

**CA FOUNDATION**



**MARATHON**

**JUNE 2024**

**Business Laws**



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# *Chapter Name*

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**Indian Contract Act**



# Basics

Offer

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Acceptance

Agreement

Every promise or Set of promise forming consideration for each other Sec. 2(e)

Enforceable by law

Contract (Commercial agreement) [Sec. 2h]

Not enforceable by law

Social / Agreement domestic Religious (Not contract because there is no intention to create legal relationship )

## Difference between Agreement and Contract

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

# Types of contract

## Creation

1. **Expressed contract**  
Oral or written
2. **Implied Contract**
  - Otherwise than express
  - Tacit or quasi
3. **E-Contract**  
Via Internet

## Validity

1. **Valid Contract**
2. **Void ab initio contract/ void agreement**
3. **Void contract**
4. **Voidable contract**
5. **Illegal agreement**
6. **Unenforceable contract**

## Performance

1. **Executed contract**
2. **Executory contract**
  - a) **Unilateral contract**
  - b) **Bilateral contract**

## English law

1. **Formal contract**
  - a) **Contract of Record**
  - b) **Contract under seal**
2. **Simple contract**

# Question

State which of the following agreements are valid contract under the Indian Contract Act, 1872?

- (a) A, who owns two cars is selling red car to B. B thinks he is purchasing the black car.
- (b) A threatened to shoot B if he (B) does not lend him ₹2,00,000 and B agreed to it.
- (c) A agrees to sell his house to B against 100 kgs of cocaine (drugs).
- (d) A ask B if he wants to buy his bike for ₹ 50,000. B agrees to buy bike.
- (e) Mr. X agrees to write a book with a publisher. But after few days, X dies in an accident.

[RTP June 2023]

# Answer

- (a) A, who owns two cars is selling red car to B. B thinks he is purchasing the black car. There is no consensus ad idem and hence not a valid contract.
- (b) A threatened to shoot B if he (B) does not lend him ₹2,00,000 and B agreed to it. Here the agreement is entered into under coercion and hence not a valid contract.
- (c) A agrees to sell his house to B against 100 kgs of cocaine (drugs). Such agreement is illegal as the consideration is unlawful.
- (d) A ask B if he wants to buy his bike for ₹ 50,000. B agrees to buy bike. It is agreement which is enforceable by law. Hence, it is a valid contract.
- (e) Mr. X agrees to write a book with a publisher. But after few days, X dies in an accident. Here the contract becomes void due to the impossibility of performance of the contract.



## Question

**Distinguish between Void Contract and Voidable Contract according to the Indian Contract Act, 1872.**

**[June 2023 (5 Marks)]**



# Answer

**The differences between void contract and voidable contract are as follows:**

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

# Question

29. Mr. Y is a devotee and wants to donate an elephant to the temple as a core part of ritual worship. He contacted Mr. X who wanted to sell his elephant. Mr. X contracted with Mr. Y to sell his elephant for ₹ 20 Lakhs. Both were unaware that the elephant was dead a day before the agreement. Referring to the provisions of the Indian Contract Act, 1872, explain whether it is a void, voidable or a valid contract.

[RTP Nov 2022]

# Answer

As per Section 2(j) of the Indian Contract Act, 1872 a contract which ceases to be enforceable by law becomes void when it ceases to be enforceable. The fact of impossibility may be known or unknown to the promisor or promisee.

It may be added by clarification here that the term “contract” shall be understood as an “agreement”.

Thus, when the parties agree on doing something which is obviously impossible in itself the agreement would be void.

In this case, Mr. X and Mr. Y were ignorant of the fact that the elephant was dead and therefore the performance of the contract was impossible from the very start (impossibility ab initio).

Hence, this contract is void being not enforceable by law.

# Question

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

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

**(b) Obligation of finder of lost goods to return them to the true owner.**

**(c) A contract with B (owner of the factory) for the supply of 10 tons of sugar, but before the supply is affected, the fire caught in the factory, and everything was destroyed. [MTP Nov 2022(4 Marks)]**

# Answer

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

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

(b) Obligation of finder of lost goods to return them to the true owner cannot be said to arise out of a contract even in its remotest sense, as there is neither offer and acceptance nor consent. These are said to be quasi-contracts.

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

(c) The above contract is a void contract.

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

## Essentials of a valid contract

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

# Types of offer

## 1. General offer:

- offer made to public at large
- anyone performing the conditions of the offer can be considered to have accepted the offer.
- **Case Law: Carlill Vs. Carbolic Smoke Ball Co. (1893)**

## 2.Special/specific offer:

- offer made to a specific or an ascertained person
- can be accepted only by that specified person to whom the offer has been made

## 3.Cross offer:

- identical offers in ignorance at the time of each other's offer,
- There is no binding contract in such a case

## 4.Counter offer:

- When the offeree offers to qualified acceptance of the offer subject to modifications and variations in the terms of original offer
- Counter-offer amounts to rejection of the original offer. It is also called as Conditional Acceptance.

## 5.Standing or continuing or open offer:

An offer remain open for acceptance over a period of time



# Offer and Acceptance

Offer + Acceptance = Agreement

Valid Offer + Valid Acceptance = Contract

## Rules regarding valid offer Sec 2(a)

1. May be expressed or implied
  2. May be specific or general
  3. Made with a view to create legal relationship (Balfour vs Balfour)
  4. must be made with a view to obtaining the assent of the other party
  5. Offer must be communicated to the offeree [Lalman Shukla vs Gauri Dutt]
  6. Certain, definite and not vague
  7. May be conditional
  8. Should not contain a term non compliance of which will amount to be acceptance
  9. A statement of price is not an offer [Harvey vs Facey]
  10. Offer should be distinguished from invitation to offer
- Examples →

## Rules for valid Acceptance Sec 2(b)

1. Absolute and unqualified [Neale vs. Merret]
2. Given by person to whom offer is made
3. The acceptance must be communicated Brogden vs. Metropolitan Railway Co. (1877)
4. must be in the prescribed mode
5. Given within fixed time before offer lapses
6. Mere silence is not acceptance
7. Rejected offer can be accepted only when it is renewed

1) Catalogue of goods 2) Tender 3) Prospectus 4) Menu Card 5) Newspaper Advertisement

# Question

3. A mobile phone was displayed in a shop with a price tag of ₹10,000 attached to the mobile display box. As the price displayed was very less as compared to M.R.P. of the mobile phone, Y, a customer rushed to the cash counter and asked the shopkeeper to receive the payment and pack up the mobile phone. The shopkeeper refused to hand over the mobile phone to Y in consideration of the price indicated in the price tag attached to the mobile phone. Y seeks your advice whether he can sue to shopkeeper for the above cause under the Indian Contract Act, 1872.

[Dec 2023 (3 Marks)]

# Answer

**An invitation to offer is different from offer. Quotations, menu cards, price tags, advertisements in newspaper for sale are not offer. These are merely invitations to public to make an offer. An invitation to offer is an act precedent to making an offer.**

**Acceptance of an invitation to an offer does not result in the contract and only an offer emerges in the process of negotiation.**

**In the instant case, Y reaches to shop and selects a Mobile Phone with a price tag of ₹ 10,000 but the shopkeeper refused to hand over the mobile phone to Y in consideration of the price indicated in the price tag attached to the mobile phone.**

**On the basis of above provisions and facts, the price tag with the Mobile Phone was not offer. It is merely an invitation to offer. Hence, it is Y who is making the offer and not the shopkeeper. Shopkeeper has the right to reject Y's offer. Therefore, Y cannot sue the shopkeeper for the above cause.**

# Question

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

# Answer

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

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

# Question

**Mr. Parth applied for a job as principal of a school. The school management decided to appoint him. One member of the school management committee privately informed Mr. Parth that he was appointed but official communication was not given by the school. Later, the management of the school decided to appoint someone else as a principal. Mr. Parth filed a suit against the school for cancellation of his appointment and claimed damages for loss of salary. State with reasons, will Mr. Parth be successful in suit filed against school under the Indian Contract Act, 1872? (RTP June 2024)**

**Hint – No as acceptance not communicated by offerree**

# Consideration

## Basics

- Sec 2(d)
- “When at the desire of the promisor, the promisee or any other person has done or abstained from doing, or does or abstains from doing or promises to do or abstain from doing something, such an act or abstinence or promise is called consideration for the promise”.

## Legal Rules

1. Must move at desire of Promisor.
2. Move from Promisee or any other person. [Chinnayya vs. Ramayya (1882)]
3. Executed and executory consideration
4. May be past, present or Future.
5. Need not be adequate.
6. Must be real and not illusory
7. something a party is not already bound by law to perform.
8. Must not be illegal, Immoral or opposed to Public policy

## Exception to-No-Consideration No Contract

See Next Slide



## Question

**48. Define consideration. State the characteristics of a valid consideration under the Indian Contract Act, 1872.**

**[MTP Apr 2023(5 Marks)]**

CAWALLAH

## Question

**44. “To form a valid contract, consideration must be adequate”.**

**Comment.**

**[MTP Nov 2022(3 Marks)]**

# Answer

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

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

# Exception to –No-consideration No Contract(sec 25)

## 1. Love and affection

- a) out of natural love and affection
- b) Near Relation
- c) Written & Registered

## 2. Compensate past voluntary service

## 3. Pay Time barred debt

- a) Written
- b) Signed by debtor or agent

## 4. Gift

Written & Registered

## 5. Remission

## 6. Charity

To extent of Liability incurred

## 7. Special Contracts

- a) Bailment
- b) Agency
- c) Guarantee

## 8. Contract Under Seal

## Question

**"The general rule is that an agreement made without consideration is void." State the exceptions of this general rule as per the Indian Contract Act, 1872.**

**[May 2022 (7 Marks)]**

# Question

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

[RTP June 2023]

# Answer

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

**In the given problem, the transfer of house made by Mr. Shyam Mundra on account of natural love and affection between the parties standing in near relation to each other is written but not registered. Hence, this transfer is not enforceable.**

**Note – Alternatively you can also solve question through Completed gift provision**



# Question

**11. Explain the following statements in the light of provisions of Indian Contract Act, 1872:**

**(i) "Agreements made out of love and affection are valid agreements."**

**(ii) "Promise to pay a time barred debt cannot be enforced."**

**[Nov. 2022 (7 Marks)]**

# Answer

**(i) Agreements made out of love and affection are valid agreements: A written and registered agreement based on natural love and affection between the parties standing in near relation (e.g., husband and wife) to each other is enforceable even without consideration. The various conditions to be fulfilled as per Section 25(1) of the Indian Contract Act, 1872:**

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

**Hence, the agreements made out of love and affection, without consideration, shall be valid, if the above conditions are fulfilled.**

**(ii) Promise to pay a time barred debt cannot be enforced: According to Section 25(3) of the Indian Contract Act, 1872, where a promise in writing signed by the person making it or by his authorised agent, is made to pay a debt barred by limitation is valid without consideration.**

**Hence, this statement is not correct.**

**Note: The above statement can be correct also on the basis of the “Discharge of Contract by Lapse of time” as per Limitation Act, 1963, and accordingly it can be mentioned that contract should be performed within a specified period as prescribed by the Limitation Act, 1963 and if no action is taken by the promisee within the specified period of limitation, he is deprived of remedy at law.**

# Doctrine of Privity of Contract



Only a person who is party to a contract can sue on it. Stranger to contract cannot sue



Exception (Shortcut – BF ki MAACC)



1. Beneficiary of trust [Chinnayya vs Ramayya]
2. Family / → Writing
3. Marriage Settlement
4. Assignment of Contract
5. Acknowledgement of Liability/Estoppel
6. Contract through agent
7. Covenants running with land.

## Question

**7. As per the general rule, "Stranger to a contract cannot file a suit in case of breach of contract". Comment and explain the exceptions to this rule as per the provisions of the Indian Contract Act, 1872.**

**[June 2023 (7 Marks)]**

# Answer

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

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

1. In the case of trust, a beneficiary can enforce his right under the trust, though he was not a party to the contract between the settler and the trustee.
2. In the case of a family settlement, if the terms of the settlement are reduced into writing, the members of family who originally had not been parties to the settlement, may enforce the agreement.
3. In the case of certain marriage contracts/arrangements, a provision may be made for the benefit of a person, who may file a suit though he is not a party to the agreement.
4. In the case of assignment of a contract, when the benefit under a contract has been assigned, the assignee can enforce the contract but such assignment should not involve any personal skill.
5. Acknowledgement or estoppel – Where the promisor by his conduct acknowledges himself as an agent of the third party, it would result into a binding obligation towards third party.
6. In the case of covenant running with the land, the person who purchases land with notice that the owner of land is bound by certain duties affecting land, the covenant affecting the land may be enforced by the successor of the seller.
7. Contracts entered into through an agent: The principal can enforce the contracts entered by his agent where the agent has acted within the scope of his authority and in the name of the principal.

# Capacity to Contract

## Following are incompetent to contract

**Minor: Sec.3 Indian Majority Act, 1875: Minor who is under 18 years.**

1. Agreement with or by minor is void-ab-initio agreement ***Mohori Bibi vs. Dharmo Das Ghose (1903)***
2. Cannot be ratified on attaining majority.
3. Minor can be a beneficiary or can take benefit out of a contract.
4. Minor can always plead minority.
5. Minor's estate is liable for necessities.
6. Minor is personally liable for contracts for his benefit or supply of necessities entered by guardian within scope of authority.
7. No specific performance can be claimed.
8. Minor cannot be adjusted insolvent.
9. Minor cannot enter into partnership.

10. Minor can be an agent without incurring any personal liability.
11. Parents/guardians are not liable for the contract entered into by him.
12. In case of joint contract by adult and minor, only adult is liable.
13. If adult is surety for minor, adult is liable as direct contract between adult and third party.
14. Shares cannot be allotted to minor but minor can become a shareholder by transfer or transmission of fully paid shares to him.
15. Minor is Liable for torts.

1. Contract with person of unsound mind is void.
2. Person usually Unsound. sometimes sound - can contract when sound.
3. Person usually sound. sometimes unsound - cannot contract when unsound.

### **Disqualified by Law**

1. Foreign sovereigns (Rulers)
2. Alien Enemy
3. Corporations
4. Convicts.

## Question

**32. “Though a minor is not competent to contract, nothing in the Contract Act prevents him from making the other party bound to the minor”. Discuss.**

**[RTP Nov 2022]**

CAWALLAH



# Question

16. Srishti, a minor, falsely representing her age, enters into an agreement with an authorised Laptop dealer Mr. Gupta, owner of SP Laptops, for purchase of Laptop on credit amounting ₹ 60,000/- for purchasing a laptop, on 1st August 2021. She promised to pay back the outstanding amount with interest @ 16% p.a. by 31st July 2022. She told him that in case she won't be able to pay the outstanding amount, her father Mr. Ram will pay back on her behalf. After One year, when Srishti was asked to pay the outstanding amount with interest she refused to pay the amount and told the owner that she is minor and now he can't recover a single penny from her.

She will be adult on 1st January 2024, only after that agreement can be ratified. Explain by which of the following way Mr. Gupta will succeed in recovering the outstanding amount with reference to the Indian Contract Act, 1872.

- (i) By filing a case against Srishti, a minor for recovery of outstanding amount with interest?
- (ii) By filing a case against Mr. Ram, father of Srishti for recovery of outstanding amount?
- (iii) By filing a case against Srishti, a minor for recovery of outstanding amount after she attains maturity?[RTP Dec 2023][May 2022 (6 Marks)]

# Answer

**A contract made with or by a minor is void ab-initio: Pursuant to Section 11, a minor is not competent to contract and any agreement with or by a minor is void from the very beginning.**

**(i) By following the above provision, Mr. Gupta will not succeed in recovering the outstanding amount by filing a case against Srishti, a minor.**

**(ii) Minor cannot bind parent or guardian: In the absence of authority, express or implied, a minor is not capable of binding his parent or guardian, even for necessaries. The parents will be held liable only when the child is acting as an agent for parents.**

**In the instant case, Mr. Gupta will not succeed in recovering the outstanding amount by filing a case against Mr. Ram, father of Srishti.**

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

**Hence, in this case also, Mr. Gupta will not succeed in recovering the outstanding amount by filing a case against Srishti, after she attains majority.**

# Question

Mr. Mukund wants to sell his car. For this purpose, he appoints Mr. Parth, a minor as his agent. Mr. Mukund instructs Mr. Parth that car should not be sold at price less than ₹ 2,00,000. Mr. Parth ignores the instruction of Mr. Mukund and sells the car to Mr. Naman for ₹ 1,50,000. Explain the legal position of contract under Indian Contract Act, 1872 whether:

- (a) Mr. Mukund can recover the loss of ₹ 50,000 from Mr. Parth?
- (b) Mr. Mukund can recover his car from Mr. Naman?

[RTP June 2023]

# Answer

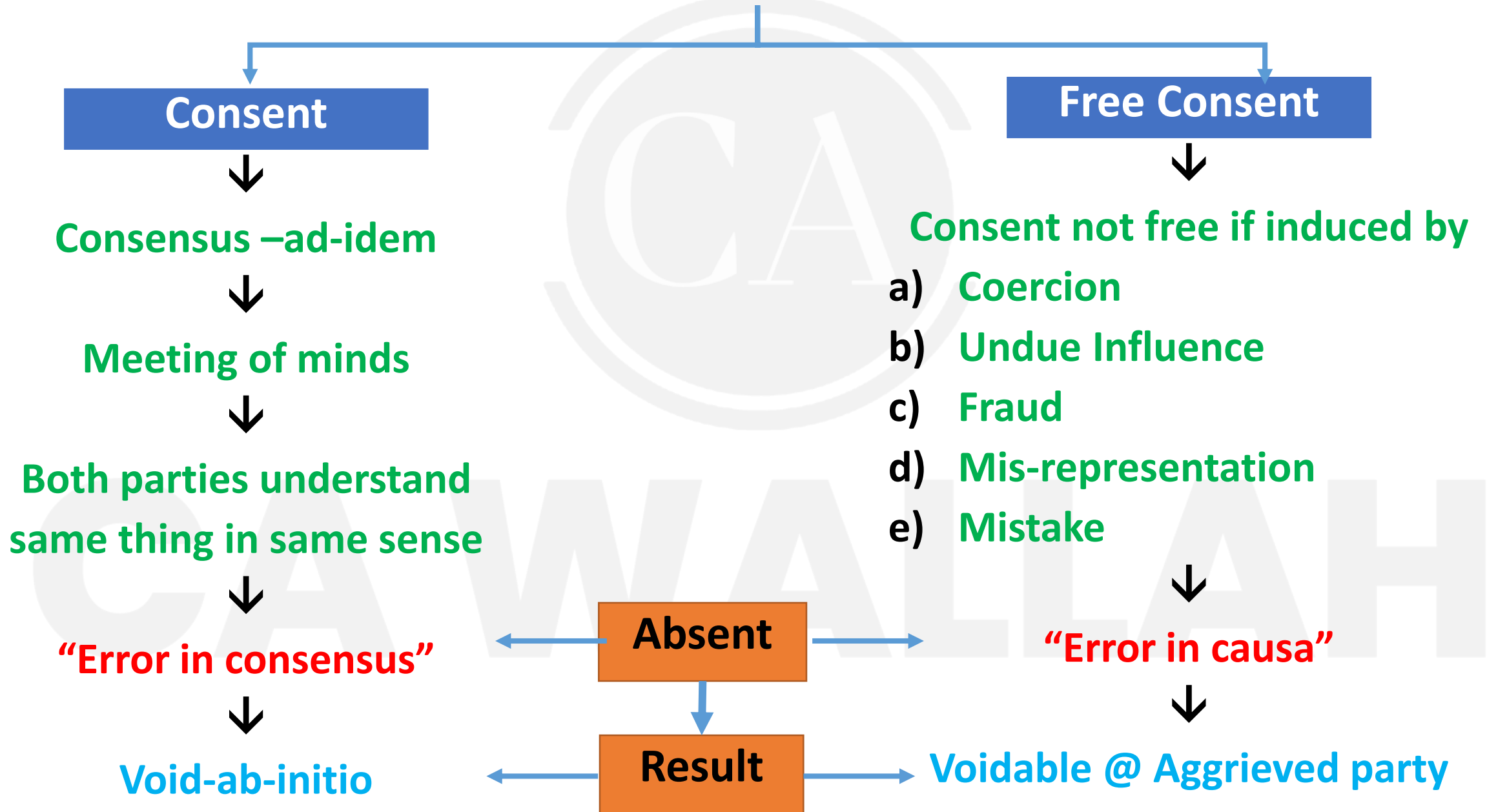
According to the provisions of Section 11 of Indian Contract Act, 1872, a minor is disqualified from contracting. A contract with minor is void-ab-initio but minor can act as an agent. But he will not be liable to his principal for his acts.

In the instant case, Mr. Mukund appoints Mr. Parth, a minor as his agent to sale his car. Mr. Mukund clearly instructed to Mr. Parth that the minimum sale price of the car should be ₹ 2,00,000 yet Mr. Parth sold the car to Mr. Naman for ₹ 1,50,000.

(a) Considering the facts, although the contract between Mr. Mukund and Mr. Parth is valid, Mr. Parth will not be liable to his principal for his acts. Hence, Mr. Mukund cannot recover the loss of ₹ 50,000.

(b) Further, Mr. Naman purchased the car from agent of Mr. Mukund, he got good title. Hence, Mr. Mukund cannot recover his car from Mr. Naman.

# Free Consent



# Question

**Mr. Joy owns two flats in a building. He wanted to sell flat no.101 to Mr. Roy. Mr. Joy offered to sell his flat no. 101 to Mr. Roy, but Mr. Roy thought that Mr. Joy wanted to sell flat no. 102 and said yes for the agreement. Considering the provisions of Indian Contract Act, 1872, discuss the validity of such a contract.**

**[MTP Jun 2022(4 Marks)]**

# Answer

Section 10 of Indian Contract Act, 1872 laid down the essential elements of a valid contract. One of the essential elements of valid contract is free consent. Consent is an express willingness or giving voluntary permission or agreeing to something. Section 13 further clarifies "two or more persons are said to consent when they agree upon the same thing in the same sense".

In the present case, both the parties have given a free consent but they are not consenting for the same thing in the same sense. Mr. Joy wants to sell flat no. 101 and Mr. Roy has agreed the contract thinking that it's flat no. 102.

Hence, the agreement would be invalidated at the inception (beginning) stage itself because both the parties did not agree about a thing (sale of flat) in the same sense. Hence, both the parties did not have mutual consent for the contract; therefore it is not a valid contract.

# Coercion Sec 15

## Meaning

- a. Committing or
  - b. Threaten to commit
  - c. Detaining or
  - d. Threaten
- Act forbidden by IPC
- Person or property

## Effect

- Contract voidable
- Person to whom money is paid or thing delivered under coercion must repay or return it.
- Burden of Proof
  - Lies on the aggrieved party

## Other Imp Pts.

1. IPC → May or May not → be in force
2. Threaten to commit suicide is coercion, not undue influence



# QUESTION

**Explain the term "coercion" and describe its effect on the validity of a contract?**

**(RTP MAY 2018)**

# Undue Influence sec 16

## Meaning

Party in position to dominate will of other

1. Real or Apparent Authority

2. Fiduciary Relation

3. Age, illness, mental / body distress

+

Uses position to take unfair Advantage in contract

## Effect

- Contract voidable
- Set aside contract absolutely or T&C as court may deems fit
- Restitution of benefit allowed
- Burden of proof



Defendant party

## Other Imp Pts.

1. Pardanashin women & unconscionable bargain → law presumes undue influence
2. Loan at higher rate due to market → no undue influence
3. Undue influence not presumed
  - a) Husband & wife
  - b) Debtor & Creditor
  - c) Landlord & Tenant
  - d) Principal & Agent

# Question

**8. Mr. A, the employer induced his employee Mr. B to sell his one room flat to him at less than the market value to secure promotion. Mr. B sold the flat to Mr. A. Later on, Mr. B changed his mind and decided to sue Mr. A. Examine the validity of the contract as per the provisions of the Indian Contract Act, 1872. [June 2023 (2 Marks)]**

Mr. Ayush, the employer induced his employee Mr. Bobby to sell his one room flat to him at less than the market value to secure promotion. Mr. Bobby sold the flat to Mr. Ayush. Later on, Mr. Bobby changed his mind and decided to sue Mr. Ayush. Examine the validity of the contract as per the provisions of the Indian Contract Act, 1872. **(RTP June 2024)**

# Answer

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

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

Hence, the contract between Mr. A and Mr. B is voidable at the option of Mr. B as it was induced by undue influence by Mr. A and therefore Mr. B can sue Mr. A.

# Question

**30. In the light of the provisions of the Indian Contract Act, 1872, answer the following:**

**(i) A student was induced by his teacher to sell his brand-new bike to the latter at a price less than the purchase price to secure more marks in the examination. Accordingly, the bike was sold. However, the father of the student persuaded him to sue his teacher. Whether the student can sue the teacher? If yes, on what grounds?**

**(ii) Give the circumstances as to when “Vindictive or Exemplary Damages” may be awarded for breach of a contract.**

**[RTP Nov 2022]**

# Answer

(i) A contract brought as a result of coercion, undue influence, fraud or misrepresentation would be voidable at the option of the person whose consent was caused. The relation of teacher and student is as such that the teacher is in a position to dominate the will of the student. As a result, the consent of the student is caused by an undue influence. Hence, the contract between them is voidable at the option of the student, and therefore, he can sue the teacher.

(ii) Vindictive or Exemplary damages

These damages may be awarded only in two cases:

(a) for breach of promise to marry because it causes injury to his or her feelings; and

(b) for wrongful dishonour by a banker of his customer's cheque because in this case the injury due to wrongful dishonour to the drawer of cheque is so heavy that it causes loss of credit and reputation to him.

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

# Question

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

[RTP May 2022]

# Answer

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

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

- (a) where he holds a real or apparent authority over the other, or
- (b) where he stands in a fiduciary relation to the other; or
- (c) where he makes a contract with a person whose mental capacity is temporarily or permanently affected by reason of age, illness, or mental or bodily distress.

Section 19A provides that when consent to an agreement is caused by undue influence, the agreement is a contract voidable at the option of the party whose consent was so caused. Any such contract may be set aside either absolutely or, if the party who was entitled to avoid it has received any benefit thereunder, upon such terms and conditions as to the Court may seem just.

From the facts of the case, Chandan signed the promissory note under undue influence applied by doctor. Hence, Dr. Jhunjhunwala cannot recover the amount of promissory note but can claim his normal consultation fee from Chandan.



# Diff between Coercion & Undue influence

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

# Fraud(sec 17 )

## Meaning

1. False Statement
2. Active concealment
3. Promise made without intention to perform
4. Any other act of deceit
5. Any law specifically declare it

## Effect

- Contract voidable
- Can rescind the contract on insist to continue if puts in better position
- Can also claim damages
- If party takes any benefit, contract is not voidable.

## Other Imp Pts.

### 1. Essential Element

Representation related to Material fact/Intention to deceive /with knowledge of falsity / Other person induce /relied on fact /other party suffered loss

1. Mere silence not fraud except
  - a) Duty to speak (e.g insurance , marriage , family settlement ,share allotment )
  - b) Silence equivalent to speech
2. Person making statement does not believe it to be true
3. Fraud even if party discover → ordinary diligence

# Question

**31. Karan agreed to purchase wooden table for his study room from Mr. X. Table was in good condition and was examined by Karan before purchasing. He found no defects in it and paid ₹ 20,000 for that table. Later on, it was found that one leg of table is broken, and Mr. X has pasted the wood and tried to hide the defects in the table. Can Karan return the table and claim the amount back? Discuss the same with reference to Indian Contract Act, 1872.**

**[RTP Nov 2022]**

# Answer

As per Section 17 of Indian Contract Act, 1872, “A false representation of material facts when made intentionally to deceive the other party to induce him to enter into a contract is termed as a fraud.” Section 17(2) further states about active concealment. When a party intentionally conceals or hides some material facts from the other party and makes sure that the other party is not able to know the truth, in fact makes the other party believe something which is false, then a fraud is committed.

In case a fraud is committed, the aggrieved party gets the right to rescind the contract. (Section 19).

In the present case, Karan has examined the study table before purchasing it from Mr. X and could not find any defect in the table as it was concealed by Mr. X.

On the basis of above provisions and facts of the case, Karan can rescind the contract and claim compensation for the loss suffered due to fraud done by Mr. X.

## Question

**“Mere silence does not amount to fraud”. Explain the statement as per the provisions contained in the Indian Contract Act, 1872.**

**[Dec 2023(5 Marks)]**

CAWALLAH

# Answer

**Mere silence not amounting to fraud: Mere silence as to facts likely to affect the willingness of a person to enter into a contract is no fraud; but where it is the duty of a person to speak, or his silence is equivalent to speech, silence amounts to fraud.**

**It is a rule of law that mere silence does not amount to fraud. A contracting party is not duty bound to disclose the whole truth to the other party or to give him the whole information in his possession affecting the subject matter of the contract.**

**The rule is contained in explanation to Section 17 of the Indian Contract Act which clearly states the position that mere silence as to facts likely to affect the willingness of a person to enter into a contract is not fraud.**

**Exceptions to this rule:**

- (i) Where the circumstances of the case are such that, regard being had to them, it is the duty of the person keeping silence to speak. Duty to speak arises when one contracting party reposes trust and confidence in the other or where one party has to depend upon the good sense of the other (e.g. Insurance Contract).**
- (ii) Where the silence is, in itself, equivalent to speech.**

# Mis-representation (sec 18 )

## Meaning

1. (i) False statement but maker believes it to be true.
2. (ii) Breach of duty without any intention to deceive.
3. (iii) Mis-representation even made innocently, the other party has actually acted.

## Effect

- Contract voidable
- Party can
  - ✓ · rescind the contract.
  - ✓ · insist for genuine performance.
- Burden of proof



**Aggrieved party**

## Other Imp Pts.

1. Representation made is untrue but person believe it to be true
2. No intention to deceive
3. Party cannot avoid contract if it can discover truth with ordinary diligence

# Fraud vs Misrepresentation

Basis of difference	Fraud	Misrepresentation
Intention	To deceive the other party by hiding the truth.	There is no such intention to deceive the other party.
Knowledge of truth	The person making the suggestion believes that the statement as untrue.	The person making the statement believes it to be true, although it is not true.
Rescission of the contract and claim for damages	The injured party can repudiate the contract and claim damages.	The injured party is entitled to repudiate the contract or sue for restitution but cannot claim the damages.
Means to discover the truth	The party using the fraudulent act cannot secure or protect himself by saying that the injured party had means to discover the truth.	Party can always plead that the injured party had the means to discover the truth.



# Mistake is an erroneous belief about something

## Mistake

### Mistake of Fact

### Mistake of Law

Unilateral	Bilateral	Law of Land	Foreign Law
<p>(a) Only one party is under a mistake about—</p> <ul style="list-style-type: none"> <li>• Subject matter, or</li> <li>• Expressing or understanding terms or legal effect of agreement.</li> </ul> <p>(a) Sec. 21: Contract is not voidable</p> <p>(b) Unilateral mistake is not allowed as a defense to avoid a Contract.</p> <p>(c) However, Contract under unilateral mistake are void in certain cases. [See cease below]</p>	<p>(a) Sec.20: Both parties are under a mistake as to a matter of fact essential to the agreement.</p> <p>(b) There is no agreement as there is absence of consensus. Hence, the agreement is void.</p> <p>(c) Bilateral Mistake may relate to —</p> <p>Subject Matter-</p> <ul style="list-style-type: none"> <li>• Existence</li> <li>• Identity</li> <li>• Quantity</li> <li>• Quality</li> <li>• Title</li> </ul> <p>Possibility of Performance</p>	<p>(a) Ignorantia Juris non excusat, i.e. Ignorance of law of land is not excuse.</p> <p>(b) Such Mistake will not affect the validity of the Contract.</p> <p>(c) Sec. 21: Contract is not voidable.</p> <p>(d) Example: A and B make a Contract on erroneous belief that a particular debt is time barred by Indian Law of Limitation. Contract is valid &amp; not voidable.</p>	<p>Sec 21</p> <p>(a) A person should be well verse with law of land i.e. Indian Law.</p> <p>(b) When it comes to foreign law we expect that person cannot have knowledge of foreign law and since foreign law is not applicable to us mistake of foreign law is treated as mistake of fact and contract is void ab initio</p>

## UNLAWFUL OBJECT AND CONSIDERATION (Sec.23)

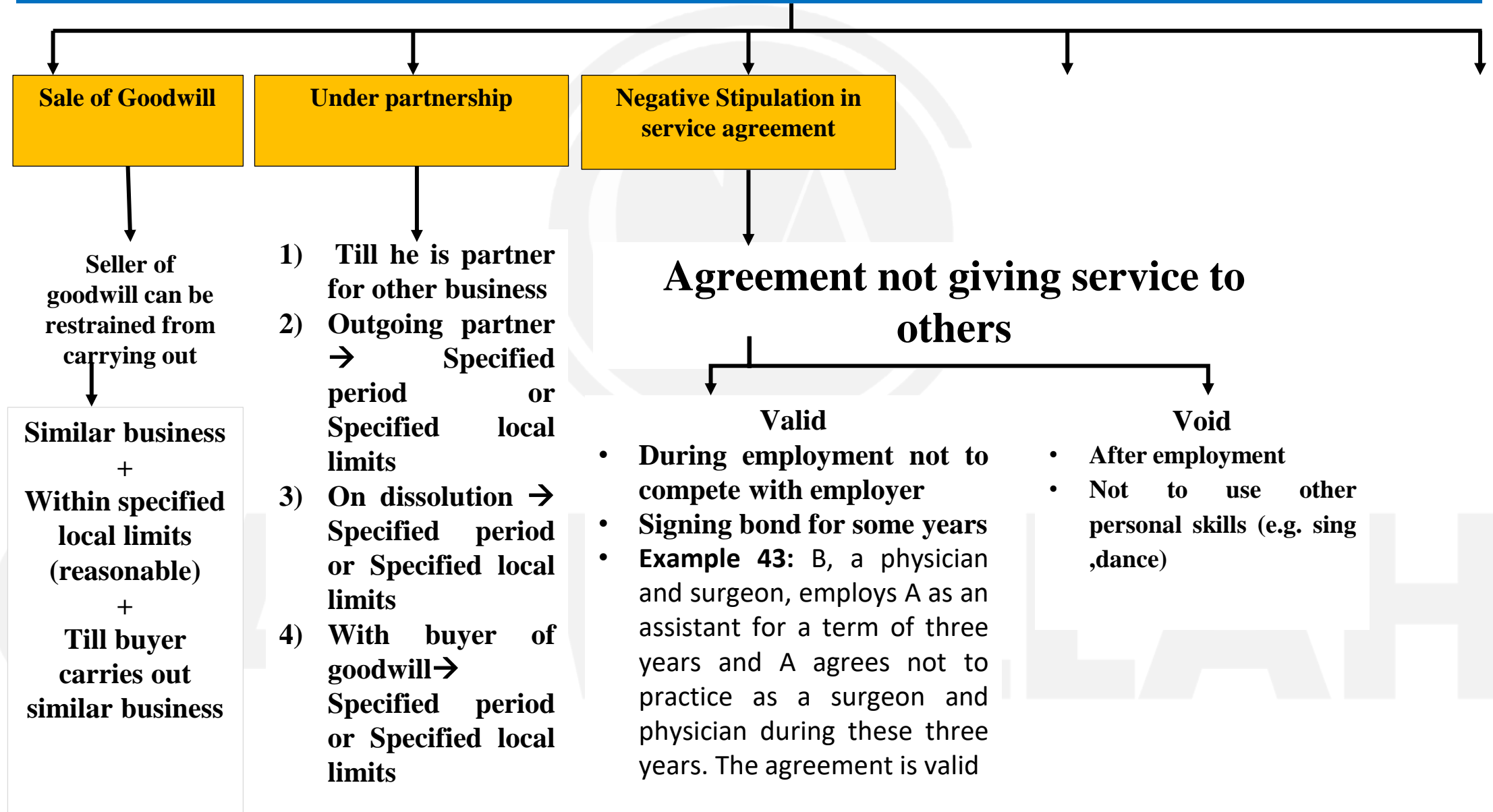
If consideration or object forbidden by law	When consideration or object is of such a nature that if permitted it would defeats provisions of law	When it is fraudulent	When consideration involves injury to person or property of another	When consideration is immoral	When consideration is opposed to public policy
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Agreements of trading with enemy	Trafficking relating to Public Offices & titles.	Interference with the course of justice
Agreement of stifling prosecution	Agreements tending to create monopolies	Interest against obligation
Maintenance & champerty	Marriage brokerage agreements	Consideration unlawful in part

## VOID AGREEMENTS

Made by Incompetent Parties(S.11)	Without consideration (S.25)	With uncertain meaning (S.29)
Under a mutual mistake of fact (S.20)	In restraint of marriage (S.26) except <b>minor</b>	Wagering Agreements (S.30)
Unlawful consideration or object (S.23)	In restraint of trade (S.27)	To do impossible act (S.56)
Unlawful consideration or object in part(S.24)	In restraint of legal proceedings (S.28)	

# Exception to rule – All agreement in restraint of trade are void



# Question

**23. Kashish was running a business of artificial jewellery since long. He sold his business to Naman and promises, not to carry on the business of artificial jewellery and real diamond jewellery in that area for a period of next one year. After two months, Kashish opened a show room for real diamond jewellery. Naman filed a suit against Kashish for closing the business of real diamond jewellery business as it was against the agreement. Whether Kashish is liable to close his business of real diamond jewellery following the provisions of Indian Contract Act, 1872? (MTP Apr. 24) (7 Marks)**

# Question

23. Mr. Seth (an industrialist) has been fighting a long-drawn litigation with Mr. Raman (another industrialist). To support his legal campaign, Mr. Seth enlists the services of Mr. X, a legal expert stating that an amount of ₹ 5 lakhs would be paid, if Mr. X does not take up the case of Mr. Raman. Mr. X agrees, but at the end of the litigation, Mr. Seth refused to pay. Decide whether Mr. X can recover the amount promised by Mr. Seth under the provisions of the Indian Contract Act, 1872.

[RTP Dec 2023]

# Answer

According to Section 27 of Indian Contract Act, 1872 an agreement by which any person is restrained from exercising a lawful profession, trade or business of any kind, is to that extent void.

In the instant case, Mr. Seth is in litigation with Mr. Raman since long. Mr. Seth enlists the services of Mr. X a legal expert stating that an amount of ₹ 5 lakhs would be paid, if Mr. X does not take up the case of Mr. Raman. Mr. X agrees, but at the end of the litigation, Mr. Seth refused to pay.

As section 27 makes the contracts in restraint of trade, void, the contract between Mr. Seth and Mr. X is also void. Hence, Mr. X cannot recover the amount promised by Mr. Seth.

# Question

Mukesh is running a grocery store in Delhi. He sells his grocery business, including goodwill worth ₹1,00,000 to Rohit for a sum of ₹ 5,00,000. After the sale of goodwill, Rohit made an agreement with Mukesh. As per this agreement, Mukesh cannot open another grocery store (similar kind of business) in the whole of India for next ten years. However, Mukesh opens another store in the same city two months later. What are the rights available with Rohit regarding the restriction imposed on Mukesh with reference to Indian Contract Act, 1872?

[RTP June 2023]



# Answer

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

- (i) Where the restraint is to refrain from carrying on a similar business,
- (ii) The restraint should be within the specified local limits,
- (iii) The restraint should be not to carry on the similar business after sale of goodwill to the buyer for a price,
- (iv) The restriction should be reasonable. Reasonableness of restriction will depend upon number of factors as considered by court.

In the given case, Mukesh has sold the goodwill and there is restraint for not carrying on the same business of grocery store. However, the restriction imposed on Mukesh is unreasonable as he cannot carry similar business in whole of India for next 10 years. The restriction on restraint to similar kind of trade should be reasonable to make it a valid agreement.

Hence, Rohit cannot take any legal action against Mukesh as the restriction is unreasonable as per Section 27 of Indian Contract Act, 1872. Hence, the agreement made between in restraint of trade between Mukesh and Rohit is void agreement.

## Question

**2. Explain the terms “Trafficking relating to public offices and titles” and “Stifling prosecution” as per the Indian Contract Act, 1872.**

**[Dec 2023 (7 Marks)]**

# Answer

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

- (1) An agreement to pay money to a public servant in order to induce him to retire from his office so that another person may secure the appointment is void.
- (2) An agreement to procure a public recognition like Padma Vibhushan for reward is void.

**Stifling Prosecution:** An agreement to stifle prosecution i.e. “an agreement to prevent proceedings already instituted from running their normal course using force” tends to be a perversion or an abuse of justice, therefore, such an agreement is void. The principle is that one should not make a trade of felony. The compromise of any public offence is generally illegal.

For example, when a party agrees to pay some consideration to the other party in exchange for the later promising to forgo criminal charges against the former is an agreement to stifle prosecution and therefore is void.

Under the Code of Criminal Procedure, there is however, a statutory list of compoundable offences and an agreement to drop proceeding relating to such offences with or without the permission of the Court, as the case may be, in consideration the accused promising to do something for the complainant, is not opposed to public policy.

# Question

**22. State with reason(s) whether the following agreements are valid or void as per the Indian Contract Act, 1872:**

**(i) Where two courts have jurisdiction to try a suit, an agreement between the parties that the suit should be filed in one of those courts alone and not in the other.**

**(ii) X offers to sell his Maruti car to Y. Y believes that X has only Wagon R Car but agrees to buy it.**

**(iii) X, a physician and surgeon, employs Y as an assistant on a salary of ₹ 75,000 per month for a term of two years and Y agrees not to practice as a surgeon and physician during these two years.**

**[RTP Dec 2023]**

# Answer

**(i) The given agreement is valid.**

**Reason:** An agreement in restraint of legal proceeding is the one by which any party thereto is restricted absolutely from enforcing his rights under a contract through a Court (Section 28 of the Indian Contract Act, 1872). A contract of this nature is void. However, in the given statement, no absolute restriction is marked on parties on filing of suit. As per the agreement, suit may be filed in one of the courts having jurisdiction.

**(ii) The said agreement is void.**

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

**(iii) The said agreement is valid.**

**Reason:** An agreement by which any person is restrained from exercising a lawful profession, trade or business of any kind, is to that extent void (Section 27). But, as an exception, agreement of service by which an employee binds himself, during the term of his agreement, not to compete with his employer is not in restraint of trade.

# Performance of Contract(sec 37)

[Obligation/Promise → Fulfill → Discharge]

**Actual Performance**

**Attempted /Tender Performance**

[Offer to Perform]

Conditions	Tender of Goods		Tender of Money	
	1. Unconditional 2. At proper time, proper place, to proper person, of proper Quantity, & in proper form 3. By able & willing person. 4. Seller should give sufficient time for inspection of goods	Obligation	✗	Obligation
	Rights	✓	Further Interest	✗

# Question

On 1st March 2023, T Readymade Dress Garments, Shimla enters into a contract with J Readymade Garments, Jaipur for the supply of different sizes of shirts 'S' (Small), 'M' (Medium), and 'L' (Large). As per the terms of the contract, 300 pieces of each category i.e. 'S' @ ₹900; 'M' @ 1,000 and 'L' @ 1,100 per piece have to be supplied on or before 31st May, 2023.

However, on 1st May, 2023, T Readymade Dress Garments, Shimla informed J Readymade Garments, Jaipur that the firm is not willing to supply the shirts at the above rate due to the rise of prices in the raw material cost. In the meantime, prices for similar shirts have gone up in the market to the tune of ₹ 1,000; ₹ 1,100; and ₹ 1,200 for 'S', 'M' and 'L' sizes respectively.

Examine the rights of J Readymade Garments, Jaipur in this regard as per the provisions of the Indian Contract Act, of 1872.

[Dec 2023(3 Marks)]



# Answer

As per the provisions of Section 39 of the Indian Contract Act, 1872, when a party to a contract has refused to perform, or disabled himself from performing, his promise in its entirety, the promisee may put an end to the contract, unless he has signified, by words or conduct, his acquiescence in its continuance.

J Readymade Garments in the given situation has two options, out of which he has to select any one:

- (i) Either to treat the contract as rescinded and sue T Readymade Dress Garments for damages from breach of contract immediately without waiting until the due date of performance or
- (ii) He may elect not to rescind but to treat the contract as still operative and wait for the time of performance and then hold the other party responsible for the consequences of non-performance.

**Important Note:** The answer can also be given as per Section 73 of the Indian Contract Act, 1872 which lays down that when a contract has been broken, the party who suffers by such breach is entitled to receive from the party who has broken the contract, compensation for any loss or damage caused to him thereby which naturally arose in the usual course of things from such breach or which the parties knew when they made the contract to be likely to result from the breach of it.

In the instant case, J Readymade Garments, Jaipur would be entitled to get the damages i.e. difference between the contract price and the market price on the day of default from T Readymade Dress Garments, Shimla. In other words, the amount of damages would be ₹ 90,000 [300 piece @ ₹ 100 (Small), 300 piece @ ₹ 100 (Medium) and 300 piece @ ₹ 100 (Large)].



# Question

14. Sheena was a classical dancer. She entered into an agreement with Shital Vidya Mandir for 60 dance performances. As per the contract, she was supposed to perform every weekend and she will be paid ₹ 10,000/- per performance. However, after a month, she was absent without informing, due to her personal reasons. Answer the following questions as per the Indian Contract Act, 1872.

(i) Whether the management of Shital Vidya Mandir has right to terminate the contract?

(ii) If the management of Shital Vidya Mandir informed Sheena about its continuance, can the management still rescind the contract after a month on this ground subsequently?

(iii) Can the Shital Vidya Mandir claim damages that it has suffered because of this breach in any of the above cases? [RTP Dec 2023][May 2022 (4 Marks)] [RTP May 2022] (RTP June 2024)

# Answer

Section 39 provides that when a party to a contract has refused to perform or disabled himself from performing his promise in its entirety the promisee may put an end to the contract unless he had signified, by words or conduct his acquiesce in its continuance. Further, in term of Section 40, the promisee shall be required to perform personally, if there is such an apparent intention of the parties.

Also, as per Section 75 of the Act, a person who rightfully rescinds a contract is entitled to compensation for any damage which he has sustained through non-fulfilment of the contract.

Therefore, in the instant case,

- (i) Since, Sheena could not perform as per the terms of contract, Shital Vidya Mandir can terminate the contract.
- (ii) In the second situation, the management of Shital Vidya Mandir informed Sheena about the continuance of the contract. Hence, the management cannot now rescind the contract after a month on this ground subsequently.
- (iii) As per Section 75, Shital Vidya Mandir can claim damages that it has suffered because of this breach in part (i).

# Who Can Perform...??

PROMISOR HIMSELF	AGENT OF PROMISOR	LEGAL HEIR	THIRD PERSON	JOINT PROMISOR (sec 42)
<p>↓</p> <p>Specially Personal Nature Contracts</p>	<p>↓</p> <p>He can perform contracts of impersonal Nature</p>	<p>↓</p> <p>On Death of Promisor</p> <p><b>Personal nature contracts</b></p> <p>↓</p> <p>Becomes void</p> <p><b>Impersonal Contracts</b></p> <p>↓</p> <p>Transfer to Legal Heir</p> <p>↓</p> <p>Liabe Subject to Such Amount of Property transferred</p>	<p>↓</p> <p>If accepted performance from 3<sup>rd</sup> party (Stranger)</p> <p>↓</p> <p>Then cannot ask again performance from promisor</p>	<p>↓</p> <ol style="list-style-type: none"> <li>Normally Contributes Equally</li> <li>If any promisor die, his LR will join</li> <li>Any deficit because of non transfer of property to L.R or if any party sets a limit → Borne by other Joint Promisors</li> <li>Every Joint Promisor are Jointly &amp; Severally liable</li> <li>If any joint Promisor was compelled to pay the entire amount</li> </ol> <p>↓</p> <p>He can afterwards take contribution from others</p> <ol style="list-style-type: none"> <li>If promisee release a joint promisor from his share(SEC 44)</li> </ol> <p>↓</p> <p>Remaining Joint Promisors shall pay the Balance amount But released promisee liable to make contribution to other promisors</p>

# Who Can Demand Performance ...??

PROMISOR HIMSELF	AGENT OF PROMISOR	LEGAL HEIR	THIRD PERSON	JOINT PROMISEE
<p>↓</p> <p>Specially Contracts of Personal Nature</p>	<p>↓</p> <p>He can ask performance</p> <p>↓</p> <p>impersonal Nature Contracts</p>	<p>↓</p> <p>On Death of Promisor</p> <p><b>Personal nature contracts</b></p> <p>↓</p> <p>Becomes void</p> <p><b>Impersonal Contracts</b></p>		<p>(Devolution of Joint Rights )</p> <p>↓</p> <p><b>Same as Before</b></p>

# Question

9. Mr. S promises Mr. M to paint a family picture for ₹ 20,000 and assures to complete his assignment by 15th March, 2023. Unfortunately, Mr. S died in a road accident on 1st March, 2023 and his assignment remains undone. Can Mr. M bind the legal representative of Mr. S for the promise made by Mr. S? Suppose Mr. S had promised to deliver some photographs to Mr. M on 15th March, 2023 against a payment of ₹ 10,000 but he dies before that day. Will his representative be bound to deliver the photographs in this situation?

Decide as per the provisions of the Indian Contract Act, 1872.

(RTP June 2024)[June 2023 (4 Marks)]

# Answer

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 this Act, or of any other law.

Promises bind the representatives of the promisors in case of the death of such promisors before performance, unless a contrary intention appears from the contract. (Section 37 of the Indian Contract Act, 1872).

As per the provisions of Section 40 of the Indian Contract Act, 1872, if it appears from the nature of the case that it was the intention of the parties to any contract that any promise contained in it should be performed by the promisor himself, such promise must be performed by the promisor. In other cases, the promisor or his representative may employ a competent person to perform it.

In terms of the provisions of Section 40 stated above, in case where Mr. S has to paint a family picture for Mr. M, Mr. M cannot ask the legal representative of Mr. S to complete the painting work on Mr. S's death, since painting involves the use of personal skill.

In terms of the provisions of Section 37 stated above, in case where Mr. S had promised to deliver some photographs to Mr. M, the legal representatives of Mr. S shall be bound to deliver the photographs in this situation.

# Reciprocal Promises

- Promise in Exchange of Promise
- Both parties are PROMISOR & PROMISEE

## MUTUAL & CONCURRENT



- Performed Simultaneously
- If a party does not perform, the other should also not perform
- E.g.: Cash Sales

## MUTUAL & INDEPENDENT



- Performance of a party is Not dependent on Performance of Other
- Even if other does not perform, he has to perform his part.

## CONDITIONAL & DEPENDENT



- Performance of one party depends upon Performance of other
- **If one does not perform, the other should also not perform.**

# APPROPRIATION OF PAYMENTS:

## Rules

- 1. Debtor will express as to which Debt amount should be adjusted.(sec 59)**
- 2. Sometime debtor doesn't express but it is implied then it should be accordingly adjusted. (sec 59)**
- 3. If debtor neither expresses not it is implied, then creditor can adjust any debt including time barred debt but excluding disputed debt. (sec 60)**
- 4. If neither party appropriates, then there will be appropriation by law which says appropriation will be made by order of time(whether or not barred by time)(. If the debts are of equal standing, the payments shall be applied in discharge of each proportionately).**
- 5. Note : If both principle & interest is due first interest will be appropriated then principle will be appropriated.**



# Question

1. T owes G, the following debts as per the table given below:

Amount of the Debt (in ₹)	Position of Debt
5,000	Time barred on 01 <sup>st</sup> July, 2023 as per the provisions of the Limitation Act,1963
3,000	Time barred on 01 <sup>st</sup> July, 2023 as per the provisions of the Limitation Act,1963
12,500	Due on 1 <sup>st</sup> April, 2022
10,000	Due on 15 <sup>th</sup> July, 2023
7,500	Due on 25 <sup>th</sup> November, 2023

G makes payment on 1st April, 2023 mentioned as below without any notice regarding how to appropriate the amount/ payment.

- (i) A cheque of ₹ 12,500
- (ii) A cheque of ₹ 4,000.

In such a situation how the appropriation of the payment is done against the debts as per the provisions of the Indian Contract Act, 1872 by assuming that T also has not appropriated the amount received towards any particular debt.  
[Dec 2023 (4 Marks)] [RTP June 2023]

# Answer

In the present case, G made two payments by way of two cheques. Also, neither G nor T said anything as to the appropriation of the amount towards any particular debt.

Since one of the issued cheques was exactly the amount of the debt due i.e. of ₹ 12,500, by applying the provisions of Section 59 we can say that this is a circumstance indicating for appropriation against that particular debt.

Cheque of ₹ 4,000 can be appropriated in terms of the provisions of Section 61 since neither of the parties, have made any appropriation. The amount will be appropriated in discharging of the debts in order of time against any lawful debt whether they are or are not barred by the law in force for the time being as to the limitation of suits.

Hence cheque of ₹ 12,500 will be appropriated against the debt of ₹ 12,500 which is due on 1st April, 2022.

As per the scenario given in the question, since two debts are persisting in order of time which were treated as time barred on 1st July 2023, the amount of ₹ 4,000 will be appropriated proportionately, i.e. in proportion of 5,000:3,000. Therefore as per the provisions of the Indian Contract Act, 1872, ₹2,500 will be appropriated for the first debt and ₹ 1,500 will be appropriated towards the second debt

# Question

21. Mr. Sohan, a wealthy individual provided a loan of ₹ 80,000 to Mr. Mukesh on 26th February, 2021. The borrower, Mr. Mukesh asked for a further loan of ₹ 1,50,000. Mr. Sohan agreed but provided the loan in parts on different dates. He provided ₹ 1,00,000 on 28th February, 2021 and remaining ₹ 50,000 on 3rd March, 2021.

On 10th March, 2021 Mr. Mukesh while paying off part ₹ 75,000 to Mr. Sohan insisted that the lender should adjusted ₹ 50,000 towards the loan taken on 3rd March, 2021 and balance as against the loan on 26th February, 2021.

Mr. Sohan objected to this arrangement and asked the borrower to adjust in the order of date of borrowal of funds.

Now you decide:

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

[RTP Dec 2023]

# Answer

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

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

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

(ii) As per the provisions of 60 of the Act, where the debtor has omitted to intimate and there are no other circumstances indicating to which debt the payment is to be applied, the creditor may apply it at his discretion to any lawful debt actually due and payable to him from the debtor, where its recovery is or is not barred by the law in force for the time being as to the limitation of suits.

Hence in case Mr. Mukesh fails to specify the manner of appropriation of debt on part repayment, Mr. Sohan the creditor, can appropriate the payment as per his choice.

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

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

# Contracts which need not be performed

1. If the parties mutually agree to substitute the original contract by a new one (Novation) or to rescind (rescission) or alter (alteration) it.
2. If the promisee dispenses with or remits, wholly or in part the performance of the promise made to or extends the time for such performance or accepts any satisfaction for it. (Waiver)
3. If the person, at whose option the contract is voidable, rescinds it.
4. If the promisee neglects or refuses. (Breach)
5. If it is illegal. Or becomes subsequently impossible

## Question

**Explain any five circumstances under which contracts need not be performed with the consent of both the parties.  
(MTP Apr. 24) (6 Marks)**

## Question

**13. Differentiate between Novation and Alteration as per the Indian Contract Act, 1872.**

**[Nov. 2022 (5 Marks)]**

# Answer

**Novation and Alteration:** The law pertaining to novation and alteration is contained in Sections 62 to 67 of the Indian Contract Act, 1872. In both these cases, the original contract need not be performed. Still there is a difference between these two.

- 1. Meaning:** Novation means substitution of an existing contract with a new one. But in case of alteration the terms of the contract may be altered by mutual agreement by the contracting parties.
- 2. Change in terms and conditions and parties:** Novation may be made by changing in the terms of the contract or there may be a change in the contracting parties. But in case of alteration the terms of the contract may be altered by mutual agreement by the contracting parties but the parties to the contract will remain the same.
- 3. Substitution of new contract:** In case of novation, there is altogether a substitution of new contract in place of the old contract. But in case of alteration, it is not essential to substitute a new contract in place of the old contract. In alteration, there may be a change in some of the terms and conditions of the original agreement.



# Question

47. Mr. Gaurav and Mr. Vikas entered into a contract on 1st July, 2022, according to which Mr. Gaurav had to supply 100 tons of sugar to Mr. Vikas at a certain price strictly within a period of 10 days of the contract. Mr. Vikas also paid an amount of ₹ 70,000 towards advance as per the terms of the above contract. The mode of transportation available between their places is roadway only. Severe flood came on 2nd July, 2022 and the only road connecting their places was damaged and could not be repaired within fifteen days. Mr. Gaurav offered to supply sugar on 20th July, 2022 for which Mr. Vikas did not agree. On 1st August, 2022, Mr. Gaurav claimed compensation of ₹ 20,000 from Mr. Vikas for refusing to accept the supply of sugar, which was not there within the purview of the contract. On the other hand, Mr. Vikas claimed for refund of ₹ 70,000, which he had paid as advance in terms of the contract. Analyse the above situation in terms of the provisions of the Indian Contract Act, 1872 and decide on Mr. Vikas contention.

[MTP Apr 2023(6 Marks)]

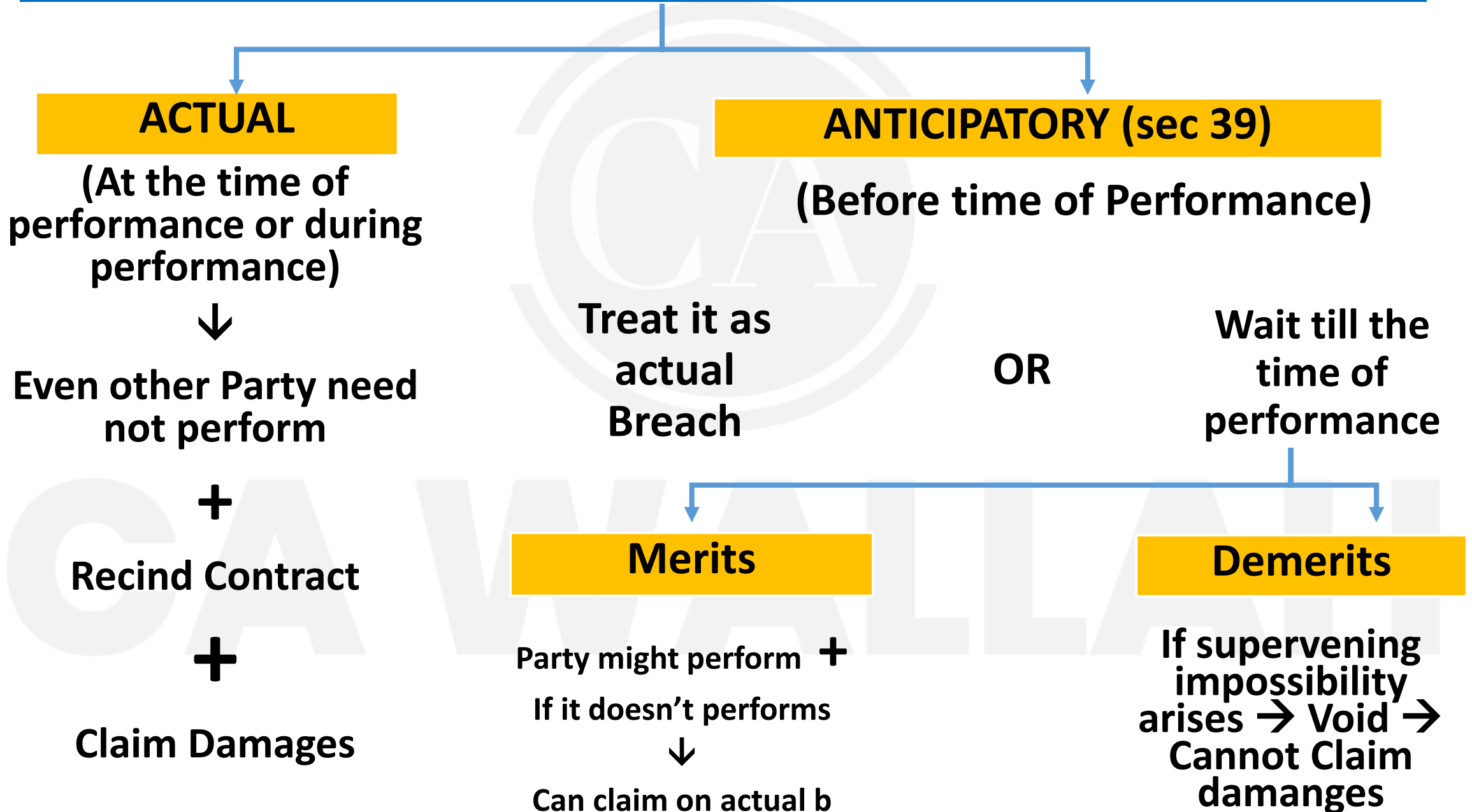
# Answer

**Subsequent or Supervening impossibility (Becomes impossible after entering into contract):** When performance of promise become impossible or illegal by occurrence of an unexpected event or a change of circumstances beyond the contemplation of parties, the contract becomes void e.g. change in law etc.

Also, according to section 65 of the Indian Contract Act, 1872, when an agreement is discovered to be void or when a contract becomes void, any person who has received any advantage under such agreement or contract is bound to restore it, or to make compensation for it to the person from whom he received it.

In the given question, after Mr. Gaurav and Mr. Vikas have entered into the contract to supply 100 tons of sugar, the event of flood occurred which made it impossible to deliver the sugar within the stipulated time. Thus, the promise in question became void. Further, Mr. Gaurav has to pay back the amount of ₹ 70,000 that he received from Mr. Vikas as an advance for the supply of sugar within the stipulated time. Hence, the contention of Mr. Vikas is correct.

# BREACH OF CONTRACT [NON-PERFORMANCE]



## Question

**38. "An anticipatory breach of contract is a breach of contract occurring before the time fixed for performance has arrived". Discuss stating also the effect of anticipatory breach on contracts.**

**[RTP May 2022] (MTP Apr. 24) (6 Marks)**

# SUIT FOR DAMAGES (MONETARY COMPENSATION)(sec 73)

TYPES OF DAMAGES	DETAILS	CAN IT BE CLAIMED
1. Direct / Ordinary Damages	<ul style="list-style-type: none"><li>➤ Which Naturally arises</li><li>➤ Probable Consequence</li><li>➤ Which can be directly related</li></ul> <p><b>Note:</b> Normally amount of will be difference between contract price &amp; market price.</p>	yes
2. Indirect or Remote Damages	<ul style="list-style-type: none"><li>➤ Which does not occur Naturally</li></ul>	no
3. Special Damages	<ul style="list-style-type: none"><li>➤ Claiming Profits for the loss of profit.</li><li>➤ Can be claimed only if defaulting party knew about such loss.</li></ul>	Only if party know
4. Nominal damages	<ul style="list-style-type: none"><li>➤ Normally there is no loss</li><li>➤ Court allow a nominal amount just to conclude that one party is at default</li><li>➤ Just for name sake</li></ul>	yes

# Question

**34. Seema was running a boutique in New Delhi. She has to deliver some cloth to her friend Kiran who was putting up an exhibition at Mumbai. Seema delivered the sewing machine and some cloth to a railway company to be delivered at a place where the exhibition was to be held. Seema expected to earn an exceptional profit from the sales made at this exhibition however she did not bring this fact to the notice of the railway's authorities. The goods were delivered at the place after the conclusion of the exhibition. On account of such breach of contract by railways authorities, can Seema recover the loss of profits under the Indian Contract Act, 1872? [RTP May 2022]**

# Answer

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

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

# SUIT FOR DAMAGES (MONETARY COMPENSATION)

TYPES OF DAMAGES	DETAILS		CAN IT BE CLAIMED
5. Vindictive or Exemplary or Punitive Damages	<ul style="list-style-type: none"> <li>➤ <b>Contract act is compensatory in nature, it is not punitive in nature.</b></li> <li>➤ <b>Exception:</b> <ol style="list-style-type: none"> <li>1) <b>Breach of promise to marry.</b></li> <li>2) <b>Dishonour of cheque</b></li> </ol> <p style="text-align: center;"><b>or</b></p> <b>Bouncing of cheque by banker even when your have sufficient Balance in you're a/c</b> </li> </ul>		no
6. Liquidated Damages & Penalty (sec 74)	<ul style="list-style-type: none"> <li>➤ When Party decides in advance the amount to be paid in case of damages</li> </ul> <p style="text-align: center;"><b>Such money</b></p>		Only to extent of damages
	Actual loss ↓ Genuine Pre-estimation ↓ Liquidated Damages ↓ ✓	+	



# Question

**17. "Liquidated damage is a genuine pre-estimate of compensation of damages for certain anticipated breach of contract whereas Penalty on the other hand is an extravagant amount stipulated and is clearly unconscionable and has no comparison to the loss suffered by the parties". Explain the statement by differentiating between liquidated damages and penalty with reference to provisions of the Indian Contract Act, 1872.**

**[May 2022 (5 Marks)]**

# Answer

Liquidated damages is a genuine pre-estimate of compensation of damage for certain anticipated breach of contract. This estimate is agreed to between parties to avoid at a later date detailed calculation and the necessity to convince outside parties.

Penalty on the other hand is an extravagant amount stipulated and is clearly unconscionable and has no comparison to the loss suffered by the parties.

## Distinction between liquidated damages and penalty

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

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

# Question

M Ltd. contract with Shanti Traders to make and deliver certain machinery to them by 30th June 2023 for ` 11.50 lakhs. Due to labour strike, M Ltd. could not manufacture and deliver the machinery to Shanti Traders. Later, Shanti Traders procured the machinery from another manufacturer for ` 12.75 lakhs. Due to this, Shanti Traders was also prevented from performing a contract which it had made with Zenith Traders at the time of their contract with M Ltd. and were compelled to pay compensation for breach of contract. Advise Shanti Traders the amount of compensation which it can claim from M Ltd., referring to the legal provisions of the Indian Contract Act, 1872. (MTP May 24) (7 Marks)

# Answer

Section 73 of the Indian Contract Act, 1872 provides for consequences of breach of contract. According to it, when a contract has been broken, the party who suffers by such breach is entitled to receive from the party who has broken the contract, compensation for any loss or damage caused to him there by which naturally arose in the usual course of things from such breach or which the parties knew when they made the contract, to be likely to result from the breach of it. Such compensation is not given for any remote and indirect loss or damage sustained by reason of the breach. It is further provided in the explanation to the section that in estimating the loss or damage from a breach of contract, the means which existed of remedying the inconvenience caused by the non - performance of the contract must be taken into account.

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

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

## REMEDIES FOR BREACH OF CONTRACT

Suit for Damages	Rescission of Contract	Suit for Specific Performance	Suit for Injunction	Quantum Meruit
<p><b><u>Monetary Compensation</u></b>  <b><u>Kinds of Damages</u></b></p> <p>1. <b>Ordinary Damages-</b>            Equal to actual loss but not for indirect or remote loss.</p> <p>2. <b>Special Damages-</b>            Decided at the time of contract entered.</p> <p>3. <b>Exemplary Damages-</b>            Granted only in-case of</p>	<p>Termination of contract by promisee when promisor refuses to perform.</p>	<p>Where damages are not an adequate remedy, court may direct party in breach to carry out his promise according to terms of contract.</p>	<p><b><u>Order of the court</u></b>            Where a party does something <u>which</u> he promised not to do, the Court may issue an order, prohibit him from doing so.</p>	<p><b><u>As much as earned</u></b>            When a person has done some work under a contract, and other party repudiated the contract, or some event happens which makes the further performance of contract impossible</p>

# Question

- **What do you mean by Quantum Meruit and state the cases where the claim for Quantum Meruit arises?(MTP May 24) (6 Marks)**
- *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 the 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 meruit is restitutory. It is but reasonable compensation awarded on implication of a contract to remunerate.
- **The claim for quantum meruit arises in the following cases:**
  - When an agreement is discovered to be void or when a contract becomes void.
  - When something is done non gratuitously
  - Where there is no agreement as to remuneration.
  - Where a contract is divisible and the party not in default has enjoyed the benefit of part performance.
  - When an indivisible contract for a lump sum is completely performed but badly performed

# Question

In light of provisions of the Indian Contract Act, 1872 answer the following:

- i. Mr. S and Mr. R made contract wherein Mr. S agreed to deliver paper cup manufacture machine to Mr. R and to receive payment on delivery. On the delivery date, Mr. R did not pay the agreed price. Decide whether Mr. S is bound to fulfil his promise at the time of delivery?
- ii. Mr. Y has given loan to Mr. G of ` 30,00,000. Mr. G defaulted the loan on due date and debt became time barred. After the time barred debt, Mr. G agreed to settle the full amount to Mr. Y. Whether acceptance of time barred debt Contract is enforceable as per the Indian Contract Act, 1872?

A & B entered into a contract to supply unique item, alternate of which is not available in the market. A refused to supply the agreed unique item to B. What directions could be given by the court for breach of such contract? (MTP May 24) (7 Marks)

# Contingent Contract

## Basics

- **Contract (sec 31)**
  - ↓
  - To do or not to do something**
  - ↓
  - If some Collateral event**
  - ↓
  - Happen or does not happen**
- **Does or Collateral event is which is neither performance directly promised nor whole of obligation**
- **If event depends upon mere will of promisor does not happen**

### Void-ab-initio

#### ➤ Essentials

- a) Contingency
- b) Collateral Event
- c) Event – uncertain

## Rules(sec 32 to 36)

Sr. No.	Depend Upon	Valid	Void
1	Happening	Event Happens	a) Event does not happen b) Becomes impossible
2	Non-Happening	a) Does not happen b) Happening becomes impossible	Happens
3	Happening with Fixed Time	1 (+) within Fixed time	1 (+) within Fixed time
4	Non-happening within Fixed Time	2 (+) within Fixed time	2 (+) within Fixed time
5	Conduct of a person	Person conducts that way	Person do not conduct that way
6	Impossible Event	Void-ab-initio	



# Wagering Agreement

## Meaning: Agreement

between two parties by which one promises to pay money or money's worth on the happening of same uncertain event in consideration of the other party's promises to pay if the event does not happen.

## Essentials

- (i) Promises to pay money
- (ii) Uncertain event
- (iii) Mutual Chances of win or lose.
- (iv) No control over the event
- (v) No other interest in the event.

## Effects

- (i) Agreement is void
- (ii) No suit to recover amount won.

## Transactions are not Wager

- (i) Chit Fund
- (ii) Share market transactions in which delivery of stocks and shares is intended to be given & taken.
- (iii) Game of skill, crossword, etc.
- (iv) a contribution toward any prize value of Rs. 500 or above to be awarded to the winner or winners of a horse race.
- (v) A contract of insurance.

## Distinction between Contract of Insurance and Wagering Agreement



	<b>Basis</b>	<b>Contracts of Insurance/Contingent</b>	<b>Wagering Agreement</b>
1.	<b>Meaning</b>	It is a contract to indemnify the loss.	It is a promise to pay money or money's worth on <u>the happening</u> or non- happening of an uncertain event.
2.	<b>Consideration</b>	The crux of insurance contract is the mutual consideration (premium and compensation amount).	There is no consideration between the two parties. There is just gambling for money.
3.	<b>Insurable Interest</b>	Insured party has insurable interest in the life or property sought to be insured.	There is no property in case of wagering agreement. There is betting on other's life and properties.
4.	<b>Contract of Indemnity</b>	Except life insurance, the contract of insurance indemnifies the <u>insured person</u> against loss.	Loser has to pay the fixed amount on the happening of uncertain event.
5.	<b>Enforceability</b>	It is valid and enforceable	It is void and unenforceable agreement.

# Question

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

**[RTP May 2022]**

# Answer

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

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

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

# QUASI CONTRACTS Sec. 68 to 72

## Basics

- 'Similar to' Contract
- Contract act not define it but it says it is certain relations resembles to those created by contract
- Many essential elements [Sec.10] obligation not Created by contract it is imposed by law
- Base : Equity, Justice, Good Conscience i.e. No man should be enriched at the cost of other.
- Also known as Natural, implied, imputed
- Contractual is law but not in fact
- Explain the term 'Quasi Contracts' and state their characteristics. (RTP June 2024)

## Types / Examples

1. **Necessity supply to minor: Sec. 68**
  - Can recover from their estate property.
  - To the extent of property
  - Can also recover if supplied to their dependent.
2. **To recover money paid for another person Sec. 69 Conditions:**
  - a) Bonafide to another
  - b) Payee → obligation
  - c) Payment → involuntary
3. **Obligation of person enjoying benefit of non gratuitous Act**
4. **Finder of goods**
5. **Money or things delivered by Mistake**

# TYPES OF QUASI-CONTRACTS [Sections 68 to 72]

Cases	Explanation
<b>(1) Claim for necessities supplied to persons incapable of contracting (Sec. 68)</b>	<ul style="list-style-type: none"><li>• If necessities are supplied to a person who is incapable of contracting, Example: A minor or a person of unsound mind, the supplier is entitled to claim their price from the property of such a person.</li></ul>
<b>(2) Right to recover money paid for another person (Sec. 69)</b>	<p>A person who has paid a sum of money which another is obliged to pay, is entitled to be reimbursed by that other person</p> <p><u>Conditions:</u></p> <ul style="list-style-type: none"><li>• The payment made should be bona fide for the protection of one's interest.</li><li>• The payment should be involuntary one.</li><li>• The payment must be such as the other party was bound by law (or contract) to pay</li></ul>

# Question

12. Mr. Y aged 21 years, lost his mental balance after the death of his parents in an accident. He was left with his grandmother aged 85 years, incapable of walking and dependent upon him. Mr. M their neighbour, out of pity, started supplying food and other necessaries to both of them. Mr. Y and his grandmother used to live in the house built by his parents. Mr. M also provided grandmother some financial assistance for her emergency medical treatment. After supplying necessaries to Mr. Y for four years, Mr. M approached the former asking him to payback ₹ 15 Lakhs inclusive of ₹ 7 Lakhs incurred for the medical treatment of the lady (grandmother). Mr. Y pleaded that he has got his parent's jewellery to sell to a maximum value of ₹ 4 Lakhs, which may be adjusted against the dues. Mr. M refused and threatened Mr. Y of legal suit to be brought against for recovering the money.

Now, you are to decide upon based on the provisions of the Indian Contract Act, 1872:

- (i) Will Mr. M succeed in filing the suit to recover money? Elaborate the related provisions?
- (ii) What is the maximum amount- of money that can be recovered by Mr. M?
- (iii) Shall the provisions of the above act also apply to the medical treatment given to the grandmother?

[Nov. 2022 (6 Marks)]

# Answer

**(i) Claim for necessaries supplied to persons incapable of contracting (Section 68 of the Indian Contract Act, 1872):**

If a person, incapable of entering into a contract, or anyone whom he is legally bound to support, is supplied by another person with necessaries suited to his condition in life, the person who has furnished such supplies is entitled to be reimbursed from the property of such incapable person.

In the instant case, Mr. M supplied the food and other necessaries to Mr. Y (who lost his mental balance) and Mr. Y's grandmother (incapable of walking and dependent upon Mr. Y), hence, Mr. M will succeed in filing the suit to recover money.

**(ii) Supplier is entitled to be reimbursed from the property of such incapable person. Hence, the maximum amount of money that can be recovered by Mr. M is ₹ 15 Lakhs and this amount can be recovered from Mr. Y's parent's jewellery amounting to ₹ 4 Lakhs and rest from the house of Y's Parents. (Assumption: Y has inherited the house property on the death of his parents)**

**(iii) Necessaries will include the emergency medical treatment. Hence, the above provisions will also apply to the medical treatment given to the grandmother as Y is legally bound to support his grandmother.**



# TYPES OF QUASI-CONTRACTS [Sections 68 to 72]

Cases	Explanation
<b>(3) Obligation of a person enjoying benefits of non-gratuitous act (Section 70):</b>	<ul style="list-style-type: none"><li>◆ Where a person lawfully does anything for another person, or delivers anything to him</li><li>◆ nongratuitously, and</li><li>◆ such other person enjoys the benefit thereof,</li><li>◆ The latter is bound to make compensation to the former in respect of, or to restore, the thing so done or delivered”.</li></ul>

CA WW ALLAN

# TYPES OF QUASI-CONTRACTS [Sections 68 to 72]

Cases	Explanation
<p><b>(4)</b> <b>Responsibility of a finder of goods (Section 71)</b></p>	<ol style="list-style-type: none"><li>1. A person who finds goods and takes possession of it is responsible as a bailee.</li><li>2. That is, he is liable-<ul style="list-style-type: none"><li>▪ To try and find out the true owner and</li><li>▪ To take due care of the property</li></ul></li><li>1. Finder is entitled to a lien until paid compensation, but cannot file a suit to recover such compensation.</li><li>2. Finder is entitled to possession against all except the true owner.</li><li>3. When owner declares reward, finder can sue for reward.</li><li>4. Right of re-sale: If the owner is not found or if he refuses to pay lawful charges, the finder may sell-<ul style="list-style-type: none"><li>▪ When the thing is in danger of perishing or losing the greater part of its value.</li><li>▪ When the lawful charges amount to two-thirds of its value.</li></ul></li></ol>

# Question

Rohan found a wallet in a restaurant. He enquired all the customers present there but the true owner could not be found. He handed over the same to the manager of the restaurant to keep the wallet till the true owner is found. After a week, Rohan went back to the restaurant to enquire about the wallet. The manager refused to return it to Rohan, saying that it did not belong to him. In the light of the Indian Contract Act, 1872, can Rohan recover the wallet from the Manager?

[RTP Dec 2023]

# Answer

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

**Thus, Finder is entitled to possession against all except the true owner..**

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

**CAWALLAH**

# TYPES OF QUASI-CONTRACTS [Sections 68 to 72]

Cases	Explanation	
<b>(5) Liability for money paid or thing delivered by mistake or under coercion (Section 72)</b>	“A person to whom money has been paid, or anything delivered by mistake or under coercion must repay or return it (Sec. 72)”.	<p>(1) A pays some money to B by mistake. It is really due to C. B must refund the money to A. C, however cannot recover the amount from B as there is no privity of contract between B and C.</p> <p>(2) A, a tradesman, leaves goods at B's house by mistake. B treats the goods as his own. He is bound to pay A for them.</p> <p>(3) A and B jointly owe Rs.100 to C, A alone pays the amount to C, and B, not knowing this fact, pays 100 rupees over again to C. C is bound to repay the amount of Rs.100 to B.</p>

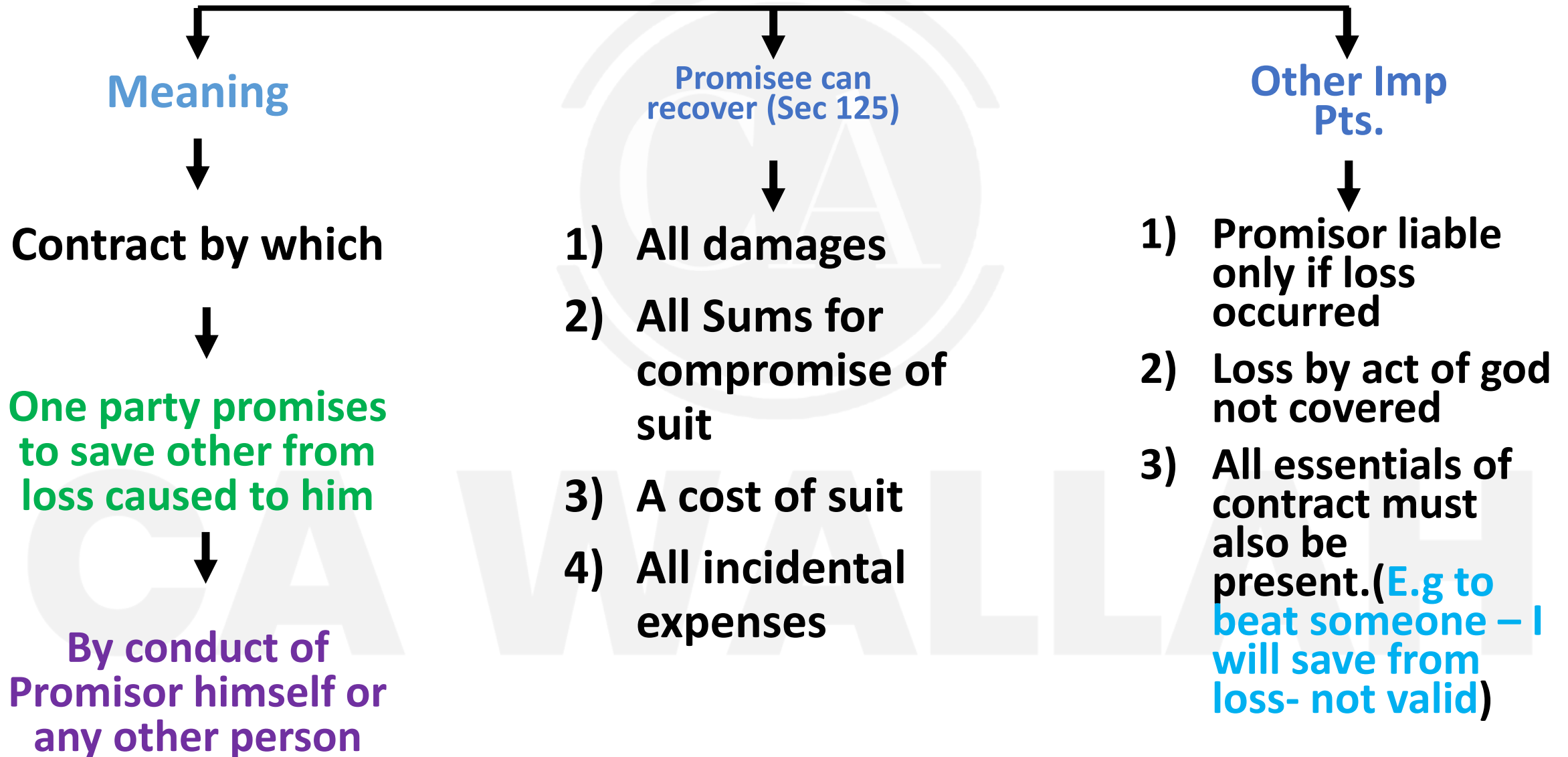
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## Indemnity and guarantee

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# CONTRACT OF INDEMNITY (Sec 124)



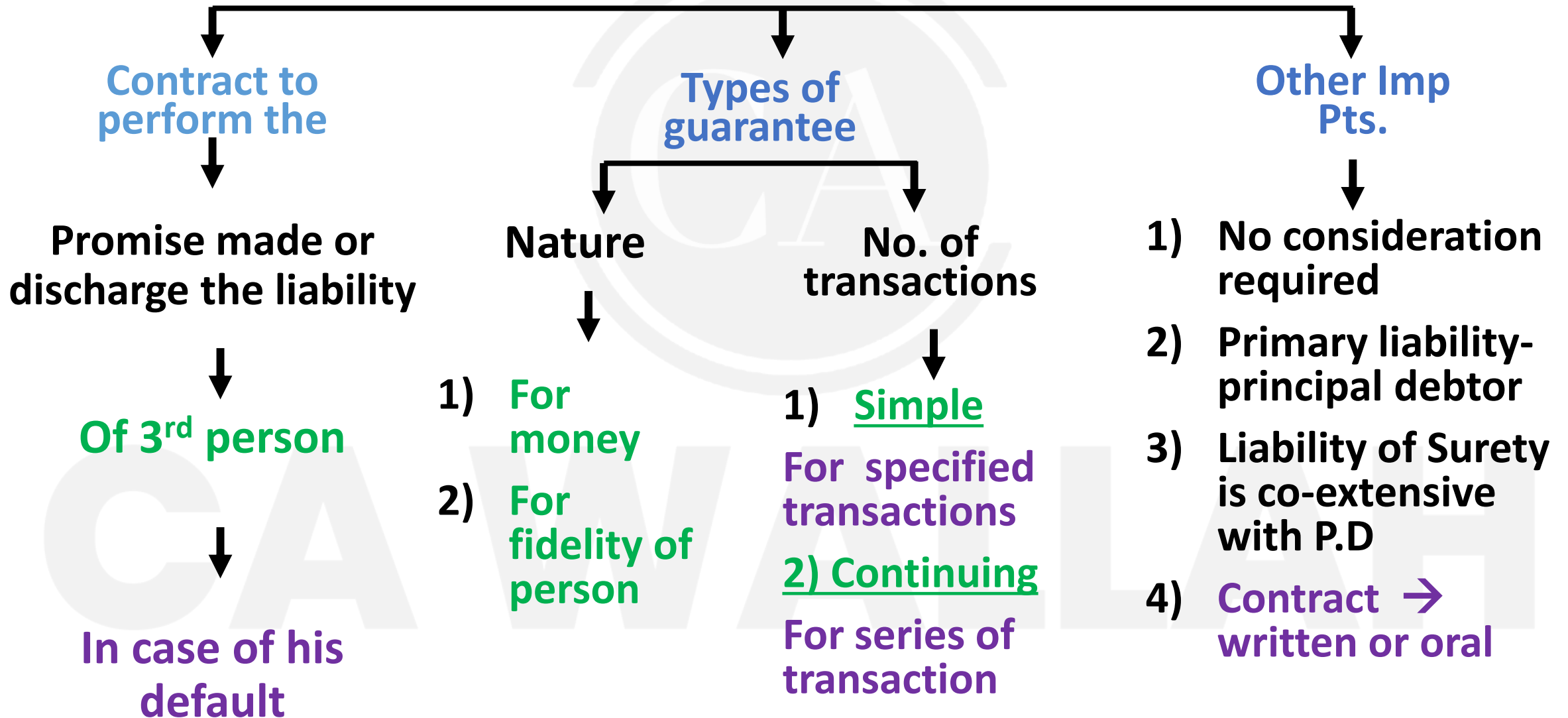
# Theory Question

**State the rights of the indemnity-holder when sued?**

**(MTP MAY 2018)**



# CONTRACT OF GUARANTEE



Mr. Salil purchased furniture of worth ` 1,00,000 from Mr. Pooran on credit. Mr. Raman entered in contract with Mr. Pooran for the guarantee of the payment by Mr. Salil. On due date, Mr. Salil could not make the payment due to his financial crisis. Mr. Pooran filed the suit against Mr. Raman for payment. Meanwhile father of Mr. Salil paid ` 20,000 to Mr. Pooran on behalf of his son. Mr. Raman, in ignorance of above payment, paid `1,00,000 to Mr. Pooran as surety. Afterwards, when Mr. Raman knew the facts, he asked Mr. Pooran for refund of ` 20,000. Mr. Pooran denied for refund with the words, that's only Mr. Salil who can claim the amount of ` 20,000. Explain, with reference to Indian Contract Act 1872, whether Mr. Raman (surety) can claim the refund of ` 20,000 from Mr. Pooran? (RTP Mar 23)

**Hinti:** As per the provisions of section 128 of the Indian Contract Act, 1872, the liability of the surety is co-extensive with that of the principal debtor, unless it is otherwise provided by the contract. In other words, the surety is liable for all those amounts, the principal debtor is liable for.

In the given question, before Mr. Raman makes the payment (on default of Mr. Salil), the father of Mr. Salil paid ` 20,000 to Mr. Pooran on behalf of his son. Unaware of the payment of ` 20,000, Mr. Raman paid the full amount to Mr. Pooran.

The liability of Mr. Raman (surety) is co-extensive with that of Mr. Salil (principal debtor). As the father of Mr. Salil made payment of ` 20,000 on Salil's behalf, Mr. Raman is liable only for ` 80,000 to Mr. Pooran (creditor). Mr. Raman made the full payment without the knowledge of facts. Therefore, he can claim the refund of ` 20,000 from Mr. Pooran.

C A W W A L L A H

# Distinguish between Indemnity and Guarantee

Shortcut → **P C LE Rahi P.C** → in guarantee

Basis	Indemnity	Guarantee
(1) <b>P</b> – No. of <b>P</b> arties	2 parties – Indemnifier and Indemnity holder	3 parties – Creditor, P.D, Surety
(2) <b>C</b> – No. of <b>C</b> ontracts	One	Three
(3) <b>L</b> – Primary <b>L</b> iability	Indemnifier	P.D
(4) <b>E</b> – <b>E</b> xistence of debt.	Doesn't exist at time of contract	Exist
(5) <b>R</b> – <b>R</b> ight to recover	From no one	Surety can recover from P.D
(6) <b>P</b> – <b>P</b> urpose	Reimbursement of losses	Security to creditor

Distinguish between a contract of Indemnity and a contract of Guarantee as per the Indian Contract Act, 1872. (4 Marks) (MTP Oct. 22)

# Essentials of Contract

- 1) Must have all the essentials of a valid contract.
- 2) Primary liability of principal debtor.  
Debt must be enforceable and not time barred.
- 3) The contract must be conditional –  
Surety → Secondary liability → Only when principal debtor makes default.
- 4) No misrepresentation or concealment or else contract invalid (sec 142) **Example** : A engages B as clerk to collect money for him. B fails to account for some of his receipts, and A in consequence calls upon him to furnish security for his duly accounting. C gives his guarantee for B's duly accounting. A does not acquaint C, with his previous conduct. B afterwards make default. The guarantee is invalid.
- 5) Contract → written or oral
- 6) Surety's liability co-extensive with that of P.D
- 7) If co-sureties fail to join – Contract invalid(sec 144)

# DISCHARGE OF GUARANTEE

## By Revocation

### 1) By notice of revocation (Sec 130)

- Future transactions – revoked
- Transactions already entered – liable

### 2) By surety's death (Sec 131)

### 3) Novation

## By Conduct of creditor

### 1) By variation of terms & conditions (Sec 133)- without consent of surety

### 2) By release of principal debtor (Sec 134)

### 3) Composition with P.D to give him more time or not to sue (Sec 135)

### 4) Creditors act or omission (Sec 139)

## Invalidation of contract

### 1) Mis – representation (Sec 142)

### 2) Fraud

### 3) Co-surety fails to join as per terms of contract

# Practical Question - 1

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

- i. Whether 'Amit' is discharged from all the liabilities to 'Chander' for any subsequent loan given to 'Bikram'?**
- ii. What would be your answer in case 'Bikram' makes a default in paying back to 'Chander' the already borrowed amount of Rs. 10000?**

**(May 2006)(Nov. 2015/2002/2017) (May 2019) (RTP N 20)**

## **Practical Question - 3**

**A gives to C a continuing guarantee to the extent of Rs. 5000 for the vegetables to be supplied by C to B from time to time on credit. Afterwards, B became embarrassed, and without the knowledge of A, B and C contract that C shall continue to supply B with vegetables for ready money, and that the payments shall be applied to the then existing debts between B and C.**

**Examining the provision of the Indian Contract Act, 1872, decide whether A is liable on his guarantee given to C.**

**(Nov. 2008/2017) (RTP M 19)**

# Note

- 1) Forbearance to sue does not discharge surety (sec 137)**
- 2) If agreement made with 3<sup>rd</sup> person not to sue does not discharge contract. (sec 136)**

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## **Practical Question - 5**

**C, the holder of an over due bill of exchange drawn by A as surety for B, and accepted by B, contracts with X to give time to B. Is A discharged from his liability?**

**(Nov. 2006) (RTP N 18) (MTP M 19/20)**

## **Practical Question - 6**

**B owes C a debt guaranteed by A. C does not sue B for a year after the debt has become payable. In the meantime, B becomes insolvent. Is A discharged? Decide with reference to the provisions of the Indian Contract Act, 1872.**

**(Nov. 2008)**

## Practical Question - 7

**Sarthak is employed as a cashier on a monthly salary of ` 50,000 by ABC bank for a period of three years. Mohit gave surety for Sarthak's good conduct. After nine months, the financial position of the bank deteriorates. Then Sarthak agrees to accept a lower salary of ` 40,000 per month from the Bank. Two months later, it was found that Sarthak had misappropriated cash from the time of his appointment. What is the liability of Mohit taking into account the provisions of the Indian Contract Act, 1872? (RTP June 2024)**

# Example

- A puts M as apprentice to B and gives a guarantee to B for M's fidelity. B promises on his part that he will, at least once a month, see that M make up the cash. B omits to see this done as promised, and M embezzles. A is not liable to B on his guarantee
- .

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Ricky is the owner of electronics shop. Prisha reached the shop to purchase an air conditioner whose compressor should be of copper. As Prisha wanted to purchase the air conditioner on credit, Ricky demand a guarantor for such transaction. Mr. Shiv (a friend of Prisha) came forward and gave the guarantee for payment of air conditioner. Ricky sold the air conditioner of a particular brand, misrepresenting that it is made of copper while it is made of aluminium. Neither Prisha nor Mr. Shiv had the knowledge of fact that it is made of aluminium. On being aware of the facts, Prisha denied for payment of price. Ricky filed the suit against Mr. Shiv. Explain with reference to the Indian Contract Act 1872, whether Mr. Shiv is liable to pay the price of air conditioner? (MTP Oct. 22)

(c) As per the provisions of section 142 of the Indian Contract Act 1872, where the guarantee has been obtained by means of misrepresentation made by the creditor concerning a material part of the transaction, the surety will be discharged. Further according to provisions of section 134, the surety is discharged by any contract between the creditor and the principal debtor, by which the principal debtor is released, or by any act or omission of the creditor, the legal consequence of which is the discharge of the principal debtor.

In the given question, Prisha wanted to purchase air conditioner whose compressor should be of copper, on credit from Ricky. Mr. Shiv has given the guarantee for payment of price. Ricky sold the air conditioner of a particular brand on misrepresenting that it is made of copper while it is made of aluminium of which both Prisha & Mr. Shiv were unaware. After being aware of the facts, Prisha denied for payment of price. Ricky filed the suit against Mr. Shiv for payment of price.

On the basis of above provisions and facts of the case, as guarantee was obtained by Ricky by misrepresentation of the facts, Mr. Shiv will not be liable. He will be discharged from liability.

# What are the Rights of Surety?

## AGAINST PRINCIPAL DEBTOR

- 1) **Right of subrogation (Sec 140)**
- 2) **Right of indemnity (Sec 145)**

## AGAINST CREDITOR

- 1) **Right to securities (Sec 141)- whether known or not**
- 2) **Right to set-off**
- 3) **Right to share reduction**

## AGAINST CO- SURETIES

- 1) **Equal contribution (Sec 146)**
- 2) **Liabilities of co-sureties bound in different sums (Sec 147)**

- **Example 32:** C advances to B, his tenant, 2,00,000 rupees on the guarantee of A. C has also a further security for the 2,00,000 rupees by a mortgage of B's furniture. C cancels the mortgage. B becomes insolvent, and C sues A on his guarantee. A is discharged from liability to the amount of the value of the furniture.
- **Set off** - 'X' took a loan of ₹ 50,000 from 'Y' which was guaranteed by 'Z'. There was one another contract between 'X' and 'Y' in which 'Y' had to pay ₹ 10,000 to 'X'. On default by 'X', 'Y' filed suit against 'Z'. Now 'Z' is liable to pay ₹ 40,000 (₹ 50,000 – ₹ 10,000).
- **Reduction - Example 34:** 'X' took a loan of ₹ 50,000 from 'Y' which was Guaranteed by 'Z'. 'X' became insolvent and only 25% is realised from his property against liabilities. Now 'Y' will receive ₹ 12,500 from 'X' and Now 'Z' is liable to pay ₹ 37,500 (₹ 50,000 – ₹ 12,500).

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## Bailment and Pledge

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# Bailment is

**Delivery** of goods (Only movable goods)

By one person to another for some **Purpose**

Once that purpose is accomplished, goods will be **returned**

- 2 parties → (i) Bailor (the one who delivers goods)  
(ii) Bailee (to whom the goods are delivered)

- Types → (i) Gratuitous  
(ii) Non-gratuitous

*State the essential elements of a contract of bailment. (MTP Apr. 24) (6 Marks)*

- *Delivery of goods*—The essence of bailment is delivery of goods by one person to another.
- *Bailment is a contract*—In bailment, the delivery of goods is upon a contract that when the purpose is accomplished, the goods shall be returned to the bailor.
- *Return of goods in specific*—The goods are delivered for some purpose and it is agreed that the specific goods shall be returned.
- *Ownership of goods*—In a bailment, it is only the possession of goods which is transferred, and the bailor continues to be the owner of the goods.
- *Property must be movable*—Bailment is only for movable goods and never for immovable goods or money.

- For **example**, servant of a master who is in custody of goods of the master does not become a bailee.
- 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.
- Deposit of money in a bank is not bailment since the money returned by the bank would not be identical currency notes.

*1. Examine whether the following constitute a contract of 'Bailment' under the provisions of the Indian Contract Act, 1872: (module) (RTP June 2024)*

*(i) V parks his car at a parking lot, locks it, and keeps the keys with himself.*

*(ii) Seizure of goods by customs authorities.*

1. As per the provisions of the Indian Contract Act, 1872, what is the meaning of:

(1) Continuing guarantee

(2) Gratuitous Bailment (4 Marks) (MTP Sep. 22)

**Hint**

(1) Continuing guarantee: A guarantee which extends to a series of transaction is called a continuing guarantee. A surety's liability continues until the revocation of the guarantee.

The essence of continuing guarantee is that it applies not to a specific number of transactions but to any number of transactions and makes the surety liable for the unpaid balance at the end of the guarantee.

(2) 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.

2. Shweta and Mira are very good friends. Shweta bailed her jewellery with Mira on the condition to safeguard it in a bank's safe locker. However, Mira kept it in safe locker at her residence, where she usually keeps her own jewellery. After a month all jewellery was lost in a religious riot. Shweta filed a suit against Mira for recovery. Referring to provisions of the Indian Contract Act, 1872, state whether Shweta will succeed. (4 Marks) (MTP Sep. 22)

**Hint:** According to section 152 of the Indian Contract Act, 1872, 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 reasonable care as required under section 151.

In the given question, Shweta and Mira agreed to keep Shweta's jewellery (bailed to Mira) at the Bank's safe locker and not at the latter's residence (i.e. Mira's residence). So, Mira is liable to compensate Shweta for her negligence to keep jewellery at her (Mira's) residence. Thus, Shweta will succeed in her claim.

3. Mrs. A delivered her old silver jewellery to Mr. Y a Goldsmith, for the purpose of making new a silver bowl out of it. Every evening she used to receive the unfinished good (silver bowl) to put it into box kept at Mr. Y's Shop. She kept the key of that box with herself. One night, the silver bowl was stolen from that box. Whether the possession of the goods (actual or constructive) delivered, constitute contract of bailment or not?

(MTP MAY 2020)

# DUTIES OF BAILEE

1. To take reasonable care
2. No unauthorized use of goods.
3. Not to mix goods with own goods.
4. To return goods (after purpose accomplished)
5. Duty to deliver accretion from goods.
6. Not acquire adverse title.

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- *R gives his umbrella to M during raining season to be used for two days during Examinations. M keeps the umbrella for a week. While going to R's house to return the umbrella, M accidentally slips and the umbrella is badly damaged. Who bear the loss and why? (module)*
- *Amar bailed 50 kg of high quality sugar to Srijith, who owned a kirana shop, promising to give ` 200 at the time of taking back the bailed goods. Srijith's employee, unaware of this, mixed the 50 kg of sugar belonging to Amar with the sugar in the shop and packaged it for sale when Srijith was away. This came to light only when Amar came asking for the sugar he had bailed with Srijith, as the price of the specific quality of sugar had trebled. What is the remedy available to Amar? (module)*

# Duties of bailor- Disclose faults in goods [Sec.150]

## Liability for Defects in Goods

### In case of Gratuitous Bailment

Bailor is liable only for those losses which arise due to non-disclosed risks

### In case of Non- Gratuitous Bailment

Bailor is liable for damages whether or not he was aware of the existence of faults

# Bear Expenses [Sec. 158]

## Expenses of Bailment

### In case of Gratuitous Bailment

all necessary expenses e.g - Dog

### In case of Non- Gratuitous Bailment

only extra-ordinary expenses, and not the ordinary expenses. E.g car lent

# Indemnify Bailee [Sec. 159 & 164]

## To indemnify Bailee

### Premature Termination of Gratuitous Bailment

- Bailor has the right to terminate the Gratuitous Bailment even if is for particular period.
- In such a case, Bailor has to indemnify the Bailee the excess of loss over benefit.

### When Bailor's title is defective

Bailor is responsible to the Bailee for any loss which the Bailee may sustain by reason that the Bailor was not entitled to make Bailment



*1. A hires a carriage from B and agrees to pay ` 500 as hire charges. The carriage is unsafe, though B is unaware of it. A is injured and claims compensation for injuries suffered by him. B refuses to pay. Discuss the liability of B. (module)*

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# RIGHTS OF BAILEE

- 1) Enforcement of bailor's duties.
- 2) Deliver goods to any of the joint bailor .
- 3) Deliver goods to bailor (without title) without incurring any liability to true owner.
- 4) Particular lien (some labour or skill applied )
- 5) general lien(Bankers , factors , wharfinger , attorney , policy broker )
- 6) Right to claim necessary expenses in gratuitous bailment and extraordinary exp in non-gratuitous

**Mr. Dhannaseth delivers a rough blue sapphire to a jeweller, to be cut and polished. The jeweller carries out the job accordingly. However, now Mr. Dhannaseth refuses to make the payment and wants his blue sapphire back. The jeweller denies the delivery of goods without payment. Examine whether the jeweler can hold blue sapphire. Give your answer as per the provisions of the Contract Act, 1872. (MTP NOV 2019)**

# RIGHTS OF BAILOR

1. **Right to claim compensation if bailee does not fulfill duty**
2. **To terminate bailment (anytime) if unauthorized use**
3. **Demand return of goods anytime in gratuitous bailment (No compensation except if loss exceeds profit.)**
4. **Right to file suit against a wrong doer.**

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# Finder of goods

## Rights

- 1) Can retain possession against anybody except true owner.
- 2) To claim necessary expenses incurred & lien for it
- 3) To claim reward (if announced ) & sue for it
- 4) Sale if
  - a) Perishable goods danger of perishing
  - b) Lawful charges amount to  $\frac{2}{3}$ <sup>rd</sup> of total value

## Duties

- 1) Take reasonable care
- 2) Find true owner of goods & return
- 3) Deliver accretion
- 4) No unauthorize use
- 5) Not to mix goods

# Pledge

- 1) Pledge is bailment only for purpose of keeping goods as security
- 2) It is also bailment so all duties/ rights of bailor and bailee applies to Pawnor and Pawnee
- 3) Pawnee can retain goods for
  - a) Payment
  - b) Interest
  - c) All necessary exp.
- 4) Lien also applicable for fresh advance
- 5) Pawnee can also claim extra ordinary expenses
- 6) If Pawnor makes default, Pawnee can
  - a) Sue pawnor
  - b) Lien
  - c) Re-sell(after notice)

# Pledge by Non-owners-When valid

- 1) Pledge by Mercantile Agent [Sec 178] –  
Valid (whether he is authorized by owner or not)
- 2) Pledge in case of Voidable Contract [Sec 178 A] –  
Valid (if not rescinded at the time of pledge)
- 3) Pledge goods for limited interest [Sec 179] –  
Valid (to the extent of interest)
- 4) Pledge by a co-owner in possession.  
Valid (with the consent of other co owners)
- 5) Pledge by seller or buyer in possession.  
Valid (after prior permission of seller)

Srushti acquired a valuable diamond at a very low price by a voidable contract under the provisions of India Contract Act, 1872. The voidable contract was not rescinded. Srushti pledged the diamond with Mr. VK. Is this a valid pledge under the Indian Contract Act, 1872? (Nov. 2019) (module)

# Difference between Bailment and Pledge.

## Bailment

1) Bailment means delivery of goods by one person to another for some purpose, once the contract is accomplished, be returned.

2) Two parties are involved –

**Bailor and Bailee**

3) Bailment may be made for any purpose (e.g. safe custody, for repairs, etc.)

4) Can be gratuitous

5) No right to sell.

6) Bailee may use the goods as specified in the contract of bailment.

7) Bailment includes Pledge.

Every bailment is not pledge

## Pledge

1) The bailment of goods as security for payment of a debt or performance of a promise is called as 'pledge'.

2) Two parties are involved –

**Pawnor and Pawnee**

3) Pledge is made for the purpose of delivering the goods as security for payment of a debt or performance of a promise.

4) Consideration is always present in case of pledge.

5) Right to sell the goods if the pawnor fails to redeem the goods.

6) No right to use the goods.

7) Pledge is a special kind of bailment. Every pledge amounts to bailment.

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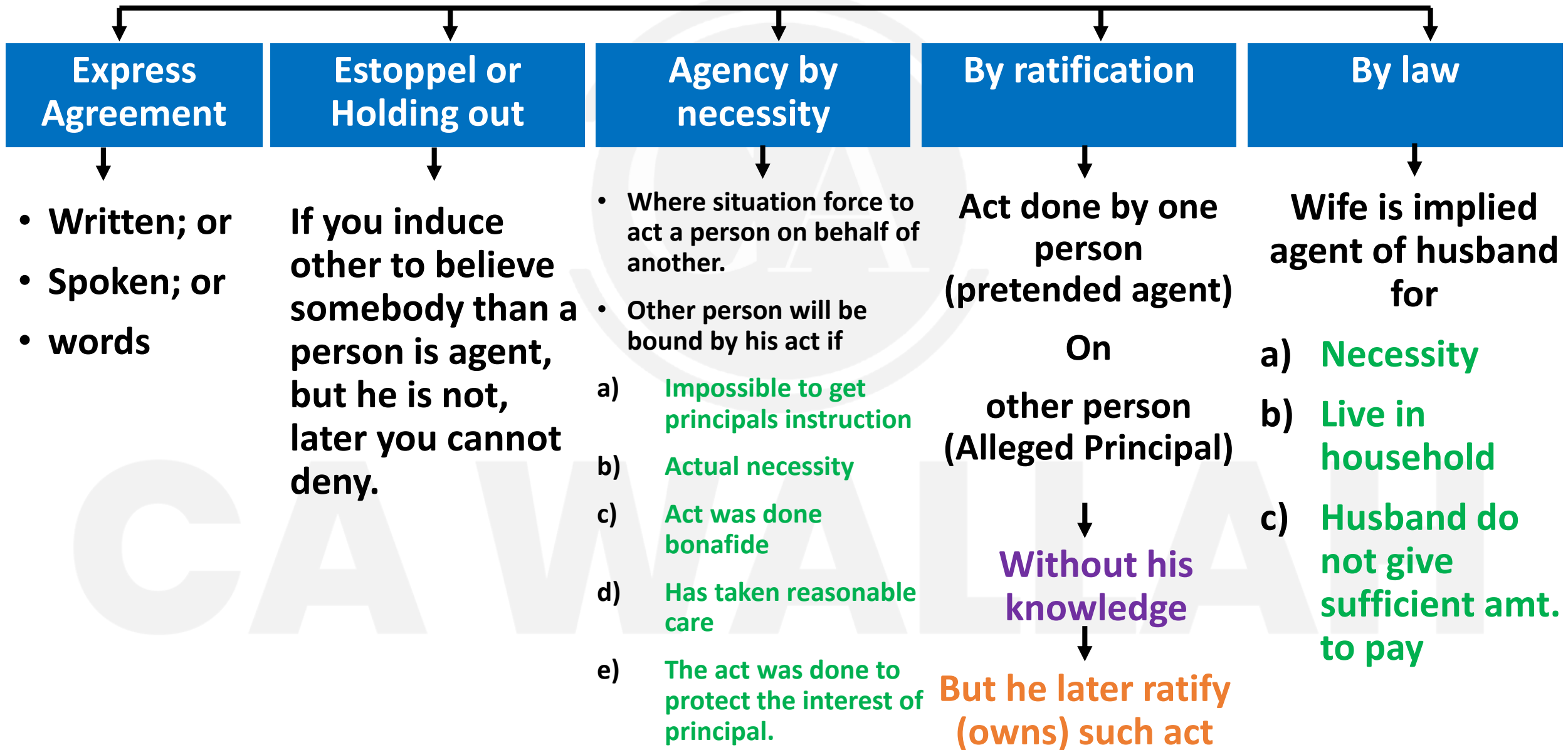
## Contract of Agency

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# Modes of Creating Agency



# Examples - Modes of Creating Agency

## Express Agreement

P appoints A to appear in a court hearing on his behalf. For the said purposes P signs a 'vakalatnama' empowering A to act for and on his behalf. A is holding express authority from P.

## Estoppel or Holding out

A tells T in the presence and within the hearing of P that he (A) is P's agent. P keeps quiet and does not contradict this statement. Later T enters into a contract with A honestly believing that A is P's agent. P is bound by this contract of agency by estoppel.

## Agency by necessity

A consignment of butter which was in danger of becoming useless owing to delay in transit was sold by the railway company for the best available price and where it was not possible to obtain instructions of the consignor, the sale was held to be binding upon the consignor, as the railway company acted as an agent for consignor by necessity.

## By ratification

A, without P's authority, lends P's money to T. Afterwards P accepts interest on the money from T. P's conduct implies a ratification of the loan given.

## By law

For example, in case of partnership, a partner is the agent of the firm for the purpose of the business of the firm and the act of a partner which is done to carry on, in the usual way, business of the kind carried on by the firm, binds the firm.

- *R is the wife of P. She purchased sarees on credit from Nalli. Nalli demanded the amount from P. P refused. Nalli filed a suit against P for the said amount. Decide in the light of provisions of the Indian Contract Act, 1872, whether Nalli would succeed. (ICAI study Material )*

# Essentials of Valid Ratification

- 1) Principal must have **full knowledge** of all the material facts.
- 2) Only **lawful acts** to be ratified
- 3) Ratification of **Whole transaction** to be considered.
- 4) No ratification at the cost of third parties.(Unauthorised/wrong act )
- 5) Acts of **Pretended agent**
- 6) Acts within the scope of principal.
- 7) Ratification only by principal
- 8) Principal should be **competent** to enter into a contract.
- 9) Principal existence is must.
- 10) Ratification to be informed to 3<sup>rd</sup> party and bind them.
- 11) Ratification to be done in reasonable time.

- *State with reason whether the following statement is correct or incorrect:  
Ratification of agency is valid even if knowledge of the principal is materially defective. (ICAI study Material )*

# Extent of Agent's Authority

1. the nature of the act or the business he is **appointed** to do.
2. things which are **incidental** to the business or are usually done in the course of such business.
3. the **usage of trade or business**.

## Agent's authority is governed by two principles –

- **Agent's authority in normal circumstances [Section 188]**  
e.g. 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.
- **Agent's authority in an emergency [Section 189]**  
e.g. A consigns perishable goods to B at Srinagar, with directions to send them immediately to C at Tamilnadu. B may sell the good if they begin to perish before reaching its destination.

*QRahul, a transporter was entrusted with the duty of transporting tomatoes from a rural farm to a city by Aswin. Due to heavy rains, Rahul was stranded for more than two days. Rahul sold the tomatoes below the market rate in the nearby market where he was stranded fearing that the tomatoes may perish. Can Aswin recover the loss from Rahul on the ground that Rahul had acted beyond his authority? (ICAI study Material ) (MTP Apr. 24) (3 Marks)*

**Ans - Agent's authority in an emergency (Section 189 of the Indian Contract Act, 1872):** An agent has authority, in an emergency, to do all such acts for the purpose of protecting his principal from loss as would be done by a person of ordinary prudence, in his own case, under similar circumstances.

- In the instant case, Rahul, the agent, was handling perishable goods like 'tomatoes' and can decide the time, date and place of sale, not necessarily as per instructions of the Aswin, the principal, with the intention of protecting Aswin from losses.
- Here, Rahul acts in an emergency as a man of ordinary prudence, so Aswin will not succeed against him for recovering the loss.

Mr. Shiv, a cargo owner, chartered a vessel to carry a cargo of wheat from a foreign port to Tuticorin. The vessel got stranded on a reef in the sea 300 miles from the destination. The ship's managing agents signed a salvage agreement for Mr. Shiv. The goods (wheat) being perishable, the salvors stored it at their own expense. Salvors intimated the whole incident to the cargo owner. Mr. Shiv refuse to reimburse the salvor, as it is the Ship-owner, being the bailee of the cargo, who was liable to reimburse the salvor until the contract remained unterminated. Referring to the provision of The Indian Contract Act 1872, do you acknowledge or decline the act of salvor, as an agent of necessity, for Mr. Shiv. Explain? (4 Marks) (MTP Sep. 22)

**Hint :** Section 189 of the Indian Contract Act, 1872 defines agent's authority in an emergency. An agent has authority, in an emergency, to do all such acts for the purpose of protecting his principal from loss as would be done by a person of ordinary prudence, in his own case, under similar circumstances.

In certain circumstances, a person who has been entrusted with another's property may have to incur expenses to protect or preserve it. This is called an agency of necessity. Hence, in the above case the Salvor had implied authority from the cargo owner to take care of the cargo. They acted as agents of necessity on behalf of the cargo owner. Cargo owner were duty-bound towards salvor. Salvor is entitled to recover the agreed sum from Mr. Shiv and not from the ship owner, as a lien on the goods.

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# Duties of Agent

## 1. Act on direction of principal (otherwise liable for loss) [Sec 211]

e.g. A, an agent engaged in carrying on for 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**. As per Sec. 211, A must make good to B the interest usually obtained by such investments.

## 2. Act with reasonable diligence [Sec 212]

e.g. A, an agent for the sale of goods, having authority to sell on credit, sells to B in credit, **without making the proper and usual enquiries** as to the solvency of B. B at the time of such sale, is insolvent. As per Sec. 212, A must make compensation to his principal in respect of any loss thereby sustained.

## 3. Render proper accounts when asked [Sec 213]

## 4. Pay all sums to principal when asked for [Sec 218]

## 5. In difficulty or unusual cases, ask for instructions [Sec 214]

## 6. Not to deal on his own accounts / not to make secret profit. (else principal will recover) [Sec 215-216]

e.g. A directs B to sell A's estate. B buys the estate for himself in the name of C. As per Sec. 215, A may repudiate sale, if he can show that the sale has been disadvantageous to him.

- *ABC Ltd. sells its products through some agents and it is not the custom in their business to sell the products on credit. Mr. Pintu, one of the agents sold goods of ABC Ltd. to M/s. Parul Pvt. Ltd. (on credit) which was insolvent at the time of such sale. ABC Ltd. sued Mr. Pintu for compensation towards the loss caused due to sale of products to M/s. Parul Pvt. Ltd. Will ABC Ltd. succeed in its claim? (ICAI study Material )*

- *Mr. Ahuja of Delhi engaged Mr. Singh as his agent to buy a house in West Extension area. Mr. Singh bought a house for ₹ 20 lakhs in the name of a nominee and then purchased it himself for ₹ 24 lakhs. He then sold the same house to Mr. Ahuja for ₹ 26 lakhs. Mr. Ahuja later comes to know the mischief of Mr. Singh and tries to recover the excess amount paid to Mr. Singh. Is he entitled to recover any amount from Mr. Singh? If so, how much? Explain. (ICAI study Material )*

# Rights of Agent

## 1) Retain

a) Remuneration

b) Money /Expenses paid by him From total money

## 2) To receive remuneration (but not for misconduct part)

e.g. P employs A to recover Rs. 10,000 rupees from T. Through A's misconduct the money is not recovered. A is entitled to no remuneration for his services, and must make good the loss.

## 3) Lien until amount is paid

## 4) Right to be indemnified for

a) Lawful act done

e.g. A, a broker at Delhi, by the orders of P, a merchant there, contracts with T for the purchase of 10 casks of oil for P. Afterwards P refuses to receive the oil, and T sues A. A informs P, who repudiates the contract altogether. A defends, but unsuccessfully, and has to pay damages and costs and incurs expenses. P is liable to A for such damages, costs and expenses.

b) Injury to 3<sup>rd</sup> person

e.g. A, at the request of P, sells goods in the possession of P, but which P had no right to dispose of. A does not know this, and hands over the proceeds of the sale to P. Afterwards O, the true owner of the goods, sues A and recovers the value of the goods and costs. P is liable to indemnify A for what he has been compelled to pay to O, and for A's own expenses.

## 5) To claim compensation for injury caused because of principal's neglect.

e.g. P employs A as a bricklayer in building a house. P puts up the scaffolding himself. The scaffolding is unskillfully put up, and A is in consequence hurt. P must make compensation to B.

# Where agent personally liable

## Shortcut – **FEATURES**

- F** → Foreign principal
- E** → Expressly provides
- A** → Agency coupled with interest
- T** → Trade usage or custom
- U** → Undisclosed principal
- R** → Receives money or pay money by mistake/fraud
- E** → Principal doesn't **E**xist (e.g. Promoter)
- S** → Principal cannot be **S**ued (e.g. minor, idiot)

# Agency coupled with Interest(sec 202)

Agency created for securing benefit to the agent.



Existence of interest  
(before creation of agency)



No Termination in case of

- Death/insanity;
- Prejudice of interest;



Irrevocable to the extent of interest

e.g. A, gives authority to B to sell A's land, and to pay himself, out of the proceeds, the debts due to him from A. A cannot revoke the authority of B. Also, the agency cannot be terminated even in case of insanity or death of A.

**Explain whether the agency shall be terminated in the following cases under the provisions of the Indian Contract Act, 1872:**

- (i) A gives authority to B to sell A's land, and to pay himself, out of the proceeds, the debts due to him from A. Afterwards, A becomes insane.**
- (ii) A appoints B as A's agent to sell A's land. B, under the authority of A, appoints C as agent of B. Afterwards, A revokes the authority of B but not of C. What is the status of agency of C? (4 Marks) (MTP Oct. 22) (MTP May 24) (6 Marks)**

**Hint:**

- (i) According to section 202 of the Indian Contract Act, 1872, 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 to the prejudice of such interest.  
In other words, when the agent is personally interested in the subject matter of agency, the agency becomes irrevocable.  
In the given question, A gives authority to B to sell A's land, and to pay himself, out of the proceeds, the debts due to him from A.  
As per the facts of the question and provision of law, A cannot revoke this authority, nor it can be terminated by his insanity.**
- (ii) According to section 191 of the Indian Contract Act, 1872, a "Sub-agent" is a person employed by, and acting under the control of, the original agent in the business of the agency.  
Section 210 provides that, the termination of the authority of an agent causes the termination (subject to the rules regarding the termination of an agent's authority) of the authority of all sub-agents appointed by him.  
In the given question, B is the agent of A, and C is the agent of B. Hence, C becomes a sub-agent.  
Thus, when A revokes the authority of B (agent), it results in termination of authority of sub-agent appointed by B i.e. C (sub-agent).**

*Q. Bhupendra borrowed a sum of ` 3 lacs from Atul. Bhupendra appointed Atul as his agent to sell his land and authorized him to appropriate the amount of loan out of the sale proceeds. Afterward, Bhupendra revoked the agency. Decide under the provisions of the Indian Contract Act, 1872 whether the revocation of the said agency by Bhupendra is lawful. (ICAI study Material )*

Solution - According to Section 202 of the Indian Contract Act, 1872 an agency becomes irrevocable where the agent has himself an interest in the property which forms the subject-matter of the agency, and such an agency cannot, in the absence of an express provision in the contract, be terminated to the prejudice of such interest.

- In the instant case, the rule of agency coupled with interest applies and does not come to an end even on death, insanity or the insolvency of the principal.
- Thus, when Bhupendra appointed Atul as his agent to sell his land and authorized him to appropriate the amount of loan out of the sale proceeds, interest was created in favor of Atul and the said agency is not revocable. The revocation of agency by Bhupendra is not lawful.



# Legal relationship b/w Principal and Sub-agent and agent

## A] Where sub-agent properly appointed

Principal → responsible → 3<sup>rd</sup> Parties (for the acts of sub-agent)

Agent → responsible → Principal (for the acts of sub-agent)

Sub-agent → responsible → Agent (for the acts done by him)

Sub-agent → not responsible → Principal (except in case of fraud)

## B] Where sub-agent not properly appointed

Principal → not responsible → 3<sup>rd</sup> Parties (for the acts of sub-agent)

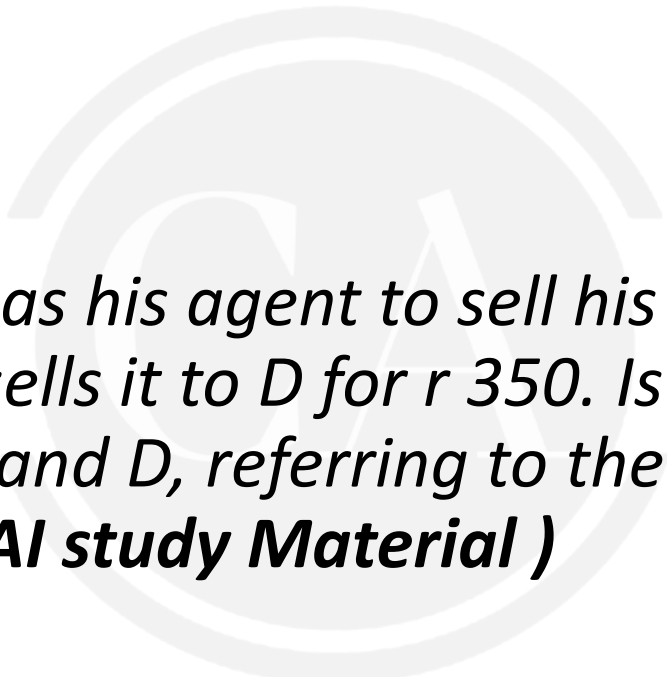
Agent → responsible → Principal + 3<sup>rd</sup> parties (for the acts of sub-agent)

Sub-agent → responsible → Agent (for the acts done by him)

Sub-agent → not responsible → Principal

- *Comment on the statement 'Principal is not always bound by the acts of a sub-agent'. (ICAI study Material )*

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- 
- *A appoints M, a minor, as his agent to sell his watch for cash at a price not less than ₹ 700. M sells it to D for ₹ 350. Is the sale valid? Explain the legal position of M and D, referring to the provisions of the Indian Contract Act, 1872. (ICAI study Material )*

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# *Chapter Name*

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**Companies Act**

# Definition of company (Sec.2(20))

**Company**

**Incorporated  
under this Act**

**Or**

**Under any  
other  
previous law**

**2013**

➤ **1913**

➤ **1942**

➤ **1956**

# Sec. 1 of Companies Act, 2013

## Short title

Companies Act,  
2013

## Extent

Extent to  
whole of  
India

## Application

1. Companies defined u/s 2(20)
2. Banking company – Except, if inconsistent with Banking Regulation Act, 1949
3. Insurance company – Except, if inconsistent with Insurance Act, 1938 or IRDA, 1999
4. Electricity company – Except, if inconsistent with Electricity Act, 2003
5. Statutory Company unless inconsistent with it's Special Act.

# \* FEATURES OF COMPANY

## PLASTIC<sup>2</sup>

P	Perpetual Succession	<ul style="list-style-type: none"><li>• Members may go, members may come</li><li>• Company continues to exist</li><li>• Only law has created, only law has power to dissolve it.</li></ul>
L	Limited Liability	<ul style="list-style-type: none"><li>• Liability of members in company is Ltd</li><li>• Unpaid value of shares / guarantee.</li></ul>
A	Artificial /person separate legal entity	<ul style="list-style-type: none"><li>• Co. is distinct from members of company</li><li>• In eye of law</li><li>• A Co. can own property, have bank A/c, enter into contract in its own name</li><li>• It is a separate legal person</li></ul>
S	Separation of ownership from Mgt.	<ul style="list-style-type: none"><li>• Owned by members</li><li>• Managed by BOD</li></ul>
T	Transferability of Shares	<ul style="list-style-type: none"><li>• In Public Co → Shares are freely transferable from one person to another</li><li>• In Private Co. → ask BOD if transfer to outsiders</li></ul>
I	Incorporated Association	<ul style="list-style-type: none"><li>• Comes into existence once registered under companies Act.</li></ul>
C	Capacity of sue or being sued	<ul style="list-style-type: none"><li>• In his own name</li></ul>
C	Common Seal	<ul style="list-style-type: none"><li>• Metallic seal in which name of Co. engraved.</li><li>• Used where signature required</li><li>• Now not compulsory → instead → 2 director or 1 dir + 1 secretary can authorize</li></ul>

# Question

**In the Flower Fans Private Limited, there are only 5 members. All of them go in a boat on a pleasure trip into an open sea. The boat capsizes and all of them died being drowned. Explain with reference to the provisions of Companies Act, 2013:**

**(i) Is Flower Fans Private Limited no longer in existence?**

**(ii) Further is it correct to say that a company being an artificial person cannot own property and cannot sue or be sued? [RTP June 2023] [MTP Jun 2022(3 Marks)]**



# Answer

**(i) Perpetual Succession – A company on incorporation becomes a separate legal entity. It is an artificial legal person and have perpetual succession which means even if all the members of a company die, the company still continues to exist. It has permanent existence. The existence of a company is independent of the lives of its members. It has a perpetual succession.**

**In this problem, the company will continue as a legal entity. The company's existence is in no way affected by the death of all its members.**

**(ii) The statement given is incorrect. 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.**

# Macaura vs Northern Assurance Co. Ltd.

## Fact of Case

Macaura was holder of nearly all shares and also major creditor of Co.



M insured Co.'s timber in his own name



Timber lost in fire



Can M claim insurance compensation

## Law

A member do not have insurable interest on property of company

## Conclusion

Held, insurance company was not liable to Macaura, as shareholders have not right on any item held by company

# Concept of Separate Legal entity

- Company is separate from members
- Members are shielded from act of company
- Ref. Case Salomon vs Salomon Co. Ltd.

## Fact

Salomon → shoe manufacturer from a company – Saloman & Co. Ltd. and took over his shoe business.

### Consideration

- 20,000 shares of 1 each
- 10,000 – Debenture with charge on Co.'s Asset
- 8782 – Cash

Co. – wound up unsecured creditor claimed that salomon and Co. is one and the same , they should be paid first

## Law

**Company is a separate legal person from member**

## Conclusion

Held, Saloman is different from company. Even if he virturally holds all the shares, he as a member and as a creditor different from company. So he will have rights as secure creditor for his debentures on assets of company.

# Lifting of Corporate Veil

- Means disregarding company as a separate legal entity and pay regards to actual realities
- Can be lifted under following cases.

## 1) To determine enemy character.

- If affairs of Co./ Control under people of enemy country
- Co. Can be held as enemy Co.
- Ref. Case → Daimler Co. Ltd. vs Continental type and Rubber Co.

## 2) To Protect Tax

- To protect revenue of govt.
- Ref. case → Sir Dinshaw manickjee pettitt

## 3) To avoid legal obligation

- If sole purpose to form Co. to reduce amt to be paid by way of bonus.
- Ref. Case → workman of Associated Rubber industries vs Associated Rubber Industries Ltd.

## 4) Forming Subsidiary to act as agent

- Ref. Case → Merchandise transport Ltd. vs British Transport commission

## 5) Fraud or improper Conduct

- Where SLE used for illegal / fraudulent purpose
- Gilford motors Ltd. vs Horne

## Question

**Explain the concept of 'Corporate Veil'. Briefly state the circumstances when the corporate veil can be lifted as per the provisions of the Companies Act, 2013.**

**[June 2023 (6 Marks)]**

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# Answer

**Corporate Veil:** Corporate Veil refers to a legal concept whereby the company is identified separately from the members of the company. Due to this, members of a company are shielded from liability connected to the company's actions.

**Lifting of Corporate Veil:** The following are the cases where company law disregards the principle of corporate personality or the principle that the company is a legal entity distinct and separate from its shareholders or members:

(1) **To determine the character of the company i.e. to find out whether co-enemy or friend:** It is true that, unlike a natural person, a company does not have mind or conscience; therefore, it cannot be a friend or foe. It may, however, be characterised as an enemy company, if its affairs are under the control of people of an enemy country. For this purpose, the Court may examine the character of the persons who are really at the helm of affairs of the company.

(2) **To protect revenue/tax:** In certain matters concerning the law of taxes, duties and stamps particularly where question of the controlling interest is in issue. Where corporate entity is used to evade or circumvent tax, the Court can disregard the corporate identity.

(3) **To avoid a legal obligation:** Where it was found that the sole purpose for the formation of the company was to use it as a device to reduce the amount to be paid by way of bonus to workmen, the Supreme Court upheld the piercing of the veil to look at the real transaction.

(4) **Formation of subsidiaries to act as agents:** A company may sometimes be regarded as an agent or trustee of its members, or of another company, and may therefore be deemed to have lost its individuality in favour of its principal. Here the principal will be held liable for the acts of that company.

(5) **Company formed for fraud/improper conduct or to defeat law:** Where the device of incorporation is adopted for some illegal or improper purpose, e.g., to defeat or circumvent law, to defraud creditors or to avoid legal obligations.

# Question

A transport company wanted to obtain licences for its vehicles but could not obtain licences 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 company. The vehicles were to be transferred to the subsidiary company. Will the parent and the subsidiary company be treated as separate commercial units? Explain in the light of the provisions of the Companies Act, 2013.

[RTP Nov 2022]

# Answer

If the subsidiary is formed to act as agent of the Principal Company, it may be deemed to have lost its individuality in favour of its principal. The veil of Corporate Personality is lifted and the principal will be held liable for the acts of subsidiary company.

The facts of the case are similar to the case of *Merchandise Transport Limited vs. British Transport Commission (1982)*, wherein a 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 the 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 held to be one commercial unit and the application for licences was rejected.

Hence, in this case the parent and the subsidiary company shall not be treated as separate commercial units.



- *A, an assessee, had large income in the form of dividend and interest. In order to reduce his tax liability, he formed four private limited company and transferred his investments to them in exchange of their shares. The income earned by the companies was taken back by him as pretended loan. Can A be regarded as separate from the private limited company he formed? (module)*

# ANSWER

- In the instant case, the four private limited companies were formed by A, the assessee, purely and simply as a means of avoiding tax and the companies were nothing more than the façade of the assessee himself. Therefore, the whole idea of Mr. A was simply to split his income into four parts with a view to evade tax. No other business was done by the company.
- Hence, A cannot be regarded as separate from the private limited companies he formed.

## Private company [Sec. 2(68)]

## Public company [Section 2(71)]

1. Prohibits any invitation to the public to subscribe for any securities of the company.
2. Cannot invite deposits from public
3. Restricts the right to transfer its shares;
4. limits the number of its members to 200

- Is not a private company
- Is a private company which is a subsidiary of a public company,

### Rules for calculation of 200

1. Joint members of shares = 1 member
2. Past and present employee not counted

# Question

**24. Aqua Limited was registered as a public company. There are 230 members in the company as noted below:**

<b>(a) Directors and their relatives</b>	<b>190</b>
<b>(b) Employees</b>	<b>15</b>
<b>(c) Ex-Employees (Shares were allotted when they were employees</b>	<b>10</b>
<b>(d) 5 couples holding shares jointly in the name of husband and wife (5*2)</b>	<b>10</b>
<b>(e) Others</b>	<b>5</b>

**The Board of Directors of the company proposes to convert it into a private company. Also advise whether reduction in the number of members is necessary.**

**[MTP Apr 2023(3 Marks)]**

# Answer

According to section 2(68) of the Companies Act, 2013, "Private company" means a company having a minimum paid-up share capital as may be prescribed, and which by its articles, except in case of One Person Company, limits the number of its members to two hundred.

However, where two or more persons hold one or more shares in a company jointly, they shall, for the purposes of this clause, be treated as a single member.

It is further provided that—

- (A) persons who are in the employment of the company; and
  - (B) persons who, having been formerly in the employment of the company, were members of the company while in that employment and have continued to be members after the employment ceased,
- shall not be included in the number of members.

In the instant case, Aqua Limited may be converted into a private company only if the total members of the company are limited to 200.

# OPC [Sec. 2(62)]

## Basics

- **Company formed by only 1 person**
- **Private Company**
- **Appointing nominee compulsory**

## Qualification for Member/nominee

- Natural Person
- Indian Citizen
- Resident of India or otherwise
- For Resident – stay of Atleast 120 days in Previous (F.Y)

## Restrictions

- One person member of only one OPC
- 1 person nominee of only 1 opc
- If he becomes member of 2 opcs by virtue of death where he was nominee , he shall decide which opc to continue within 180 days
- Minor cannot become nominee or member
- Cannot be converted into sec. 8 companies
- Cannot invest into securities of any company
- Cannot carry non banking financial activity

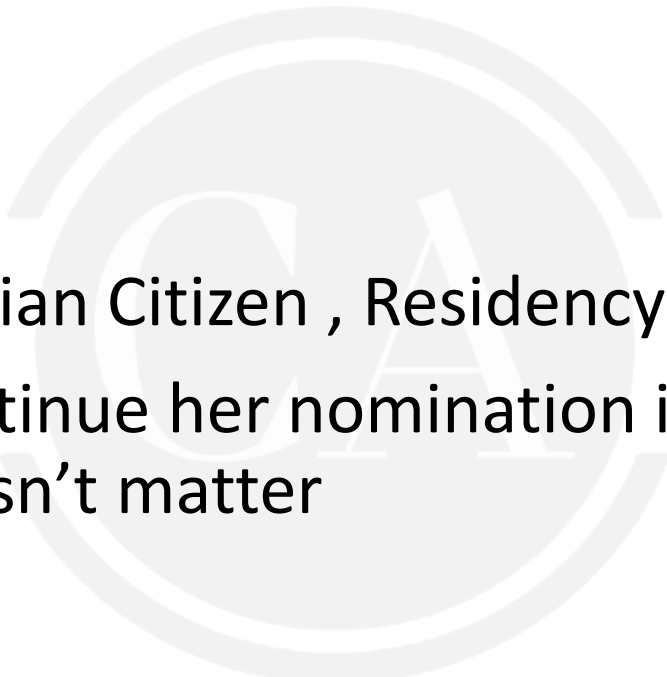
## Other imp points

- Now no limit on P.U.C or turnover
- No provision of compulsory conversion
- OPC can anytime convert into any other Co except sec 8 co

*Naveen incorporated a “One Person Company” making his sister Navita as the nominee. Navita is leaving India permanently due to her marriage abroad. Due to this fact, she is withdrawing her consent of nomination in the said One Person Company. Taking into considerations the provisions of the Companies Act, 2013 answer the questions given below.*

*a) If Navita is leaving India permanently, is it mandatory for her to withdraw her nomination in the said One Person Company?*

*b) If Navita maintained the status of Resident of India after her marriage, then can she continue her nomination in the said One Person Company?  
(module)*

- 
- (A) No , since she is Indian Citizen , Residency doesn't matter
  - (B) Yes, Navita can continue her nomination in the said OPC maintaining status doesn't matter

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# Question

**13. Mr. R is an Indian citizen, and his stay in India during the immediately preceding financial year is for 130 days. He appoints Mr. S, a foreign citizen, as his nominee, who has stayed in India for 125 days during the immediately preceding financial year. Is Mr. R eligible to be incorporated as a One-Person Company (OPC)? If yes, can he give the name of Mr. S in the Memorandum of Association as his nominee? Justify your answers with relevant provisions of the Companies Act, 2013.**

**[May 2022 (3 Marks)]**

# Answer

**Law - As per the provisions of the Companies Act, 2013, only a natural person who is an Indian citizen and resident in India or otherwise can become member or even nominee in OPC**

**Resident in india means -person who stayed in India for a period of not less than 120 days during immediately preceding financial year)**

**R can be member as he is Indian Citizen  
and S cannot be nominee as not Indian citizen**

**CAWALLAH**

# Question

**8. Mr. Anil formed a One Person Company (OPC) on 16 April, 2018 for manufacturing electric cars. The turnover of the OPC for the financial year ended 31 March, 2019 was about ₹ 2.25 crores. His friend Sunil wanted to invest in his One Person Company (OPC), so they decided to convert it voluntarily into a private limited company. Can Anil do so, as per the provisions of the Companies Act, 2013?**

**[Nov. 2022 (4 Marks)]**

# Answer

**Section 2(62) of the Companies Act, 2013 defines one person company as a company which has only one person as a member. However, a private company shall have minimum 2 members without any restriction on the share capital or turnover. If OPC is converted into private company Mr. Anil and Mr. Sunil both can be the members of the company and investment from Mr. Sunil can be accepted.**

**A One Person Company can voluntarily convert itself into a private company by following the compliances given under the Companies Act, 2013.**

**In the instant case, OPC formed by Mr. Anil can be voluntarily converted into a private company by following the compliances given under the Companies Act, 2013. Here, the information given relating to turnover for the financial year ended 31st March, 2019 is immaterial.**

# SMALL COMPANY [SEC. 2 (85)]

## Conditions

(1) Paid up share capital

- Does not exceed 4 cr

&

(2) Turnover (as per last P &L)

- Does not exceed 40 cr.

## Following cannot be small company

- (a) Public company
- (b) Holding company of any company
- (c) Subsidiary of any company
- (d) Sec. 8 company
- (e) Statutory company

# ON THE BASIS OF CONTROL

**Holding & Subsidiary Co.**

**Sec 2 (87)**



Relation exist between 2 Co. if

- i. **A Company**
  - **Itself**
  - **Itself & subsidiary**
  - **Through subsidiaries**

↓

**Holds more than 50% voting rights in other company**
- ii. **It controls composition of BOD in other company** (i.e can appoint or remove majority of BOD)

**Associate Co. 2(6)**



If other co. hold significant influence in that co. but not subsidiary



**i.e. atleast 20% ,Max 50% of total voting powers**  
**Includes joint venture co.**

# Question

**Explain the classification of the companies on the basis of control as per the Companies Act, 2013.**

**[RTP June 2023]**

**CAWALLAH**

# Question

14. BC Private Limited and its subsidiary KL Private Limited are holding 90,000 and 70,000 shares respectively in PQ Private Limited. The paid-up share capital of PQ Private Limited is ₹ 30 Lakhs (3 Lakhs equity shares of ₹ 10 each fully paid). Analyse with reference to provisions of the Companies Act, 2013 whether PQ Private Limited is a subsidiary of BC Private Limited. What would be your answer if KL Private Limited is holding 1,60,000 shares in PQ Private Limited and no shares are held by BC Private Limited in PQ Private Limited?

[RTP Dec 2023]



# Answer

In the instant case, BC Private Limited together with its subsidiary KL Private Limited is holding 1,60,000 shares (90,000 + 70,000 respectively) which is more than one half in nominal value of the Equity Share Capital of PQ Private Limited. Hence, PQ Private Limited is subsidiary of BC Private Limited.

(ii) In the second case, the answer will remain the same. KL Private Limited is a holding 1,60,000 shares i.e., more than one half in nominal value of the Equity Share Capital of PQ Private Limited (i.e., holding more than one half of voting power). Hence, KL Private Limited is holding company of PQ Private Company and BC Private Limited is a holding company of KL Private Limited.

Hence, by virtue of Chain relationship, BC Private Limited becomes the holding company of PQ Private Limited.

# Question

4. ABC Limited has allotted equity shares with voting rights to XYZ Limited worth ₹ 15 crores and convertible preference shares worth ₹ 10 crores during the financial year 2022-23. The total share capital of the company is ₹ 100 crores.

Comment on whether XYZ Limited would be called an Associate Company as per the provisions of the Companies Act, 2013? Also define an Associate Company.

[June 2023 (4 Marks)]

# Answer

In the instant case, ABC Limited has allotted equity shares with voting rights to XYZ Limited worth ₹ 15 crore and convertible preference shares worth ₹10 crore during the financial year 2022-23 out of the total share capital of ABC Limited of ₹ 100 crore.

Since XYZ Limited is holding only 15% significant influence (₹ 15 crore equity shares with voting rights) in ABC Limited, which is less than twenty per cent, XYZ Limited is not an Associate company of ABC Limited.

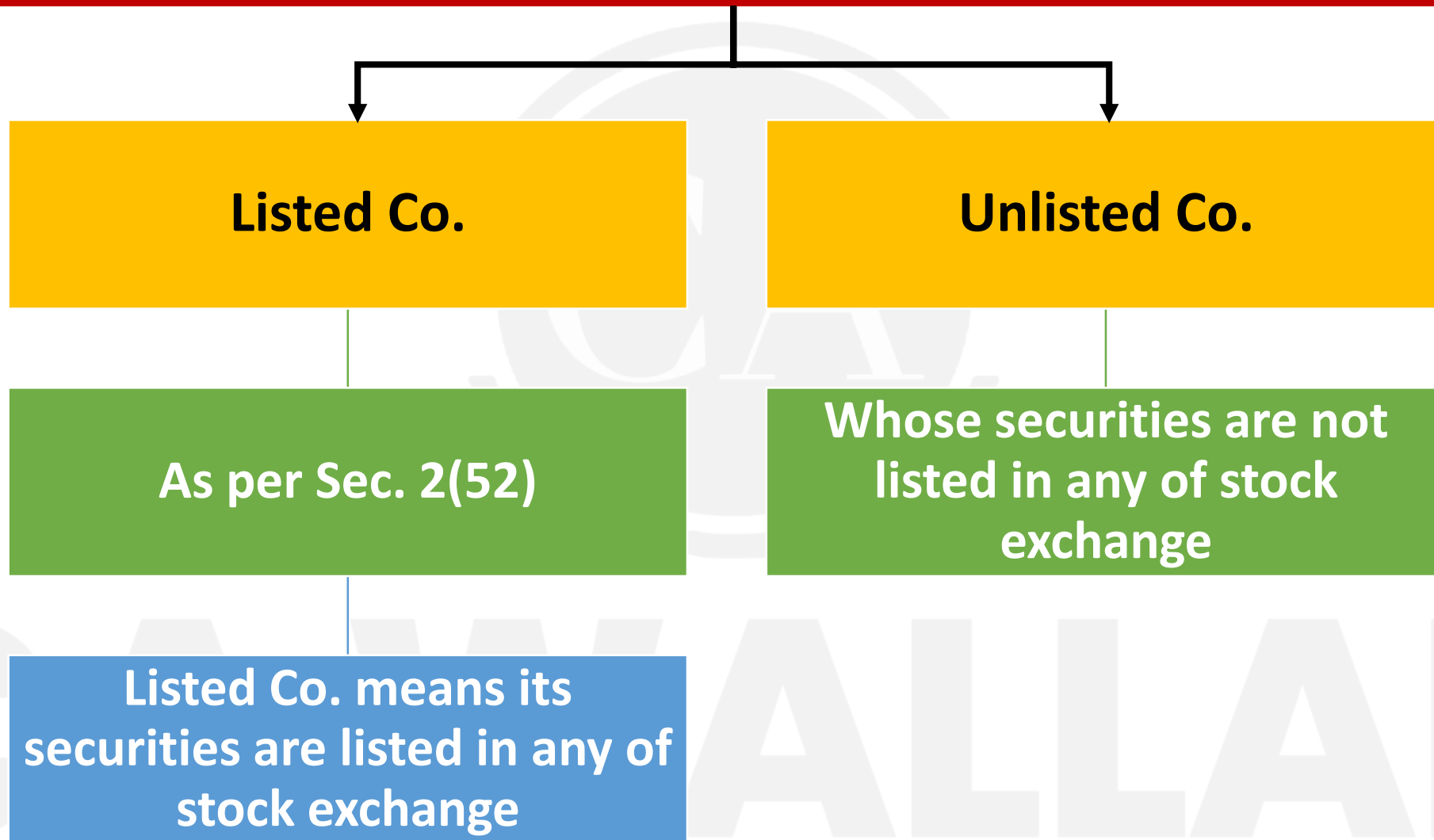
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# Classification

## On the Basis of Liability



# Classification on basis of listing



Note: -To be listed company only it's equity shares should be listed that too in India.

# Question

**Explain listed company and unlisted company as per the provisions of the Companies Act, 2013.**

**[Nov. 2022 (2 Marks)]**

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# GOVERNMENT COMPANY SEC. 2 (45)

Means any company in which **not less than fifty- one per cent.** of the paid-up share capital (**having voting rights** ) 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;

# Question

**15. Narendra Motors Limited is a Government Company. Shah Auto Private Limited have share capital of ₹ 10 crore in the form of 10,00,000 shares of ₹ 100 each. Narendra Motors Limited is holding 5,05,000 shares in Shah Auto Private Limited. Shah Auto Private Limited claimed the status of Government Company. Advise as legal advisor, whether Shah Auto Private Limited is government company under the provisions of Companies Act, 2013?**

**[RTP Dec 2023]**



# Answer

**Law – Quote both sec 2(45 ) and sec 2(87)**

**Conclusion - By virtue of provisions of Section 2(87) of Companies Act, 2013, Shah Auto Private Limited is a subsidiary company of Narendra Motors Limited because Narendra Motors Limited is holding more than one-half of the total voting power in Shah Auto Private Limited. Further as per Section 2(45), a subsidiary company of Government Company is also termed as Government Company. Hence, Shah Auto Private Limited being subsidiary of Narendra Motors Limited will also be considered as Government Company.**

# Question

The State Government of X, a state in the country is holding 48 lakh shares of Y Limited. The paid up capital of Y Limited is ₹ 9.5 crore (95 lakh shares of ₹ 10 each). Y Limited directly holds 2,50,600 shares of Z Private Limited which is having share capital of ₹ 5crore in the form of 5 lakh shares of ₹ 100 each. Z Private Limited claimed the status of a subsidiary company of ₹ 100 each. Z Private Limited claimed the status of a subsidiary company of Y Limited as well as a Government company. Advise as a legal advisor, whether Z Private Limited is a subsidiary company of Y Limited as well as a Government company under the provisions of the Companies Act, 2013?

[Dec 2023(4 Marks)]

# Answer

According to Section 2(45) of the Companies Act, 2013, Government Company means any company in which not less than 51% of the paid-up share capital is held by-

- (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.

As per Section 2(87) of the Companies Act, 2013, “subsidiary company” in relation to any other company (that is to say the holding company), means a company in which the holding company—

- (i) controls the composition of the Board of Directors; or
- (ii) exercises or controls more than one-half of the total voting power either at its own or together with one or more of its subsidiary companies.

In the instant case, the State Government of X, a state in the country is holding 48 Lakh shares in Y Limited which is below 51% of the paid up share capital of Y Limited i.e. 48.45 Lakh shares (51% of 95 Lakh shares). Hence Y Limited is not a Government Company.

Further, Y Limited directly holds 2,50,600 shares in Z Private Limited, which is more than one-half of the total shares of Z Limited i.e. 2,50,000 shares (50% of 5 Lakh shares). Thus, the Company controls more than one-half of the total voting power of Z Limited. Hence Z Private Limited is a subsidiary of Y Limited.

Therefore, we can conclude that Z Private Limited is a subsidiary of Y Limited but not a Government Company since Y Limited is not a Government Company.

## FOREIGN COMPANY 2(42)

**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**

CAWALLAH

## Question

**10. Mike LLC incorporated in Singapore having an office in Pune, India. Analyse whether Mike LLC would be called as a foreign company as per the provisions of the Companies Act, 2013? Also explain the meaning of foreign company.**

**[Nov. 2022 (3 Marks)]**

# Answer

**Mike LLC is incorporated in Singapore and having a place of business in Pune, India. Since, Mike LLC is incorporated outside India and having a Place of business in India, hence it is a foreign Company.**

**Foreign Company [Section 2(42) of the Companies Act, 2013]: It means any company or body corporate incorporated outside India which—**

- (i) has a place of business in India whether by itself or through an agent, physically or through electronic mode; and**
- (ii) conducts any business activity in India in any other manner.**

# SEC. 8 COMPANY NOT FOR PROFIT

## Conditions

1. Object to promote Art, Science, sports, Education, Social welfare, etc.
2. Apply profit only for its purpose
3. No payment of dividend to members

## Applications

- To C.G
- ROC issues license
- Note - Firm can also become member in sec 8 Co

## Effect of license

- No use of word Ltd. or Pvt. Ltd.
- Many tax benefits

## Revocation of license

- C.G may revoke
- If breach in conditions

## Effect of Revocation

- Needs to register in any other company
- Wind up
- Amalgamate with other Sec 8 Co having similar object

## Question

**23. Can a non-profit organization be registered as a company under the Companies Act, 2013? If so, what procedure does it have to adopt?**

**[MTP Nov 2022(6 Marks)]**

**CAWALLAH**



# Question

**20. A Company registered under Section 8 of the Companies Act, 2013, has been consistently making profits for the past 5 years after a major change in the management structure. Few members contented that they are entitled to receive dividends. Can the company distribute dividend? If yes, what is the maximum percentage of dividend that can be distributed as per provisions of the Companies Act, 2013? Also, to discuss this along with other regular matters, the company kept a general meeting by giving only 14 days' notice. Is this valid?**

**[RTP Nov 2022]**

# Answer

**A company registered under Section 8 of the Companies Act, 2013 is prohibited from the payment of any dividends to its members.**

**Hence in the given case, the contention of the members to distribute dividend from the profits earned is wrong.**

**Also, Section 8 company is allowed to call a general meeting by giving 14 days instead of 21 days.**

# Question

**21. A, B and C has decided to set up a new club with name of ABC club having objects to promote welfare of Christian society. They planned to do charitable work or social activity for promoting the art work of economically weaker section of Christian society. The company obtained the status of section 8 company and started operating from 1st April, 2017 onwards.**

**However, on 30th September 2019, it was observed that ABC club was violating the objects of its objective clause due to which it was granted the status of section 8 Company under the Companies Act 2013.**

**Discuss what powers can be exercised by the central government against ABC club, in such a case?**

**[RTP May 2022]**

# Answer

**Section 8 of the Companies Act, 2013 deals with the formation of companies which are formed to promote the charitable objects of commerce, art, science, education, sports etc. Such company intends to apply its profit in promoting its objects. Section 8 companies are registered by the Registrar only when a license is issued by the Central Government to them.**

**Since ABC Club was a Section 8 company and it was observed on 30 th September, 2019 that it had started violating the objects of its objective clause. Hence in such a situation the following powers can be exercised by the Central Government:**

- (i) The Central Government may by order revoke the licence of the company**
- (ii) Where a licence is revoked, the Central Government may, by order, if it is satisfied that it is essential in the public interest, direct that the company be wound up under this Act or amalgamated with another company registered under this section.**
- (iii) However, no such order shall be made unless the company is given a reasonable opportunity of being heard.**

# Public Financial Institutions [Sec 2(72)]

## Specified

- a) LIC
- b) Infrastructure development finance company ltd.
- c) UTI
- d) Institutions already notified under 1956 Act
- e) Any other notified by CG in consultation with RBI

## Notified

### Rules to notify

- a) Constituted under any Central or State Act
- b) Not less than 51%

↓  
Paid up Capital

↓  
CG/SG/ Partly by CG and partly by SG

# DORMANT COMPANY

- A company which has no significant accounting transaction, is called as a Dormant Company

"Significant accounting transaction" means any transaction other than- (RAAM)

- R**- payment of fees by a company to the Registrar;
- A**-payments made by it to fulfil the requirements of this Act or any other law
- A**-allotment of shares to fulfil the requirements of this Act; and
- M** - payments for maintenance of its office and records.

**Note - "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

# Question

**3. MTK Private Limited is a company registered under the Companies Act, 2013 on 5th January, 2021. The company has not started its business till now. On 7th April, 2023, a notice has been received from ROC for non-filing of FORM No-INC-20A. Identify under which category MTK Private Limited company is classified. Explain the definition of the category of the company in detail.**

**[Dec 2023(3 Marks)]**

# Answer

**“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. [Explanation (i) to Section 455 of the Companies Act, 2013]**

**“Significant accounting transaction” means any transaction other than—**

- (a) payment of fees by a company to the Registrar;**
- (b) payments made by it to fulfil the requirements of this Act or any other law;**
- (c) allotment of shares to fulfil the requirements of this Act; and**
- (d) payments for maintenance of its office and records.**

**[Explanation (ii) to Section 455 of the Companies Act, 2013]**

**In the instant case, MTK Private Limited was registered on 5th January, 2021 and has not started its business till now. On 7th April, 2023, a notice has been received from ROC for non-filing of Form No. INC-20A. Since the Company has not started its business and a period of more than two years have already elapsed, it will be treated as an inactive company.**



# Nidhi Company [Sec. 406]

- created mainly to cultivate habit of



**Cost thrift & saving**



**Amounts it's members**

- Main function to



**Borrow money**

**Lend money**



**Among it's members**

- A.K.A mutual benefit society

# MEMORANDUM OF ASSOCIATION

## Definition

**MOA is MOA**

Either originally framed Or Altered from time to time

## Object

**2 Fold**

1) **Outsider**

- Object or Scope of Company
- Company deal

✓

X

2) **Investor**

If they invest their money will be utilized for said purpose

## Content

1. **Name Clause**
2. **Situation Clause**
3. **Object Clause**
4. **Liability Clause**
5. **Capital Clause**
6. **Subscription Clause**
7. **Nominee Clause (Only for OPC)**

## Format

Table

A

B

C

D

E

Type of Company

Limited by Shares

Limited by Guarantee

Both

Unlimited company not having share capital

Unlimited company having share capital

## Other Imp Points

- Also known as charter of company constitution of Company

- **MOA should be:**

- ✓ Printed
- ✓ Divided into para
- ✓ Consecutively numbered
- ✓ Signed by required subscribed

OPC – 1 Member

Pvt. Co. - 2 Member

Public Co. – 7 member

# ARTICLES OF ASSOCIATION

## Definition

**AOA is AOA**

Either originally framed

Or

Altered from time to time

## Object

**Internal Management of the company**

## Content

**Contains Rules regarding**

- Shares
- Debentures
- Prospectus
- Meetings
- BOD
- General powers of company

## Format

**Table**

F

G

H

I

J

**Type of Company**

Limited by Shares

Both

Limited by Guarantee

Unlimited company having share capital

Unlimited company not having share capital

## Other Imp Points

▪ **AOA should be**

- ✓ Printed
- ✓ Divided into paragraphs
- ✓ Consecutively numbered
- ✓ Signed by required Subscribers

**OPC – 1 Member**

**Pvt. Co. - 2 Member**

**Public Co. – 7 member**

# DOCTRINE OF ULTRA VIRES ACT (Beyond the power)

	Meaning	Effect on Contract	Ratification	Other important points
Ultra vires the 'MOA'	Any act not authorised by: a) Companies Act b) Object Clause	Void-ab-initio	✘	1) Member may obtain injunction 2) Director personally liable, if funds misapplies or wasted.
Ultra vires the 'AOA'	Any act not authorised or against articles	Voidable @ option of shareholders	can be ratified by altering AOA	
Ultra vires the 'Director'	Any act beyond powers of directors	Voidable @ option of shareholders	can be ratified by altering AOA	

# Question

**Explain the 'Doctrine of ultra vires under the Companies Act, 2013. What are the consequences of 'ultra vires' acts of the company?**

**[May 2022 (6 Marks)]**

**CAWALLAH**

# Question

ABC Limited was into sale and purchase of iron rods. This was the main object of the company mentioned in the Memorandum of Association. The company entered into a contract with Mr. John for some finance related work. Later on, the company repudiated the contract as being ultra vires.

With reference to the same, briefly explain the doctrine of “ultravires” under the Companies Act, 2013. What are the consequences of ultravires acts of the company?

[RTP June 2023]

# Answer

**Law - Doctrine of ultra vires**

**Conclusion - Hence in the given case, ABC Limited cannot enter into a contract outside the purview of its object clause of Memorandum of Association as it becomes ultra vires and thus null and void.**

CAWALLAH

# ASHBURY RAILWAY CARRIAGE AND IRON CO. LTD V/S RICHIE

## Object clause of company

- a) Make, Sell, lend, hire → railway carriage, wagons
- b) Carry on mechanical engineering & gen contractors
- c) Purchase, lease, work, sell → mine, minerals, land & building

## Contract by company

For financing of construction of railway line in Belgium

## Decision by court

- ultra vires act
- Financing is different from mechanical engineering
- Even general contractor can define its meaning from mechanical engineer.



# Doctrine of Constructive Notice

- i. MOA, AOA is a public document. It is available to outsiders at a reasonable cost**
- ii. So, it is presumed that anybody dealing with company have read MOA & AOA of the company**
- iii. If not, outsider is at fault and such contract will not be enforceable on company**
- iv. This doctrine operates in favour of company & protects company from outsider**
- v. Ref. Case → Kotla Venkata Swamy vs C. Ram Murti**

# Kotal Venkata Swamy vs C. Ram Murthi

## Facts

Whether Co. will be liable on contract where AOA specified signature of M.D, Sec. & WTD, However on a mortgage deed, only secretary and WTD signed

## Law

Doctrine of Constructive

## Conclusion

No contract will not be enforceable on the company

# Doctrine of Indoor Management

- i. It is exception to doctrine of constructive notice**
- ii. Although outsider dealing with co. should appraise themselves with MOA, AOA, but they are not require to inquire into internal management of company**
- iii. So, if it is a case of internal irregularity, company is at fault and such contracts will be enforceable on company.**
- iv. This doctrine protects outsider form company and operates in favour of outsiders**
- v. Ref. Case → Royal British Bank vs Turquand**

# Royal British Bank vs Turquand

## Facts

AOA specified that Co. can borrow money only when resolution by shareholders will be passed but co. borrowed money without consent of shareholders whether co. will be liable on the contract

## Law

Doctrine of Indoor Management

## Conclusion

Contract will be liable on company

# Question

**11.** The Articles of Association of Aarna Limited empowers its managing agents to borrow loans on behalf of the company. Ms. Anika, the director of the company, borrowed ₹ 18 Lakhs in name of the company from Quick Finance Limited, a non-banking finance company. Later on, Aarna Limited refused to repay the money borrowed on the pretext that no resolution authorizing such loan have been actually passed by the company and therefore the company is not liable to pay such loan.

Decide whether the contention of Aarna Limited is correct in accordance with the provisions of the Companies Act, 2013?

[May 2022 (4 Marks)]

# Answer

## Law – Quote Doctrine of Indoor Management

**Conclusion -In the given question, Quick Finance Limited being external to the company, need not enquire whether the necessary resolution was passed properly. Even if Aarna Limited claims that no resolution authorizing the loan was passed, Aarna Limited is bound to repay the loan to Quick Finance Limited.**

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# Exceptions to Indoor Management

**1. Knowledge of irregularity**

**Howard vs Patent Ivory Manufacturing company**

**2. Negligence  
Suspicious  
Circumstances or  
unusual magnitude of  
transactions**

**Anand Bihari Lal vs Dinshaw & Company**

**3. Forgery**

**Ruben vs Great Fingall Consolidated Company**

**4. No knowledge of  
articles**

**Rama Corporation vs Proved Tin & General Investment  
Company Ltd.**

**5. Illegal  
ransactions**

----

- *Explain clearly the doctrine of 'Indoor Management' as applicable in cases of companies registered under the Companies Act, 2013. Explain the circumstances in which an outsider dealing with the company cannot claim any relief on the ground of 'Indoor Management'. (module)*



# Question

7. Mr. R, a manufacturer of toys approached MNO Private Limited for supply of raw material worth ₹ 1,50,000/-. Mr. R was offered a credit period of one month. Mr. R went to the company prior to the due date and met Mr. C, an employee at the billing counter, who convinced the former that the payment can be made to him as the billing-cashier is on leave.

Mr. R paid the money and was issued a signed and sealed receipt by Mr. C. After the lapse of due date, Mr. R received a recovery notice from the company for the payment of ₹ 1,50,000/-.

Mr. R informed the company that he has already paid the above amount and being an outsider had genuine reasons to trust Mr. C who claimed to be an employee and had issued him a receipt.

The Company filed a suit against Mr. R for non-payment of dues. Discuss the fate of the suit and the liability of Mr. R towards company as on current date in consonance with the provision of the Companies Act 2013? Would your answer be different if a receipt under the company seal was not issued by Mr. C after receiving payment?

[Nov. 2022 (4 Marks)]

# Answer

**(i) Fate of the suit and the liability of Mr. R towards the company:**

## **Doctrine of the Indoor Management**

According to the Doctrine of the Indoor Management, the outsiders are not deemed to have notice of the internal affairs of the company. They are entitled to assume that the acts of the directors or other officers of the company are validly performed, if they are within the scope of their apparent authority. So long as an act is valid under the articles, if done in a particular manner, an outsider dealing with the company is entitled to assume that it has been done in the manner required. This is the indoor management rule, that the company's indoor affairs are the company's problem. This rule has been laid down in the landmark case-the Royal British Bank vs. Turquand. (Known as "Turquand Rule")

In the instant case, Mr. R is not liable to pay the amount of ₹ 1,50,000 to MNO Private Limited as he had genuine reasons to trust Mr. C, an employee of the company who had issued him a signed and sealed receipt.

**(ii) Liability of Mr. R in case no receipt is issued by Mr. C:**

Exceptions to doctrine of indoor management: Suspicion of irregularity is an exception to the doctrine of indoor management. The doctrine of indoor management, in no way, rewards those who behave negligently. It is the duty of the outsider to make necessary enquiry, if the transaction is not in the ordinary course of business.

If a receipt under the company seal was not issued by Mr. C after receiving payment, Mr. R is liable to pay the said amount as this will be deemed to be a negligence on the part of Mr. R and it is his duty to make the necessary enquiry to check that whether Mr. C is eligible to take the payment or not.

# Howard vs Patent Ivory Manufacturing company

**AOA specified resolution for borrowing more than Rs. 1000**



**Co. borrowed money from Directors themselves**



**But no resolution passed**



**Held directors had knowledge of irregularity so they cannot claim defense from indoor management**



**Contract liable only for 1000**

# Ruben vs Great Fingall Consolidated Company

**Secretary issued share certificate by forging signature  
of 2 directors**



**Held that in forgery, protection of indoor  
management will not apply & contract will not be  
liable on company**

CAWALLAH

# Promoters Sec. 2 (69)-PAC + Act = PACT

- a) who has been named as such in a **Prospectus** or
- b) is identified by the company in the **Annual return**
- c) who has **Control** over the affairs of the company, directly or indirectly
- d) in accordance with whose advice, directions or instructions the Board of Directors of the company is accustomed to **Act**.

**Note** - If Person is acting in his professional capacity he is not Promoter

Mr. Abhi is a Chartered Accountant and MBA by profession, has been appointed as an Executive Director on the Board of XYZ Limited. His job profile includes advising the Board of Directors of the company on various compliance matters, strategies, business plans, and risk matters relating to the company. Keeping in view of above position whether Mr. Abhi can be classified as the Promoter of XYZ Limited? Please examine the same under the provisions of the Companies Act, 2013. (RTP May 2022)

## **Hint**

As the job profile of Mr. Abhi is only limited to advise the Board of Directors on various compliance matters, strategies, business plans and risk matters relating to business of the company and that too only in a professional capacity, he will not be classified as a Promoter of XYZ Limited.

# Step to incorporate company [Sec. 7]

**Step 1 → Obtain Name of Company (Spice + Part A )**

**Step 2 → File application for incorporation (Spice + Part B) (Inc.32)**

**Step 3 → Attach with application form**



**DM – DADA**



**D → Details of Subscriber and first directors**

**M → MOA signed by required subscribers**

**D → Declaration from professional (CA / CS / CMA / Advocate) → That all requirement of act and rules for incorporation complied**

**A → AOA signed by required subscribers**

**D → Declaration from Subscribers & 1<sup>st</sup> Directors**

→ **Not convicted for any offence connected with formation / mgt. of Co.**

→ **Not been found guilty of fraud under Co. Act. → Previous 5 years**

→ **Documents filed with ROC and information – correct and complete**

**A → Address of regd. Office/ correspondence**

**Step 4 → Submit to ROC (Central registration Centre)**

**Step 5 → ROC issue certificate of Incorporation (Inc-11)**

# Sec. 9 Effect of Registration

## On Incorporation / Registration

**COMPANY**

Becomes

**BODY CORPORATE**

**SUBSCRIBERS**

Becomes

**MEMBERS OF  
COMPANY**

**MOA & AOA**

**(Sec. 10)**

Binding on  
members

**AS IF THEY THEMSELVES HAVE  
SIGNED**

CAWALLAH

# Consequences Of Furnishing False Information For Incorporation

Action by CG / Tribunal / ROC

Against PERSON

Against COMPANY

- (a) Promoters;
- (b) First Directors;
- (c) Professionals incorporating company

- i. Direct Limited liability to Unlimited
- ii. Removal of name
- iii. Pass order to wound up Company
- iv. Any order which they deem fit.

Liabe u/s 447



# Classification of Capital

Authorised / Nominal Capital

Max capital that can be raised by company

Issued Capital

Unissued

- That part of authorized capital that is issued for subscription
- Two types

That part of authorized capital that has not yet be issued

Subscribed

Unsubscribed

- That part of issued capital that has been subscribed by members
- Two types

That part of issued capital that has not been subscribed

Called up

Uncalled

- That part of subscribed capital that has been called for payment
- two types

That part of subscribe capital that has not been called payment

Paid

Unpaid

That part of called up capital which is paid by members

that part of called up capital which is unpaid by members

# \*Shares

- Share means share in share capital of company
- Movable property (Sec 44)
- Every share have distinct no. (Sec. 45)  
except in demat form
- Two types of shares (Sec. 43)

## Equity Shares



- Which are not preference shares
- Two types
  - (i) Normal Equity shares
  - (ii) Equity shares with Differential Voting Rights (DVR)
    - Voting /dividend different from normal shares
- Normally can vote in all matters in general meeting

## Preference Shares



→ Preference as to

Payment of dividend

→ Fixed dividend

Requirement of capital @  
wind up

→ Can vote in matters related to them

## Question

**2. Explain the kinds of share capital as per the Companies Act, 2013. Also explain when the capital shall be deemed to be preference capital.**

**[Dec 2023(6 Marks)]**

CAWALLAH

# Answer

**Kinds of share capital:** Section 43 of the Companies Act, 2013 provides the kinds of share capital. According to the said provision, the share capital of a company limited by shares shall be of two kinds, namely:—

**1. “Equity share capital”, with reference to any company limited by shares, means all share capital which is not preference share capital;**

**Equity share capital— can be**

- (i) with voting rights; or**
- (ii) with differential rights as to dividend, voting or otherwise in accordance with such rules as may be prescribed;**

**2. “Preference share capital”, with reference to any company limited by shares, means that part of the issued share capital of the company which carries or would carry a preferential right with respect to—**

**(a) payment of dividend, either as a fixed amount or an amount calculated at a fixed rate, which may either be free of or subject to income-tax; and**

**(b) repayment, in the case of a winding up or repayment of capital, of the amount of the share capital paid-up or deemed to have been paid-up, whether or not, there is a preferential right to the payment of any fixed premium or premium on any fixed scale, specified in the memorandum or articles of the company;**

**Capital shall be deemed to be preference capital, despite that it is entitled to either or both of the following rights, namely:—**

**(a) that in respect of dividends, in addition to the preferential rights to the amounts specified as above, it has a right to participate, whether fully or to a limited extent, with capital not entitled to the preferential right aforesaid;**

**(b) that in respect of capital, in addition to the preferential right to the repayment, on a winding up, of the amounts specified above, it has a right to participate, whether fully or to a limited extent, with capital not entitled to that preferential right in any surplus which may remain after the entire capital has been repaid.**

# *Chapter Name*

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**Negotiable  
Instrument Act**



# Negotiable Instrument Act, 1881

By Kunal Sir



# Basics

- Negotiable → **Transferable**
- Instrument → **Document in writing**
- It is a instrument in writing which can be transferred from one person to another.
- Came into force from 1<sup>st</sup> Mar. 1882
- Act applies to whole of India.
- Main Objective → To legalise system

↓

By which instruments made under it

↓

Could pass from hand to hand

↓

By negotiation like any other goods

# Essential Characteristic of N.I

## Shortcut

Negotiable

Instrument

Of SUM

Crores

Delivered

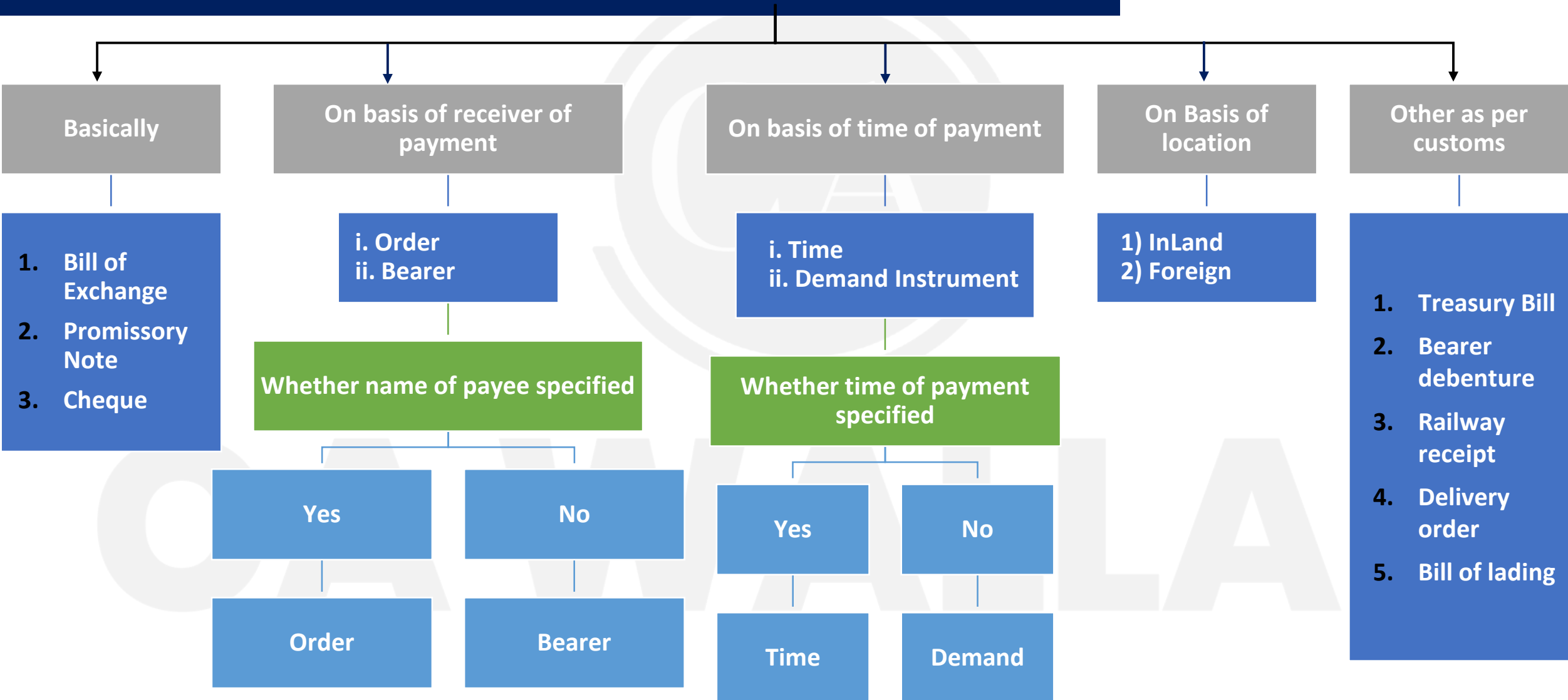
For Free

## Characteristics

- 1) **Transferable** from one person to another
- 2) Can be **transferred** any no of times
- 3) Has to be in **writing**
- S → 4) **Signed** by drawer
- U → 5) Contains **unconditional** promise / order
- M → 6) Promise/ order to pay **money** only
- C → 7) Amt/ Time / Payee → **Certain**
- 8) Instrument made should be **delivered**
- 9) Holder in due course (HDC) gets title **FREE** from defect



# Types of N.I



**Note : 1) If last /only endorsement is blank, it is bearer instrument**

# Question

As per Negotiable Instruments Act, 1881,

Negotiable Instruments means(module)

a.Promissory Note

b.Bills of Exchange

c.Cheque

d.All the above



**D**

CAWALLAH

# Question

On which of the followings, even not defined in Negotiable Instruments Act 1881, provisions of Act are applicable: **(module)**

- a. Hundies
- b. Treasury Bills
- c. Bearer Debentures
- d. All of the above



**D**

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# Promissory Note [Sec. 4]

## Meaning

Instrument in writing

Containing a unconditional undertaking

Signed by maker

To pay certain sum of money only

To order of certain person or bearer

## Parties

(1) **Maker**  
→ who promise to pay  
→ Debtor

(2) **Payee**  
To whom amt. payable

**Note : P.N cannot be bearer at all only  
RBI/ C.G can make bearer P.N. e.g.  
currency note.**

## Essential Characteristics

Shortcut → **WE – US – CM**

**W** → **Writing** → oral not allowed

**E** → **Express** Promise to pay  
(mere acknowledgement not sufficient)

**U** → **Unconditional** → Promise  
→ If condition then should be certain to happen

**S** → **Signed** by maker

**S** - Stamped

**C** → **Certain**

Sum

→ Maker

→ Payee

**M** → **Money** → Promise to pay **money** only

# Question

State whether the following statements are promissory notes or not?

1. "I promise to pay B or order Rs. 500"
2. "Mr. B, I owe you Rs. 500"
3. "I acknowledge myself to be indebted to B in Rs. 1,000 to be paid on demand, for value received".
4. "I am liable to B, in a sum of Rs. 500 to be paid by instalments.
5. "I am bound to pay the sum of Rs. 500 which I received from you".
6. "I promise to pay B Rs. 500 and all other sums which shall be due to him".
7. "I promise to pay B Rs. 1000 and the fine according to the rules".
8. "I promise to pay B Rs. 500, first deducting there out any money which he may owe me".
9. "I promise to pay B Rs. First deducting there out any money which he may owe me".
10. "I promise to pay B a sum of Rs. 500 when convenient or able".
11. "I promise to pay B Rs. 500 when he delivers the goods".
12. "I promise to pay B Rs. 500 seven days after my marriage with C".
13. "I promise to pay B Rs. 500 on D's death
14. "I promise to pay B Rs. 500 on D's death, provided D leaves me enough to pay that sum".
15. "I promise to pay B Rs. 500 and to deliver to him my black horse on 1st January next"
16. "I promise to pay B in 20 shares and 10 bonds of XY Ltd.

# Solution

1. Yes.
2. No , only acknowledgement of debt
3. Yes
4. No , conditional
5. No , mere acknowledgement of debt
6. No , sum uncertain
7. Yes , sum can be calculated as fine fixed
8. No , sum uncertain
9. No , sum uncertain
10. No , conditional
11. No , conditional
12. No , conditional
13. Yes as death is certain
14. No , conditional
15. No. Promise to pay money only
16. No. Promise to pay money only



Rama executes a promissory note in the following form, 'I promise to pay a sum of `10,000 after three months'. Decide whether the promissory note is a valid promissory note. (module)

Hint - The promissory note is an unconditional promise in writing. In the above question the amount is certain but the date and name of payee is missing, thus making it a bearer instrument. As per Reserve Bank of India Act, 1934, a promissory note cannot be made payable to bearer - whether on demand or after certain days. Hence, the instrument is illegal as per Reserve Bank of India Act, 1934 and cannot be legally enforced.

# Bills of Exchange (Sec. 5) [BOE]

## Meaning

Instrument in writing

Containing a unconditional undertaking

Signed by maker

Directing a certain person

To pay certain sum of money only

to certain person or his order

## Parties

(1) **Drawer**  
maker of BOE

(2) **Drawee**  
→ Who is directed to pay  
→ On acceptance he become acceptor  
→ Liability primary & unconditional

(3) **Payee**  
To whom money paid

## Essential Characteristics

Shortcut → WE – US – CM

W → Writing

E → Express → order to pay

U → Unconditional and definite

S → Signed by drawer

C → Certain

Drawer

Drawee

Payee

Sum

(Note : BOE cannot be made payable to bearer on demand)

M → Money → order to pay money only

# Question

How many parties in Bills of exchange:  
**(module)**

a.2

b.3

c.4

d.5



**C**

CAWALLAH

# Question

Which is not the essential characteristic of Bill of exchange: **(module)**

- a. Must be in writing
- b. Must contain an express promise to pay
- c. Instrument must be signed
- d. Must be stamped



**B**

CA WALLAH

# Distinguish Between BOE & P.N

Shortcut → Jisko

Definition

Yaad hogi →

Accept

My

liability

And

Promise

To give Party  
to

Bearer

Basis	BOE	P.N
1) Definition	'Refer previous slides'	"Refer Previous Slides'
2) Acceptance	Requires acceptance	Do not require acceptance
3) Primary Liable	Drawee/Acceptor	Maker
4) Promise /Order	Order to pay	Promise to Pay
5) Parties	3 Parties (1) Drawer (2) Drawee (3) Payee	2 Parties Maker and payee
6 Bearer	Cannot be bearer on demand	Cannot be bearer at all

# Cheque → Sec. 6

## Meaning

- ↓
- Cheque is BOE
- ↓
- Drawn on specified banker
- ↓
- Not expressed to be payable otherwise than demand
- ↓
- Includes
- a) Electronic image of truncated cheque
- b) Cheque in electronic form

## Parties to cheque

- ↓
- (1) **Drawer**
- Who draws cheque
- Debtor
- liability is primary and conditional
- (2) **Drawee**
- Bank who makes payment
- Always banker
- (3) **Payee**
- Named in N.I to whom money is paid or his order

## Essential Elements

- ↓
- 1) All essentials of BOE
- 2) Drawee always banker
- 3) Always a demand instrument
- 4) All cheque are bill all bill are not cheque

## Punishment →

- 1) Cheque issued for discharge of debt
- 2) Cheque presented within validity period (3 months)
- 3) Reason for Dishonour –

## Dishonor of cheque (Sec. 138)

- ↓
- 2x amt of cheque or 2 years imprisonment or both
- ↓
- Conditions

Insufficient fund or stop payment

Within 30 days →

Give notice to demand payment

↓

15 days →

Time to pay

↓

Within 1 month →

File complaint with court



# Question

Where any cheque drawn by a person is dishonoured due to insufficiency of funds, such person shall be punished with:

**(module)**

- a. imprisonment for a term which may extend to two years,
- b. with fine which may extend to twice the amount of the cheque,
- c. imprisonment for a term which may extend to two years, or with fine which may extend to twice the amount of the cheque, or with both,
- d. No punishment



**C**

CAWALLAH

Bholenath drew a cheque in favour of Surendar. After having issued the cheque; Bholenath requested Surendar not to present the cheque for payment and gave a stop payment request to the bank in respect of the cheque issued to Surendar. Decide, under the provisions of the Negotiable Instruments Act, 1881 whether the said acts of Bholenath constitute an offence? (module)

Hint - the act of Bholenath, i.e., his request of stop payment constitutes an offence under the provisions of the Negotiable Instruments Act, 1881.

# \* Inland Instrument or Foreign Instrument [Sec. 11 & 12]

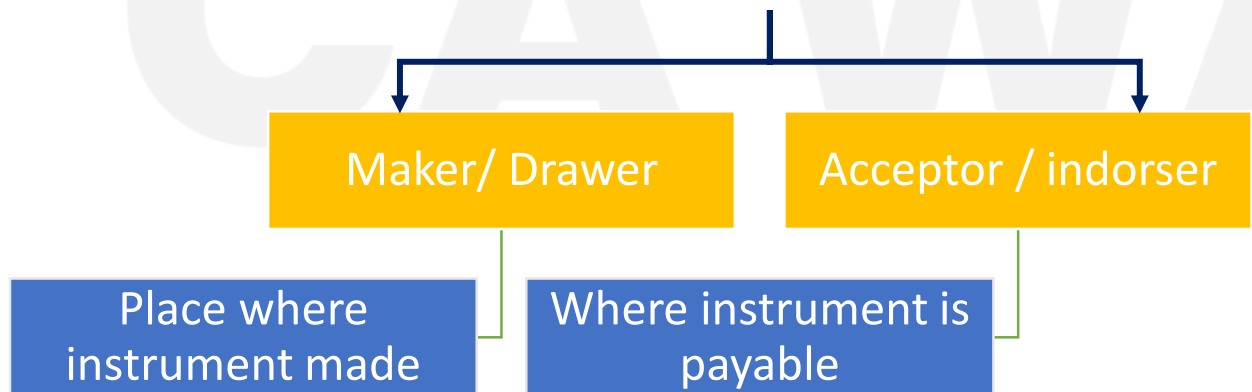
- Foreign Instrument → which is not inland
- Inland Instrument → (1) Drawn in India



- + (2) Payable in India
- or
- (3) Drawn upon Indian resident

Condition no. (1) Should always satisfy & atleast 1 condition should satisfy out of (2) & (3)

- Inland remains inland even if endorsed in foreign country
- Foreign bill → liability of (Sec. 134)



## Example

A bill of exchange is drawn by A in Berkley where the rate of interest is 15% and accepted by B payable in Washington where the rate of interest is 6%. The bill is indorsed in India and is dishonoured. An action on the bill is brought against B in India. He is liable to pay interest at the rate of 6% only. But if A is charged as drawer, he is liable to pay interest at 15%.

Which is not an Inland Instrument: **(module)**

- a. P/N made in India + payable in India + drawn upon person resident in India
- b. P/N made in India + payable in India + drawn upon person resident outside India
- c. P/N made in India + payable outside India + drawn upon person resident in India
- d. P/N made in India + payable outside India + drawn upon person resident outside India



**D**

CAWALLAH

# Question

State with reasons whether each of the following instruments is an Inland Instrument or a Foreign Instrument:

1. A bill drawn in Delhi upon a merchant in Agra and accepted payable in London.
2. A bill drawn in Delhi upon a merchant in London and accepted payable in Agra.
3. A bill drawn in Delhi upon a merchant in London and accepted payable in London.
4. A bill drawn in London upon a merchant in Agra and accepted payable in Delhi.
5. A bill drawn in Delhi on a merchant in Agra but endorsed in London.
6. A bill drawn in London on a merchant in Agra and endorsed in Delhi.



# Solution

1. Inland
2. Inland
3. Foreign
4. Foreign
5. Inland
6. Foreign



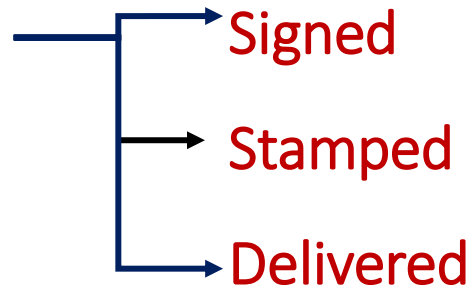
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## \*Inchoate Instrument [Sec. 20]

- Valid + Wholly Partially Blank



SSD



- Effect

- 1) Holder / original parties can recover only upto consideration between parties i.e. amount intended to be paid when made.
- 2) Holder in due course (HDC) can claim any amt. mentioned in instrument subject to stamp duty

# Question of Inchoate Instrument



Note:

- 1) Holder in Due Course (HDC) means
- 2) If not HDC then holder
- 3) Holder gets title of transferor
- 4) HDC gets better title than transferor

Obtained Instrument

- (1) Against Consideration
- (2) Before Maturity
- (3) In good faith

# Solution of Inchoate Instrument

If Instrument held by following till maturity

Hardik Pandya

- Original party
- Can recover to amt of consideration between immediate party
- 50 cr

They can recover

Ishan

- Gift so holder only
- Gets title of transferor Hardik
- 50 Cr.

Rishabh

- Gift so Holder only
- Gets Title of transferor Ishan
- 50 Cr.

Rohit

- HDC
- Can Recover amt mentioned
- 60 Cr.

Ritika

- Holder
- Gets Title of Transferor Rohit
- 60 Cr.

## \*Ambiguous Instrument [Sec. 17]

- An instrument which is vague and cannot be clearly identified either as a bill of exchange, or as a promissory note
- Holder as to assume one and transferred accordingly

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## Question

An instrument which is vague and cannot be clearly identified either as a bill of exchange, or as a promissory note, is called as: (module)

- a) bearer instrument
- b) Ambiguous instrument
- c) Order instrument
- d) Inland instrument



**B**

CA WALLAH

# Question

Negotiable Instrument which can be treated either P/N or BOE, is known as: **(module)**

- a. Inland Instrument
- b. Inchoate Instrument
- c. Ambiguous Instrument
- d. Foreign Instrument

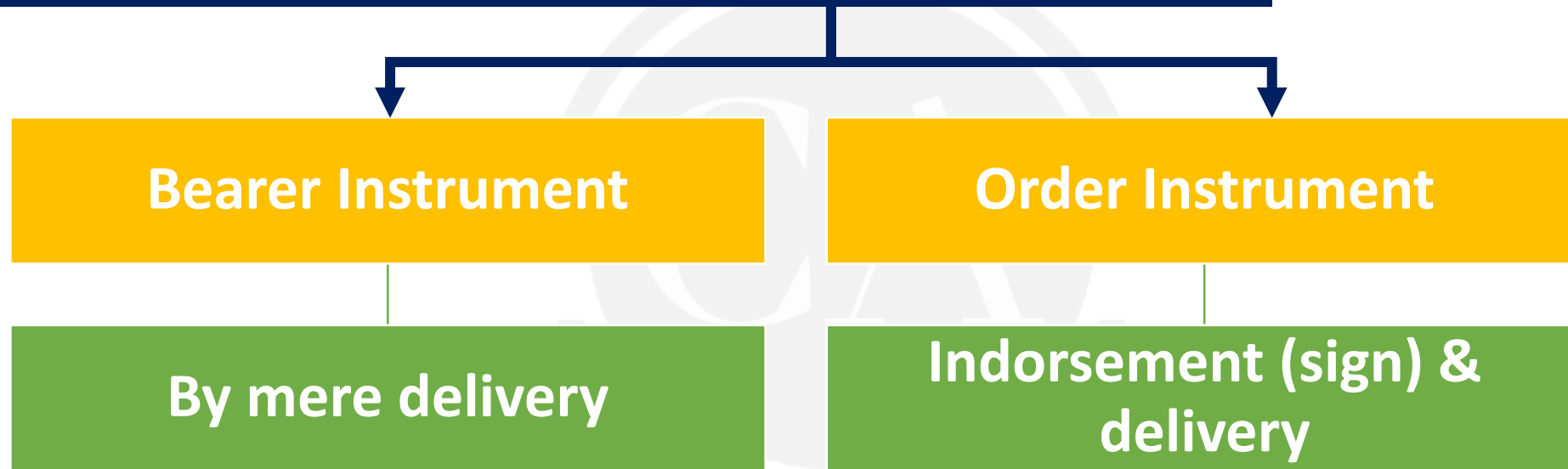




**C**

CAWALLAH

# Negotiation (transfer)



- **Delivery can be actual or constructive**
- **If delivered to transferee's agent → delivery ✓**
- 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.

# Question

A negotiable instrument is an instrument which is freely transferable from one person to another by:  
(module)

a. Simple delivery

b. Indorsement and delivery

c. Indorsement

d. Registered post



**B**

CA WALLAH

Order Instrument can be negotiated by: **(module)**

- a. By delivery only
- b. By endorsement only
- c. By endorsement & delivery
- d. None of above

CAWALLAH



**C**

CAWALLAH

M drew a cheque amounting to ` 2 lakh payable to N and subsequently delivered to him. After receipt of cheque N indorsed the same to C but kept it in his safe locker. After sometime, N died, and P found the cheque in N's safe locker. Does this amount to Indorsement under the Negotiable Instruments Act, 1881?  
(module)

- No, P does not become the holder of the cheque as the negotiation was not completed by delivery of the cheque to him. (Section 48, the Negotiable Instruments Act, 1881)

M owes money to N. Therefore, he makes a promissory note for the amount in favor of N, for safety of transmission he cuts the note in half and posts one half to N. He then changes his mind and calls upon N to return the half of the note which he had sent. N requires M to send the other half of the promissory note. Decide how rights of the parties are to be adjusted.  
**(module)**

Hint -Delivery refers to the whole of the instrument and not merely a part of it. Delivery of half instrument cannot be treated as constructive delivery of the whole. So, the claim of N to have the other half of the P/N sent to him is not maintainable. M is justified in demanding the return of the first half sent by him. He can change his mind and refuse to send the other half of the P/N.



**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 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)

<b>To whom</b>	<b>Maker (P/N), Acceptor (BOE), Drawee (CH)</b>
<b>If default in presentment</b>	<b>No party liable thereto</b>
<b>Exception</b>	<b>If P/N is payable on demand and is not payable at a specified place, no presentment is necessary.</b>
<b>Time</b>	<b>During usual business hours</b>
<b>If instrument payable after date or sight</b>	<b>Must be presented for payment at maturity</b>
<b>P/N payable by instalments</b>	<b>Must be presented for payment on 3<sup>rd</sup> day after date fixed for payment of each instalment.</b>
<b>Instrument payable at specified place</b>	<b>Must be presented for payment at that place.</b>
<b>Where no exclusive place specified</b>	<b>Must be presented for payment at the place of business (if any) or at the usual residence</b>
<b>No known place of business or residence</b>	<b>Presentment may be made to him in person wherever he can be found</b>
<b>Instrument payable on demand</b>	<b>Must be presented for payment within a reasonable time after it is received by the holder.</b>

**Note: Delay in presentment for acceptance or payment is excused if the delay is caused by circumstances beyond the control of the holder.**

# \* When Presentment for payment unnecessary [Sec. 76]

Instrument dishonored on due date

CA → FEW → KID → Unnecessary

C → Closed POB during business day / hrs → if payable at POB.

A → Absent from place → if instrument payable at some place.

F → If cannot be Found after due search → place not specified

E → Expressed to pay → notwithstanding non presentment

W → Waives to Present

K → Knowledge of Non-Presentment

I → Party Intentionally prevents presentment

D → No Damages suffered → By Drawer → due to non Presentment

Part payment

Promise to pay on future date

## Rules as to Compensation (Sec. 117)

In case of dishonor 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 realization.

Note: In case of foreign currency, current rate of exchange.

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