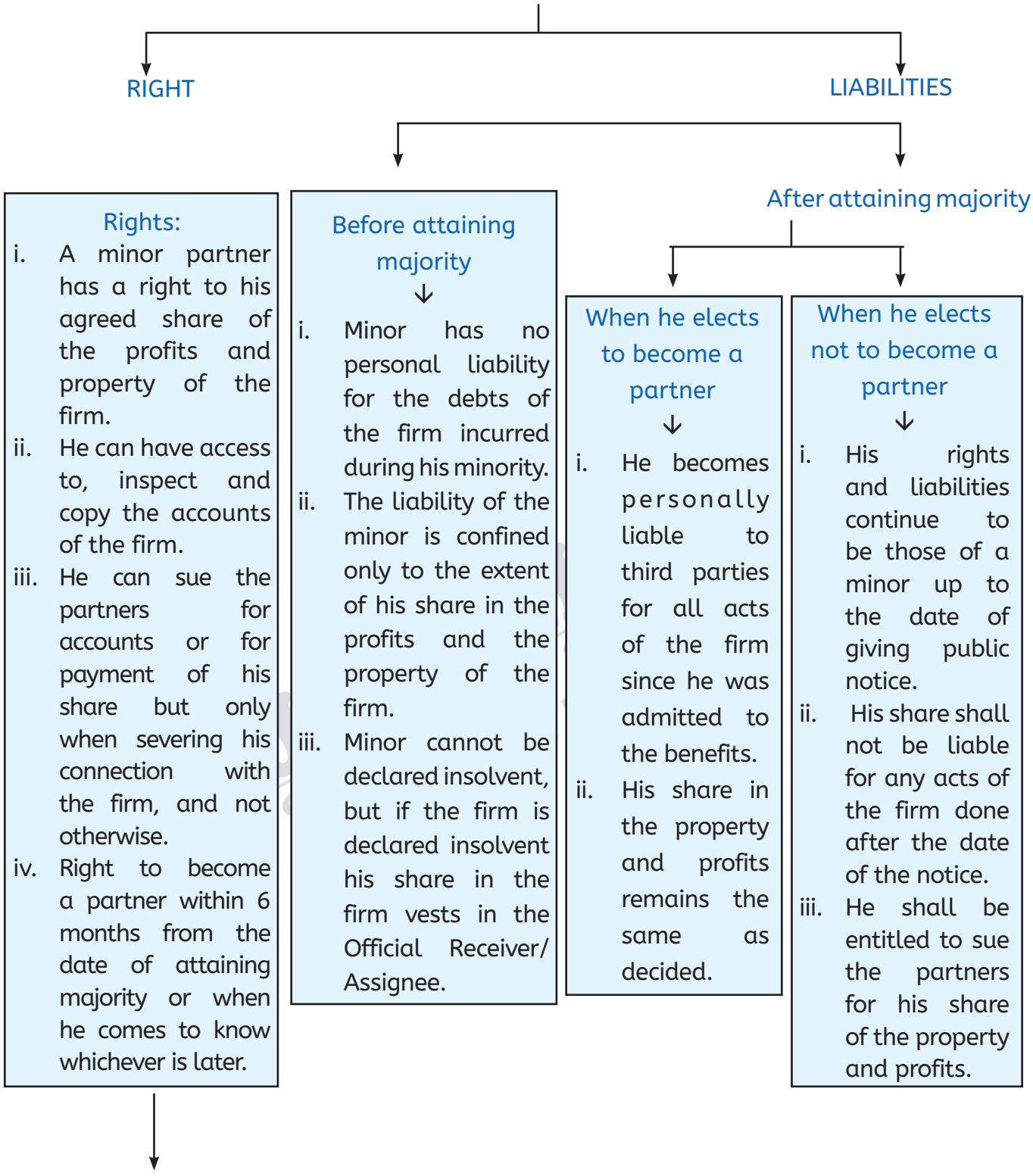
2) On the dissolution of the firm or on the retirement of the transferring partner, the transferee will be entitled, against the remaining partners:
   a) to receive the share of the assets of the firm to which the transferring partner was entitled, and
   b) for the purpose of ascertaining the share, he is entitled to an account as from the date of the dissolution.

MINOR'S POSITION IN PARTNERSHIP FIRM (Section 30)

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

- Note: We have put the rights and liabilities of minor in a chart for convenience of students. However, students are requested to write all the points in a paragraph/point form in exam.

❖ The rights and liabilities of such a partner are as follows:



Where he has elected not to become partner he has to give public notice that he has elected not to become partner and such notice shall determine his position as regards the firm. If he fails to give such notice he shall become a partner in the firm on the expiry of the said six months.

CONSEQUENCES OF PARTNER COMING IN AND GOING OUT- RECONSTITUTION OF A FIRM (SECTION 31- 38)

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

(1) Admission of a new partner (Section 31)
(2) Retirement of a partner (Section 32)
(3) Expulsion of a partner (Section 33)
Rights of Outgoing Partner (Section 36 &37)
(4) Insolvency of a partner. (Section 34)
(5) Death of a partner (Section 35)
(6) Revocation of continuing guarantee (Section 38)

(1) Admission of a Partner (Section 31)

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

(2) Retirement of a Partner (Section 32)

- A partner may also retire from an existing firm. The partner who retires from an existing firm is known as a 'retiring partner' or an 'outgoing partner'.
- A partner may retire from the firm in anyone of the following three modes :
  (a) By consent. A partner may retire, at any time with the consent of all other partners.
  (b) By agreement. The partners may enter into an express agreement about the retirement of a partner. In such cases, a partner may retire according to the terms of the agreement.
  (c) By notice. In case of partnership at will, a partner may retire by given a written notice of retirement to all other partners.

- Retirement of a partner from a firm does not dissolve it unless the firm has only 2 partners.
- The liability of a retiring partner may be discuss as under :
  1. Liability for the acts of the firm done before retirement:
     A retiring partner continues to be liable to third parties for the acts of the firm done before his retirement 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.
  2. Liability for the acts of the firm done after retirement:
     A retiring partner also continues to be liable to third parties for the acts of the firm done even after his retirement until a public notice of his retirement is given This liability of a retiring partner is based on the principle of 'holding out'.

(3) Expulsion of a Partner (Section 33)

- A partner cannot be ordinarily expelled from the firm.
- However, in certain exceptional cases, he can be expelled by following a prescribed procedure.
  He can be expelled only if the following conditions are satisfied:
  (a) The power of expulsion should be given to the partners by an express contract between them.
  (b) The power of expulsion should be exercised by majority of partners.
  (c) The power of expulsion should be exercised in absolute good faith.
  The test of good faith includes three things:
  (1) That the expulsion must be in the interest of the partnership
  (2) That the partner to be expelled is given a notice to that effect
  (3) That he was given an opportunity of being heard.

- It these conditions are not fulfilled the expulsion is null and void and the expelled partner can demand re-instatement in the firm

- Example:
  A, B and C are partners in a partnership firm. They were carrying their business successfully for the past several years. Spouses of A and B fought in ladies club on their personal issue and A's wife was hurt badly. A got angry on the incident and he convinced C to expel B from their partnership firm. B was expelled from partnership without any notice from A and C. According to the test of good faith as required expulsion of Partner B is not valid.

- An expelled partner continues to be liable to third parties for the acts of the firm done even after his expulsion until a public notice of his expulsion is given.
- The public notice can be given either by the expelled partner himself or by the firm.

RIGHTS OF AN OUTGOING PARTNER (Section 36 & 37):

The rights of an outgoing partner are as follows:

1) To carry on competing business (section 36):

An outgoing partner may carry on a business, but it can be restricted by an agreement (below mentioned).

However he cannot:

(a) Use the firm name.

(b) Represent himself as carrying on the business of the firm, or

(c) Solicit the customers of the old firm.

Restraint of trade agreement:

A partner may make an agreement with his partners that on ceasing to be a partner he will not carry on any business similar to that of the firm within a specified period or within specified local limits, such agreement shall be valid if the restrictions imposed are reasonable (Section 27 of the Indian Contract Act, 1872).

2) To share subsequent profits (Section 37):

If settlement of accounts is not yet done, then,

Right of outgoing partner to share subsequent profits — OR — Right to claim interest@ 6%p.a

(4) Insolvency of a Partner (Section 34)

- The partner declared an insolvent; he ceases to be a partner on the date on which the order of adjudication is made.
- The firm is dissolved on the date of the order of insolvency unless the contract specifies that firm will continue.
- The estate of the insolvent is not liable for any act of the firm after the date of the order of insolvency.
- The firm cannot be held liable for any acts of the insolvent partner after the date of the order of insolvency.

(5) Death of a Partner (Section 35)

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

UNIT 3 : DISSOLUTION OF FIRM (SECTION 39 TO 55)

DISSOLUTION OF PARTNERSHIP

The term 'dissolution of partnership' may be defined as a change in the relations of partners, and not the extinction of relationship. In this case, the firm as a whole is not closed down. But only the relations between some of the partners come to an end, and the remaining partners continue to carry on the business of the firm. Thus, the 'dissolution of firm' is different from 'dissolution of partnership.'

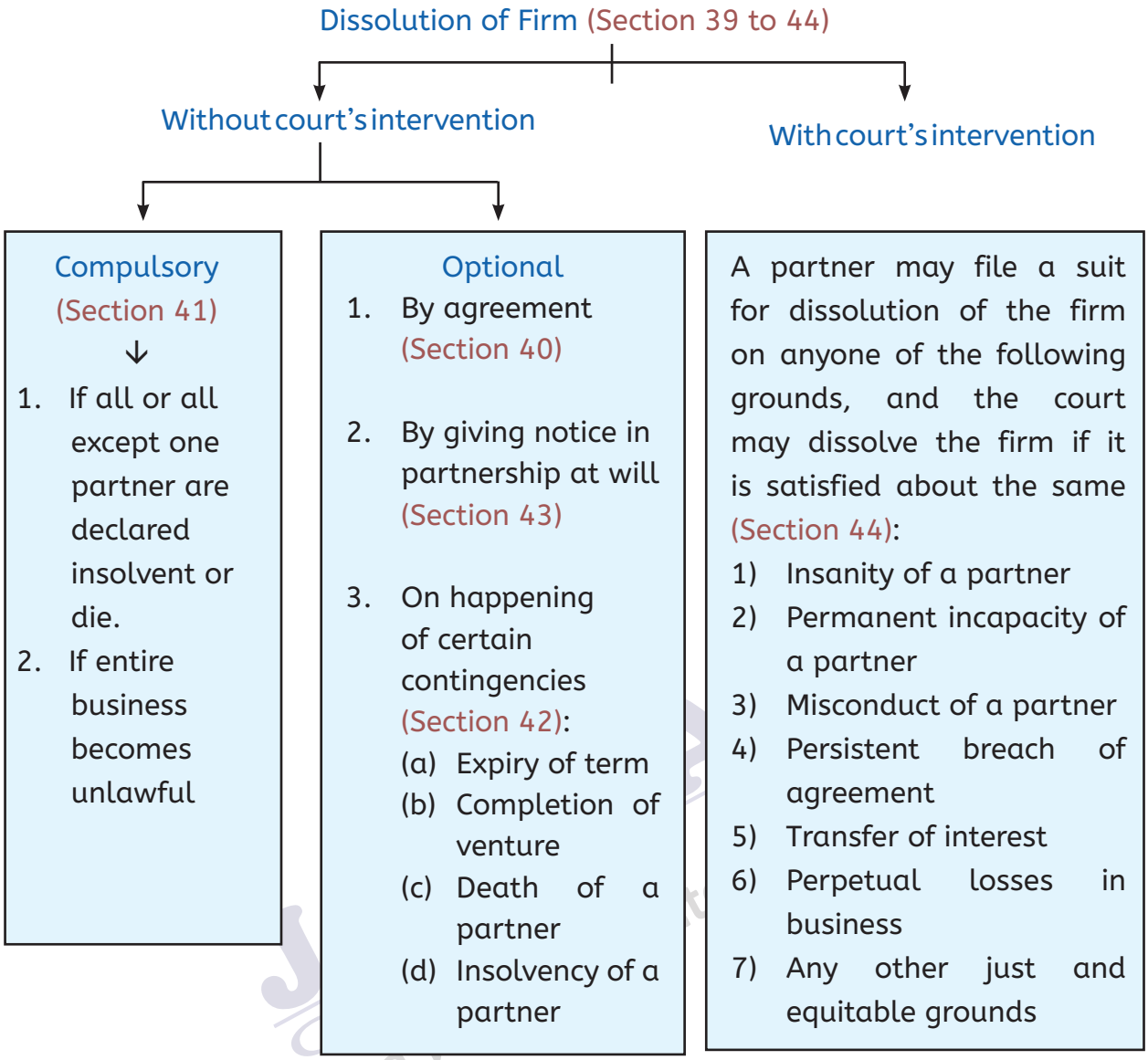
Example :

A, B and C were partners in a firm. A retires. Only the partnership between A, B and C is dissolved and a new partnership between B and C comes into existence. The new firm is called the 'reconstituted firm'. Thus, only the relations between the partners are changed on A's retirement.

DISSOLUTION OF FIRM (Section 39)

When the firm as a whole is closed down, it is called the dissolution of the firm. Thus, in case of dissolution of the firm, the business of the firm is stopped and the relations between all the partners come to an end.

S. No.	Basis of difference	Dissolution of firm	Dissolution of Partnership
1.	Continuation of business	It Involves discontinuation of business in partnership.	It dose not affect continuation of business. It involves only reconstitution of the firm.
2.	Winding Up	It involves winding up of the firm and requires realization of assets and settlement of liabilities.	It involves only reconstitution and requires only revaluation of assets and liability of the firm.
3.	Order to court	A firm may be dissolve by the order of the court.	Dissolution of partnership is not ordered by the court.
4.	Scope	It necessarily involves dissolution of partnership.	It does not involve dissolution of firm.
5.	Final closure of books	It involves final closure of books of the firm.	It does not involve final closure of the book.



CONSEQUENCES OF DISSOLUTION (Section 45 to 55)

1. Liabilities for the acts done after dissolution (Section 45):

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

Example: X and Y who carried on business in partnership for several years, executed on December 1, a deed dissolving the partnership from the date, but failed to give a public notice of the dissolution. On December 20, X borrowed in the firm's name a certain sum of money from R, who was ignorant of the dissolution. In such a case, Y also would be liable for the amount because no public notice was given.

2. Continuing Authority for Winding Up (Section 47):

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

(a) If it is necessary to wind up the affairs of the firm, and

(b) If it is necessary to complete the transactions started but not completed at the time of dissolution.

3. Partner's Right for Utilization of Assets (Section 46)

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

(a) He is entitled to have the property of the firm utilized in payment of its debts and liabilities.

(b) He is entitled to have the surplus distributed among all the partners according to their rights.

The surplus here means the surplus amount left after the payment of all the debts and liabilities of the firm.

4. Mode of Settlement of Accounts (Section 48):

After the dissolution of a firm, the accounts of the firm are settled according to the terms of partnership. If there is no specific agreement, then the accounts are settled according to the following fundamental rules contained in the Indian Partnership Act.

A. Payment of losses:

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

(a) First of all, the losses shall be paid out of the profits.

(b) If the profits, are not sufficient to pay the losses, then the balance of loss shall be paid out of capital, and

(c) If still some balance of losses remains, it shall be paid by the partners individually in the proportion in which they were entitled to share profits.

B. Utilization of assets:

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

(a) First of all, the assets shall be utilized in paying the debts of the firm to the third parties.

(b) If there is any surplus, the same shall be utilized in paying each partner the amount of loan advanced to the firm other than the capital. This is done in proportion to the advances made by the partners.

(c) If there is still any surplus, the same shall be utilized in paying each partner towards the amount of his capital. This is done in proportion to the amount of capital contributed by the partners.

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

SUMMARY

UNIT 1: NATURE OF PARTNERSHIP

INTRODUCTION

- ❖ It came into force on 1st October, 1932.
- ❖ Prior to the passing of the Act, the law of partnership was included in Chapter XI of the Indian Contract Act.
- ❖ Where the Partnership Act is silent on any point, the general principles of the law of contract apply. The partnership is a specialized branch of the Contract Act.

PARTNERSHIP (Section 4)

PARTNER& FIRM

ESSENTIAL ELEMENTS OF PARTNERSHIP

1. It is an association of two or more persons
2. There must be an agreement
3. There must be business.
4. Sharing of Profits
5. Business carried on by all or any of them acting for all

TRUE TEST OF PARTNERSHIP (Section 5 & 6)

DISTINCTION BETWEEN

1. Partnership and HUF
2. Partnership and Co-ownership
3. Partnership and Company
4. Partnership and Club/ Association

TYPES OF PARTNERSHIP

1. Partnership at will (Section 7)
2. Partnership for a fixed period
3. Particular Partnership
4. General Partnership

TYPES OF PARTNERS

1. Active/Actual Partner
2. Sleeping or Dormant Partner
3. Nominal Partner
4. Partner for profits only

5. Sub-Partner
6. Partner by Holding Out or by Estoppel (Section 28)
7. Incoming Partner
8. Outgoing Partner

- PARTNERSHIP DEED
- REGISTRATION OF FIRM (Section 58, 59, 59A-1, 69)

UNIT 2: Relation of Partners

- RIGHTS OF PARTNERS
- DUTIES OF PARTNERS

(Section 10,12,13,16)

- DETERMINATION OF RIGHTS AND DUTIES OF PARTNERS BY CONTRACT BETWEEN THE PARTNERS (Section 11)
- RIGHTS AND DUTIES OF PARTNERS AFTER A CHANGE IN THE FIRM (Section 17)
- PROPERTY OF THE FIRM (Section 14 & 15)
- AUTHORITY OF A PARTNER (Section 18 to 24)
- LIABILITY OF A FIRM AND ITS PARTNERS TO A THIRD PARTY (Section 25 to 27)
- TRANSFER OF A PARTNER'S INTEREST (Section 29)
- MINOR'S POSITION IN PARTNERSHIP FIRM (Section 30)
- RECONSTITUTION OF A FIRM

(1) Admission of a new partner (Section 31)
(2) Retirement of a partner (Section 32)
(3) Expulsion of a partner (Section 33)
Rights of Outgoing Partner (Section 36 &37)
(4) Insolvency of a partner. (Section 34)
(5) Death of a partner (Section 35)
(6) Revocation of continuing guarantee (Section 38)

UNIT 3: DISSOLUTION OF FIRM

DISSOLUTION OF PARTNERSHIP

DISSOLUTION OF FIRM (Section 39 to 44)

CONSEQUENCES OF DISSOLUTION (Section 45 to 55)

ICAI Module has not covered Section 50 to 55

LIST OF CASE LAWS

SR. NO.	NAME OF CASE LAW	PAGE NO. (This column is to be filled by students)
1.	*KD Kamath & Co.*	
2.	*Santiranjan Das Gupta Vs. Dasyran Murzamull (Supreme Court)*	

LIST OF LEGAL TERMS

SR. NO.	LEGAL WORD	MEANING	PAGE NUMBER (This column is to be filled by students)
1.	Cardinal Principle	Very important principle	
2.	Render	Give	
3.	To indemnify	To Compensate	
4.	Exclusively	Only	
5.	Admission/ Representation by a partner	Statement made by a partner	
6.	Bind the firm	Make the firm liable	
7.	Interest of the partnership	Advantageous to the firm	
8.	Opportunity of being heard	Opportunity to speak	
9.	Re-instatement in the firm	Taking back in the firm	
10.	Solicit the customers	directly asking potential customers to purchase goods or services, rather than using advertisements	

6. THE LIMITED LIABILITY PARTNERSHIP ACT, 2008

INTRODUCTION

1. The Parliament passed the Limited Liability Partnership Bill on 12th December, 2008. The President of India has assented the Bill on 7th January, 2009 and called as the Limited Liability Partnership Act, 2008.
   Many of its sections got enforced from 31st March 2009.
2. This Act have been enacted to make provisions for the formation and regulation of Limited Liability Partnerships and for matters connected with LLPs
3. The LLP Act, 2008 has 81 sections and 4 schedules.
4. The First Schedule deals with mutual rights and duties of partners, as well limited liability partnership and its partners where there is absence of formal agreement with respect to them.
5. The Second Schedule deals with conversion of a firm into LLP.
6. The Third Schedule deals with conversion of a private company into LLP.
7. The Fourth Schedule deals with conversion of unlisted public company into LLP.
8. The Ministry of Corporate Affairs (MCA) and the Registrar of Companies (ROC) are entrusted with the task of administrating the LLP Act, 2008. The Central Government has the authority to frame the Rules with regard to the LLP Act, 2008, and can amend them by notifications in the Official Gazette, from time to time.
9. Need of new form of Limited Liability Partnership:
   A need has been felt for a new corporate form that would provide an alternative to the traditional partnership with unlimited personal liability on the one hand and the statute-based governance structure of the limited liability company on the other hand, in order to enable professional expertise and entrepreneurial initiative to combine, organize and operate in flexible, innovative and efficient manner.
   It provides the benefits of limited liability but allows its members the flexibility of organizing their internal structure as a partnership based on a mutually arrived agreement. The LLP form enables entrepreneurs, professionals and enterprises providing services of any kind or engaged in scientific and technical disciplines, to form commercially efficient vehicles suited to their requirements.

LLP- MEANING & CONCEPT

1. A LLP is a new form of legal business entity with limited liability.
2. 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.
3. 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.
4. Limited liability partnership [Section 2(n)]: Limited Liability Partnership means a partnership formed and registered under this Act

SMALL LIMITED LIABILITY PARTNERSHIP [Section 2(ta)]

As per Section 2(ta), it means a limited liability partnership–

(i) the contribution of which, does not exceed ₹25,00,000 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 ₹40,00,000 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.

PARTNER

- **Types of Partners**

Designated Partner (Section 7)
- ➢ Can manage the business of LLP
- ➢ Legal Compliances

Normal Partner
- ➢ Can only manage the business of LLP

- Every LLP shall have at least two designated partners and at least one of them shall be a resident in India.
- Resident in India: For the purposes of this section, the term "resident in India" means a person who has stayed in India for a period of at least 120 days during the immediately preceding one year.

- **Who can be a partner?**

Individual (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–

- he has been found to be of unsound mind by a Court of competent jurisdiction and he is still is of unsound mind;
- he is an undischarged insolvent; or
- he has applied to be adjudicated (declared) as an insolvent and his application is pending; or
- He is a minor

Body Corporate [Section 2(1)(d)]

1. It means a company defined in section 2(20) of the Companies Act, 2013
2. Foreign Company
3. Indian LLP
4. Foreign LLP

but does not include—

- a corporation sole;
- a co-operative society registered under any law for the time being in force; and
- any other body corporate (not being a company as defined in section 2(20) 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.

At least two individuals who are partners of such LLP or nominees of such bodies corporate shall act as designated partners.

- **Number of partners** (Section 6)
  - Every LLP shall have at least two partners. Maximum: No limit
  - If at any time the number of partners of a LLP is reduced below 2 and the LLP carries on the business for more than 6 months while the number is so reduced, the person, who is the only partner of the LLP during the time that it so carries on business after those 6 months and has the knowledge of the fact that it is carrying on business with him alone, shall be liable personally for the obligations of the LLP.

NON-APPLICABILITY OF THE INDIAN PARTNERSHIP ACT, 1932 (SECTION 4)

Unless otherwise provided, the provisions of the Indian Partnership Act, 1932 shall not apply to a LLP.

INCORPORATION OF LLP

Step 1: LLP Name

1. 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. LLP shall not be registered by a name which, in the opinion of the Central Government is–
        1. undesirable; or
        2. 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.
2. Reservation of name (Section 16):
    1. A person has to 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 the name of a proposed LLP; or
    2. Upon receipt of an application and on payment of the prescribed fee, the Registrar may, if he is satisfied, reserve the name for a period of 3 months from the date of intimation by the Registrar.

Step 2: Incorporation Document (Section 11)

1. For a LLP to be incorporated:
    1. two or more persons associated for carrying on a lawful business with a view to profit shall subscribe their names to an incorporation document;
    2. 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
    3. Statement to be filed:
        1. Along with the incorporation document, a statement in the prescribed form shall also be filed,
            1. 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
            2. by anyone who subscribed his name to the incorporation document,
        2. that all the requirements of this Act and the rules made there under have been complied with,in respect of incorporation and matters related to it.

2. The incorporation document shall–
    1. be in a form as may be prescribed;
    2. state the name of the LLP;
    3. state the proposed business of the LLP;

4. state the address of the registered office of the LLP;
5. state the name and address of each of the persons who are to be partners of the LLP on incorporation;
6. state the name and address of the persons who are to be designated partners of the LLP on incorporation;
7. contain such other information concerning the proposed LLP as may be prescribed.

3. If a person makes a statement as discussed above which he knows to be false; or shall be punishable
   1. with imprisonment for a term which may extend to 2 years and
   2. with fine which shall not be less than ₹10,000 but which may extend to ₹5 Lakhs.

Step 3: Incorporation Registration (Section 12)

- When the requirements imposed by Section 11 have been complied with, the Registrar shall retain the incorporation document & accept the statement as mentioned above and, he shall, within a period of 14 days–
  - o register the incorporation document; and
  - o give a certificate that the LLP is incorporated by the name specified therein.
- The certificate issued 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.

Step 4: Effect of registration (Section 14)

1. On the incorporation of a LLP, the persons who subscribed their names to the incorporation document shall be its partners .
2. On registration, a limited liability partnership shall, by its name, be capable of-
   1) suing and being sued;
   2) acquiring, owning, holding and developing or disposing of property, whether movable or immovable, tangible or intangible;
   3) having a common seal, if it decides to have one; and
   4) doing and suffering such other acts and things as bodies corporate may lawfully do and suffer.

CHANGE OF NAME OF LLP (SECTION 17)

1. Where the Central Government is satisfied that a LLP has been registered (whether through inadvertence or otherwise and whether originally or by a change of name) under a name which –
   1. resembles the name of any other LLP or Company
   2. 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, the Central Government may direct that such limited liability partnership to change its name or new name within a period of 3 months from the date of issue of such direction.

2. But the above application of the proprietor of the registered trade marks shall be maintainable within a period of 3 years from the date of incorporation or registration or change of name of the limited liability partnership under this Act.

3. Where a LLP changes its name or obtains a new name, it shall within a period of 15 days from the date of such change, give notice of the change to Registrar along with the order of the Central Government, who shall carry out necessary changes in the certificate of incorporation and within 30 days of such change in the certificate of incorporation, such limited liability partnership shall change its name in the limited liability partnership agreement.

4. If the LLP is in default in complying with any direction given, 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.
However, LLP can change the name subsequently in accordance with the provisions of section 16.

DIFFERENCES WITH OTHER FORMS OF ORGANISATION

1. Distinction between LLP and Limited Liability Company (LLC)

	Basis	LLP	LLC
1.	Regulating Act	The LLP Act, 2008.	The Companies Act, 2013.
2.	Members / Partners	The persons who contribute to LLP are known as partners of the LLP.	The persons who invest the money in the shares are known as members of the company.
3.	Internal governance structure	The internal governance structure of a LLP is governed by agreement between the partners.	The internal governance structure of a company is regulated by statute (i.e., Companies Act, 2013).

4.	Name	Name of the LLP to contain the word "Limited liability partnership" or "LLP" as suffix.	Name of the public company to contain the word "limited" and Private company to contain the word "Private Limited'
5.	Number of members/ partners	Minimum - 2 members Maximum - No such limit on the members in the Act. The members of the LLP can be individuals /or body corporate through the nominees.	Private company: Minimum - 2 members Maximum - 200 members Public company: Minimum - 7 members Maximum - No such limit on the members.
6.	Liability of members/ partners	Liability of a partners is limited to the extent of agreed contribution except in case of wilful fraud.	Liability of a member is limited to the amount unpaid on the shares held by them.
7.	Management	The business of the company managed by the partners including the designated partners authorized in the agreement.	The affairs of the company are managed by board of directors elected shareholders.
8.	Minimum number of directors/ partners	Minimum 2 partners.	Private Co. - 2 directors Public Co. - 3 directors

SUMMARY

INTRODUCTION

- The Parliament passed the Limited Liability Partnership Bill on 12th December, 2008 and the President of India has assented the Bill on 7th January, 2009 and called as the Limited Liability Partnership Act, 2008, and many of its sections got enforced from 31st March 2009.
- The LLP Act, 2008 has 81 sections and 4 schedules.
- The First Schedule deals with mutual rights and duties of partners, as well limited liability partnership and its partners where there is absence of formal agreement with respect to them.
- The Second Schedule deals with conversion of a firm into LLP.
- The Third Schedule deals with conversion of a private company into LLP.
- The Fourth Schedule deals with conversion of unlisted public company into LLP.

LLP- MEANING & CONCEPT

CHARACTERISTICS OF LLP

SMALL LIMITED LIABILITY PARTNERSHIP [Section 2(ta)]

PARTNER

FOREIGN LLP

LLP AGREEMENT

FINANCIAL YEAR

NON-APPLICABILITY OF THE INDIAN PARTNERSHIP ACT, 1932

INCORPORATION OF LLP

Step 1: LLP Name

- Name (Section 15)
- Reservation of name (Section 16)

Step 2: Incorporation Document (Section 11)

Step 3: Incorporation Registration (Section 12)

Step 4: Effect of registration (Section 14)

REGISTERED OFFICE OF LLP AND CHANGE THEREIN (SECTION 13)

CHANGE OF NAME OF LLP (SECTION 17)

LIST OF LEGAL TERMS

SR. NO.	LEGAL WORD	MEANING	PAGE NUMBER (This column is to be filled by students)
1.	Hybrid	Mixture	
2.	Official Gazette	It is a periodical publication that has been authorised to publish public or legal notices.	
3.	Undischarged insolvent	Not declared as solvent	
4.	Conclusive evidence	Conclusive Evidence is evidence that cannot be contradicted by any other evidence. It is so strong as to overbear any other evidence to the contrary.	

7. THE COMPANIES ACT, 2013

INTRODUCTION

- The Companies Act, 2013 was enacted to consolidate and amend the law relating to the companies. The Companies Act, 2013 was preceded by the Companies Act, 1956.

- Due to changes in the national and international economic environment and to facilitate expansion and growth of our economy, the Central Government decided to replace the Companies Act, 1956 with a new law. The Companies Act, 2013 contains 470 sections and seven schedules. The entire Act has been divided into 29 chapters. The Companies Act, 2013 aims to improve corporate governance, simplify regulations, and strengthen the interests of minority investors. Thus, this enactment seeks to make our corporate regulations more contemporary

DEFINITION OF COMPANY

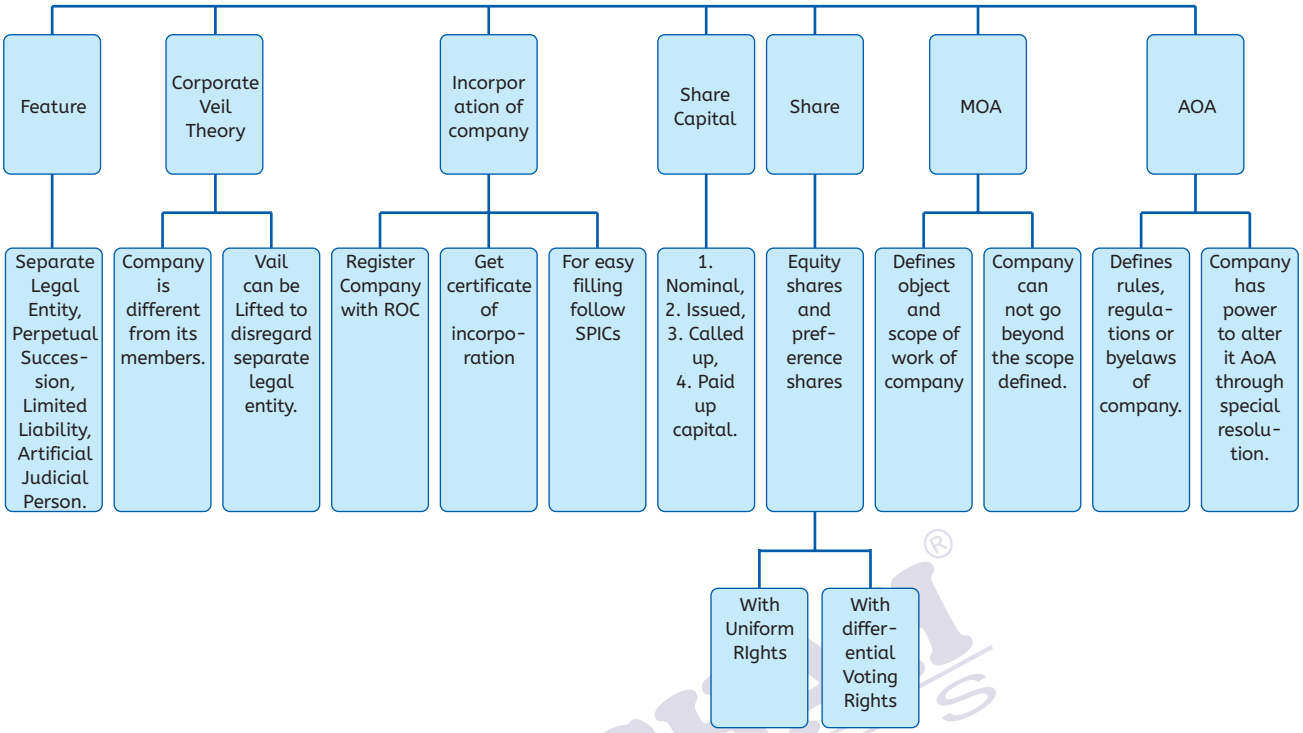
The term 'company' has been defined under Section 2(20) of the Companies Act, 2013. As per this, 'company' means a company incorporated under Companies Act, 2013 or under any of the previous laws relating to companies.

ACT APPLICABLE TO:

The provisions of this Act shall apply to-

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

OVERVIEW OF CHAPTER



CHARACTERISTICS OF COMPANY

Following are the characteristics of a company:

1. Separate legal entity: A company is an artificial person having a personality which is distinct from the members constituting it. Thus, a company has got an entity which is separate from its members. And since this separate entity concept is conferred by law, it is said that a company has got a separate legal entity.

Case law: *Macaura vs. Northern Assurance Co. Ltd.*

M was the holder of nearly all the shares except one of a timber company. He was also a substantial creditor of the company. He insured the company's timber in his own name. The timber was destroyed by fire & M claimed the loss from Insurance Company.

Held that, the Insurance Company was not liable to him. A shareholder cannot insure the company's property in his own name even if he is the owner of all or most of the company's shares.

2. Perpetual Succession: An incorporated company never dies. Perpetual succession, therefore, means that the membership of a company may keep changing from time to time but does not affect its continuity. Members may come and go but the company will continue forever.

3. Limited liability: A company limited by shares is a registered company having the liability of its members limited to the amount, if any, unpaid on the shares respectively held by them. If his shares are fully paid - up, he has nothing more to pay.
   (i) Thus, in the case of a limited liability company, the debts of the company in totality do not become the debts of the shareholders. The liability of the members of the company is limited to the extent of the nominal value of shares held by them. In no case can the shareholders be asked to pay anything more than the unpaid value of their shares.
   (ii) 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.
   (iii) However, if it is an unlimited company, the liability of its members is unlimited as well.

4. Artificial Legal Person:
   1) A company is an artificial person as it is created by a process other than natural birth, it is created by law. It is a person since it is clothed with all the rights of an individual.
   2) 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.
   3) As the company is an artificial person, it can act only through some human agency, i.e., directors. The directors can either act on their own or through the common seal (of the company) can authenticate its formal acts.

5. Common Seal: Since a company has no physical existence, it must act through its agents. All the important documents of a company must be under the seal of the company. The common seal, thus, acts as the official signature of a company.
   The Companies (Amendment) Act, 2015 has made the common seal optional. Reason for this amendment is that common seal is considered as an old concept now. This amendment provides that, now common seal is optional. The documents which need to be authenticated by a common seal will be required to be so done, only if the company opts to have a common seal. In case a company does not have a common seal, the authorization shall be made by two directors or by a director and the Company Secretary, wherever the company has appointed a Company Secretary.

IS COMPANY A CITIZEN?

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

DOES A COMPANY HAVE NATIONALITY AND RESIDENCE?

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

LIFTING OR PIERCING THE CORPORATE VEIL

Corporate veil: 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 protected 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. Thus, the shareholders are protected from the acts of the company.

Effect of corporate veil: Only company is liable for the acts/defaults done in name of company, even though directors/employees acted on behalf of company.

Case law: *Salomon v. Salomon & Co. Ltd.*

Salomon had, for some years, carried on a prosperous business as a leather merchant and boot manufacturer. He formed a limited company consisting of himself, his wife and a daughter, and his 4 sons as the shareholders, all of whom subscribed for one share of 1 pound each. Salomon was the managing director and two of his sons were other directors.

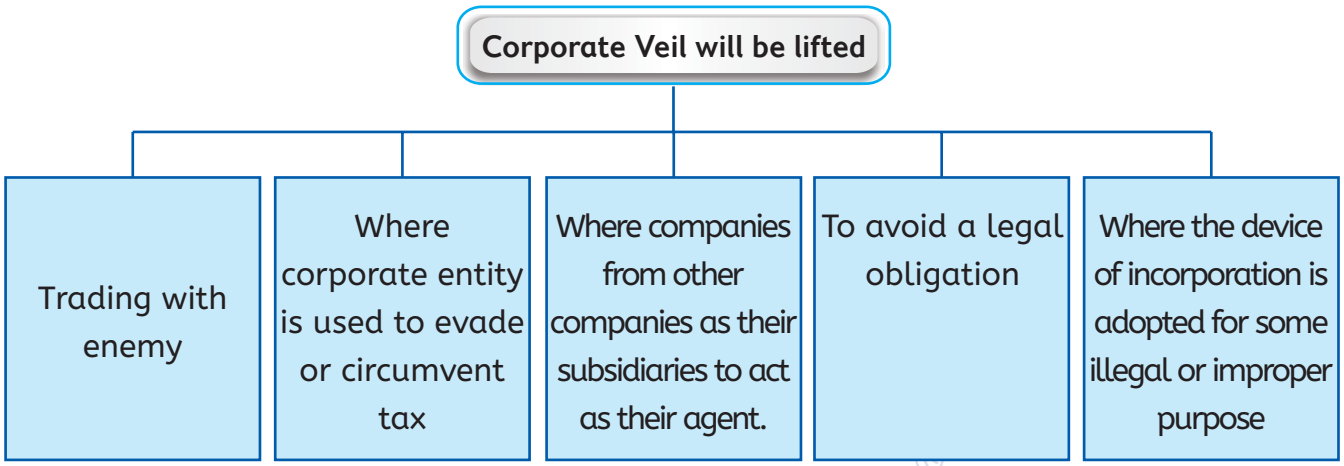
Salomon sold his business (which was perfectly solvent at that time) to the Company for the sum of 38,782 £. He got the following consideration:-

10,000	Secured Debentures of 1£ each
20,000	Fully - paid Shares of 1 £ each
8,782	Cash

The company soon ran into difficulties and the debenture holders appointed a receiver and the company went into liquidation. The total assets of the company amounted to 6,050£, its liabilities were 10,000£ secured debentures and 8,000£ owing to unsecured trade creditors. The unsecured trade creditors claimed the whole of the company's assets, viz. 6,050 £ on the ground that as the company was a mere agent for Salomon and thus they were entitled to payment of their debts in priority to debentures.

The House of Lords rejected these contentions and held that a company, on registration, has its own existence or personality separate and distinct from its members and, as a result, a shareholder cannot be equated with a company, even if he holds virtually the entire share capital of the company.

Lifting of corporate veil: It means looking behind the company as a legal person, i.e., disregarding the corporate entity. The court will lift the corporate veil and treat company and member as same. Only in appropriate circumstances, the Courts shall lift the corporate veil.



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

1. Where the device of incorporation is adopted for some illegal or improper purpose, e.g., to defeat or circumvent law, to defraud creditors or to avoid legal obligations.

Case law: *Gilford Motor Co. v. Horne*

Mr. Horne, a past employee of Gilford Motors company was conditioned not to start a similar business with that of the company. So, he formed a company to carry on his business and started doing similar business. An injunction order was granted against him and the company to stop them.

2. For determining residence and character : The Courts also look behind the facade of the company and its place of registration in order to determine its residence for the purposes of taxation or the character of the company, for example whether it is enemy.

Case law: *Daimler Co. Ltd. vs. Continental Tyre & Rubber Co.*

C company was floated in London for marketing tyres manufactured in Germany. The majority of the C's shares were held by German nationals residing in Germany. During World War I, C Company filed a suit against D company for the recovery of trade debt. The D company contented that C company was an alien enemy company (Germany being at war with England at that time) and that the payment of the debt would be trading with the enemy. The court agreed with the contention of the defendants.

3. Formation of Companies to divide income and avoid tax or avoid any welfare laws:

Case law: *Sir Dinshaw Maneckjee Petit*

D was a rich man having dividend and interest income. He wanted to avoid income-tax. For this purpose, he formed four private companies, in all of which he was the majority share holder. The companies made investments and whenever interest and dividend income were received by the companies, D applied to the companies for loans, which were immediately granted and he never repaid. In a legal proceeding the corporate veil of all the companies were lifted and the income of the companies treated as if they were of 'D'.

4. 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

Case law: *Workmen employed in Associated Rubber Industries Ltd v. Associated Rubber Industries Ltd*

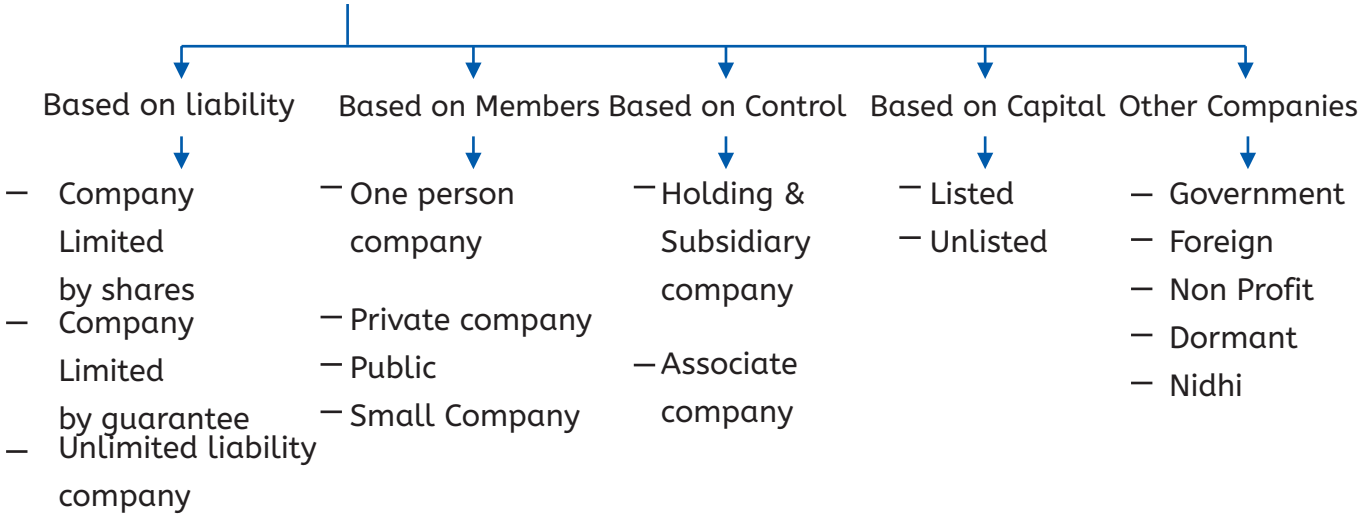
A subsidiary company was formed wholly by the holding company with no assets of its own except those transferred to it by the holding company, with no business or income of its own except receiving dividend from shares transferred to it by the holding company. Court held that the new company was formed as a device to reduce the profits of the holding company and thereby reduce the bonus to workmen.

5. Where companies form other companies as their subsidiaries to act as their agent:
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. Here the principal will be held liable for the acts of that company.

Case law: *Merchandise Transport Limited vs. British Transport Commission (1982)*

Transport Company wanted to obtain licences for its vehicles, but could not do so if applied in its own name. It, therefore, formed a subsidiary company, and the application for licence was made in the name of the subsidiary. The vehicles were to be transferred to the subsidiary company. Held, the parent and the subsidiary were one commercial unit and the application for licences was rejected.

CLASSIFICATION OF COMPANY



A. BASED ON LIABILTY

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

2. **Company limited by guarantee:**
   - As per Section 2(21), a company limited by guarantee or a "guarantee company" is a company having the liability of its members limited to such an amount as the members may respectively thereby undertake, by the memorandum of association of the company, to contribute to the assets of the company.
   - A special feature of this type of company is that the liability of members to pay their guaranteed amounts arises only when the company has gone into liquidation and not when it is a going concern.
   - Clubs, trade associations and societies for promoting different objects are examples of companies limited by guarantee.
   - The point of distinction between these two types of companies is that in the company limited by guarantee, the members may be called upon to discharge their liability only after commencement of the winding up and only subject to certain conditions; but in company limited by shares, they may be called upon to do so at any time, either during the company's life-time or during its winding up.

Case law: In *Narendra Kumar Agarwal vs. Saroj Maloo*, the Supreme court has laid down that the right of a guarantee company to refuse to accept the transfer by a member of his interest in the company is on a different footing than that of a company limited by shares. The membership of a guarantee company may carry privileges much different from those of ordinary shareholders.

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

B. BASED ON MEMBERS

1. Private Company:
   - As per Section 2(68), private company is a company which by its articles,–
     (i) Restricts the right to transfer its shares;
     (ii) Limits the number of its members to 200 (except in case of One Person Company):
     The clause provides that where two or more persons hold one or more shares in a company jointly, they shall be treated as a single member:
     However following shall not be included in the number of members:
     persons who are in the employment of the company; and persons who, having been in the employment of the company in the past and they are still members of the company
     (iii) Prohibits any invitation to the public to subscribe for any securities of the company.
   - There should be at least two persons to form a private company i.e., the minimum no. of members in a private company is two. A private company should have at least two directors. The name of a private limited company must end with the words "Private Limited".

2. Public Company:
   - As per Section 2(71), public company is a company which-
     - is not a private company and
     - has a minimum share capital as prescribed.
     - Seven or more members are required to form the company.
     - a private company which is a subsidiary of a public company shall also be deemed to be a public company for the purposes of this Act, even where such subsidiary company continues to be a private company in its articles (three restrictions).

- There should be at least seven persons to form a public company i.e., the minimum no. of members in a public company is seven. A public company should have at least 3 directors. The name of a public limited company must end with the word "Limited".

3. One Person Company:

- Definition: As per Section 2(62),one person company is a company which-
  One Person Company' means a company which has only one person as a member.
  It is basically a private company with some unique features.
  As regards the name of a One Person Company, the Act provides that the words "One Person Company" or 'OPC' shall be mentioned in brackets below the name of such Company, wherever its name is printed, affixed or engraved.

- Law with respect to formation of OPC provides that–
  - ✓ The memorandum of OPC shall indicate the name of the other person, who shall, in the event of the subscriber's death or his incapacity to contract, become the member of the company.
  - ✓ The other person whose name is given in the memorandum shall give his prior written consent in prescribed form and the same shall be filed with Registrar of companies at the time of incorporation.
  - ✓ Such other person may be given the right to withdraw his consent.
  - ✓ The member of OPC may at any time change the name of such other person by giving notice to the company and the company shall intimate the same to the Registrar.
  - ✓ Any such change in the name of the person shall not be deemed to be an alteration of the memorandum.
  - ✓ Only a natural person who is an Indian citizen and whether resident in India or otherwise (person who has stayed in India for a period of not less than 120 days during the immediately preceding one financial year)-
    a) Shall be eligible to incorporate a OPC;
    b) Shall be a nominee for the sole member of a OPC.

- ✓ A natural person shall not be a member of more than a OPC at any point of time and the said person shall not be a nominee of more than a OPC.
- ✓ No minor shall become member or nominee of the OPC or can hold share with beneficial interest.

  Example 1: Rajesh has formed a 'One Person Company (OPC)' with his wife Roopali as nominee. For the last two years, his wife Roopali is suffering from terminal illness and due to this hard fact he wants to change her as nominee. He has a trusted and experienced friend Ramnivas who could be made nominee or his (Rajesh) son Rakshak who is of seventeen years of age. In the instant case, Rajesh can appoint his friend Ramnivas as nominee in his OPC and not Rakshak because Rakshak is a minor.
- ✓ 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. The procedure of conversion is given in the rules 6 & 7 of the Chapter II.
- ✓ Such Company cannot carry out Non-Banking Financial Investment activities including investment in securities of anybody corporate.

4. Small Company:
   - Definition: As per Section 2(85),small company means a company, other than a public company, -
     (i) Paid-up share capital of which does not exceed 4 crore rupees or such higher amount as may be prescribed which shall not be more than ten crore rupees;

     and

     (ii) Turnover of which as per as per profit and loss account for the immediately preceding financial year does not exceed 40 crore rupees or such higher amount as may be prescribed which shall not be more than one hundred crore rupees.

   - Provided that nothing in this clause shall apply to-
     (i) a holding company or a subsidiary company;
     (ii) a company registered under section 8; or
     (iii) a company or body corporate governed by any special Act.

     It is basically a private company meeting prescribed threshold.

C. BASED ON CONTROL

1. Holding & Subsidiary Company

- As per Section 2(87) provides that a company shall be a subsidiary of another, if any of the following conditions are satisfied :-
  (a) That other controls the composition of its Board of Directors;
  (b) That other exercises or-controls more than one-half of the total voting power either on its own or together with one or more of its subsidiary companies; or
  (c) The first-mentioned company is a subsidiary of any company which is that other's subsidiary.

  Provided that such class or classes of holding companies as may be prescribed shall not have layers of subsidiaries beyond such numbers as may be prescribed.
- For the purpose of clause (a) above, the control of the composition of the Board of directors of a company means that the holding company has power, at its discretion, to appoint or remove all or majority of the directors of the subsidiary company without the consent of the other persons.
- It should be noted that holding and subsidiary companies are incorporated companies and each is a separate legal entity.
- For the purpose of this clause, the term 'company' includes anybody corporate. Thus, holding and subsidiary relationship can be established between an Indian Company and a Foreign Company.
- As per Section 2(46), 'Holding Company', in relation to one or more other companies, means a company of which such companies are subsidiary companies.
- Provided that such class or classes of holding companies as may be prescribed shall not have layers of subsidiaries beyond such numbers as may be prescribed.
- Example 1: A will be subsidiary of B, if B controls the composition of the Board of Directors of A, i.e., if B can, without the consent or approval of any other person, appoint or remove a majority of directors of A.

  Example 2: A will be subsidiary of B, if B holds more than 50% of the share capital of A.

  Example 3: B is a subsidiary of A and C is a subsidiary of B. In such a case, C will be the subsidiary of A.

2. Associate company

- As per Section 2(6), In relation to another company, means a company in which that other company has a significant influence, but which is not a subsidiary company of the company having such influence and includes a joint venture company.

- The term "significant influence" means control of at least 20% of total share capital, or of business decisions under an agreement
- The term "Total Share Capital", means the aggregate of the - paid-up equity share capital; and convertible preference share capital.
- This is a new definition inserted in the 2013 Act.

D. BASED ON CAPITAL

1. Listed company:

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

Provided that such class of companies, which are listed or intend to list such class of securities as may be prescribed in consultation with Securities and Exchange Board of India, shall not be considered as listed company

2. Unlisted company:

Means a company other than listed company.

E. OTHER COMPANIES

1. Government Company

- As per Section 2(45), government company means any company in which not less than fifty- one per cent. of the paid-up share capital is held by-
  (i) the Central Government, or
  (ii) by any State Government or Governments, or
  (iii) partly by the Central Government and partly by one or more State Governments,
- And the section includes a company which is a subsidiary company of such a Government company
- "Paid-up share capital" shall be construed as "total voting power", where shares with differential voting rights have been issued.

2. Foreign Company

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

(i) Has a place of business in India whether by itself or through an agent, physically or through electronic mode; and

(ii) Conducts any business activity in India in any other manner

3. Company not for profit/Non-Profit companies

- Object of formation of Section 8 Company: Section 8 of the Companies Act, 2013 deals with the formation of companies which are formed to promote the charitable objects of commerce, art, science, sports, education, research, social welfare, religion, charity, protection of environment etc.

- Examples of section 8 companies are FICCI, ASSOCHAM, National Sports Club of India, CII etc.

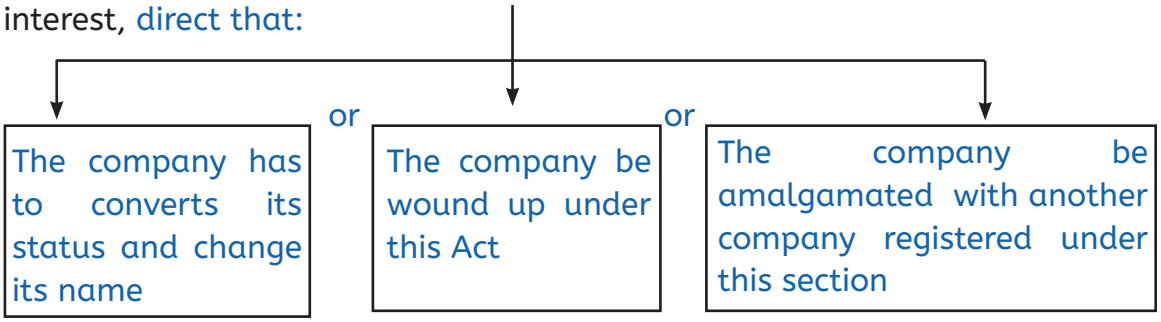
- Restrictions on such company:
  (i) Such company is prohibited from declaring any dividend to its members
  (ii) Such company has to apply its surplus only in promoting its objects

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

- Privileges of Limited Company: On registration the company shall enjoy same privileges and obligations as of a limited company.

- Revocation of license:
  - ✓ The Central Government may by order revoke the licence of the company where the company contravenes any of the requirements or the conditions of this sections subject to which a licence is issued or where the affairs of the company are conducted fraudulently, or violative of the objects of the company or prejudicial to public interest, and on revocation the Registrar shall put 'Limited' or 'Private Limited' against the company's name in the register.
  - ✓ But before such revocation, the Central Government must give it a written notice of its intention to revoke the licence and opportunity to be heard in the matter.
  - ✓ Such order shall be made only after the company is given a reasonable opportunity of being heard.

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



- Penalty/ punishment in contravention: If a company makes any default in complying with any of the requirements laid down in this section,
  the company shall, be punishable with
  Fine: Minimum 10 lakhs upto 1 crore
  and
  The directors and every officer of the company who is in default shall be punishable with:
  Fine: Minimum 25000 upto 25 lakhs rupees,
  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.

4. Dormant company (Section 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.

- "Significant accounting transaction" means any transaction other than–
  (i) payment of fees by a company to the Registrar;
  (ii) payments made by it to fulfil the requirements of this Act or any other law;
  (iii) allotment of shares to fulfil the requirements of this Act; and
  (iv) Payments for maintenance of its office and records.

5. Nidhi Company:

As per section 406(1) 'Nidhi or Mutual Benefit Society' means a company which the Central Government may, by notification in Official Gazette declare to be a 'Nidhi or Mutual Benefit Society.'

6. Public financial institutions

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

(i) The Life Insurance Corporation of India, established under the Life Insurance Corporation Act, 1956;
(ii) The Infrastructure Development Finance Company Limited,

(iii) Specified company referred to in the Unit Trust of India (Transfer of Undertaking and Repeal) Act, 2002;

(iv) Institutions notified by the Central Government under section 4A(2) of the Companies Act, 1956 so repealed under section 465 of this Act;

(v) Such other institution as may be notified by the Central Government in consultation with the Reserve Bank of India:

Provided that no institution shall be so notified unless–

(A) it has been established or constituted by or under any Central or State Act other than this Act or the previous company law; or

(B) 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

MODE OF REGISTRATION/ INCORPORATION OF COMPANY

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

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

(a) Who has been named as such in a prospectus or is identified by the company in the annual return referred to in section 92; or

(b) Who has control over the affairs of the company, directly or indirectly whether as a shareholder, director or otherwise; or

(c) In accordance with whose advice, directions or instructions the Board of Directors of the company is accustomed to act.

INCORPORATION OF COMPANIES (SECTION 7)

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

I. Selection of the type of company: The promoters of a company may however select the type of a company as they wish to form themselves into viz, One person company, private company, public company, non-profit company, etc.

II. Preliminary Requirements:

All the directors of the proposed company must ensure that they are having Director's Identification Number (DIN). Out of all the directors of the proposed company, atleast one director should have digital signature to digitally sign the incorporation and other related documents.

III. Reservation of Name:

Any of the promoters should apply to the Registrar of Companies (ROC) regarding the reservation of name.

IV. Preparation of the Memorandum of Association and Articles of Association:

Drafting of the MOA and AOA is generally a step subsequent to the reservation of name made by the Registrar. These two documents are basically the charter and internal rules and regulations of the company. Therefore, it must be drafted with utmost care and with the advice of the experts and the ancillary clause for attainment of the main object clause should be drafted in a very broader sense.

V. Filing of the documents with the Registrar of Companies:

An application shall be filed, with the Registrar of Companies within whose jurisdiction the registered office of the company is proposed to be situated.

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.

1. The memorandum and articles of the company duly signed by all the subscribers to the memorandum.

2. 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.

3. 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 5 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;

4. The address for correspondence till its registered office is established;

5. 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.

6. 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

7. 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.

   - Maintenance of copies of all documents and information: The company shall maintain and preserve at its registered office copies of all documents and information as originally filed, till its dissolution under this Act.

VI. Certificate of Incorporation and allotment of Corporate Identity Number: If the Registrar of Companies is satisfied that everything has been complied with in regard to incorporation of companies, he shall issue a certificate of incorporation in to the company signed & dated under his hand.

VII. Effect of Registration [Sec. 9]:

- Section 9 provides that from the date of incorporation, the subscribers become the members of the company. The company shall be a body corporate with a name, capable of exercising all the functions of an incorporated company under this Act and shall have perpetual succession with power to acquire, hold and dispose of property, to contract, to sue and be sued, by the said name.

- From the date of incorporation mentioned in the certificate, the company becomes a legal person separate from the incorporators; and there comes into existence a binding contract between the company and its members as evidenced by the Memorandum and Articles of Association

- It may be noted that under the provisions of the Act, a company may purchase shares of another company and thus become a controlling company. However, merely because a company purchases all shares of another company it will not end the corporate character of another company and each company is a separate juristic entity.

EFFECT OF FURNISHING OF FALSE OR INCORRECT INFORMATION OR SUPPRESSION OF MATERIAL FACT

Furnishing of false or incorrect information or suppression of material factat the time of incorporation (i.e. at the time of incorporation process)

↓

If any person furnishes any false or incorrect particulars of any information or suppresses any material information, of which he is aware in any of the documents filed with the Registrar in relation to the registration of a company, he shall be liable for action for fraud under section 447.

Furnishing of false or incorrect information or suppression of material factor representation or by suppressing any material fact (i.e. post incorporation)

↓

1. The promoters, the persons named as the first directors of the company and the persons making declaration under this section shall each be liable for action for fraud under section 447.

2. Order of the Tribunal:

The Tribunal may, on an application made to it, on being satisfied that the situation so warrants–

(i) Pass such orders, as it may think fit, for regulation of the management of the company including changes, if any, in its memorandum and articles, in public interest or in the interest of the company and its members and creditors; or

(ii) Direct that liability of the members shall be unlimited; or

(iii) Direct removal of the name of the company from the register of companies; or

(iv) Pass an order for the winding up of the company; or

(v) Pass such other orders as it may deem fit:

Provided that before making any order,–

(i) The company shall be given a reasonable opportunity of being heard in the matter; and

(ii) The Tribunal shall take into consideration the transactions entered into by the company, including the obligations, if any, contracted or payment of any liability.

SIMPLIFIED PROFORMA FOR INCORPORATING COMPANY ELECTRONICALLY (SPICe)

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

MEMORANDUM OF ASSOCIATION

Meaning:	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 base of the company is built.
Object of registering a Memorandum of Association:	1. 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. 2. It enables shareholders, creditors and all those who deal with company to know what its powers are and what activities it can engage in. A memorandum is a public document under Section 399 of the Companies Act, 2013. Consequently, every person entering into a contract with the company is presumed to have the knowledge of the conditions contained therein. 3. 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. 4. A company cannot go beyond the provisions contained in the memorandum however necessary it might be. It cannot enter into a contract or engage in any trade or business, which is beyond the power confessed on it by the memorandum. If it does so, it would be ultra vires (i.e. beyond the powers)the company and void.
Form of Memorandum [Section 4]:	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 applicable to companies limited by shares; ➢ Table B is applicable to companies limited by guarantee and not having a share capital; ➢ Table C is applicable to the companies limited by guarantee and having a share capital;

	➢ Table D is applicable to unlimited companies and not having a share capital; ➢ Table E is applicable to unlimited companies and having a share capital.
Contents of the Memorandum:	
1. Name clause	➢ The first clause in the memorandum must state the name by which a company is known. ➢ The name of the company with the last word "Limited" in the case of a public limited company, or the last words "Private Limited" in the case of a private limited company. This clause is not applicable on the companies formed under section 8 of the Act. ➢ The name including phrase 'Electoral Trust' may be allowed for Registration of companies to be formed under section 8 of the Act, in accordance with the Electoral Trusts Scheme, 2013 notified by the Central Board of Direct Taxes (CBDT). For the Companies under section 8 of the Act, the name shall include the words foundation, Forum, Association, Federation, Chambers, Confederation, council, Electoral trust, etc.
2. Situation or registered office clause	The name of the State in which the registered office of the company is to be situated must be given in the memorandum. But the exact address of the registered office is not required to be stated therein.
3. Object clause	➢ The objects for which the company is proposed to be incorporated and any matter considered necessary in furtherance thereof; ➢ If any company has changed its activities which are not reflected in its name, it shall change its name in line with its activities within a period of six months from the change of activities after complying with all the provisions as applicable to change of name.
4. LiabilityClause:	The liability of members of the company, 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–

	➢ 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 or of such debts and liabilities as may have been contracted before he ceases to be a member, as the case maybe; and ➢ to the costs, charges and expenses of winding-up and for adjustment of the rights of the contributories among themselves;
5. Capital Clause (only in the case of a company having a share capital):	The amount of authorized capital divided into share of fixed amounts and the number of shares with the subscribers to the Memorandum has agreed to take, indicated opposite their names, which shall not be less than one share. A company not having share capital need not have this clause.
6. Association Subscription Clause	In this clause, the persons (includes a body corporate) subscribing to the memorandum declare their desire to be formed into a company and agree to take the shares indicated opposite their respective names. Following are the statutory requirements regarding subscription of memorandum:- (i) The memorandum must be signed by each subscriber in the presence of at least one witness who must attest the signatures; (ii) Each subscriber must take at least one share; if any and (iii) Each subscriber must write opposite his name the number of shares (if any) which he agrees to take.
7. Succession Clause (only in the case of OPC):	This clause shall state the name of the person who, in the event of the death of the subscriber, shall become the member of the company.

- The 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.

- It is to be noted that a company being a legal person can through its agent, subscribe to the memorandum. However, a minor cannot be a signatory to the memorandum as he is not competent to contract. The guardian of a minor, who subscribes to the memorandum on his behalf, will be deemed to have subscribed in his personal capacity.

- The Memorandum of Association of a company cannot contain anything contrary to the provisions of the Companies Act. If it does, the same shall be devoid of any legal effect. Similarly, all other documents of the company must comply with the provisions of the Memorandum

ARTICLES OF ASSOCIATION

Meaning:	➢ The articles of association of a company are its rules and regulations, which are framed to manage its internal affairs. 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 ➢ These general functions of the articles have been aptly summed up by Lord Cairns as follows: "The articles play a part subsidiary to memorandum of association. They accept the memorandum as the charter of incorporation. ➢ The document containing the articles of association of a company (the Magna Carta) is a business document; hence it has to be construed strictly. It regulates domestic management of a company and creates certain rights and obligations between the members and the company. ➢ The articles of association are in fact the bye-laws 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.
Contents and model of articles of association. (Section 5)	(1) Contains regulations: The articles of a company shall contain the regulations for management of the company. (2) Inclusion of matters: The articles shall also contain such matters, as are prescribed under the rules. However, a company may also include such additional matters in its articles as may be considered necessary for its management. (3) Entrenchment Provision: A new provision on entrenchment has been provided under the Companies Act, 2013 which provides that articles may contain provision for entrenchment. Entrenchment provision is an additional restriction which the company has to fulfill apart from passing special Resolution for altering articles of association.

	Such provision for entrenchment in the articles can be made either at the time of formation of a company, or by an amendment in the articles agreed to by all the members of the company in the case of a private company and by a special resolution in the case of a public company. It is further provided that the company shall give notice to the ROC of entrenchment provisions in the prescribed form. (4) 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. (5) Model articles: A company may adopt all or any of the regulations contained in the model articles applicable to such company. A company may adopt all or any of the regulations of the aforesaid Model Articles. If duly registered articles of a company do not expressly exclude or modify the regulations contained in applicable model articles, such regulations shall apply as if they were contained in the duly registered articles of a company.

DIFFERENCES BETWEEN THE MEMORANDUM OF ASSOCIATION VS.ARTICLES OF ASSOCIATION:

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

1. Objectives: Memorandum of Association defines and delimits the objectives of the company whereas the Articles of association lays down the rules and regulations for the internal management of the company. Articles determine how the objectives of the company are to be achieved.

2. Relationship: Memorandum defines the relationship of the company with the outside world and Articles define the relationship between the company and its members.

3. Alteration: Memorandum of association can be altered only under certain circumstances and in the manner provided for in the Act. In most cases permission of the Regional Director or the Tribunal is required. The articles can be altered simply by passing a special resolution.

4. Ultra Vires: Acts done by the company beyond the scope of the memorandum are ultra-vires and void. These cannot be ratified even by the unanimous consent of all the shareholders. The acts ultra-vires the articles can be ratified by a special resolution of the shareholders provided they are not beyond the provisions of the memorandum.

EFFECT OF MEMORANDUM AND ARTICLES

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

DOCTRINE OF ULTRA VIRES

- The meaning of the term 'ultra vires' is 'beyond the powers of. Anything which is outside the specified objects and powers of the object clause of memorandum of association is ultra vires the company and therefore is null and void.

- An act which is ultra vires memorandum, the company cannot ratify even by the unanimous consent of all the shareholders.

- No rights and liabilities, on the part of the company, arise out of such transactions and it remains nullity even if every member assent to it.

- Consequently, an act, which is ultra vires the company, does not bind the company and neither the company nor the other contracting party can sue on it.

- But an act which is ultra vires the powers of directors, but intravires (i.e. within the powers) Memorandum can be ratified by the members of the company through a resolution passed at a general meeting.

- Similarly if an act is ultra vires the Articles but intravires Memorandum, can be ratified by altering the Articles by a Special Resolution at a general

Case law: *Ashbury Railway Carriage and Iron Company Limited v. Riche*-(1875).

The facts of the case are:

The main objects of a company were:

(a) To make, sell or lend on hire, railway carriages and wagons;

(b) To carry on the business of mechanical engineers and general contractors.

(c) To purchase, lease, sell and work mines.

(d) To purchase and sell as merchants or agents, coal, timber, metals etc.

The directors of the company entered into a contract with Riche, for financing the construction of a railway line in Belgium, and the company further ratified this act of the directors by passing a special resolution. The company however, repudiated the contract as being ultra-vires. And Riche brought an action for damages for breach of contract. His contention was that the contract was well within the meaning of the word general contractors and hence within its powers. Moreover it had been ratified by a majority of shareholders.

However, it was held by the Court that the contract was null and void. It said that the terms 'general contractors' was associated with mechanical engineers, i.e. it had to be read in connection with the company's main business. If, the term general contractors' was not so interpreted, it would authorize the making of contracts of any kind.

DOCTRINE OF CONSTRUCTIVE NOTICE

- Section 399 of the Companies Act, 2013 provides that any person can inspect by electronic means any document kept by the Registrar, or make a record of the same, or get a copy or extracts of any document, including certificate of incorporation of any company, on payment of prescribed fees.

  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 nominal fees. So, Section 399 gives the 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 with the company is within the company's Memorandum.

- Whether a person reads them or not, it will be presumed that he knows the contents of the documents. Hence, every person dealing with the company is under an obligation to know the contents of these documents.

- Whether a person reads the documents or not, he is presumed to have knowledge of the contents of the documents. He is not only presumed to have read the documents but also understood them in their true perspective,

- Thus, if a person enters into a contract which is beyond the powers of the company as defined in the memorandum, or outside the memorandum, he cannot acquire any rights under the contract against the company.

- The doctrine of "constructive notice" seeks to protect the company against the outsiders.

DOCTRINE OF INDOOR MANAGEMENT

- While persons dealing with a company are presumed to have read the public documents and understood their contents and ascertain that the transaction is not inconsistent therewith, they are entitled to assume that the PROVISIONS of the articles have been observed by the officers of the company. It is no part of the duty of an outsider to see how the company carries out its own internal proceedings or indoor management. He can assume that all is being done regularly.

- The doctrine of indoor management, thus, imposes an important restriction on the scope of doctrine of constructive "notice. While the doctrine of "constructive notice" seeks to protect the company against the outsiders, the principle of indoor management operates to protect the outsiders against the company.

Case law: *The Royal British Bank vs. Turquand*

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 units 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.

➢ Exceptions: The doctrine of indoor management is subject to the following exceptions or limitations:-

1. Actual or constructive knowledge of irregularity: The rule does not protect any person when the person dealing with the company has notice, whether actual or constructive, of the irregularity.

Case law: 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.

Case law: 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.

2. Suspicion of Irregularity: Where the person dealing with the company is put upon an inquiry, for example, where the transaction is unusual or nothing the ordinary course of business, it is the duty of the outsider to make the necessary enquiry.
The protection of the "Turquand Rule" is also not available where the circumstances surrounding the contract are suspicious and therefore invite inquiry. Suspicion should arise, for example, from the fact that an officer is purporting to act in matter, which is apparently outside the scope of his authority.

Case law: In Anand Bihari Lal vs. Dinshaw & Co. the plaintiff accepted a transferor 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.

Case law: Similarly, in Haughton & Co. v. Nothard, Lowe & Wills Ltd. where a person holding directorship in two companies agreed to apply the money of one company in payment of the debt to other, the court said that it was something so unusual "that the plaintiff were put upon inquiry to ascertain whether the persons making the contract had any authority in fact to make it" Any other rule would "place limited companies without any sufficient reasons for so doing, at the mercy of any servant or agent who should purport to contract on their behalf"

3. Forgery: The doctrine of indoor management applies only to irregularities which might otherwise affect a transaction but it cannot apply to forgery which must be regarded as nullity.
Forgery may in circumstances exclude the 'Turquand Rule'.

Case law: In Ruben v Great Fingall Consolidated, 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.

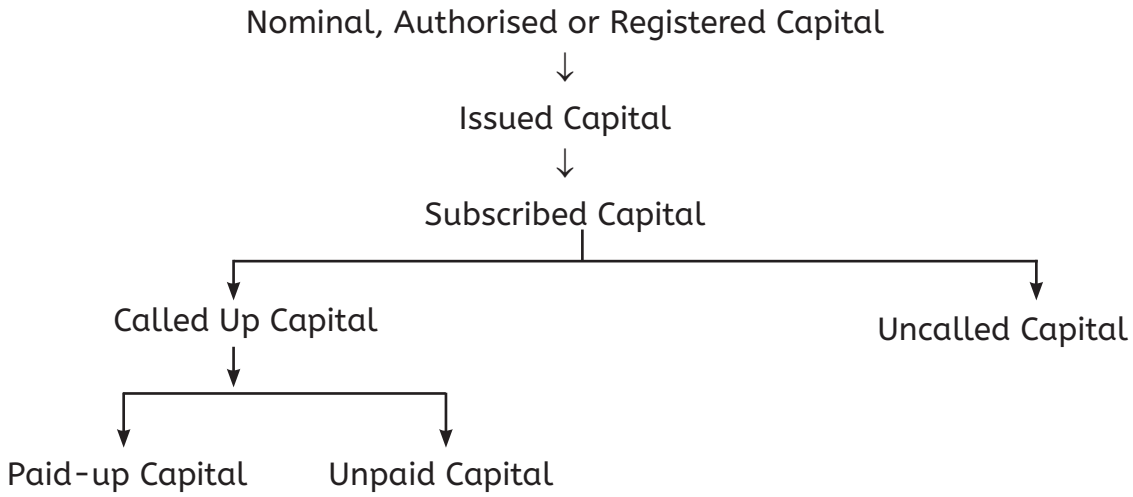
SHARE

- Definition and Meaning of Share: Section 2(84) of the Companies Act, 2013 defines the term "share". As per this, share means a share in the share capital of a company and includes stock.
- By its nature, a share is not a sum of money but a bundle of rights and liabilities. A share is a right to participate in the profits of a company, while it is a going concern and declares dividend; and a right to participate in the assets of the company, when it is wound up.
- Shares are a movable property: According to Section 44 of the Companies Act, 2013, the shares or debentures or other interests of any member in a company shall be movable property transferable in the manner provided by the articles of the company.
- Share

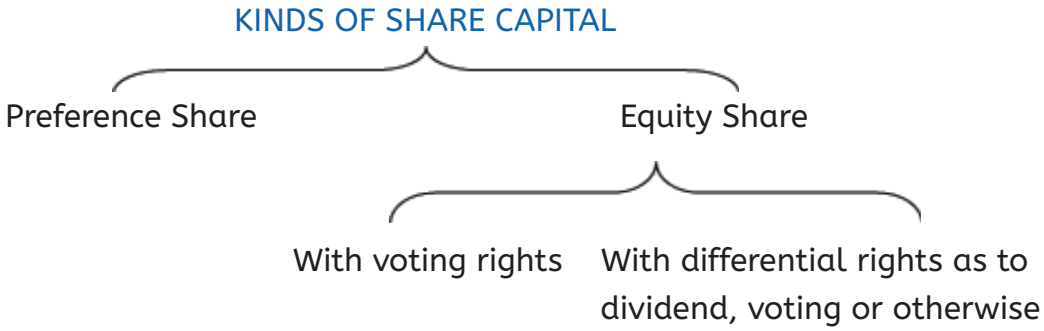
Dematerialised Shares	Physical Shares
• It mandates that every company making public offer and any class of companies as specified shall issue the securities only through dematerialized form. • Proof of ownership: Records of depository • Every share in a company having a share capital shall not be distinguished by its distinctive number (Section 45).	• Other companies may issue securities in physical or in dematerialized form. • Proof of ownership: Share Certificate • Every share in a company having a share capital shall be distinguished by its distinctive number (Section 45).

CLASSIFICATION OF SHARE CAPITAL

The share capital of a company can be classified as :



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



(A) Preference Share

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

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

(B) Equity Share

- "Equity share capital" with reference to any company limited by shares, means all share capital which is not preference share capital;

- Equity share capital –
  (1) with voting rights; or
  (2) with differential rights as to dividend, voting or otherwise in accordance with prescribed rules;

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

LIST OF CASE LAWS

SR. NO	NAME OF CASE LAW	PAGE NO. (This column is to be filled by students)
1.	Macaura vs. Northern Assurance Co. Ltd.	
2.	Salomon v. Salomon & Co. Ltd.	
3.	Gilford Motor Co. v. Home	
4.	Daimler Co. Ltd. vs. Continental Tyre & Rubber Co.	
5.	Sir Dinshaw Maneckjee Petit	
6.	Workmen employed in Associated Rubber Industries Ltd v. Associated Rubber Industries Ltd	
7.	Merchandise Transport Limited vs. British Transport Commission (1982)	
8.	Narendra Kumar Agarwal vs. Saroj Maloo	
9.	Ashbury Railway Carriage and Iron Company Limited v. Riche	
10.	The Royal British Bank vs. Turquand	

LIST OF LEGAL TERMS

SR. NO.	LEGAL TERM	MEANING	PG NO. (To be filled by students)
1.	Corporate governance	It is the technique by which companies are directed and managed. It is actually conducted by the board of Directors and the concerned committees for the company's stakeholder's benefit.	
2.	Authenticated	proved that something is real	
3.	Domicile	The place where a person lives	
4.	Revoke the licence	Take back the license	
5.	Misfeasance	the fact of someone in authority performing a legal act in an illegal way	
6.	Suppresses	ends something by force	
7.	Magna Carta	Great Charter (important document)	
8.	Ratified	Approved	

SUMMARY

INTRODUCTION

The Companies Act, 2013 contains 470 sections and seven schedules. The entire Act has been divided into 29 chapters.

DEFINITION OF COMPANY [Section 2(20)]

PPLICABILITY OF THE ACT

CHARACTERISTICS OF COMPANY

IS COMPANY A CITIZEN?

DOES A COMPANY HAVE NATIONALITY AND RESIDENCE?

LIFTING OR PIERCING THE CORPORATE VEIL

CLASSIFICATION OF COMPANY

- **Based on liability**
  - Company Limited by shares
  - Company Limited by guarantee
  - Unlimited liability company
- **Based on Members**
  - One person company
  - Private company
  - Public
  - Small Company
- **Based on Control**
  - Holding & Subsidiary company
  - Associate company
- **Based on Capital**
  - Listed
  - Unlisted
- **Other Companies**
  - Government
  - Foreign
  - Non Profit
  - Dormant
  - Nidhi

PROMOTERS [Section 2(69)]

INCORPORATION OF COMPANIES (SECTION 7)

EFFECT OF FURNISHING OF FALSE OR INCORRECT INFORMATION OR SUPPRESSION OF MATERIAL FACT

SIMPLIFIED PROFORMA FOR INCORPORATING COMPANY ELECTRONICALLY (SPICe)

- MEMORANDUM OF ASSOCIATION (Section 4)
- ARTICLES OF ASSOCIATION (SECTION 5)
- DIFFERENCES BETWEEN THE MEMORANDUM OF ASSOCIATION VS.ARTICLES OF ASSOCIATION
- EFFECT OF MEMORANDUM AND ARTICLES (Section 10)
- DOCTRINE OF ULTRA VIRES
- DOCTRINE OF CONSTRUCTIVE NOTICE
- DOCTRINE OF INDOOR MANAGEMENT
- SHARE [Section 2(84)]
- CLASSIFICATION OF SHARE CAPITAL
- KINDS OF SHARE CAPITAL

8. THE NEGOTIABLE INSTRUMENTS ACT, 1881

SECTION-A: CONCEPTS

Introduction

- The Act was introduced on 1st March, 1882.
- The main objective of the Act is to legalise the system by which instruments contemplated by it could pass from hand to hand by negotiation like any other go ods.

- The Law in India relating to negotiable instruments is contained in the Negotiable Instruments Act, 1881. It deals with
  (i) Promissory Notes
  (ii) Bills of Exchange
  (iii) Cheque.

  But Section 21 of The Reserve Bank of India Act, 1934, provides that Bank has the right to transact Government business in India, or affect any local usage relating to any instrument in an oriental language.
- The provisions of this Act are also applicable to Hundis, unless there is a local usage to the contrary.
- Recent developments: The Act was amended several times.

  Recent three amendments made in the N.I. Act:
  (1) The Negotiable Instruments (Amendment and Miscellaneous Provisions) Act, 2002
  (2) The Negotiable Instruments (Amendment) Act, 2015
  (3) Negotiable Instruments (Amendment) Act, 2018.

  The Negotiable Instruments (Amendment) Act, 2018 received the assent of the President and was notified in the official gazette on 2nd August, 2018 and came into effect from September 1, 2018.

  The Amendment Act 2018 contains two significant changes – the introduction of Section 143A and Section 148. These sections provide interim compensation during the pendency of the criminal complaint and the criminal appeal.

2.1: Applicability

It extends to:

(1) Whole of India

(2) Including Jammu & Kashmir.

2.2: Meaning and Characteristics of Negotiable Instrument

- Meaning: The Act does not define the term 'Negotiable Instruments'. However, Section 13 of the Act provides for only three kinds of negotiable instruments namely, bills of exchange, promissory notes and cheques, payable either to order or bearer.

  But it can be interpreted as a transferrable written piece of paper creating a right of a person to receive money and a corresponding liability of a person to pay money.

- Essential Characteristics of Negotiable Instrument:

  (1) It is necessarily in writing

  (2) It should be signed

  (3) It is free transferable from one person to another

  (4) Holder's title is free from defects:

  A holder in due course acquires a good title irrespective of any defect in a previous holder's title. A holder in due course is one who receives the instrument:

  (i) For consideration

  (ii) Without notice as to the defect in the title of the transferor; i.e. in good faith and

  (iii) Before maturity

  (5) It can be transferred any number of times till its satisfaction.

  (6) Every negotiable instrument must contain either a promise or order to pay money. Also, the promise or order must be unconditional.

  (7) The promise or order to pay must consist of money only. Nothing should be payable, whether in addition or in substitution of money. Also, the sum payable must be certain.

  (8) A negotiable instrument is subject to certain presumptions (Section 118).

  (i) Consideration: Every negotiable instrument was made or drawn for consideration.

  (ii) Date: Every negotiable instrument bearing a date was made or drawn on such date.

  (iii) Time of acceptance: Every accepted bill of exchange was accepted within a reasonable time after its date and before its maturity.

(iv) Time of transfer: Every transfer of a negotiable instrument was made before its maturity.

(v) Order of endorsements: Endorsements appearing upon a negotiable instrument were made in the order in which they appear thereon.

(vi) Stamp: Promissory note, bill of exchange or cheque was duly stamped.

(vii) Holder: The holder of a negotiable instrument is a holder in due course

The above presumptions are rebuttable by evidence to the contrary.

2.3: Promissory Note

- Meaning: As per Section 4,

  An instrument in writing
  (not being bank note or a currency note)
  containing an unconditional undertaking,
  signed by the maker,
  to pay a certain sum of money
  to a certain person or to the order of a certain person, or to the bearer of the instrument.

- Parties to Promissory Note:

  (1) Maker: The person who makes the promissory Note. He is Debtor who is liable to pay.

  (2) Payee: The person to whom amount is payable. He is creditor who has a right to receive money.

- Essential characteristics of a Promissory Note.

  (1) In writing- An oral promise to pay is not sufficient.

  (2) There must be an express promise to pay. Mere acknowledgment of debt is insufficient.

  Example: Mr.Ramesh, I owe you ₹2000. Not a valid promissory note as there is no promise to pay.

  Example: I acknowledge myself to be indebted to Rhea for ₹1,000, to be paid on demand, for value received. (Valid promissory note as the promise to pay is definite)

  (3) The promise to pay should be definite and unconditional. Therefore, instruments payable on performance or non-performance of a particular act or on the happening or non-happening of an event, are not promissory notes. However,

the promise to pay may be subject to a condition, which according to the ordinary experience of mankind, is bound to happen (i.e. natural event)

Example: I promise to pay Anil ₹500 seven days after my marriage with Sonam. The promissory note is invalid as marriage with Sonam may or may not happen.

Example: I promise to pay Rohan ₹500 on Tarun's death- as the death of Tarun is certain, promise in unconditional. Thus, the promissory note is valid.

Example: I promise to pay Rohan ₹500 on Tarun's death, provided Tarun leaves me enough to pay that sum. It is an invalid promissory note as promise is dependent on Tarun leaving behind money which is not certain.

(4) A promissory note must be signed by the maker otherwise it in incomplete and ineffective.

(5) Promise to pay money only.

Example: I promise to pay Raj ₹500 and a black horse on 1st January next. – It is not a valid promissory note, as the promisor needs to deliver its black horse which is not money.

(6) Promise to pay a certain sum

Example: "I promise to pay Nidhi ₹500 and all other sums which shall be due to him."- Promissory note invalid as the amount payable is not certain.

(7) The maker and payee must be certain, definite and different persons. A promissory note cannot be made payable to the bearer (Sec. 31 of RBI Act). Only the Reserve Bank or the Central Government can make or issue a promissory note 'payable to bearer' as bearer promissory notes are currency notes.

(8) Stamping: A promissory note must be properly stamped in accordance with the provisions of the Indian Stamp Act and such stamp must be duly cancelled by maker's signatures.

- Specimen of a Promissory Note.

Mumbai
March 8th, 2019

₹5,000/-

I promise to pay Rahul or his order a sum of Rupees five thousand, for value received, three months after date.

Stamp
Sd/-
Simran

Maker

To,
Mr.Rahul
A-503, Falcon Park
Mumbai

Payee

2.4: Bill of Exchange

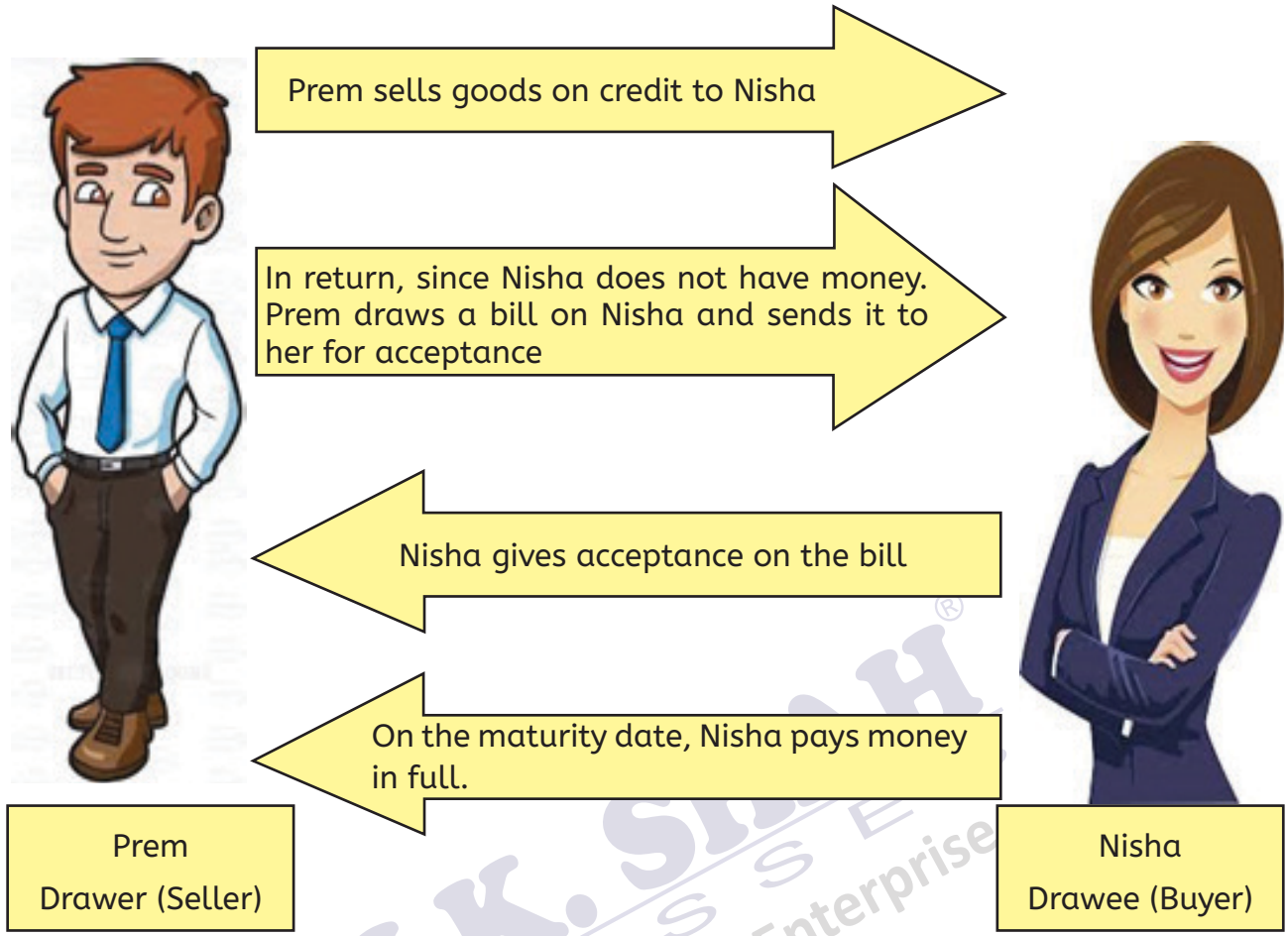
- Meaning: As per Section 5,

  An instrument in writing
  containing an uncon¬ditional order,
  signed by the maker,
  directing a certain person
  to pay a certain sum of money
  to a certain person or to the order of a certain person or to the bearer of the instrument.

- Parties to Bill of Exchange:
  (1) Drawer: The maker of a bill of exchange.
  (2) Drawee: The person directed by the drawer to pay is called the 'drawee'. He is the person on whom the bill is drawn. On acceptance of the bill he is called an acceptor and is liable for the payment of the bill. His liability is primary and unconditional.
  (3) Payee: The person named in the instrument, to whom or to whose order the money is, by the instrument, directed to be paid.

- Essential characteristics of bill of exchange
  (1) It must be in writing.
  (2) Must contain an express order to pay.
  (3) The order to pay must be definite and unconditional
  (4) The drawer must sign the instrument
  (5) Drawer, drawee and payee must be certain. All these three parties may not necessarily be three different persons. One can play the role of two. But there must be two distinct persons in any case.
  (6) The sum must be certain.
  (7) The order must be to pay money only.
  (8) It must be stamped.

- Process of Bill Of Exchange



In above image, firstly seller sells goods to the buyer /customer and then draws a bill on him. Buyer/customer received a bill and accepts it. On maturity of bill, buyer will pay a sum of amount to the payee. (Payee may be drawer himself or any other person if the bill is indorsed.)

- Specimen of a Bill of Exchange

Payee

Mr. Prem
21, Tilak Nagar, Mumbai
April 25, 2019

₹8,000/-

Three months after date, pay Mr.Ravi a sum of Rupees Eight Thousand, for value received

Drawee

To,
Ms. Nisha
55, Seacrest Colony,
Mumbai

Drawer

Signature
Mr. Prem

2.5: Cheque

- Meaning: Section 6 defines a cheque as a bill of exchange
  drawn on a specified banker and
  not expressed to be payable otherwise than on demand
  and includes the electronic image of a truncated cheque and a cheque in the electronic form.

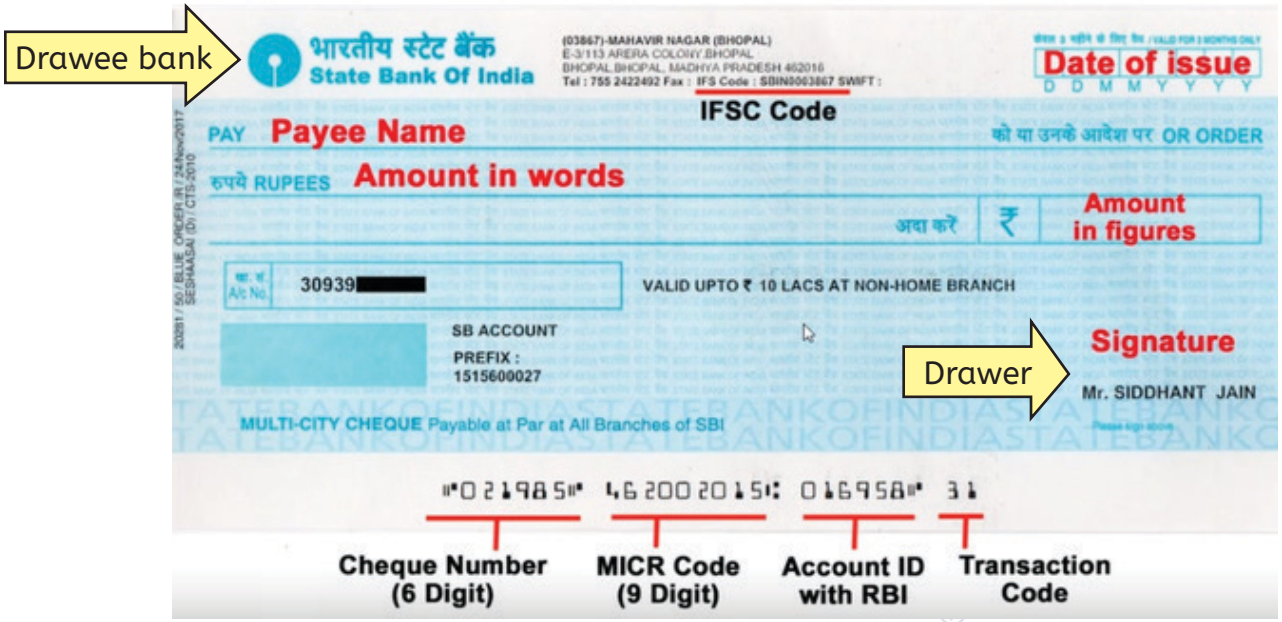
  ✓ Payable on demand means- It should be payable whenever the holder chooses to present it to the drawee (the banker).
  ✓ The expression "Banker" includes any person acting as a bank and any post office saving bank [Section 3]
  ✓ Cheque in the electronic form"-means a cheque drawn in electronic form by using any computer resource, and signed in a secure system with a digital signature;
  ✓ "A truncated cheque" means a cheque which is truncated during the course of a clearing cycle, either by the clearing house or by the bank whether paying or receiving payment, immediately on generation of an electronic image for transmission, substituting the further physical movement of the cheque in writing.

- Parties to Cheque:
  (1) Drawer: The person who draws a cheque i.e. makes the cheque. (Debtor)
  (2) Drawee: The specific bank on whom cheque is drawn.
  (3) Payee: The person named in the instrument, to whom or to whose order the money is, by the instrument, directed to be paid, is called the payee.

- Essential Characteristics of a cheque
  According to the definition of cheque under section 6, a cheque is a species of bill of exchange. Thus, it should fulfil:
  (1) All the essential characteristics of a bill of exchange
  (2) Must be drawn on a specified banker
  (3) It must be payable on demand

Note: These two additional features distinguish a cheque from bill. Thus, all cheques are bills while all bills are not cheques.

- Specimen of a Cheque



2.6: Difference between Promissory Note / Bill of Exchange / Cheque

Sr. No	Points of Distinction	Promissory Note	Bill of Exchange	Cheque
1.	Intention	It contains a promise to pay.	It contains an order to pay.	It contains an order to pay on bank.
2.	Liability of Maker	The liability of the maker of a note is primary and absolute.	The liability of the drawer is secondary. He would be liable if the drawee fails to pay the money.	The liability of maker (A/c holder) is secondary when bank fails to pay the dues.
3.	Payment to Self	It cannot be made payable to the maker himself, that is the maker and the payee cannot be the same person.	The drawer may order the payment to be made to him also. Thus, the drawer and payee may be the same person.	The person can draw cheque on bank which can be made payable to self. So drawer of cheque & payee may be same person.
4.	Parties to Instrument	There are only two parties, viz., the maker (debtor) and the payee (creditor).	In the case of a bill of exchange there are three parties, viz., drawer, drawee and payee.	In the case of a cheque of exchange there are three parties, viz., drawer, drawee bank and payee.

5.	Notice of dishonour	In case of dishonour of note, notice is not required to be given to its maker.	Notice of dishonour of a bill is required to be given to all the parties.	Notice of dishonour of a cheque is required to be given to all the parties.
6.	Noting & Protesting	There must be Noting and Protest to prove that the note has been dishonoured.	There must be Noting and Protest to prove that the bill has been dishonoured.	There is no system of Noting or Protest.
7.	Involvement of banker	The banker may or may not be involved.	The banker may or may not be involved.	The drawee of the cheque is compulsorily banker.
8.	Grace days	3 days' grace is allowed	3 days' grace is allowed	No grace is allowed in the case of a cheque, as it is as a rule, payable immediately on demand.
9.	Stamping	PN must be stamped according to law.	Bills must be stamped according to the law.	Cheques do not require to be stamped in India.
10.	Crossing	The PN is not crossed.	The bill is not crossed.	A cheque may be crossed.

2.12: Holder in Due Course (Section 9)

- "Holder in due course" means any person
  - ✓ who for consideration
  - ✓ before the amount mentioned in it became payable, and
  - ✓ without having sufficient cause to believe that any defect existed in the title of the person from whom he derived his title i.e. good faith,
  - ✓ became the possessor of a promissory note, bill of exchange or cheque (if payable to bearer), or the payee or Indorsee thereof, (if payable to order),

- Example: A draws a cheque for ₹5,000 and hands it over to B by way of gift. B is a holder but not a holder in due course as he does not get the cheque for value and consideration. As a holder he is entitled to receive ₹5000 from the bank on whom the cheque is drawn.

2.13: Classification of Instruments

(1) Bearer and Order Instruments:

- Bearer Instrument: It is an instrument where
  the name of the payee is blank or
  where the name of payee is specified with the words "or bearer" or
  where the last indorsement is blank.
  Such instrument can be negotiated by mere delivery.

- Order Instrument: It is an instrument which is payable to a person or
  Payable to a person or his order or
  Payable to order of a person or
  Where the last indorsement is full
  Such instrument can be negotiated by indorsement and delivery.

(2) Inland and Foreign Instruments (Section 11 & 12)

- Inland Instrument: Any instrument drawn or made in India and
  Either payable in or drawn upon any person resident in India shall be deemed to be an inland instrument.
  Example:
  (i) A promissory note made in Chennai and payable in Delhi.
  (ii) A bill drawn in Pune on a person resident in Jaipur, although it is stated to be payable in London.
  The Negotiable Instruments Act is applicable.
- Foreign Instruments: Instrument which is not an inland instrument.
  In the absence of a contract to the contrary,
  the liability of the maker or drawer of a foreign promissory note or bill of exchange or cheque is regulated in all essential matters by the law of the place where he made the instrument, and
  the respective liabilities of the acceptor and Indorser by the law of the place where the instrument is made payable (Section 134).
  Example: A bill of exchange is drawn by John in New York where the rate of interest is 13% and accepted by David payable in Sydney where the rate of interest is 7%. The bill is indorsed in India and is dishonoured. An action on the bill is brought against David in India. He is liable to pay interest at the rate of 7% only. But if John is charged as drawer, he is liable to pay interest at 13%.

Example:

(i) A promissory note made in Kolkata and payable in Mumbai.

(ii) A bill drawn in Varanasi on a person resident in Jodhpur (although it is stated to be payable in Singapore)

(iii) A, a resident of Agra, drew (i.e., made) a bill of exchange in Agra on B, a merchant in New York. And B accepted the bill of exchange as payable in Delhi. It is an inland bill of exchange. In this case, the bill of exchange was drawn in India and also payable in India.

(iv) A, resident of Mumbai, drew a bill of exchange in Mumbai on B, a merchant in Mathura.

And B accepted the bill of exchange as payable in London. It is also an inland bill of exchange. In this case, the bill of exchange was drawn in India on a person resident in India.

It is immaterial that the amount is payable in London.

An inland instrument remains inland even if it has been endorsed in a foreign country.

(v) If the bills of exchange mentioned in above two examples, are endorsed in France, they will remain inland bills.

(3) Inchoate and Ambiguous Instruments:

- **Inchoate Instrument (Section 20):**

It means an Instrument that is incomplete in certain respects.

(i) The person gives a blank instrument with authority to the holder to complete it with appropriate amount up to the stamp value of the instrument.

(ii) Delivery of such a paper is essential. The words "when one person signs and delivers to another" are important.

(iii) The person signing and delivering the inchoate instrument is liable both to a holder and holder in due course. However, there is a difference in their respective rights. The holder of such an instrument cannot recover the amount in excess of the amount intended to be paid by the signor. The holder in due course can, how¬ever, recover any amount on such instrument provided it is covered by the stamp affixed on the instrument (privileges of holder in due course).

Example: A bill of exchange upto the value of ₹1,000, say, requires stamps worth 50 paise. A bill with a stamp of 50 paise on it is duly signed but the amount is not filled in It is agreed that the payee will not fill in more than

₹500. Suppos¬ing, the payee fills in ₹900, the person so signing shall be liable to any holder in due course for the full amount of the bill, i.e., ₹900, being the amount covered by the stamp. However, a mere holder cannot claim more than ₹500 the amount intended.

Example: A person signed a blank acceptance on a bill of exchange and kept it in his drawer. The bill was stolen by X and he filled it up for ₹ 20,000 and negotiated it to an innocent person for value. It was held that the signer to the blank acceptance was not liable to the holder in due course because he never delivered the instrument intending it to be used as a negotiable instrument.

- Ambiguous Instrument:

  An instrument which is vague and cannot be clearly iden¬tified either as a bill of exchange, or as a promissory note, is an Ambiguous instrument. In other words, such an instrument may be construed either as prom¬issory note, or as a bill of exchange.

  Regarding such instruments, Section 17 provides that the holder may, at his discretion, treat it as either and the instru¬ment shall thereafter be treated accordingly. Thus, after exercising his option, the holder cannot change that it is the other kind of instrument.

  Example: A is the drawer as well as the drawee of an instrument. He negotiates it to B. B, the holder, may treat the bill as a promissory note made by A.

  Where amount is stated differently in figures and words [Section 18] If the amount undertaken or ordered to be paid is stated differently in figures and in words, the amount stated in words shall be the amount undertaken or ordered to be paid.

2.14: Transfer of Instrument

- One of the essential characteristics of a negotiable instrument is that it is freely transferable from one person to another. The rights in a negotiable instrument can be transferred from one person to another by
  1. Assignment under Transfer of Property Act
  2. Negotiation under the Negotiable Instruments Act

- Assignment: Assignment of a negotiable instrument means transfer of ownership of the instrument from one person (assignor) to another (assignee), whereby the assignee becomes en¬titled to recover the amount due on the instrument from the parties liable to pay.

- Negotiation: According to section 14, when a negotiable instrument is transferred to any person with a view to constitute the person holder thereof, the instrument is deemed to have been negotiated.

- Modes of negotiation of instrument?

(i) A promissory note, bill of exchange or cheque payable to bearer is negotiable by the delivery thereof (Section 47).

(ii) A promissory note, bill of exchange or cheque payable to order is negotiable by the holder by indorsement and delivery thereof (Section 48).

Example:

(1) A, the holder of a negotiable instrument payable to bearer, delivers it to B's agent to keep for B. The instrument has been negotiated.

(2) A, the holder of a negotiable instrument payable to bearer, which is in the hands of A's banker, who is at the time the banker of B, directs the banker to transfer the instrument to B's credit in the banker's account with B. The banker does so, and accordingly now possesses the instrument as B's agent. The instrument has been negotiated, and B has become the holder of it.

- Delivery [Section 46]:

❖ Delivery of an instrument is essential whether the instrument is payable to bearer or order for effecting the negotiation.

❖ The delivery must be voluntary and the object of delivery should be to pass the property in the instrument to the person to whom it is delivered.

❖ The delivery can be, actual or constructive. Actual delivery takes place when the instrument changes hand physically, constructive delivery take place when the instrument is delivered to the agent, clerk or servant of the Indorsee on his behalf or when the Indorser, after Indorsement, holds the instrument as an agent of the Indorsee.

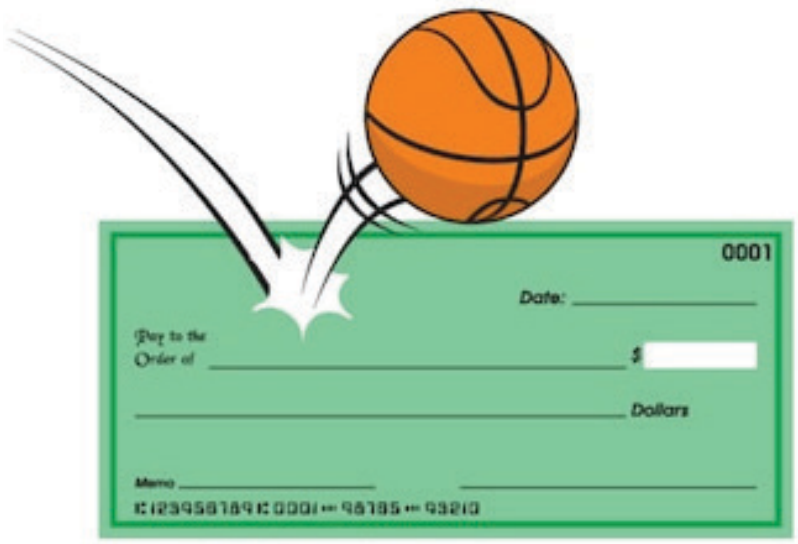
❖ The delivery is essential not only at the time of negotiation but also at the time of making or drawing of negotiable instrument.

❖ The rights in the instrument are transferred to the indorsee only after the indorsement the same has been delivered.

❖ If a person makes the indorsement of instrument but before the same could be delivered to the indorsee the indorser dies, the legal representatives of the deceased person can't negotiate the same by mere delivery thereof (Section 57).

Example: X drew a cheque for Rs. 50,000 payable to Y and delivered it to him. Y indorsed the cheque in favour of Z but kept it in his table drawer. Subsequently, Y died, and cheque was found by Z in Y's table drawer. In this case, Z does not become the holder of the cheque as the negotiation was not completed by delivery of the cheque to him.

2.19: Dishonour of Cheque



- Dishonour of cheque for insufficiency, etc., of funds in the account (Section 138)
  - ❖ Where any cheque drawn by a person on an account maintained by him with a banker-
    For payment of any amount of money
    to another person from out of that account
    for the discharge, in whole or in part, of any legal debt or other liability,
    is returned by the bank unpaid,
    either because of amount of money standing to the credit of that account is insufficient to honor the cheque, or the amount of cheque exceeds the amount arranged to be paid from that account by an agreement made with that bank,
    Then such person shall be deemed to have committed an offence and shall, be punished with:
    Imprisonment: Upto 2 years
    Or
    Fine: Upto twice the amount of the cheque,
    Or
    Both

❖ However, in order to attract the aforesaid penalty, following conditions must be satisfied:

(1) The cheque should have been presented within 3 months from the date on which it is drawn.

(2) The cheque should have been dishonoured due to insufficiency of funds in the account maintained by him with a banker for payment of any amount of money to another person from out of that account.

(i) In case of stop-payment, it shall be deemed to have been so dishonoured for in¬sufficiency of funds unless stop-payment can be justified.

(ii) Dishonour due to closure of account has also been held to be dishonoured for insufficiency of funds

(iii) Directing the payee not to present will be deemed to have the same effect

(3) The payment for which the cheque was issued should have been in discharge of a legally enforceable debt or liability in whole or part of it. Hence, a cheque given as gift or donation, or as a security or in discharge of a mere moral obligation, or for an illegal consideration, will not be covered under this section.

❖ Following procedure is to be followed before applying the aforesaid penalty:

Procedure	Example with date
(1) Cheque is issued by drawer	28th June, 2019
(2) The payee/holder presents it for payment.	1st July,2019
(3) The collecting bank informs payee/holder about dishonour of cheque.	4th July,2019
(4) The payee or the holder in due course of the cheque should have given no¬tice demanding payment within 30 days from the drawer in receipt of infor¬mation of dishonour of cheque from the bank. Notice can be served by ordi¬nary post or even telegram.	+ 30 days 3rd August,2019 (Last day for sending the notice)
(5) The drawer is liable only if he fails to make the payment within 15 days of such notice period.	+ 15 days 18th August,2019 (Last date for payment)
(6) The payee or holder in due course of the cheque dishonoured should file a complaint within one month under Sec. 138.	+ 1 month 18th Sept,2019 (Last date for filing a suit)

Example: X issued a post-dated cheque to Y on the account of discharge of its liability. Further, X instructed to the bank to stop the payment due to unavailability of the adequate amount in the account. Here, in this instance section 138 of the Act is attracted as when a cheque is dishonoured on account of stop payment instructions sent by the drawer to his banker in respect of a post- dated cheque irrespective of insufficiency of funds in the account. A post-dated cheque is deemed to have been drawn on the date it bears and the three months period for the purposes of section 138 is to be counted from that date. So, X will be liable for dishonour of cheque. Once a cheque is issued by the drawer, a presumption under section 139 must follow.

- Presumption in favour of holder [Section 139]:
  It shall be presumed that the holder of a cheque received the cheque of the nature referred to in section 138 for the discharge, in whole or in part, or any debt or other liability unless proved otherwise.

- Defense which may not be allowed in any prosecution under section 138 [Section 140]:
  The drawer cannot defend himself for the offence under section 138 by stating that he had no reason to believe when he issued the cheque, it would be dishonoured on presentment due to insufficiency of funds.

2.20: Presentment of Instruments

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

Presentment of promissory note for sight [Section 62]	A promissory note, payable at a certain period after sight, must be presented to the maker thereof for sight (if he can after reasonable search be found) by a person entitled to demand payment, within a reasonable time after it is made and in business hours on a business day. In default of such presentment, no party thereto is liable thereon to the person making such default.
Drawee's time for deliberation [Section 63]	The holder must, if so required by the drawee of a bill of exchange presented to him for acceptance, allow the drawee 48 hours (exclusive of public holidays) to consider whether he will accept it.
Presentment for payment [Section 64]	Promissory notes, bill of exchange and cheques must be presented for payment to the maker, acceptor or drawee thereof respectively, by or on behalf of the holder as hereinafter provided. In default of such presentment, the other parties thereto are not liable thereon to such holder. Where authorised by agreement or usage, a presentment through the post office by means of a registered letter is sufficient.
	Exception: Where a promissory note is payable on demand and is not payable at a specified place, no presentment is necessary in order to charge the maker thereof. Notwithstanding anything contained in section 6, where an electronic image of a truncated cheque is presented for payment, the drawee bank is entitled to demand any further information regarding the truncated cheque from the bank holding the truncated cheque in case of any reasonable suspicion about the genuineness of the apparent tenor of instrument, and if the suspicion is that of any fraud, forgery, tampering or destruction of the instrument, it is entitled to further demand the presentment of the truncated cheque itself for verification: Provided that the truncated cheque so demanded by the drawee bank shall be retained by it, if the payment is made accordingly.
Hours for presentment (Section 65)	Presentment for payment must be made during the usual hours of business, and, if at a banker's within banking hours.

Presentment for payment of instrument payable after date or sight (Section 66)	A promissory note or bill of exchange, made payable at a specified period after date or sight thereof, must be presented for payment at maturity.
Presentment for payment of promissory note payable by instalments (Section 67)	A promissory note payable by instalments must be presented for payment on the third day after the date fixed for payment of each instalment; and non-payment on such presentment has the same effect as non-payment of a note at maturity.
Presentment for payment of instrument payable at specified place and not elsewhere (Section 68)	A promissory note, bill of exchange or cheque made, drawn or accepted payable at a specified place and not elsewhere must, in order to charge any party thereto, be presented for payment at that place.
Instrument payable at specified place (Section 69)	A promissory note or bill of exchange made, drawn or accepted payable at a specified place must, in order to charge the maker or drawer thereof, be presented for payment at that place.
Presentment where no exclusive place specified (Section 70)	A promissory note or bill of exchange, not made payable as mentioned in sections 68 and 69, must be presented for payment at the place of business (if any) or at the usual residence, of the maker, drawee or acceptor thereof, as the case may be.
Presentment when maker, etc., has no known place of business or residence (Section 71)	If the maker, drawee or acceptor of a negotiable instrument has no known place of business or fixed residence, and no place is specified in the instrument for presentment for acceptance or payment, such presentment may be made to him in person wherever he can be found.

Presentment of cheque to charge drawer (Section 72)	Subject to the provisions of section 84, a cheque must, in order to charge the drawer, be presented at the bank upon which it is drawn before the relation between the drawer and his banker has been altered to the prejudice of the drawer.
Presentment of cheque to charge any other person (Section 73)	A cheque must, in order to charge any person except the drawer, be presented within a reasonable time after delivery thereof by such person.
Presentment of instrument payable on demand (Section 74)	Subject to the provisions of section 31, a negotiable instrument payable on demand must be presented for payment within a reasonable time after it is received by the holder.
Presentment by or to agent, representative of deceased, or assignee of insolvent (Section 75)	Presentment for acceptance or payment may be made to the duly authorised agent of the drawee, maker or acceptor, as the case may be, or, where the drawee, maker or acceptor has died, to his legal representative, or, where he has been declared an insolvent, to his assignee.
Excuse for delay in presentment for acceptance or payment (Section 75A)	Delay in presentment for acceptance or payment is excused if the delay is caused by circumstances beyond the control of the holder, and not imputable to his default, misconduct or negligence. When the cause of the delay ceases to operate, resentment must be made within a reasonable time.
When presentment unnecessary (Section 76)	No presentment for payment is necessary, and the instrument is dishonoured at the due date for presentment, in any of the following cases: (a) (i) If the maker, drawee or acceptor intentionally prevents the presentment of the instrument, or (ii) if the instrument being payable at his place of business, he closes such place on a business day during the usual business hours, or

	(iii) if the instrument being payable at some other specified place, neither he nor any person authorised to pay it attends at such place during the usual business hours, or (iv) if the instrument not being payable at any specified place, he cannot after due search be found; (b) as against any party sought to be charged therewith, if he has engaged to pay notwithstanding non-presentment; (c) as against any party if, after maturity, with knowledge that the instrument has not been presented– o he makes a part payment on account of the amount due on the instrument, o or promises to pay the amount due thereon in whole or in part, o or otherwise waives his right to take advantage of any default in presentment for payment; (d) as against the drawer, if the drawer could not suffer damage from the want of such presentment.
Liability of banker for negligently dealing with bill presented for payment (Section 77)	When a bill of exchange, accepted payable at a specified bank, has been duly presented there for payment and dishonoured, if the banker so negligently or improperly keeps, deals with or delivers back such bill as to cause loss to the holder, he must compensate the holder for such loss.

2.21 RULES OF COMPENSATION

Rules as to compensation (Section 117)	The compensation payable in case of dishonour of promissory note, bill of exchange or cheque, by any party liable to the holder or any endorsee, shall be determined by the following rules: (a) the holder is entitled to the amount due upon the instrument, together with the expenses properly incurred in presenting, noting and protesting it; (b) when the person charged resides at a place different from that at which the instrument was payable, the holder is entitled to receive such sum at the current rate of exchange between the two places;

	(c) an endorser who, being liable, has paid the amount due on the same is entitled to the amount so paid with interest at 18% per annum from the date of payment until tender or realisation thereof, together with all expenses caused by the dishonour and payment; (d) when the person charged and such endorser reside at different places, the endorser is entitled to receive such sum at the current rate of exchange between the two places; (e) the party entitled to compensation may draw a bill upon the party liable to compensate him, payable at sight or on demand, for the amount due to him, together with all expenses properly incurred by him. Such bill must be accompanied by the instrument dishonoured and the protest thereof (if any). If such bill is dishonoured, the party dishonouring the same is liable to make compensation thereof in the same manner as in the case of the original bill.

SUMMARY

Introduction

- The Act was introduced on 1st March, 1882.
- The Law in India relating to negotiable instruments is contained in the Negotiable Instruments Act, 1881. It deals with
  (i) Promissory Notes
  (ii) Bills of Exchange
  (iii) Cheque.
- Recent three amendments made in the N.I. Act:
  (i) The Negotiable Instruments (Amendment and Miscellaneous Provisions) Act, 2002
  (ii) The Negotiable Instruments (Amendment) Act, 2015
  (iii) Negotiable Instruments (Amendment) Act, 2018.

2.1 Applicability: Whole of India including Jammu & Kashmir

2.2: Meaning and Characteristics of Negotiable Instrument

- Meaning: Section 13 of the Act provides for only three kinds of negotiable instruments namely, bills of exchange, promissory notes and cheques, payable either to order or bearer.
  It is a transferrable written piece of paper creating a right of a person to receive money and a corresponding liability of a person to pay money.
- Essential Characteristics of Negotiable Instrument:
  (1) It is necessarily in writing
  (2) It should be signed
  (3) It is free transferable from one person to another
  (4) Holder in due course's title is free from defects:
  (5) It can be transferred any number of times till its satisfaction.
  (6) Every negotiable instrument must contain either a promise or order to pay money. Also, the promise or order must be unconditional.
  (7) The promise or order to pay must consist of money only. Nothing should be payable, whether in addition or in substitution of money. Also, the sum payable must be certain.
  (8) A negotiable instrument is subject to certain presumptions (Section 118).
    (i) Consideration

(ii) Date
(iii) Time of acceptance
(iv) Time of transfer
(v) Order of endorsements
(vi) Stamp
(vii) Holder

The above presumptions are rebuttable by evidence to the contrary.

2.3: Promissory Note (Section 4)

- Meaning: An instrument in writing (not being bank note or a currency note) containing an uncon¬ditional undertaking, signed by the maker, to pay a certain sum of money to a certain person or to the order of a certain person, or to the bearer of the instrument.
- Parties to Promissory Note:
  (1) Maker
  (2) Payee
- Essential characteristics of a Promissory Note.
  (1) In writing
  (2) An express promise to pay.
  (3) The promise to pay should be definite and unconditional. However, the promise to pay may be subject to a condition, which according to the ordinary experience of mankind, is bound to happen.
  (4) A promissory note must be signed by the maker
  (5) Promise to pay money only.
  (6) Promise to pay a certain sum
  (7) The maker and payee must be certain, definite and different persons.
  (8) A promissory note must be properly stamped.

2.4: Bill of Exchange (Section 5)

- Meaning: An instrument in writing containing an unconditional order, signed by the maker, directing a certain person to pay a certain sum of money to a certain person or to the order of a certain person or to the bearer of the instrument.
- Parties to Bill of Exchange:
  (1) Drawer
  (2) Drawee
  (3) Payee

- Essential characteristics of bill of exchange
  (1) It must be in writing.
  (2) Must contain an express order to pay.
  (3) The order to pay must be definite and unconditional
  (4) The drawer must sign the instrument
  (5) Drawer, drawee and payee must be certain.
  (6) The sum must be certain.
  (7) The order must be to pay money only.
  (8) It must be stamped.

2.5: Cheque (Section 6)

- Meaning: It defines a cheque as a bill of exchange drawn on a specified banker and not expressed to be payable otherwise than on demand and includes the electronic image of a truncated cheque and a cheque in the electronic form.

- Parties to Cheque:
  (1) Drawer
  (2) Drawee Bank
  (3) Payee

- Essential Characteristics of a cheque
  (1) All the essential characteristics of a bill of exchange
  (2) Must be drawn on a specified banker
  (3) It must be payable on demand

2.6: Difference between Promissory Note / Bill of Exchange / Cheque

2.11: Holder (Section 8)

- The "holder" of a promissory note, bill of exchange or cheque means any person entitled in his own name to the possession thereof, and to receive or recover the amount due thereon from the parties thereto.
- Holder is not a person who holds the instrument but he is a person who has a right to hold and who is entitled to receive or recover the amount due thereon from the parties thereto.
- His rights and title are dependent on the transferor

2.12: Holder in Due Course (Section 9)

- "Holder in due course" means any person who for consideration before maturity and in good faith became the possessor of a promissory note, bill of exchange or cheque.
- His rights and title are independent on the transferor

2.13: Classification of Instruments

(1) Bearer and Order Instruments:

- Bearer Instrument: It is an instrument where the name of the payee is blank or where the name of payee is specified with the words "or bearer" or where the last indorsement is blank.
- Order Instrument: It is an instrument which is payable to a person or Payable to a person or his order or payable to order of a person or where the last indorsement is full

(2) Inland and Foreign Instruments (Section 11 & 12)

- Inland Instrument: Any instrument drawn or made in India and
  Either payable in or drawn upon any person resident in India shall be deemed to be an inland instrument.
- Foreign Instruments: Instrument which is not an inland instrument.

(3) Inchoate and Ambiguous Instruments:

- Inchoate Instrument (Section 20):
  It means an Instrument that is incomplete in certain respects.
  (i) The person gives a blank instrument with authority to the holder to complete it with appropriate amount up to the stamp value of the instrument.
  (ii) Delivery of such a paper is essential. The words "when one person signs and delivers to another" are important.
  (iii) The person signing and delivering the inchoate instrument is liable both to a holder and holder in due course. However, there is a difference in their respective rights. The holder of such an instrument cannot recover the amount in excess of the amount intended to be paid by the signor. The holder in due course can, how¬ever, recover any amount on such instrument provided it is covered by the stamp affixed on the instrument.
- Ambiguous Instrument:
  An instrument which is vague and cannot be clearly iden¬tified either as a bill of exchange, or as a promissory note, is an Ambiguous instrument. In other words, such an instrument may be construed either as prom¬issory note, or as a bill of exchange.

2.19: Dishonour of Cheque

- Dishonour of cheque for insufficiency, etc., of funds in the account (Section 138)

  Sections 138 provides for criminal penalties in the event of dishonour of cheques for insufficiency of funds.

  The drawer, under Sec. 138, may be punished with imprisonment upto 2 years or with a fine up to twice the amount of the cheque or with both.

  However, in order to attract the aforesaid penalties, following conditions must be satisfied:

  (1) The cheque should have been dishonoured due to insufficiency of funds in the account maintained by him with a banker for payment of any amount of money to another person from out of that account.
    (i) In case of stop-payment, it shall be deemed to have been so dishonoured for in¬sufficiency of funds unless stop-payment can be justified.
    (ii) Dishonour due to closure of account has also been held to be dishonoured for insufficiency of funds
    (iii) Directing the payee not to present will be deemed to have the same effect

  (2) The payment for which the cheque was issued should have been in discharge of a legally enforceable debt or liability in whole or part of it.

  (3) The cheque should have been presented within 3 months from the date on which it is drawn.

2.20: Presentment

Presentment for acceptance (Only for BOE)

↓

BOE payable after sight must	Must be presented within a reasonable time & in business hours on a business day. (Note: 48 hours, excluding public holidays, are given to drawee for acceptance)	
In default of such presentment	no party liable thereto	If Drawee not found after reasonable search, BOE is is dishonored.
If BOE is directed to drawee at a particular place	must be presented at that place	

Presentment of Promissory Note for sight

↓

P/N payable at a certain period after sight	Must be presented within a reasonable time & in business hours on a business day.
In default of such presentment	no party liable thereto

Rules regarding presentment for payment (P/N, BOE, CH):

To whom	Maker (P/N), Acceptor (BOE), Drawee (CH)
If default in presentment	no party liable thereto
Exception	If P/N is payable on demand and is not payable at a specified place, no presentment is necessary.
Time	During usual business hours
If instrument payable after date or sight	must be presented for payment at maturity
P/N payable by instalments	must be presented for payment on 3rd day after date fixed for payment of each instalment
instrument payable at specified place	Must be presented for payment at that place.
where no exclusive place specified	must be presented for payment at the place of business (if any) or at the usual residence
no known place of business or residence	presentment may be made to him in person wherever he can be found
Instrument payable on demand	Must be presented for payment within a reasonable time after it is received by the holder Note: Delay in presentment for acceptance or payment is excused if the delay is caused by circumstances beyond the control of the holder

2.21 RULES OF COMPENSATION:

Rules as to Compensation (Sec.117)	In case of dishonour of NI, holder can claim: 1. Amount due on NI 2. Expenses incurred in presenting, noting & protesting. 3. Interest 18% p.a. from due date of payment to date of realisation. Note: In case of foreign currency, current rate of exchange.

LIST OF LEGAL TERMS

SR. NO.	LEGAL WORD	MEANING	PG NO. (This column is to be filled by students)
1	Rebuttable by evidence to the contrary	The fact given can be proved wrong by giving with evidence	