

CA **FOUNDATION**

Business Laws

Revisionary Notes



By CA DEEPIKA RATHI

AS PER NEW ICAI SYLLABUS

All New Revised Edition

Relevant for September 2024 and Onwards Examination

DEDICATED

To My Parents

for raising me to believe that anything was possible

Disclaimer

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4.	4.
5.	5.

Feel free to e-mail your feedback, problems or suggestions to us on drathi31@gmail.com

Happy Learning and all the best!!

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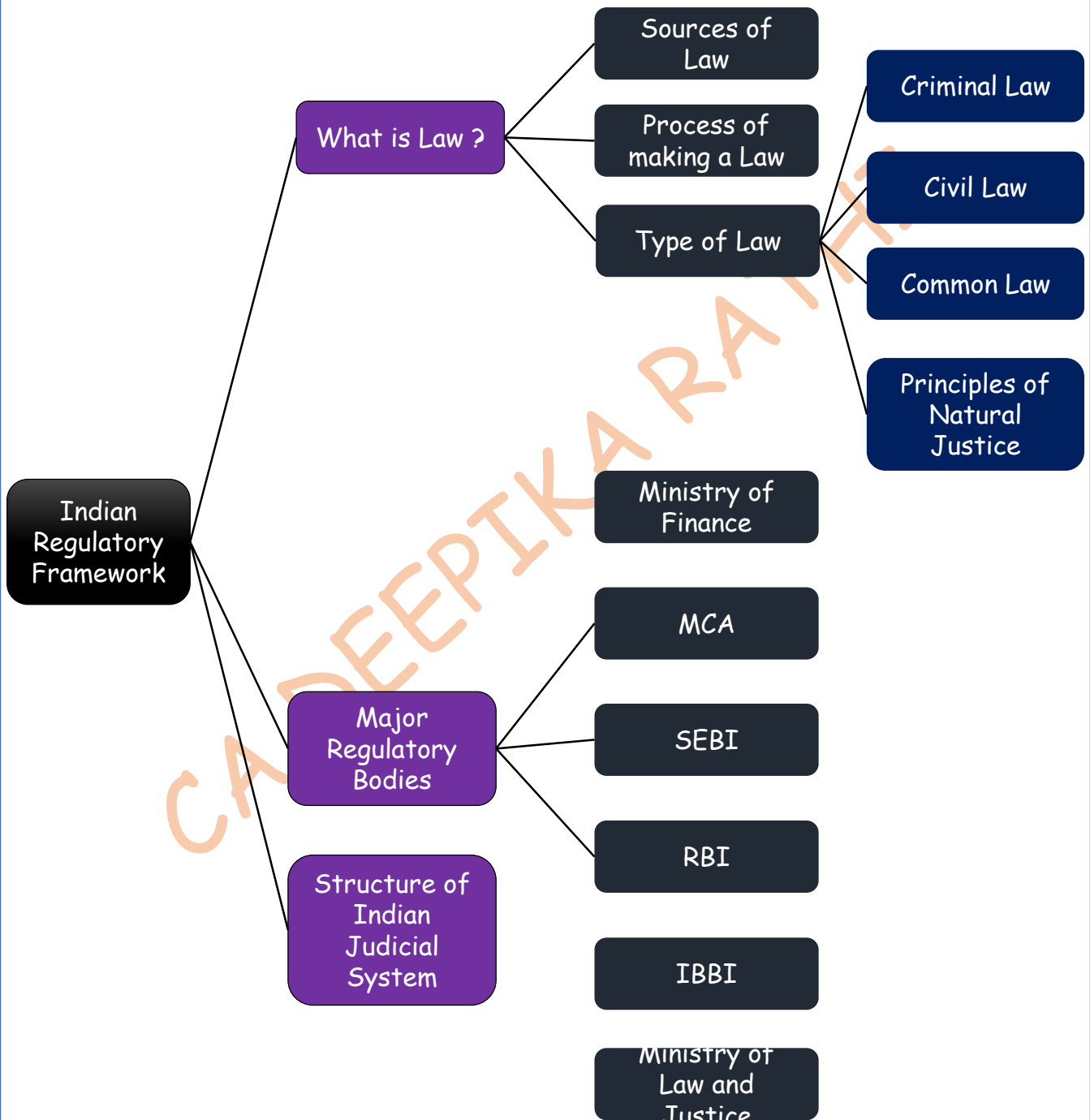


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Chapter-1 : Indian Regulatory Framework





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1. WHAT IS LAW ?

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

2. SOURCES OF LAW

The main sources of law in India are

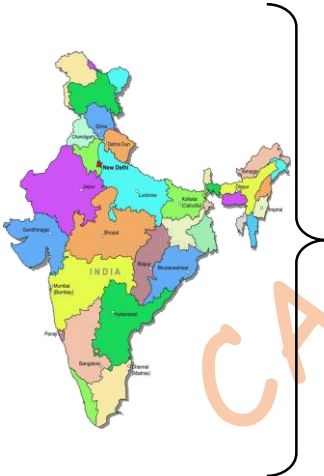
The statutes or laws made by Parliament and State Assemblies, Precedents

OR

The Judicial Decisions of various Courts

And

Established Customs and Usages



- India is a parliamentary democracy, have a constitution which is the basis and source for all laws.
- Parliament is the ultimate law-making body.
- Laws passed by parliament may apply throughout all or a portion of India, whereas the laws passed by state legislatures apply only within the borders of the states concerned

- The Government of India Act, 1935, passed by the Parliament of the United Kingdom is the precursor for the Constitution of India.
- It defined the characteristics of the Government from "unitary" to "federal". Powers were distributed between Centre and State to avoid any disputes.



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- In 1937, Federal Court was established and had the jurisdiction of appellate, original and advisory.
- The powers of Appellate Jurisdiction extended to civil and criminal cases whereas the Advisory Jurisdiction was extended with the powers to Federal Court to advise Governor-General in matters of public opinion.
- The Federal Court operated for 12 years and heard roughly 151 cases. The Federal Court was supplanted by India's current Apex Court, the Supreme Court of India.



Constitution of India 1950

The foremost law that deals with the framework within which our democratic system works and our laws

Made for the people, by the people

Also provides for and protects certain Fundamental rights of citizens.

It also lays down Fundamental duties as well as the powers and duties of Governments, both Central and State.

The laws in India are interconnected with each other forming a hybrid legal system.

The people who wrote the Constitution decided to divide the law-making power between

Central Government

And

Various State Governments



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Indian Constitution has three lists

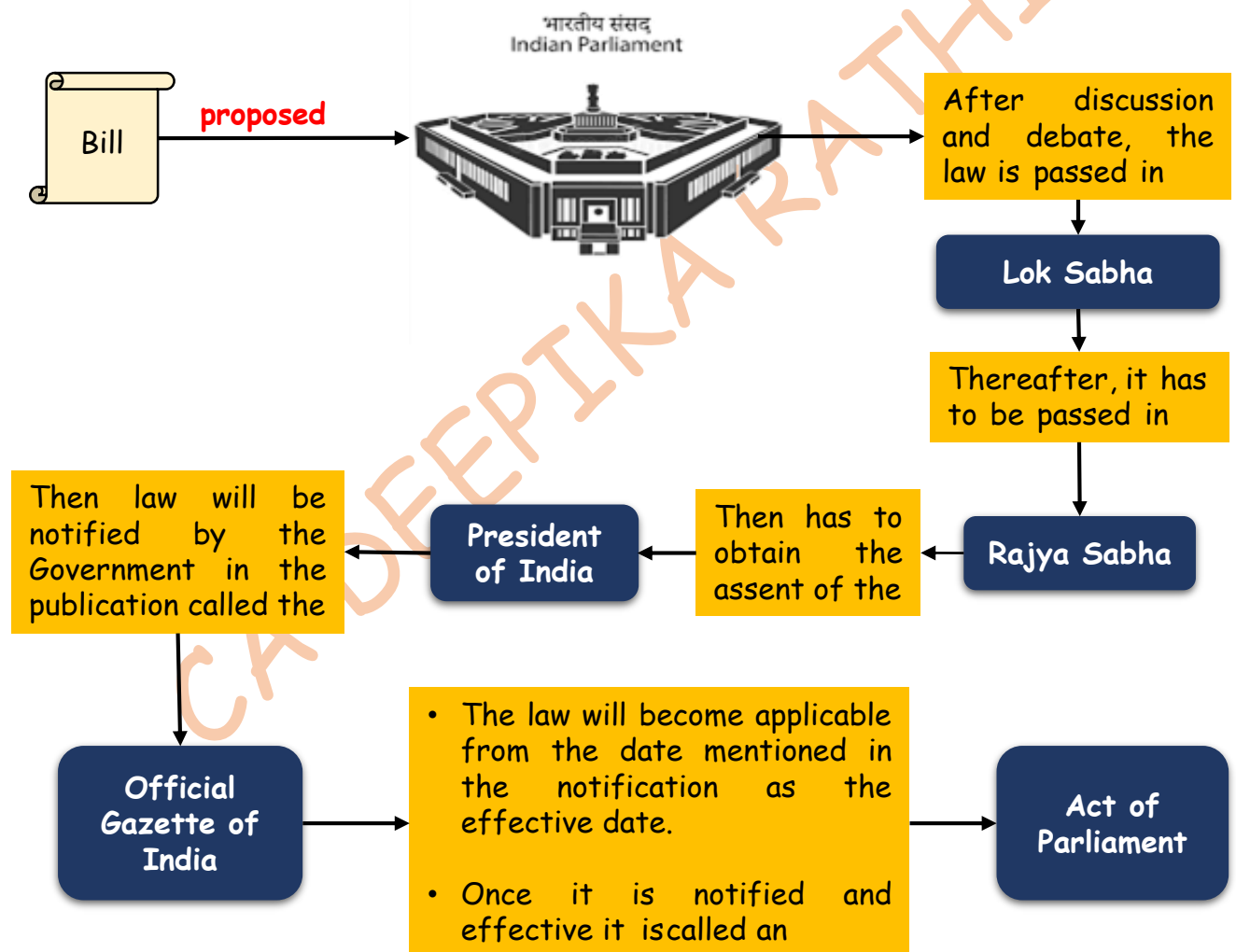
Central List

State List

Joint List

3. THE PROCESS OF MAKING A LAW

When a law is proposed in parliament it is called a Bill



Types of laws in the Indian Legal System

Criminal Law

Civil Law

Common Law

Principles of Natural Justices



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Criminal Law

- ✓ Criminal law is concerned with laws pertaining to violations of the rule of law or public wrongs and punishment of the same.
- ✓ Criminal Law is governed under the Indian Penal Code, 1860, and the Code of Criminal Procedure, 1973 (Crpc).
- ✓ The Indian Penal Code, 1860, defines the crime, its nature, and punishments whereas
- ✓ The Criminal Procedure Code, 1973, defines exhaustive procedure for executing the punishments of the crimes.
- ✓ **Example:** Murder, rape, theft, fraud, cheating and assault.

Civil Law

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

Common Law

- ✓ A judicial precedent or a case law is common law.
- ✓ A judgment delivered by the Supreme Court will be binding upon the courts within the territory of India under Article 141 of the Indian Constitution.



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- ✓ The doctrine of **Stare Decisis** is the principle supporting common law.
- ✓ It is a Latin phrase that means "**to stand by that which is decided.**"
- ✓ The doctrine of *Stare Decisis* reinforces the obligation of courts to follow the same principle or judgement established by previous decisions while ruling a case where the facts are similar or "on all four legs" with the earlier decision.

Principles of Natural Justices

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

4. ENFORCING THE LAW

- ✓ After a law is passed in parliament it has to be enforced. Somebody should monitor whether the law is being followed.
- ✓ This is the job of the executive. Depending on whether a law is a Central law or a State law the Central or State Government will be the enforcing authority.
- ✓ For this purpose government functions are distributed to various ministries.
- ✓ Some of the popular Ministries are the Ministry of Finance, the Ministry of Corporate Affairs, the Ministry of Home Affairs, the Ministry of Law and Justice and so on.
- ✓ These Ministries are headed by a minister and run by officers of the Indian administrative and other services.



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

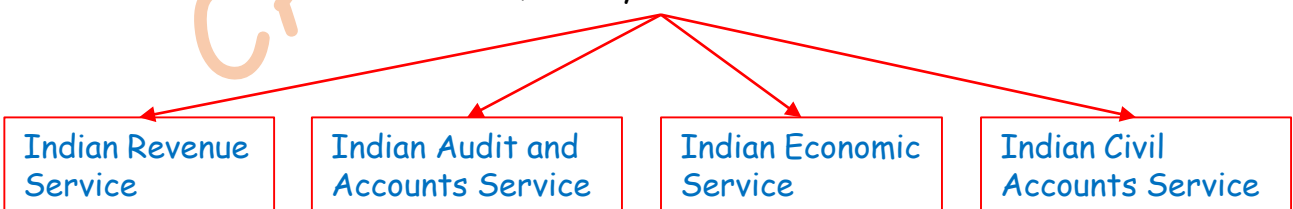
1. THE MINISTRY OF FINANCE

- The Ministry of Finance (Vitta Mantralaya) is a Ministry within the Government of India concerned with the economy of India, **serving as the Treasury of India.**
- It concerns itself with taxation, financial legislation, financial institutions, capital markets, centre and state finances, and the Union Budget.
- **One of the important functions of the Finance Ministry is the presentation of the Union Budget.**

Constitution of the Ministry of Finance

Ministry of Finance

- is the apex controlling authority
- of four Central Civil Services, namely



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

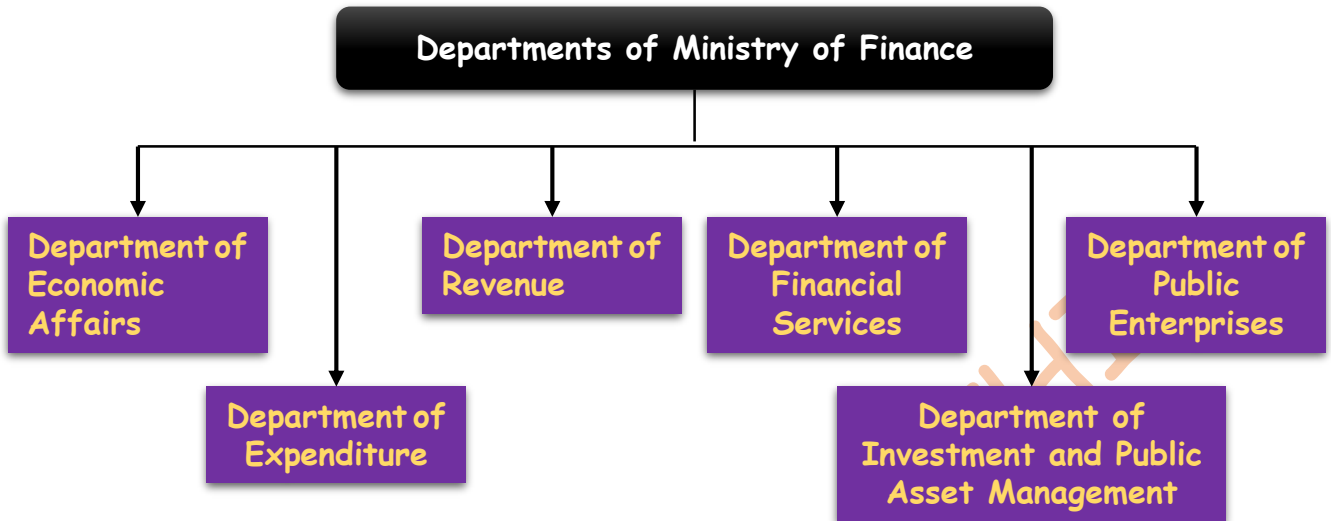


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i. Departments under the Ministry of Finance



i. Ministry of Corporate Affairs (MCA)

- ❖ It is an Indian Government Ministry
- ❖ Primarily concerned with administration of
 - Companies Act 2013
 - Companies Act 1956
 - Limited Liability Partnership Act, 2008
 - Insolvency and Bankruptcy Code, 2016
- ❖ Responsible mainly for the regulation of → Indian enterprises in the industrial and services sector.
- ❖ The Ministry is mostly run by civil servants of the → ICLS cadre.

ii. Ministry of Home Affairs (Griha Mantralaya)

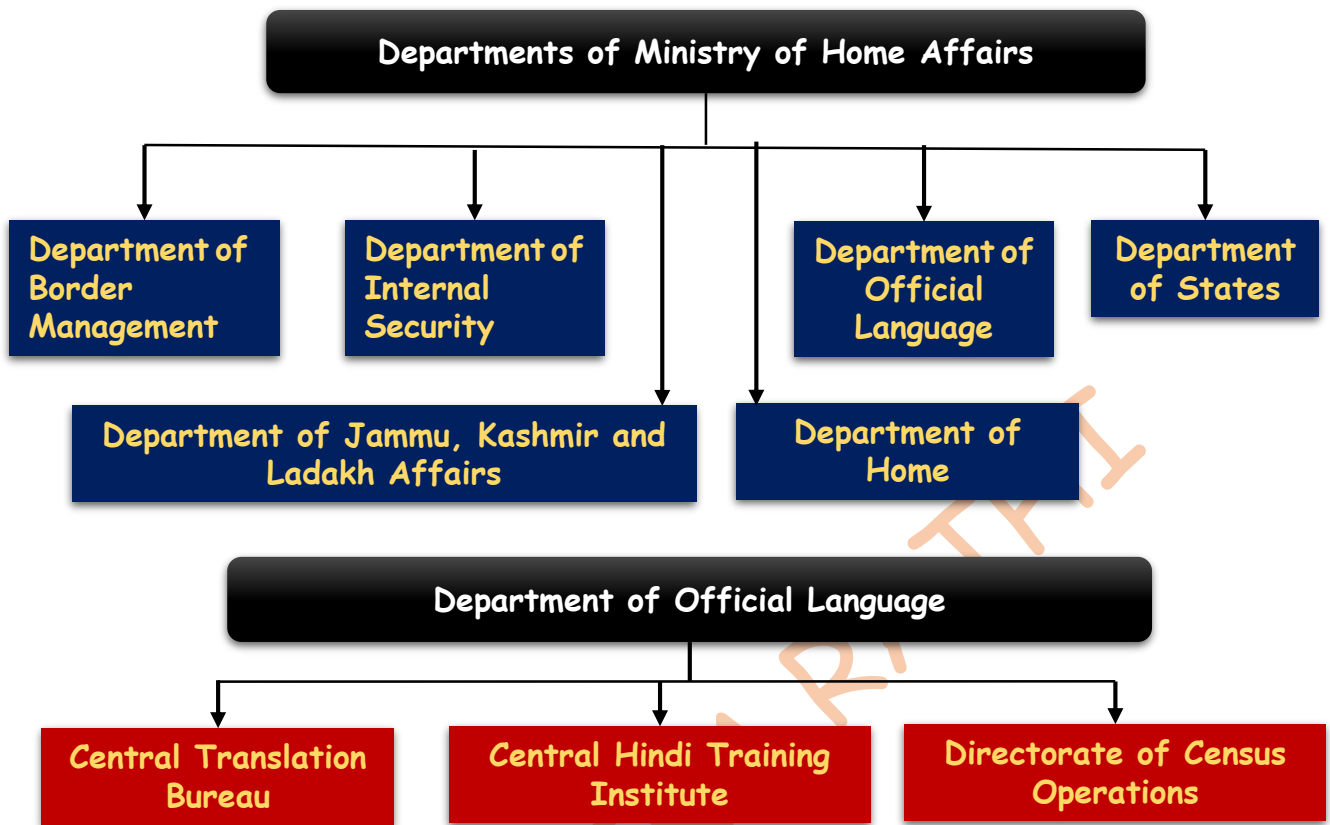
- ❖ Is a ministry of the Government of India
- ❖ It is mainly responsible for the maintenance of internal security and domestic policy.
- ❖ The Home Ministry is headed by Union Minister of Home Affairs.



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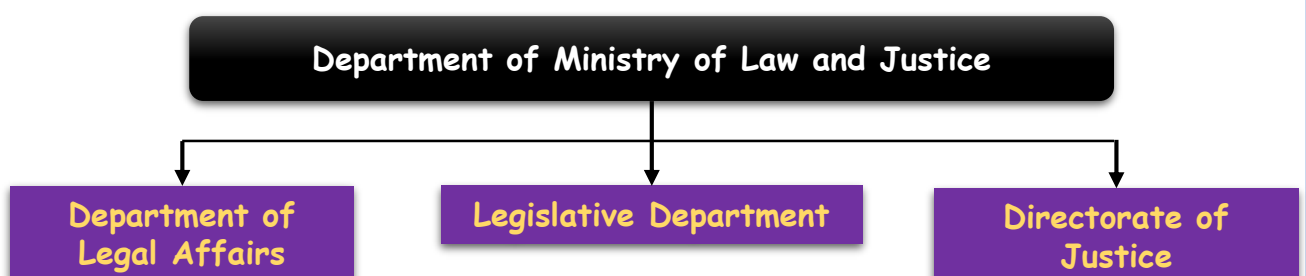


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iii. Ministry of Law and Justice

- ❖ In the Government of India is a Cabinet Ministry
- ❖ Deals with the
 - Management of the legal affairs, through the Legislative Department
 - legislative activities through the Department of Legal Affairs
 - administration of justice in India through the Department of Justice
- ❖ Legal Affairs → is concerned with advising the various Ministries of the Central Government
- ❖ Legislative Department → is concerned with drafting of principal legislation for the Central Government





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

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

iii. Reserve Bank of India

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

iv. Insolvency and Bankruptcy Board of India (IBBI)

- ❖ Regulator for overseeing insolvency proceedings and entities like Insolvency Professional Agencies (IPA), Insolvency Professionals (IP) and Information Utilities (IU) in India.
- ❖ Established on 1 October 2016 and given statutory powers through the Insolvency and Bankruptcy Code, which was passed by Lok Sabha on 5th May 2016.
- ❖ Covers Individuals, Companies, Limited Liability, Partnerships and Partnership firms.



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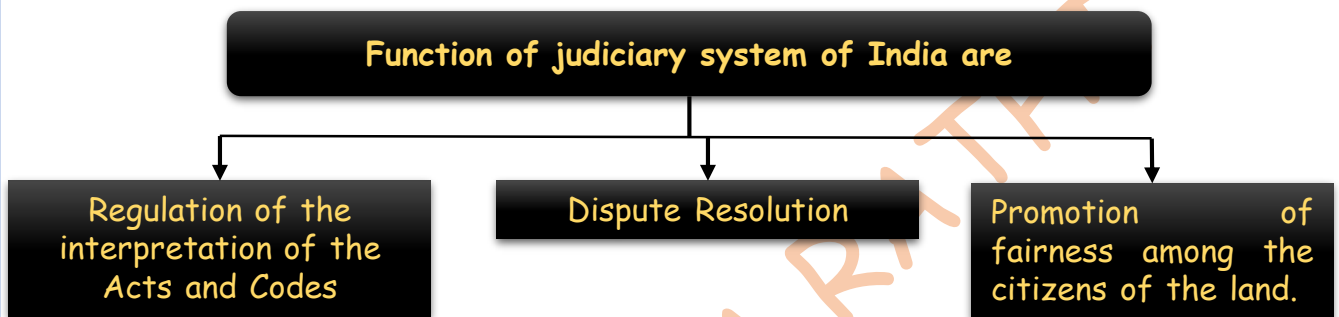


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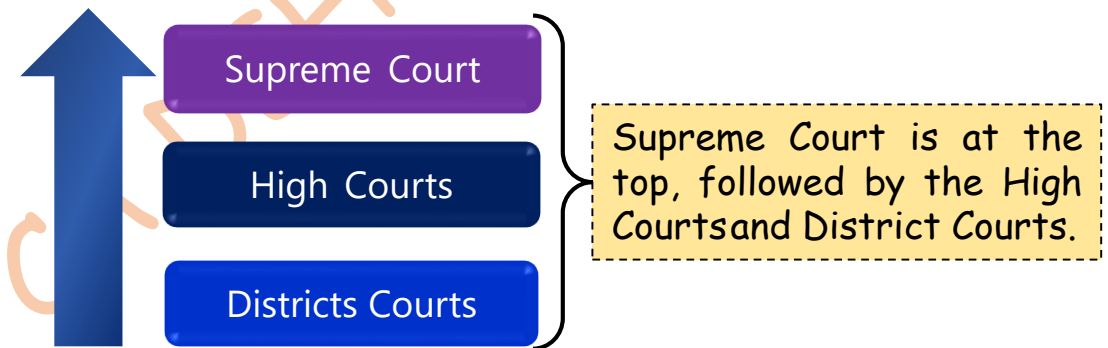
- ❖ It attempts to simplify the process of insolvency and bankruptcy proceedings.
- ❖ It handles the cases using two tribunals like NCLT (National company law tribunal) and Debt recovery tribunal

5. STRUCTURE OF THE INDIAN JUDICIAL SYSTEM

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



HIERARCHY OF COURTS



- ✓ Decisions of a High Court are binding in the respective state but are only persuasive in other states.
- ✓ Decisions of the Supreme Court are binding on all High Courts under Article 141 of the Indian Constitution.
- ✓ In fact, a Supreme Court decision is the final word on the matter.



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i. Supreme Court

- ✓ The Supreme Court is the apex body of the judiciary.
- ✓ It was established on 26th January, 1950.
- ✓ The Chief Justice of India is the highest authority appointed under Article 126.

ii. High Court

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

Which is the oldest High Court in India?

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

iii. District Court

- ✓ Below the High Courts are the District Courts.
- ✓ The Courts of District Judge deal with Civil law matters i.e. contractual disputes and claims for damages etc.
- ✓ The Courts of Sessions deal with Criminal matters.
- ✓ Under pecuniary jurisdiction, a civil judge can try suits valuing not more than Rupees two crore.
- ✓ Jurisdiction means the power to control.



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

iv. Metropolitan Courts

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

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Chapter -2 Indian Contract Act, 1872

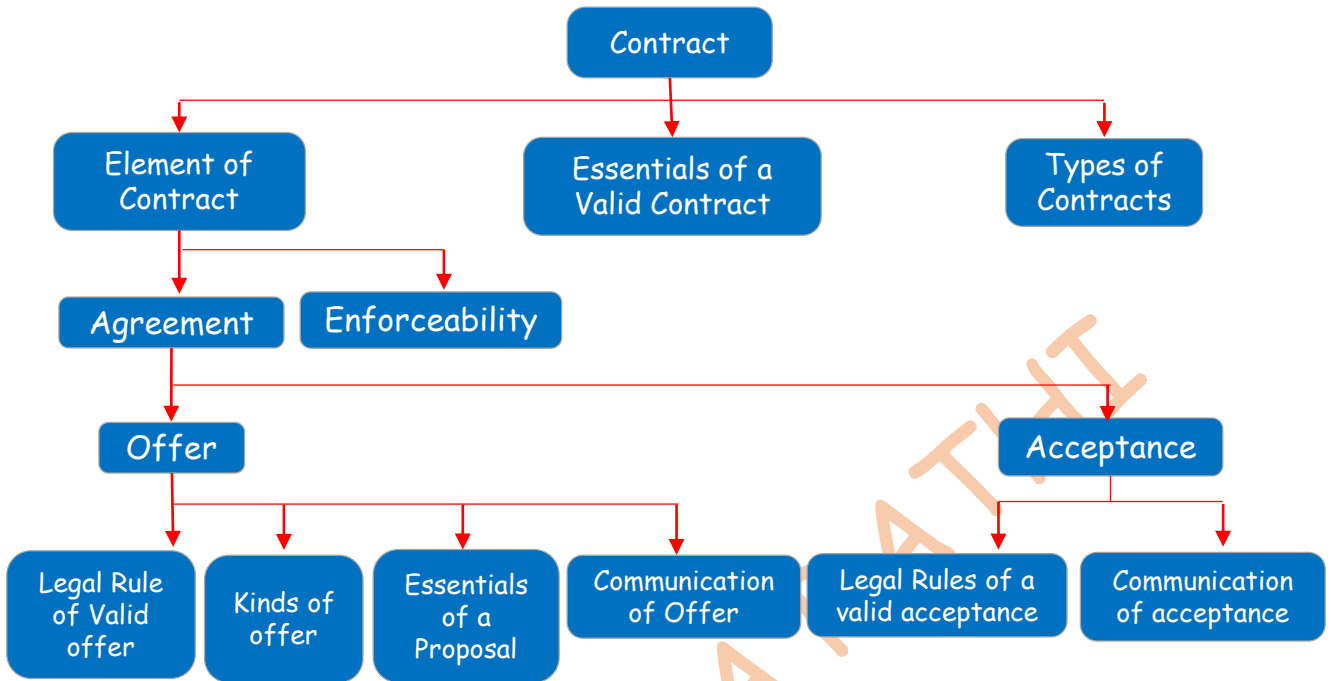


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Unit -1 : Nature Of Contracts



Governing Law, Enforcement & Applicability

- Law relating to contract is governed by the Indian Contract Act, 1872.
- Formed on : April 25, 1872
- Enforcement : September 01, 1872
- Applicability : Extends to the whole of India.
- Preamble : It is an Act to define and amend certain parts of the law relating to contract.

The Act is divisible into two parts

The First part (Section 1-75)

Deals with the General principles of the law of contract, and therefore applies to all contracts irrespective of their nature.

The Second part (Section 124-238)

Deals with Certain special kinds of contracts, e.g., Indemnity and guarantee, bailment, pledge, and agency.



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1. What is a Contract ?

Definition as per **Section 2(h)** : "An agreement enforceable by law."

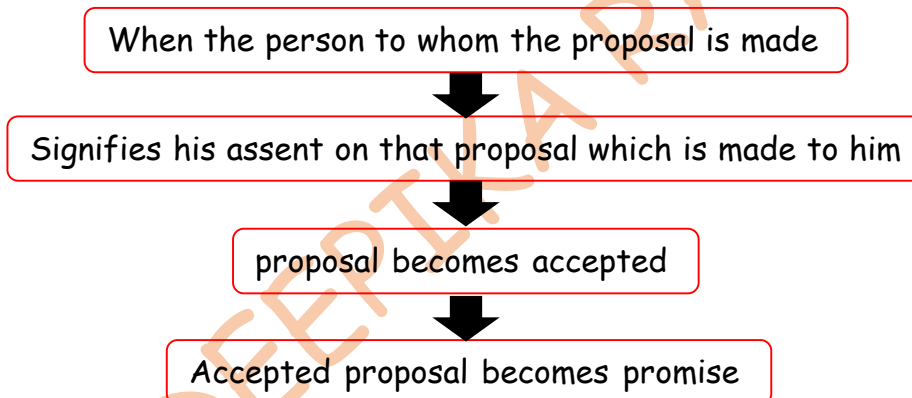
Contract = (i) Agreement + (ii) Enforceability by law

(i) Agreement

❖ **Definition as per Section 2(e)** : "Every promise and every set of promises, forming the consideration for each other".

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

Agreement = (i) Offer/ Proposal + (ii) Acceptance



(ii) Enforceability by Law

❖ An agreement to become a contract must give rise to a legal obligation which means a duly enforceable by law.

Contract = Accepted proposal/Agreement + Enforceability by law

- ❖ Contract comprises of an agreement which is a promise or a set of reciprocal promises, that a promise is the acceptance of a proposal giving rise to a binding contract.
- ❖ **Section 2(h)** : An agreement capable of being enforceable by law before it is called 'contract'.
- ❖ Where parties have made a binding contract, they created rights and obligations between themselves.
- ❖ Domestic and Social obligations are out of scope of the Contract Act, as they are not legally enforceable.



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Difference between Agreement and Contract

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

2.Essentials of valid contract

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

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

Both general essentials and elements given in Section 10 shall be present in a contract for it to be a valid contract.

General Essential

1.Two Parties

- A person cannot enter into a contract with himself, a contract involves at least two parties
- A contract can be made by either natural persons or other persons having legal existence.



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State of Gujarat vs. Ramanlal S & Co.

Fact : when on dissolution of a partnership, the assets of the firm were divided among the partners, the sales tax officer wanted to tax this transaction.

Held : It was held that it was not a sale. The partners being joint owner of those assets cannot be both buyer and seller.

2. Parties must intend to create legal obligations

- There must be an intention on the part of the parties to create legal relationship between them.
- Social or domestic type of agreements are not enforceable in court of law and hence they do not result into contracts.
- **Balfour v. Balfour**
 - ✓ **Fact :** A husband agreed to pay to his wife certain amount as maintenance every month while he was abroad. Husband failed to pay the promised amount. Wife sued him for the recovery of the amount.
 - ✓ **Held :** Wife could not recover the amount as it was a social agreement, and the parties did not intend to create any legal relations.

3. Other Formalities to be complied with in certain cases

- A contract may be written or spoken. But in the interest of the parties the contract must be written.
- In case of certain contracts some other formalities have to be complied with to make an agreement legally enforceable.

4. Certainty of meaning

- The agreement must be certain and not vague or indefinite.

5. Possibility of performance of an agreement

- The terms of agreement should be capable of performance.
- An agreement to do an act impossible in itself cannot be enforced.

Essential Elements Section 10

1. Offer and Acceptance or an Agreement

- An agreement is the first essential element of a valid contract.
- **Section 2(e) of the Indian Contract Act, 1872 :** "Every promise and every set of promises, forming consideration for each other, is an agreement"
- **Section 2(b) of the Indian Contract Act, 1872 :** "A proposal when accepted, becomes a promise"



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2. Free Consent

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

3. Capacity of the Parties

- Capacity to contract means the legal ability of a person to enter into a valid contract.
- **Section 11** : A person is competent to contract if he satisfies all the given conditions :
 1. **He attained the age of majority** : → Must be of 18 years of age.
 2. **Is of Sound Mind** :
 - He should be in his senses so that he understands the implications of the contract at the time of entering into a contract.
 - A lunatic, an idiot, a drunken person or under the influence of some intoxicant is not supposed to be a person of sound mind.
 3. **Is not disqualified by law**
Disqualified by law unless they fulfil certain formalities
 - Alien enemy,
 - Foreign sovereigns
 - Convicts

4. Consideration

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

5. Lawful Object

- The consideration and object of the agreement must be lawful.



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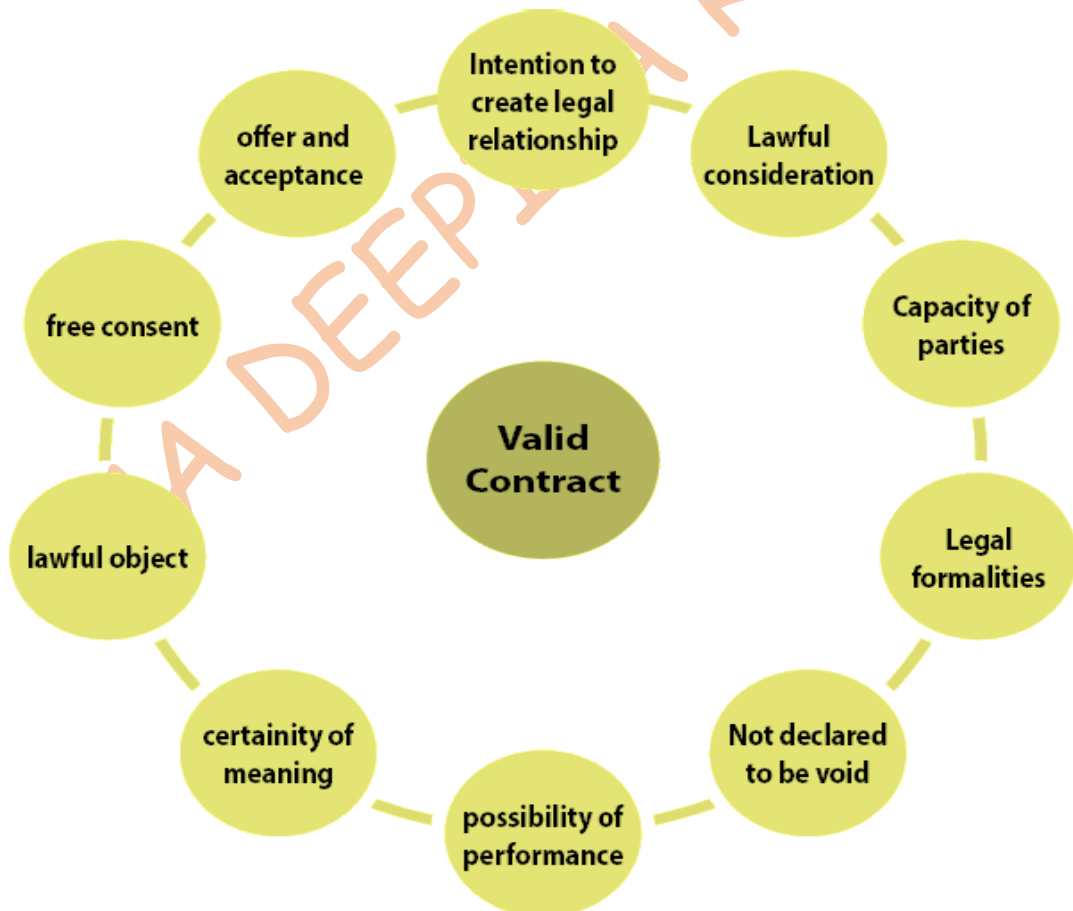


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- **Section 23 : Consideration or Object is not lawful if**
 - it is *prohibited by law*, or
 - it is such as would *defeat the provisions of law*,
 - if it is *fraudulent* or
 - *involves injury to the person or property of another* or *court* regards
 - it as *immoral* or *opposed to public policy*.

6. Not Expressly Declared to be void

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





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3. Types of Contracts

Types of Contract

Validity or Enforceability

- Valid Contract
- Void Contract
- Voidable Contract
- Illegal Contract
- Unenforceable Contract

Formation

- Express Contract
- Implied Contract
- Quasi Contract
- E- Contracts

Performance

- Executed Contract
- Executory Contract
 - Unilateral
 - Bilateral

I. On the Basis of Validity or Enforceability

1. Valid Contract

- The Valid Contract is an agreement that is legally binding and enforceable.
- It must qualify all the essentials of a contract.

2. Void Contract

- **Section 2 (j)** : "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

3. Voidable Contract

- **Section 2(i)** "An agreement which is enforceable by law at the option of one or more parties thereto, but not at the option of the other or others is a voidable contract".
- Where one of the parties to the agreement is in a position or is legally entitled or authorized to avoid performing his part, then the agreement is treated and becomes voidable.
- Consent in a contract is obtained by -
 - Coercion,
 - Undue influence,
 - Fraud or
 - Misrepresentation



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Option Available to Aggrieved Party

Cancel the Contract

OR

Continue if Beneficial

Distinction between a void contract and a voidable contract

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

4. Illegal Contract

- A contract which the law forbids to be made.
- Court will not enforce such a contract but also the connected contracts.
- All illegal agreements are void but all void agreements are not necessarily illegal. But both are void ab initio and cannot be enforced by law.



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- According to Section 2(g) of the Indian Contract Act, "**an agreement not enforceable by law is void**".

Distinction between a Void Agreement and a Illegal Agreement

Basis of Difference	Void Agreement	Illegal Agreement
Scope	A void agreement is not necessarily illegal.	An illegal agreement is always void.
Nature	Not forbidden under law.	Are forbidden under law.
Punishment	Parties are not liable for any punishment under the law.	Parties to illegal agreements are liable for punishment
Collateral Agreement	<ul style="list-style-type: none">• It's not necessary that agreements collateral to void agreements may also be void.• It may be valid also.	Agreements collateral to illegal agreements are always void.

5. Unenforceable Contract

- Unenforceable contracts are rendered unenforceable by law due to some technical defect.
- Example : Absence in writing, Barred by limitation etc.

II. On the Basis of formation of Contract

1. Express Contracts

- ❖ The terms are expressed by

Words
Or
In writing

}
- ❖ Section 9 : If a proposal or acceptance of any promise is made in words, the promise is said to be express.

2. Implied Contracts

- These contracts come into existence by implication.
- This implication is by action or conduct of parties or course of dealing.
- **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.



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- **Tacit Contracts :**

- ✓ Tacit means silent.
- ✓ Tacit contracts :→ are those that are inferred through the conduct of parties without any words spoken or written.
- ✓ It is not a separate form of contract but falls within the scope of implied contracts.

3. Quasi Contract

- It is not an actual contract but it resembles a contract.
- 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.

4. E-Contract

When a contract is entered into by two or more parties using electronics means, such as e-mails is known as e-commerce contracts.

III. On the Basis of performance of Contract

1. Executed-Contract

- When the act is done or executed or the forbearance is brought on record, then the contract is an executed contract.
- The consideration in Executed Contract could be an act or forbearance.

2. Executory-Contract

- In an executory contract the consideration is reciprocal promise or obligation.
- Such consideration is to be performed in future only and therefore these contracts are described as executory contracts.

A. Unilateral Contract

B. Bilateral Contract



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

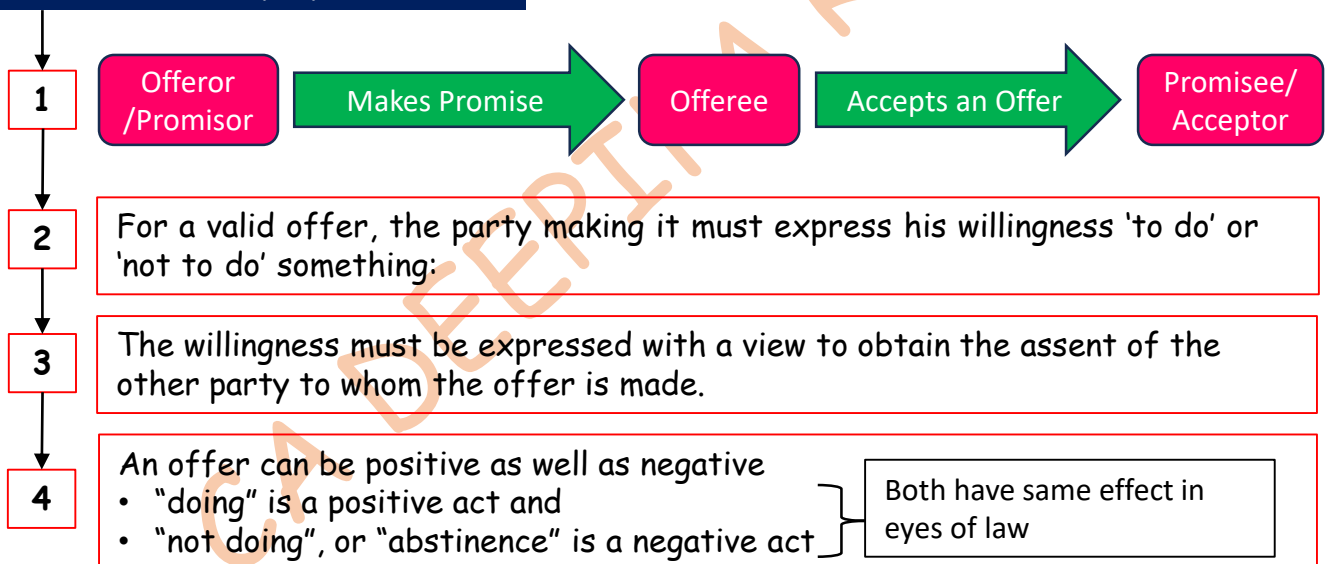
Bilateral Contract → is one where the obligation or promise is outstanding on the part of both the parties.

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

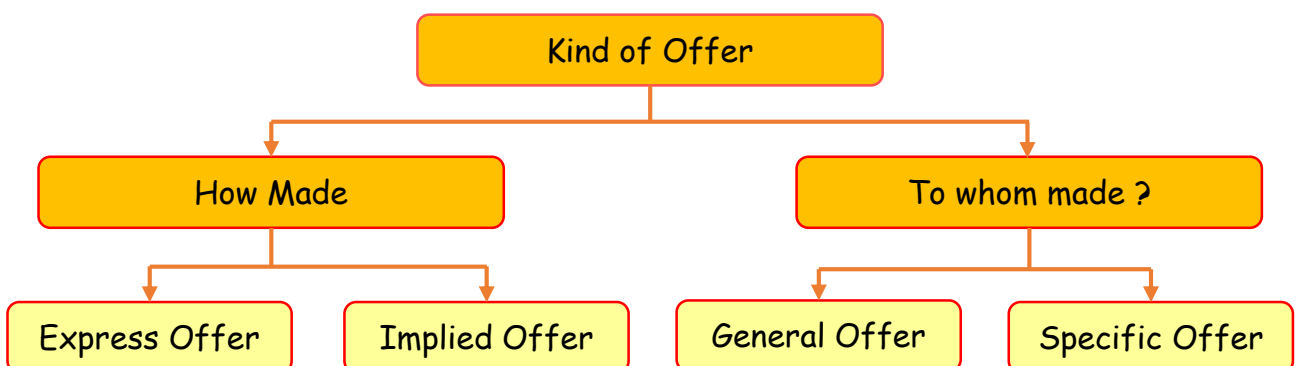
Definition of Offer/ Proposal [Section 2(a)]

- "When one person signifies to another his willingness to do or to abstain from doing anything with a view to obtaining the assent of that other to such act or abstinence, he is said to make a proposal"

Essentials of a proposal/offer



Kind of Offer

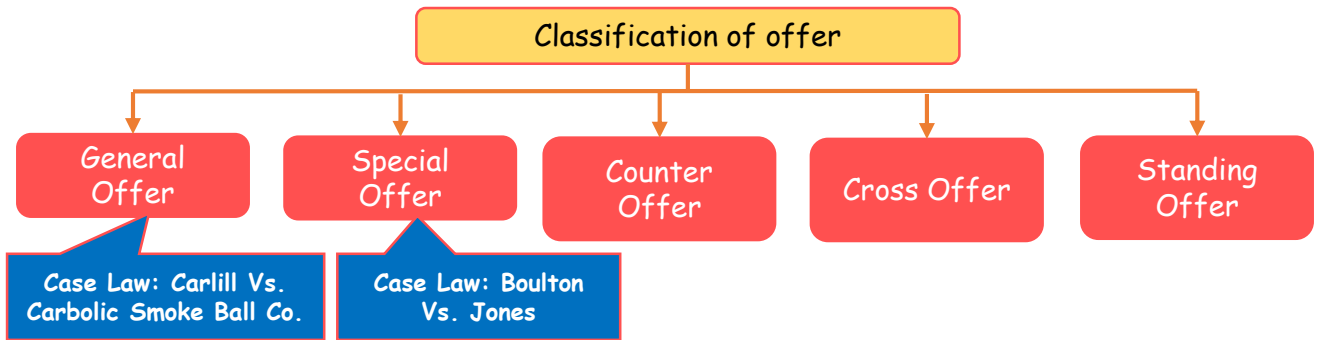




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a. General Offer

- A general Offer is an offer that is made to the **public at large**.
- **Section 8** : Anyone performing the conditions of the offer can be considered to have accepted the offer.
- Until the **general offer is retracted or withdrawn**, it can be accepted by anyone at any time as it is a continuing offer.

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

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

b. Special/Specific Offer

- When the offer is made to a **specific** or **an ascertained person**, it is known as a specific offer.
- Specific offer can be accepted only by that specified person to whom the offer has been made. **[Boulton Vs. Jones]**

c. Cross Offer

- When two parties exchange identical offers in ignorance at the time of each other's offer, the offers are called cross offers.



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- There is no binding contract in such a case because offer made by a person cannot be construed as acceptance of the another's offer.

d. Counter Offer

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

e. Standing/ Continuing/ Open Offer

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

Essentials of Valid Offer

1. It must be capable of creating legal relations

Offer must be capable of being accepted and giving rise to legal relationship

Offer which does not intend to give rise to legal consequences and creating legal relations, it is not considered as a valid offer in the eye of law.

A social invitation, even if it is accepted, does not create legal relations because it is not so intended.

2. It must be Certain, Definite, and not Vague

If the terms of an offer are vague or indefinite, its acceptance cannot create any contractual relationship.

3. It must be communicated to the offeree

An offer, to be complete, must be communicated to the person to whom it is made, otherwise there can be no acceptance of it.

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

Acceptance in ignorance of the proposal does not amount to acceptance



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Case Law: Lalman Shukla Vs. Gauri Dutt

- **Fact:** G (Gauridutt) sent his servant L (Lalman) to trace his missing nephew. He then announced that anybody who traced his nephew would be entitled to a certain reward. L traced the boy in ignorance of this announcement. Subsequently when he came to know of the reward, he claimed it.
- **Decision by Court:** He was not entitled to the reward, as he did not know the offer.

4. It must be made with a view to obtaining the assent of the other party

- Must be made with a view to obtaining the assent of the other party.

5. May be Conditional

- An offer can be made subject to any terms and conditions by the offeror.

6. Offer should not contain a term the non-compliance of which would amount to acceptance:

- One cannot say that if acceptance is not communicated by a certain time the offer would be considered as accepted.

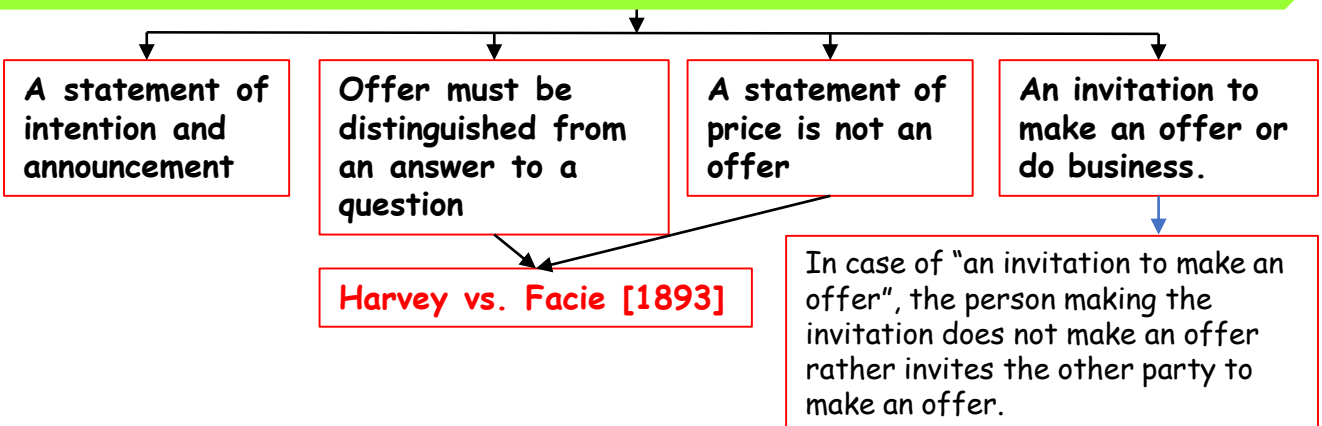
7. Offer may be General or Specific

- Any offer can be made to either public at large or to the any specific person.

8. Offer may be Express or Implied

- An offer may be made either by words or by conduct.

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





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

Fact : The plaintiffs through a telegram asked the defendants two questions namely,

- i. Will you sell us Bumper Hall Pen? And
- ii. Telegraph lowest cash price.

The defendants replied through telegram that the "lowest price for Bumper Hall Pen is £ 900".

The plaintiffs sent another telegram stating, "we agree to buy Bumper Hall Pen at £ 900".

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

Judgement: While plaintiffs had asked two questions, the defendant replied only to the second question by quoting the price but reserved their answer with regard to their willingness to sell.

The mere statement of the lowest price at which the vendor would sell contained no implied contract to sell to the person who had enquired about the price.

When goods are sold through auction :

The auctioneer does not contract with anyone who attends the sale.

The auction is only an advertisement to sell but the items are not put for sale though persons who have come to the auction may have the intention to purchase.

Prospectus issued by a company :→ is only an invitation to the public to make an offer to subscribe to the securities of the company.

10. A Statement of Price is not an Offer

Question: What is invitation to offer ?

Answer: An offer should be distinguished from an invitation to offer :

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



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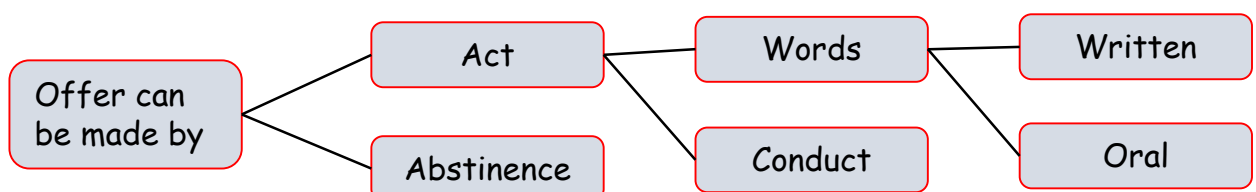


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Difference between offer and invitation to make an Offer

- **Offer** :→ Section 2(a) : An offer is the final expression of willingness by the offeror to be bound by the offer should the other party chooses to accept it.
- **Invitation to Offer** :→ Offers made with the intention to negotiate or offers to receive offers are known as invitation to offer.
- Where a party without expressing his final willingness proposes certain terms on which he is willing to negotiate he does not make an offer, but only invites the other party to make an offer on those terms.
- **Instances of invitation to offer to buy or sell :**
 - i. A Prospectus by a company to the public to subscribe for its shares.
 - ii. Display of goods for sale in shop windows.
 - iii. Advertising auction sales
 - iv. Quotation of prices sent in reply to a query regarding price.

Basis	Offer	Invitation to Offer
Meaning	Section 2(a) : An offer is the final expression of willingness by the offer or to be bound by the offer should the other party chooses to accept it.	Where a party without expressing his final willingness proposes certain terms on which he is willing to negotiate he does not make an offer, but only invites the other party to make an offer on those terms.
Intention of Parties	If a person who makes the statement has the intention to be bound by it as soon as the other accepts, he is making an offer.	If a person has the intention of negotiating on terms it is called invitation to offer.
Sequence	An offer cannot be an act precedent to invitation to offer.	An invitation to offer is always an act precedent to offer.





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5. Acceptance

- ❖ **Section 2 (b)** : "When the person to whom the proposal is made signifies his assent thereto, proposal is said to be accepted. The proposal, when accepted, becomes a promise"
- ❖ **According to Sir William Anson "Acceptance is to offer what a lighted match is to a train of gunpowder"**
 - What acceptance triggers cannot be recalled or undone.
 - But offer can be withdrawn just before it is accepted.
 - Acceptance converts the offer into a promise and then it is too late to revoke it.
 - An offer in itself cannot create any legal relationship but it is the acceptance by the offeree which creates a legal relationship.

Legal Rules regarding a valid acceptance

1. Acceptance can be given only by the person to whom offer is made

- In the case of a specific proposal or offer, it can only be accepted by the person it was made to. No third person without the knowledge of the offeree can accept the offer. **Case Law : Boulton vs. Jones (1857)**
- When the proposal is a general offer, then anyone with knowledge of the offer can accept it.

2. Acceptance must be Absolute and Unqualified

- ❖ **Section 7** : Acceptance is valid only when it is
 - Absolute and
 - Unqualified and
 - Expressed in some usual and reasonable manner unless the proposal prescribes the manner in which it must be accepted.
- ❖ If the proposal prescribes the manner in which it must be accepted, then it must be accepted accordingly.
- **Case Law: Neale vs. Merret**
- **Case Law: Union of India vs. Bahulal**

3. Acceptance must be Communicated

- ❖ To conclude a contract between the parties, the acceptance must be communicated in some perceptible form.
- ❖ Any conditional acceptance or acceptance with varying or too deviant conditions is no acceptance.



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- ❖ Such conditional acceptance is a counter proposal and has to be accepted by the proposer, if the original proposal has to materialize into a contract.
- ❖ Further when a proposal is accepted, the offeree must have the knowledge of the offer made to him.
- ❖ **Case Law : Brogden vs. Metropolitan Railway Co. (1877)**

4. Acceptance must be in prescribed mode

- ❖ Acceptance of the offer must be in the prescribed manner that is demanded by the offeror.
- ❖ If no such manner is prescribed, it must be in a reasonable manner that would be employed in the normal course of business.

5. Time

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

6. Mere silence is not acceptance

- ❖ The acceptance of an offer cannot be implied from the silence of the offeree or his failure to answer, unless the offeree has in any previous conduct indicated that his silence is the evidence of acceptance.
- ❖ **Case Law : Felthouse vs. Bindley**

7. Acceptance by Conduct/ Implied Acceptance

- ❖ Section 8 of the Indian Contract Act 1872, provides that acceptance by conduct or actions of the promisee is acceptable.
- ❖ So, if a person performs certain actions that communicate that he has accepted the offer, such implied acceptance is permissible.



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6. Communication of Offer & Acceptance

- When the contracting parties are face-to-face, there is no problem of communication because there is instantaneous communication of offer and acceptance. In such a case the question of revocation does not arise since the offer and its acceptance are made instantly.
- The difficulty arises when the contracting parties are at a distance from one another and they utilise the services of the post office or telephone or email (internet). In such cases, it is very much relevant for us to know the exact time when the offer or acceptance is made or complete.
- The Indian Contract Act, 1872 gives a lot of importance to "time" element in deciding when the offer and acceptance is complete.

Communication of Offer

- **Section 4** : "The communication of offer is complete when it comes to the knowledge of the person to whom it is made"
- When a proposal is made by post, its communication will be complete when the letter containing the proposal reaches the person to whom it is made.
- Mere receiving of the letter is not sufficient, he must receive or read the message contained in the letter.

Communication of Acceptance

There are two issues for discussion and understanding they are :

The modes of acceptance

When is acceptance complete ?

Mode of Acceptance

Section 3 : In general terms two modes of communication namely,

a. By any act

b. By omission, intending thereby, to communicate to the other or which has the effect of communicating it to the other.



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a. Communication by Act/Conduct would include

Any expression of words whether written or oral.

- Written words : → Include letters, telegrams, faxes, emails and even advertisements
- Oral words : → Include Telephone messages

Any conduct intended to communicate like positive acts or signs so that the other person understands what the person 'acting' or 'making signs' means to say or convey.

Example : when a person boards a bus, he is accepting to pay the bus fare via his conduct.

b. Communication of Acceptance by omission to do Something

Such omission is conveyed

By conduct

OR

By forbearance

- on the part of one person to convey his willingness or assent.
- However, silence would not be treated as communication by 'omission'.
- **Example** : A offers Rs.50,000 to B if he does not arrive before the court of law as an evidence to the case. B does not arrive on the date of hearing to the court. Here omission of doing an act amounts to acceptance.

When is acceptance complete ?

As per Section 4 of the Act, it is complete

A. As against the proposer

When it is put in the course of transmission to him so as to be out of the power of the acceptor to withdraw the same

B. As against the Acceptor

When it comes to the knowledge of the proposer

Where a proposal is accepted by a letter sent by the post

Communication of acceptance will be complete

- As against the proposer : → when the letter of acceptance is posted and
- As against the acceptor : → when the letter reaches the proposer.



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Acceptance over telephone or telex or fax or e-mail

When an offer is made of instantaneous communication like telex, telephone, fax or through e-mail, **the contract is only complete**

- **when the acceptance is received by the offeree, and the contract is made at the place where the acceptance is received (Entores Ltd. v. Miles Far East Corporation).**
- However, in case of a call drops and disturbances in the line, there may not be a valid contract.

Communication of Special Conditions

- Sometimes there are situations where there are contracts with special conditions.
- These special conditions are conveyed tacitly and the acceptance of these conditions are also conveyed by the offeree again tacitly or without him even realizing it.
- **Example :** Where a passenger undertakes a travel, the conditions of travel are printed at the back of the tickets, sometimes these special conditions are brought to the notice of the passenger, sometimes not. In any event, the passenger is treated as having accepted the special condition the moment he bought his ticket.
- Case Laws
 1. Mukul Datta Vs. Indian Airlines
 2. Lilly White Vs. R. Mannuswamy

7. Communication of Performance

From the viewpoint of proposer

When the acceptance is put into a course of transmission, when it would be out of the power of acceptor.

From the viewpoint of acceptor

It would be complete when it comes to the knowledge of the proposer.

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

- In this case it is not enough if the offeree merely performs the act but he should also communicate his performance unless the offer includes a term that a mere performance will constitute acceptance.



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Case : *Carlill Vs Carbolic & Smokeball Co.*

Fact of the Case : The defendant a sole proprietary concern manufacturing a medicine which was a carbolic ball whose smoke could be inhaled through the nose to cure influenza, cold and other connected ailments issued an advertisement for sale of this medicine. The advertisement also included a reward of \$100 to any person who contracted influenza, after using the medicine (which was described as 'carbolic smoke ball'). Mrs. Carlill bought these smoke balls and used them as directed but contracted influenza.

Judgment of the Court : It was held that Mrs. Carlill was entitled to a reward of \$100 as she had performed the condition for acceptance.

- As the **advertisement did not require any communication of compliance of the condition**, it was not necessary to communicate the same.
- The court thus in the process laid down the following three important principles:

i. An offer, to be capable of acceptance,
- must contain a definite promise by the offer **or**
- that he would be bound provided the terms specified by him are accepted.

ii. An offer may be made either to
- a particular person
or
- to the public at large

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

8. Revocation of Offer & Acceptance

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

1. As against the person who makes it when it is put into a course of transmission to the person to whom it is made so as to be out of the power of the person who makes it

OR

2. As against the person to whom it is made, when it comes to his knowledge.

As per Section 5 of the Act

Offer can be revoked at any time before communication of acceptance is completed as against the offeror.

Acceptance can be revoked at any time before the communication of acceptance is complete against the acceptor.



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Contract over Telephone-

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

Revocation of proposal otherwise than by communication:

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

Modes of Revocation of Offer:

1. Notice of revocation
2. **Lapse of Time:** The time for acceptance can lapse if the acceptance is not given within the specified time and where no time is specified, then within a reasonable time
3. **Non-fulfilment of condition:** Where the acceptor fails to fulfill a condition precedent to acceptance the proposal gets revoked. **(Section -6)**
4. **Death or insanity:** Death or insanity of the proposer would result in automatic revocation of the proposal but only if the fact of death or insanity comes to the knowledge of the acceptor.
5. Counter Offer
6. Non-acceptance of the offer according to the prescribed or usual mode
7. Subsequent illegality



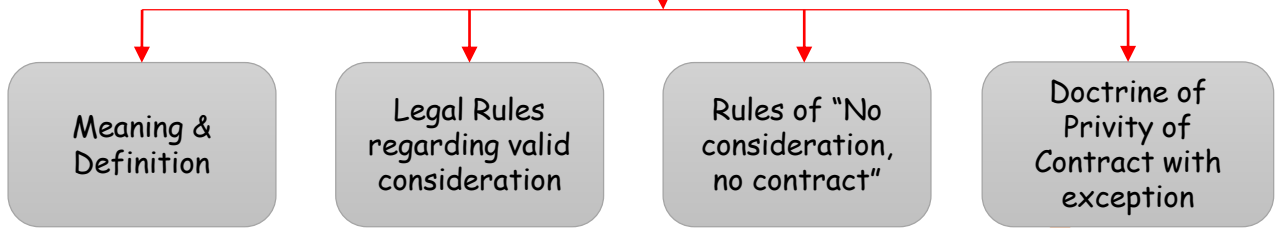
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Unit -2 : Consideration

CONSIDERATION



1.What is Consideration ?

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

A valuable consideration in the sense of law may consist either

In some right, interest, profit or benefit accruing to one party (i.e. promisor)

OR

forbearance, detriment, loss or responsibility given, suffered or undertaken by the other (i.e. the promisee)."

- ❖ Section 2(d) of Indian Contract Act 1872

When at the desire of the Promisor

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

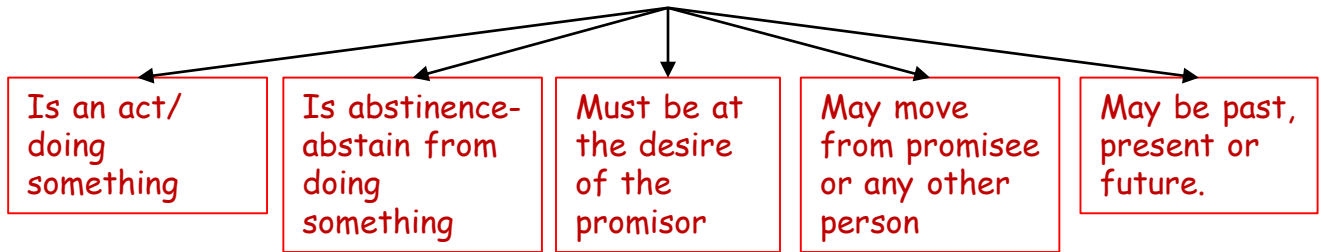


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Consideration



Consideration = Promise /Performance that parties exchange with each other.

Form of consideration = Some benefit, right or profit to one party / some detriment, loss, or forbearance to the other.

2. Legal Rules Regarding Consideration

1. Consideration must move at the desire of the promisor

- Consideration must be offered by the promisee or the third party at the desire or request of the promisor.
- Contract of marriage in consideration of promise of settlement is enforceable.
- An act done at the desire of a third party is not a consideration.

Case Law : Durga Prasad v. Baldeo

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

2. Consideration may move from promisee or any other person

- Consideration may move from the promisee or any other person who is not the party to the contract to the contract.
- There can be a stranger to consideration.

✓ Case Law : Chinnayya Vs. Ramayya

- An old lady made a gift of her property to her daughter with a direction to pay a certain sum of money to the maternal uncle by way of annuity.
- On the same day, the daughter executed a writing in favour of the brother agreeing to pay annuity.
- The daughter did not, however, pay the annuity and the uncle sued to recover it.
- **Held** : There was sufficient consideration for the uncle to recover the money from the daughter.



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3. Executed and Executory Consideration

- A consideration which consists in the performance of an act is said to be executed.
- When it consists in a promise, it is said to be executory.

4. Consideration may be past, present or future

- **Past Consideration** : → If the promise or act is performed before the contract was made.
- **Present consideration** : → When one of the parties in the contract has performed his part of the promise, which constitutes the consideration to be performed by other party.
- **Future consideration** : → When a party makes a promise in exchange for the promise from the other party and the performance of the consideration is to be done after making the contract; then it is a

5. It need not be adequate

- It is not mandatory for the consideration to be equivalent to the promise.
- Parties are free to determine the appropriate consideration at the time of negotiating the terms of contract.
- While the law allows the parties to decide an 'adequate' consideration for them, it must be real and have value in the eyes of law.
- While the Court will not consider inadequacy, it will look at it to determine if the consent was given by the party with free-will or not.

6. Performance of what one is legally bound to perform

- If the promisor is already obligated either by his promise or law to perform or abstain from a certain act, then it is not a good consideration for a promise.
- Such a contract is void for want of consideration.
- **Example** : A promise to pay money to a witness is void, for it is without consideration
- **Example** : An agreement by a client to pay to his counsel after the latter has been engaged, a certain sum over and above the fee, in the event of success of the case would be void, since it is without consideration.
- But where a person promises to do more that he is legally bound to do, such a promise provided it is not opposed to public policy, is a good consideration. It should not be vague or uncertain.



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7. Consideration must be real and not illusory

- Consideration has to be certain, definitive and competent.
- It cannot be vague, uncertain or impossible.
- It must be something real and not something imaginary

8. Consideration must not be unlawful, immoral or opposed to public policy

- Only presence of consideration is not sufficient it must be lawful.
- Anything which is immoral or opposed to public policy also cannot be valued as valid consideration.

3. Suit by a Third Party to a Contract

- Consideration for an agreement may proceed from a third party, **the third party cannot sue on contract.**
- Only a person who is party to a contract can sue on it.
- As per the 'Doctrines of Privity of Contract' a stranger to a contract cannot sue.

However in certain contract a stranger may enforce a claim these are following

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 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, he may file the 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.



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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.

4. Validity of an Agreement without Consideration

- ❖ **Section 25** : General Rule is that an agreement made without consideration is void.
- ❖ In every valid contract, consideration is very important.
- ❖ A contract may only be enforceable when consideration is there.



Exceptions to this rule.

1. Natural Love and affection [Section 25(1)]

Conditions to be fulfilled under **section 25(1)**

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

Parties must stand in near relationship to each other.

Must be in writing.

Must also be registered under the law

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

2. Compensation for past voluntary services [Section 25(2)]

- ❖ A promise to compensate, wholly or in part, a person who has already voluntarily done something for the promisor, is enforceable.



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- ❖ In order that a promise to pay for the past voluntary services be binding, the following essential factors must exist:

Services should have been rendered voluntarily.

Services must have been rendered for the promisor

Promisor must be in existence at the time when services were rendered.

Promisor must have intended to compensate the promisee.

3. Promise to pay time barred debt [Section 25(3)]

- ❖ Where a promise in writing signed by the person making it or by his authorised agent, is made to pay a debt barred by limitation it is valid without consideration

4. Agency [Section 185]

No consideration is necessary to create an agency.

5. Completed Gift

- **Explanation (1) to Section 25 :** "nothing in this section shall affect the validity as between the donor and donee, of any gift actually made."
- Thus, gifts do not require any consideration.

6. Bailment [Section 148]

No consideration is required to affect the contract of bailment.

7. Charity

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



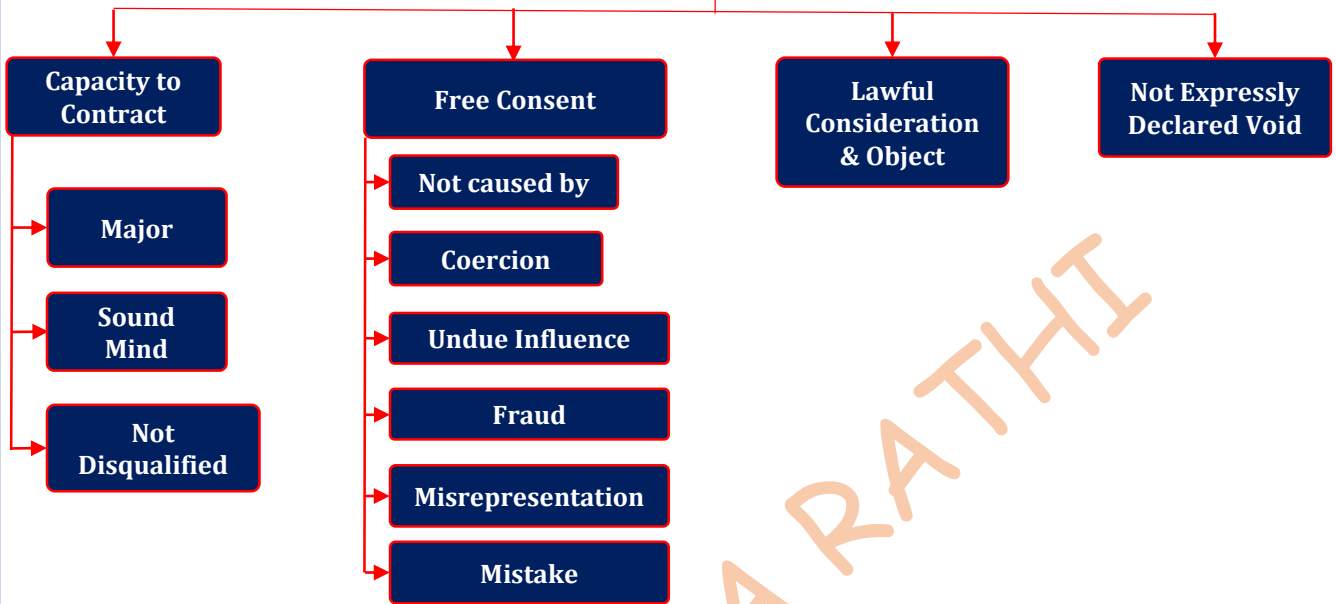
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Unit -3 : Other Essential Elements Of A Contract

Essential Elements of a Valid Contract

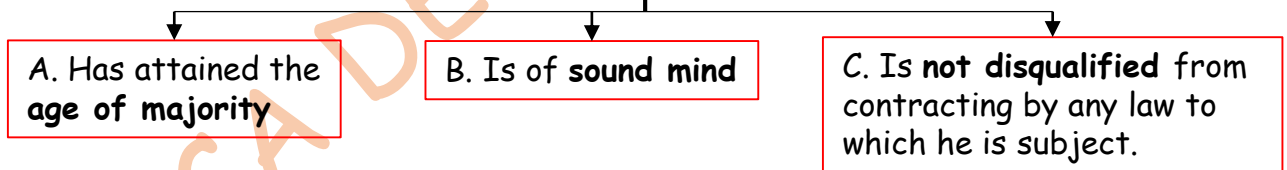


1.Capacity to Contract

❖ **Meaning** : Capacity refers to the **competence of the parties to make a contract**.

❖ **Who is competent to contract (Section 11) :**

Every person is competent to contract who



A. Age of Majority

Age of majority is regulated by the Indian Majority Act, 1875.

Every person domiciled in India shall attain the age of majority on the completion of 18 years of age and not before.

The age of majority being 18 years, a person less than that age even by a day would be minor for the purpose of contracting.



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Law relating to minor's agreement

1. A contract made with or by a minor is void ab-initio

- ❖ A minor is not competent to contract and any agreement with or by a minor is void from the very beginning.

Case Law: Mohori Bibi vs. Dharmo Das Ghose (1903)

Facts: A, a minor had borrowed some money from B (a money lender) by mortgaging his house. He became a major a few months later. The moneylender moved to take possession of the minor's house when he defaulted payment.

Judgement: A mortgage by a minor was void and B was not entitled to repayment of money.

2. No ratification after attaining majority

- ❖ A minor cannot ratify the agreement on attaining majority as the original agreement is void ab initio and a void agreement can never be ratified.

3. Minor can be a Beneficiary or can take benefit out of a contract

- ❖ Though a minor is not competent to contract, he can be a beneficiary to the contract.

4. A minor can always plead minority

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

5. Liability for Necessaries

- ❖ A claim for necessities supplied to a minor is enforceable by law.
- ❖ But a minor is not liable for any price that he may promise and never for more than the value of the necessities.
- ❖ There is no personal liability of the minor, but only his property is liable.



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

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

ii. The minor must **not have already a sufficient supply of these necessities.**

Note :→ Necessaries mean those things that are essentially needed by a minor. They do not include luxuries or costly or unnecessary articles.

6. Contract by Guardian – how far enforceable

- ❖ Where the guardian enters into a contract for the minor, which is within his competence and for the benefit of the minor, such a contract will be valid and enforceable by the minor.

7. No Specific Performance

- ❖ A minor's agreement being absolutely void, there can be no question of the specific performance of such an agreement.

8. No insolvency

- ❖ A minor **cannot be declared insolvent**

9. Partnership

A minor being incompetent to contract **cannot be a partner in a partnership firm.**

But as per Section 30 of the Indian Partnership Act, **Minor can be admitted to the benefits of partnership.**

10. Minor can be an Agent

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

11. Minor cannot bind parent or guardian

- ❖ A minor is not capable of binding his parent or guardian, even for necessities.
- ❖ They will be held liable only when the minor acts as their agent.



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12. Joint contract by Minor and Adult

- ❖ The adult will be liable on the contract and not the minor.

13. Surety (Guarantor) for a Minor

- ❖ When an adult gives a guarantee on behalf of a minor, then the adult is liable to the third party as if there is direct contract between the surety and the third party.

14. Minor as Shareholder

A Minor cannot be a shareholder of the company.

If by mistake he becomes a member, the company can rescind the transaction and remove his name from register

But a minor may, acting through his lawful guardian become a shareholder by transfer or transmission of fully paid shares to him.

15. Liability for Torts

- ❖ A tort is a civil wrong.
- ❖ A minor is liable for tort, unless the tort in reality is a breach of contract.

B. Person of Sound Mind

Section 12 : A person is said to be of sound mind for the purposes of making a contract if

at the time when he makes it is capable of understanding it

And

of forming a rational judgement as to its effect upon his interests.

- ❖ A person who is usually of unsound mind, but occasionally of sound mind, may make a contract when he is of sound mind.
- ❖ A person who is usually of sound mind, but occasionally of unsound mind, may not make a contract when he is of unsound mind.

Position of unsound mind person making a contract



A contract made by a person of unsound mind is void.



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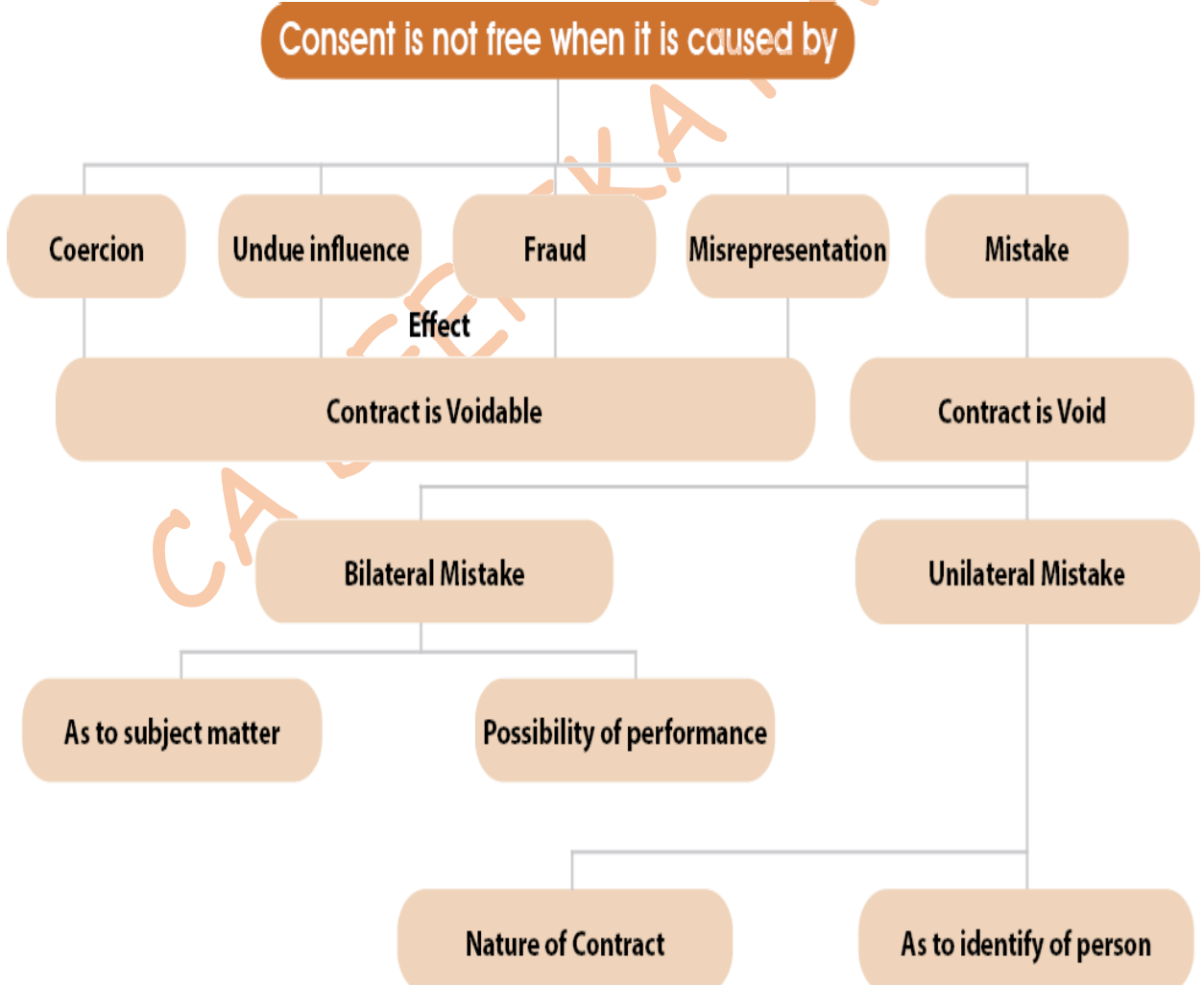


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C. Contract by Disqualified Persons

- ❖ There are also other persons who are disqualified from contracting, partially or wholly, so that the contracts by such person are void.
- ❖ Incompetency to contract may arise from political status, corporate status, legal status, etc.
- ❖ The following persons fall in this category:
 - ✓ Foreign Sovereigns and Ambassadors
 - ✓ Alien enemy
 - ✓ Corporations
 - ✓ Convicts
 - ✓ Insolvent etc.

2.Free Consent





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Consent (Section -13) : → Two or more persons are said to consent when they agree upon the same thing in the same sense.

'Same thing' must be understood as the whole content of the agreement.

if the parties to the contract do not agree in the same sense, there cannot be consent.

A contract cannot arise in the absence of consent.

Consent may be free or not free

Only free consent is necessary for the validity of a contract.

Free Consent (Section -14) :→ Consent is said to be free when it is not caused by

Coercion

Undue Influence

Fraud

Misrepresentation

Mistake

When consent to an agreement is caused by these

The agreement is a contract **voidable** at the option of the party whose consent was so caused

Contract becomes **void**

3.Elements Vitiating Free Consent

I. Coercion (Section 15)

Coercion is

Committing or threatening to commit any act forbidden by the India Penal Code

OR

the unlawful detaining or threatening to detain any property to the prejudice of any person whatever

OR

with the intention of causing any person to enter into an agreement."

In case of Coercion, it is not necessary that it should proceed from a party to a contract neither it is necessary that coercion must be done on the other party.

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

I

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

II

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



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Threat to commit suicide - Whether is it coercion ?

- ❖ A threat to commit suicide will be regarded as coercion.

II. Undue Influence (Section 16)

A contract is said to be induced by 'undue influence' where the relations subsisting between the parties are such that

one of the parties is in a position to dominate the will of the other

and

he uses that position to obtain an unfair advantage over the other

The essential ingredients under this provision are

1. Relation between the parties

- ❖ A person can be influenced by the other when a near relation between the two exists.

2. Position to dominate the will

- ❖ Relation between the parties exist in such a manner that one of them is in a position to dominate the will of the other.

A person is deemed to be in such position in the following circumstances:

Real and apparent authority

Where a person holds a real authority over the other

Fiduciary relationship

Where relation of trust and confidence exists between the parties to a contract.

Mental distress

An undue influence can be used against a person to get his consent on a contract where the mental capacity of the person is temporarily or permanently affected by the reason of mental or bodily distress, illness or of old age.

Unconscionable bargains

Where one of the parties to a contract is in a position to dominate the will of the other and the contract is apparently unconscionable



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3. The object must be to take undue advantage

- ❖ Where the person is in a position to influence the will of the other in getting consent, must have the object to take advantage of the other.

4. Burden of proof

When a party to contract decides to avoid the contract on the ground of undue influence, he has to prove that :-

The other party is in position to dominate his will

the other party actually used his position to obtain his consent

Transaction is unfair or unconscionable.

Effect of undue influence- (Section 19A)

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.

III. Fraud (Section 17)

Fraud means any of the following acts done with an intention to deceive the will of the other

- False Suggestion
- Active Concealment of facts
- Promise without intention of performing
- Other act fitted to deceive
- Act or omission which law specially declares to be fraudulent

Essential elements of the fraud

- There must be a representation or assertion and it must be false.

Silence is fraud in following situations explanation of section 17

There is duty to speak.

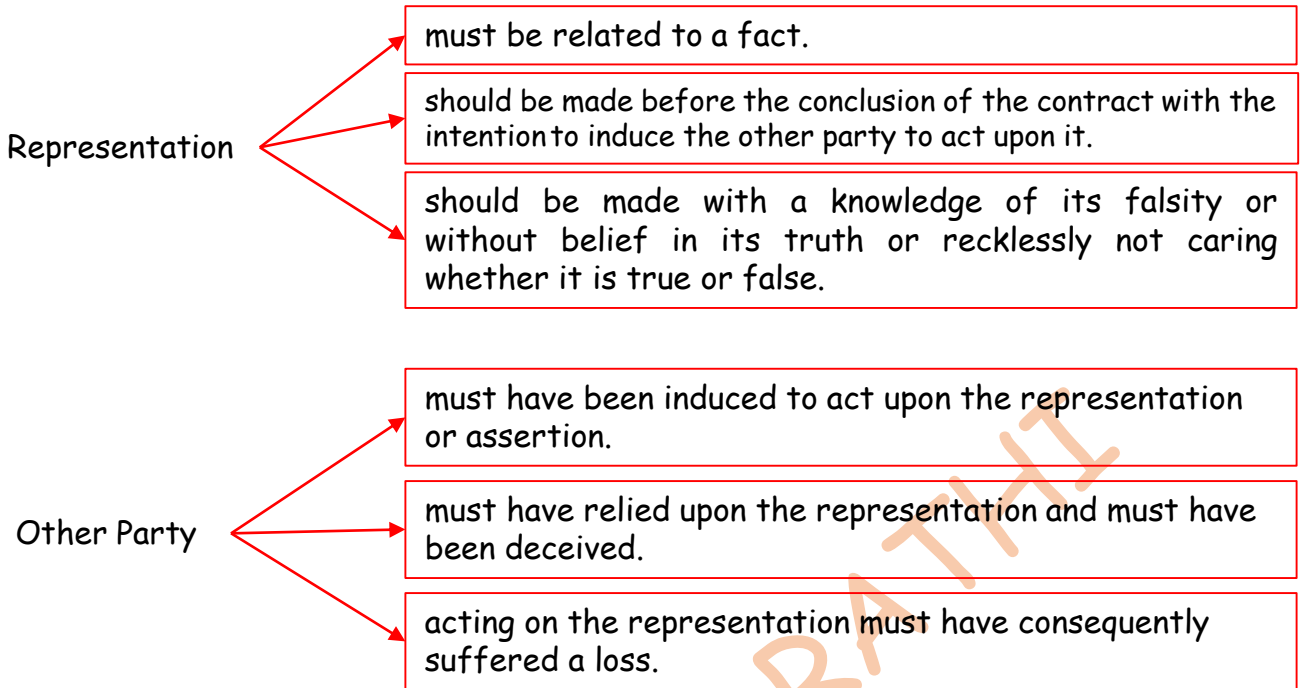
When silence is equal to speech.



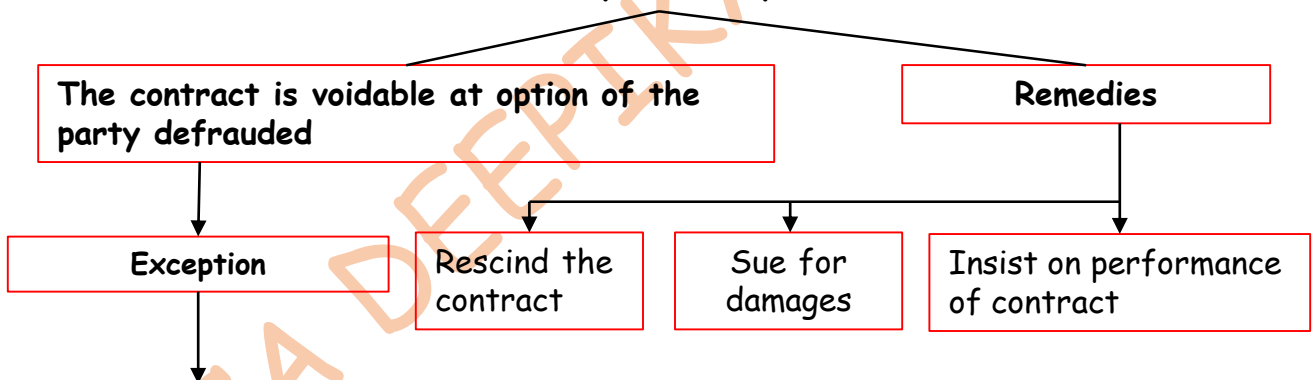
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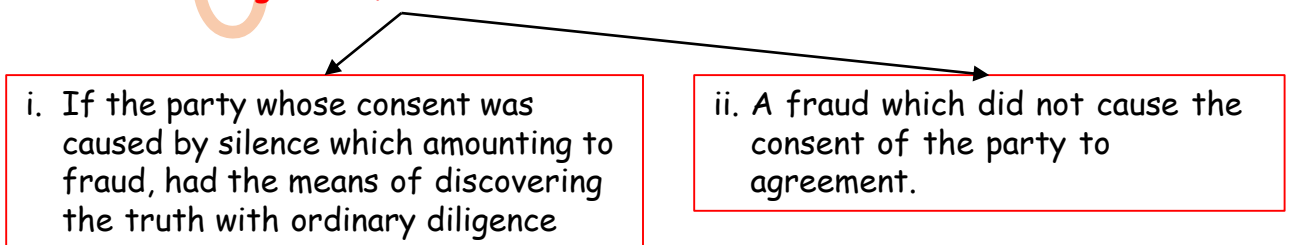
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Effect of Fraud upon validity of a Contract



In the following cases, contract is not voidable





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IV. Misrepresentation (Section 18)

Statement of fact, which of false, would constitute misrepresentation

If the maker believes it to be true but which is not justified by the information he possesses

When there is a breach of duty by a person without any intention to deceive which brings an advantage to him

When a party causes, even though done innocently, the other party to the agreement to make a mistake as to the subject matter

Difference between Coercion and Undue Influence

Basis of Difference	Coercion	Undue Influence
Nature of action	<ul style="list-style-type: none">It involves the physical force or threat.The aggrieved party is compelled to make the contract against its will.	It involves moral or mental pressure
Involvement of criminal action	It involves committing or threatening to commit and act forbidden by Indian Penal Code or detaining or threatening to detain property unlawfully.	No such illegal act is committed or a threat is given.
Relationship between parties	It is not necessary that there must be some sort of relationship between the parties.	Some sort of relationship between the parties is absolutely necessary.
Exercised by whom	Coercion need not proceed from the promisor nor need it be directed against the promisor. It can be used even by a stranger to the contract.	Undue influence is always exercised between parties to the contract.
Enforceability	The contract is voidable at the option of the party whose consent has been obtained by the coercion.	Where the consent is induced by undue influence, the contract is either voidable or the court may set it aside or enforce it in a modified form.
Position of benefits received	In case of coercion where the contract is rescinded by the aggrieved party, as per Section 64, any benefit received has to be restored back to the other party.	The court has the discretion to direct the aggrieved party to return the benefit in whole or in part or not to give any such directions.



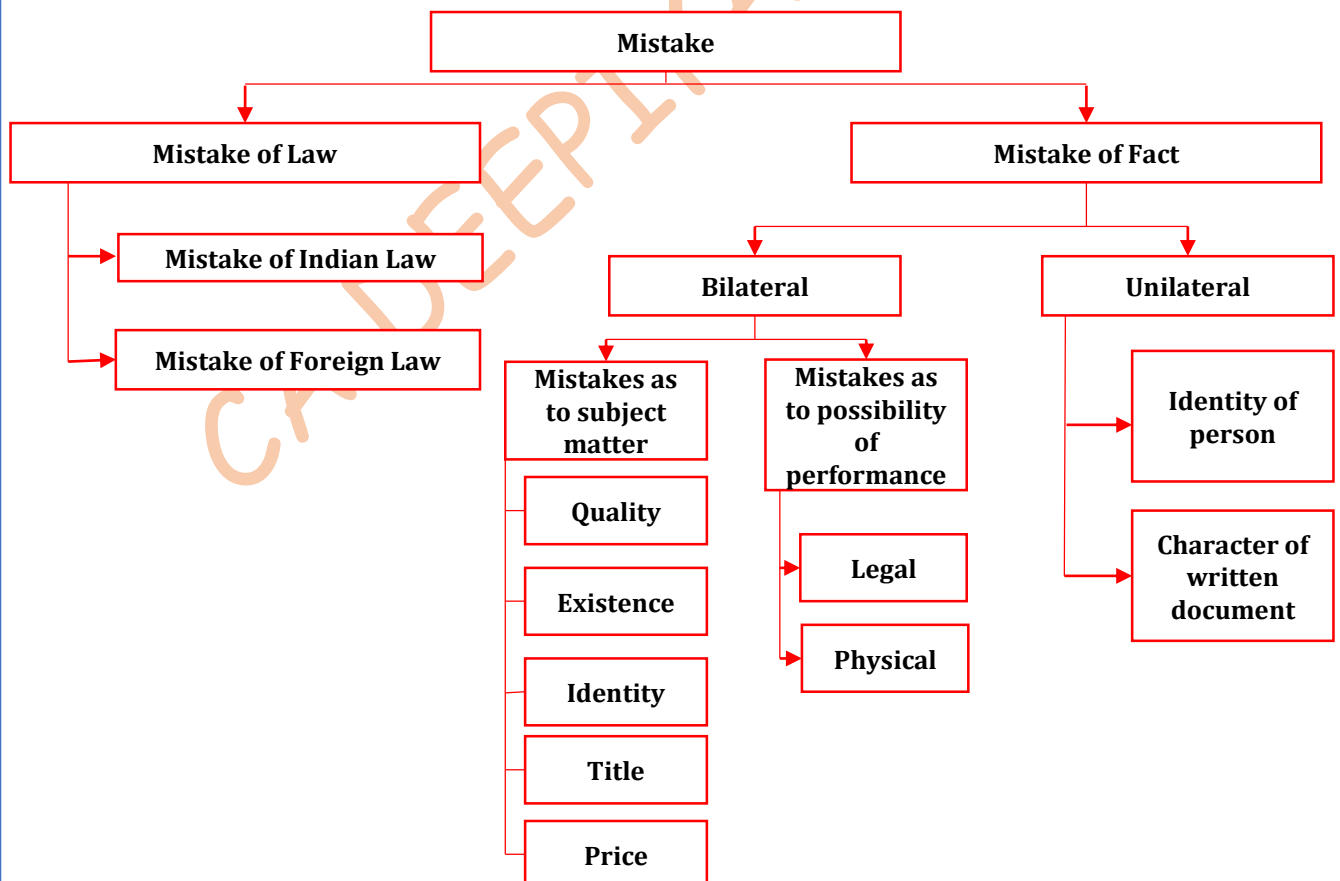
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Distinction between fraud and misrepresentation

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





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Mistake

- ❖ Mistake may be defined as innocent or erroneous belief which leads the party to misunderstand the others.

Mistake may be either

Mistake of Law

Mistake of fact

Mistake of Indian Law

A person cannot be allowed to get any relief on the ground that it had done a particular act in ignorance of law.

Mistake of Foreign Law

Such a mistake is treated as mistake of fact and the agreement in such a case is void.

Bilateral Mistake

- Where both the parties to an agreement are under a mistake as to a matter of fact essential to the agreement, there is a bilateral mistake.
- The agreement is void (Section 20).

Unilateral Mistake

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

Cases of Bilateral Mistakes

- Mistake as to the quality of the subject-matter.
- Mistake as to the existence of the subject-matter.
- Mistake as to the identity of the subject-matter.
- Mistake as to the title of the subject-matter.
- Mistake as to the price of the subject-matter.
- Mistake as to the quantity of the subject-matter.



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4. Legality of Object and Consideration

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

As per Section 23 in following cases the consideration or object of an agreement is said to be unlawful

1. When consideration or object is forbidden by law

Acts forbidden by law are those which are

- punishable under any statute as well as
- prohibited by regulations or orders

2. When consideration or object are of such a nature that if permitted it would defeat the provisions of law

If the consideration or the object of an agreement is of such a nature that not directly but indirectly, it would defeat the provisions of the law



Agreement is void

3. When it is fraudulent

Agreements which are entered into to promote fraud



Void

4. Injury

- ❖ The general term "injury" means criminal or wrongful harm.
- ❖ The object or consideration is unlawful as it involves injury to the person or property of another.

5. When Consideration is Immoral

6. When Consideration is opposed to public policy (for the good for the community)

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

1. Trading with the Enemy

Entering into an agreement with a person from a country with whom India is at war → Void



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2. Stifling Prosecution

- ❖ This is a pervasion of the natural course of law, and such contracts are → **Void**
- ❖ The principle is that one should not make a trade of felony.
- ❖ The **compromise of any public offence is generally → Illegal.**
- ❖ 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.**
- ❖ In case of an uncompoundable offence, it is → **Void.**

3. Maintenance and Champerty

1. **Maintenance agreement:** → is when a person promises to **maintain a suit** in which he has **no real interest.**
2. **Champerty:** → is when a person agrees to **assist another party in litigation** for a portion of the damages or proceeds.

The agreement for supplying funds by way of Maintenance or Champerty is **valid** unless

It is unreasonable so as to be unjust to other party

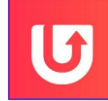
- It is made by a malicious motive and
- Not with the *bonafide* object of assisting a claim believed to be just.

4. Trafficking relating to Public Offices and Titles

- An agreement to trafficking in public office is opposed to public policy, as it interferes with the appointment of a person best qualified for the service of the public.
- Public policy requires that there should be no money consideration for the appointment to an office in which the public is interested.
- **Examples of agreements that are void**
 - 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.**
 - An agreement to procure a public recognition like Padma Vibhushan for reward is → **Void.**



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5. Agreements tending to create Monopolies

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

6. Marriage brokerage Agreements

An agreement to brokerage marriage for rewards is → **Void**.

7. Interference with the course of Justice

An agreement whose object is to induce a judicial or state officials to act corruptly and interfere with legal proceedings.

8. Interest Against Obligation

Agreements which tend to create interest against obligation are → **Void**.

9. Consideration Unlawful in Part

Section 24 : If any part of a single consideration for one or more objects, or any one or any part of any one of several considerations for a single object, is unlawful, the agreement is → **Void**.

5. Void Agreements

Expressly declared Void Agreements

1	Made by incompetent parties (Section 11)	6	Agreement in restraint of marriage (Section 26)
2	Agreements made under Bilateral mistake of fact (Section 20)	7	Agreements in restraint of trade (Section 27)
3	Agreements the consideration or object of which is unlawful (Section 23)	8	Agreement in restraint of legal proceedings (Section 28)
4	Agreement the consideration or object of which is unlawful in parts (Section 24)	9	Agreement the meaning of which is uncertain (Section 29)
5	Agreements made without consideration (Section 25)	10	Wagering Agreement (Section 30)
		11	Agreements to do impossible Acts (Section 56)



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I. Agreement in restraint of Marriage (Section 26)

- Every agreement in restraint of marriage of any person other than a minor, is void.

II. Agreement in restraint of Trade (Section 27)

- An agreement by which any person is restrained from exercising a lawful profession, trade or business of any kind, is to that extent Void.

Exception to rule that an
Agreement in Restraint
of Trade is void

Statutory Provisions

Sale of Goodwill

Indian Partnership Act
1932

III. Agreement in restraint of Legal Proceedings (Section 28)

- ❖ An agreement in restraint of legal proceeding means an agreement

By which any party thereto is
restricted absolutely from enforcing
his rights under a contract through
a Court

OR

which abridges the usual period for
starting legal proceedings.

- ❖ A contract of this nature is void

Exception

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

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



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IV. Agreement the meaning of which is uncertain (Section 29)

- An agreement, the meaning of which is not certain, is → **Void**.
- But, where the meaning thereof is capable of being made certain, the agreement is → **Valid**

V. Wagering Agreement (Section 30)

- Wagering agreement is an agreement involving payment of a sum of money upon the determination of an uncertain event.
- An agreement by way of a wager is → **Void**.
- But if one of the parties has control over the event, agreement is not a wager.

Essentials of a Wager

Promise to pay money or money's worth

Promise must Conditional on an event happening or not happening

Uncertainty of event

Two parties- each must stand to win or lose

Common intention to bet at the time of making the agreement

No interest in the event except for stake

Transactions Similar to Wager (Gambling)

Lottery Transactions

- A game of chance and not of skill or knowledge.
- Prime motive of participant is gambling, the transaction amounts to a wager.
- The person responsible for running the lottery will not be punished under the Indian Penal Code
- **Section 294A of IPC** :→ Lotteries are illegal and even collateral transactions to it are tainted with illegality

Crossword Puzzles and Competitions

- **Crossword puzzles** → in which prizes depend upon the correspondence of the competitor's solution with a previously prepared solution kept with the editor of a newspaper is a lottery and therefore, a wagering transaction.
- Crossword puzzles, picture competitions and athletic competitions where prizes are awarded on the basis of skill and intelligence are the games of skill and hence such competitions are valid.



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

Crossword Puzzles and Competitions

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

Facts of the Case : A crossword puzzle was given in magazine. A solved his crossword puzzle and his solution corresponded with previously prepared solution kept with the editor.

Held : This was a game of chance and therefore a lottery (wagering transaction).

Speculative Transactions

An agreement or a share market transaction where

- the parties intend to settle the difference between the contract price and the market price of
- certain goods or shares on a specified day, is a gambling and
- hence void.

Horse Race Transactions

A horse race competition where prize payable to the bet winner is less than Rs.500 is a wager.

Transactions resembling with wagering transactions but are not void

Chit Fund

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

Commercial transactions or share market transactions

In these transactions in which

→ delivery of goods or shares is intended to be given or taken, do not amount to wagers.



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Games of Skill and Athletic Competition

- Crossword puzzles, picture competitions and athletic competitions where prizes are awarded on the basis of skill and intelligence are the games of skill and hence such competition are valid.
- According to the Prize Competition Act, 1955 prize competition in games of skill are not wagers provided the prize money does not exceed ₹1,000.

Contract of Insurance

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

Distinction between Contract of Insurance and Wagering Agreement

	Basis	Contracts of Insurance	Wagering Agreement
1	Meaning	It is a contract to indemnify the loss.	It is a promise to pay money or money's worth on the happening or non-happening of an uncertain event.
2	Consideration	The crux of insurance contract is the mutual consideration (premium and compensation amount).	There is no consideration between the two parties. There is just gambling for money.
3	Insurable Interest	Insured party has insurable interest in the life or property sought to be insured.	There is no property in case of wagering agreement. There is betting on other's life and properties.
4	Contract of Indemnity	Except life insurance, the contract of insurance indemnifies the insured person against loss.	Loser has to pay the fixed amount on the happening of uncertain event.
5	Enforceability	It is valid and enforceable	It is void and unenforceable agreement.
6	Premium	Calculation of premium is based on scientific and actuarial calculation of risks.	No such logical calculations are required in case of wagering agreement.
7	Public Welfare	They are beneficial to the Society	They have been regarded as against the public welfare.

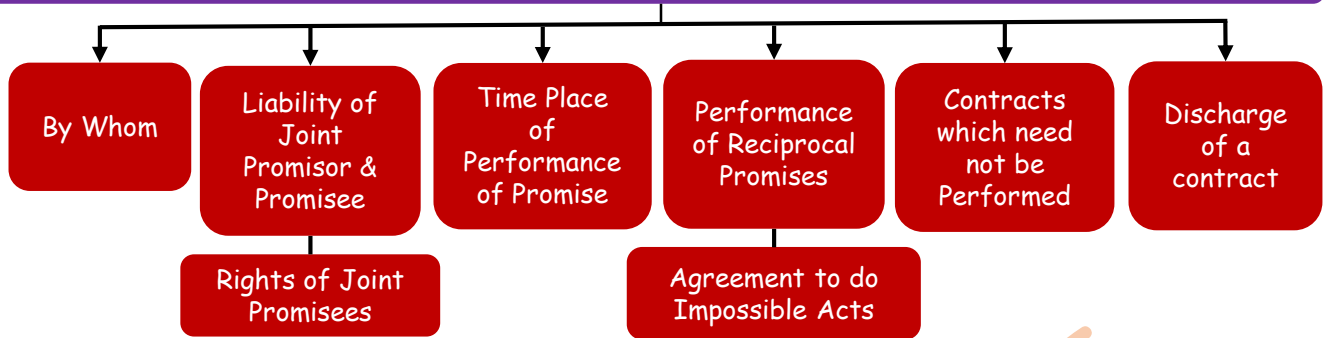


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Unit -4 : Performance of Contract



1. Performance of Contract

❖ **Meaning** : Fulfilment of obligations to the contract

❖ **Section 37** : The parties to a contract must either perform, or offer to perform, their respective promises unless such performance is dispensed with or excused under the provisions of the Contract Act or of any other law.

Types: As per Section 37, "Performance of Contract" may be :-

A. Actual Performance

Where a party to a contract has

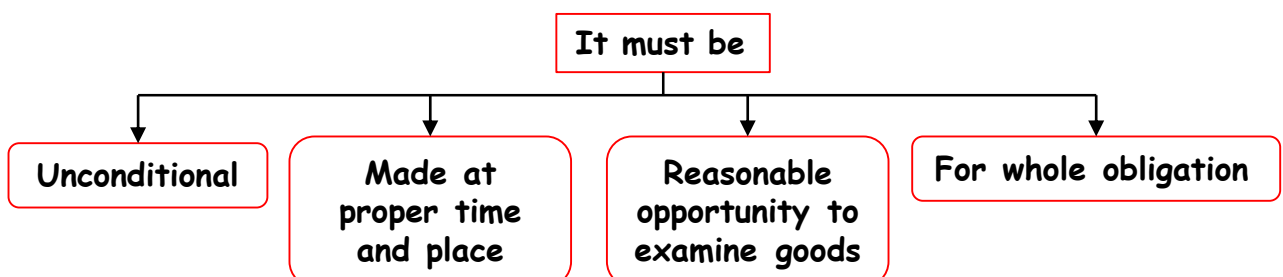
- done what he had undertaken to do or
- Either of the parties have fulfilled their obligations
- under the contract within the time and in the manner prescribed.

B. Offer to perform or attempted performance or tender of performance

When the performance becomes due,

- the promisor offers to perform his obligation but
- the promisee refuses to accept the performance.

2. Conditions to be Satisfied for a Valid Tender or Attempted Performance



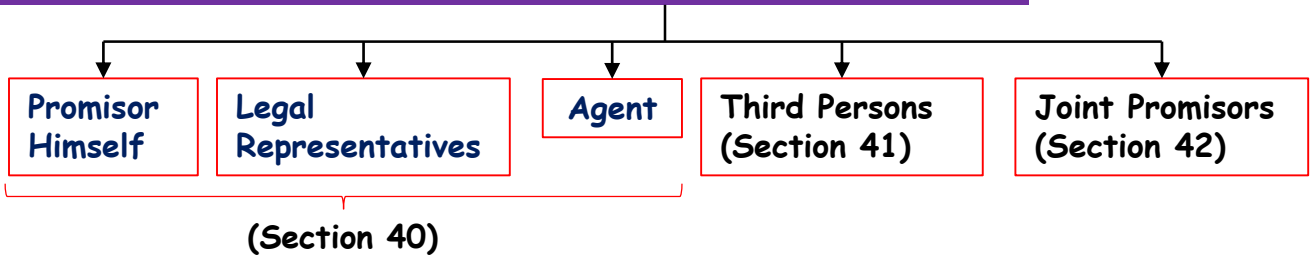


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3. By Whom a Contract may be Performed (Section -40,41,42)



1. Promisor Himself

If there is something in the contract to show that
- it was the intention of the parties that the promise should be performed by the promisor himself,

Then such promise must be performed by the → Promisor

Contracts which involve the exercise of
- personal skill or
- diligence, or
- which are founded on personal confidence between the parties

Must be performed by the promisor himself

2. Agent

❖ Where personal consideration is not the foundation of a contract, the promisor or his representative may employ a competent person to perform it.

3. Legal Representatives

❖ A contract which involves the use of personal skill or is founded on personal consideration comes to an end on the death of the promisor.

❖ As regards any other contract the legal representatives of the deceased promisor are bound to perform it unless a contrary intention appears from the contract **(Section 37, para 2).**

❖ But their liability under a contract is limited to the value of the property they inherit from the deceased.



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4. Third Persons : Effect of accepting performance from third person Section 41

- ❖ When a promisee accepts performance of the promise from a third person, he cannot afterwards enforce it against the promisor.
- ❖ That is, performance by a stranger, if accepted by the promisee, this results in discharging the promisor, although the latter has neither authorised nor ratified the act of the third party.
- ❖ **Example :** A received certain goods from B promising to pay Rs. 100,000/-. Later on, A expressed his inability to make payment. C, who is known to A, pays Rs. 60,000/- to B on behalf of A. However, A was not aware of the payment. Now B is intending to sue A for the amount of Rs.100,000/-. Therefore, in the present instance, B can sue only for the balance amount i.e., Rs.40,000/- and not for the whole amount.

5. Joint promisors (Section 42)

- ❖ When two or more persons have made a joint promise, then unless a contrary intention appears by the contract, all such persons must jointly fulfil the promise.
- ❖ **If any of them dies** → his legal representatives must, jointly with the surviving promisors, fulfil the promise.
- ❖ **If all of them die** → the legal representatives of all of them must fulfil the promise jointly.

4. Distinction between Succession and Assignment

Succession

- In case of succession both the burden and benefits attaching to the contract are succeeded by process of law.
- However, the successor's liability is limited to the extent to the property inherited by him.

Assignment

- In case of assignment, the benefit of the contract can only be assigned but not the liabilities.
- Benefit is coupled with a liability OR when a personal consideration is involved, then benefit cannot be assigned.



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5. Liability of Joint Promisor & Promisee

Devolution of Joint Liabilities (Section 42)

- ❖ If two or more persons have made a joint promise, ordinarily all of them during their life-time must jointly fulfil the promise.
- ❖ **After death of any one of them**; → his legal representative jointly with the survivor or survivors should do so.
- ❖ **After the death of the last survivor** : → the legal representatives of all the original co-promisors must fulfil the promise.

Section 42 deals with voluntary discharge of obligations by joint promisors.

Any one of Joint promisors may be compelled to perform (Section 43)

- ❖ When two or more persons make a joint promise,
 - the promisee may, in the absence of express agreement to the contrary, compel
 - any one or more of such joint promisors to perform the whole of the promise.
- ❖ **Each promisor may compel contribution** - Each of two or more joint promisors may compel every other joint promisor to contribute equally with himself to the performance of the promise, unless a contrary intention appears from the contract.
(if one of the joint promisors is made to perform the whole contract, he can call for a contribution from others)
- ❖ **Sharing of loss by default in contribution** : - If any one of two or more joint promisors makes default in such contribution, the remaining joint promisors must bear the loss arising from such default in equal shares.

Effect of release of one joint promisor (Section 44)

Where two or more persons have made a joint promise, a release of one of such joint promisors by the promisee

Does not discharge the other joint promisor or joint promisors,

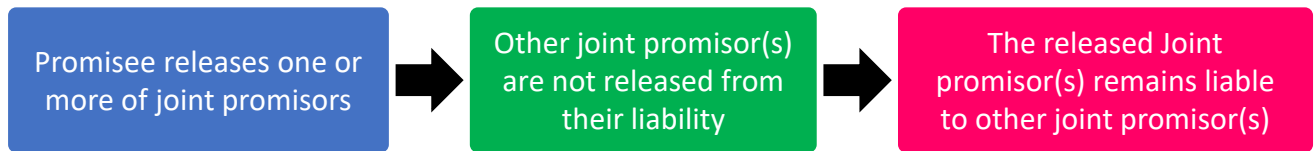
Neither does it free the joint promisors so released from responsibility to the other joint promisor or promisors.



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Right of Joint Promisees (Section 43)

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

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

Summary

If a person make a promise to two or more persons jointly (i.e., joint promisees), ordinarily all of them during their life-time have joint right to claim the performance.

After death of any one of them, :
His legal representative jointly with the survivor or survivors have joint right to do so.

After the death of the last survivor
The legal representatives of all the original joint promisees have the right to claim the performance.

6. Time of Place for Performance of the Promise

Section 46 : Where no application is to be made by the promisee and no time is specified



Performance should be within a reasonable time (it differs from case to case, based on facts and circumstances).

Section 47 : Where time is specified and no application to be made by the promisee



Perform at any time during the usual hours of business, on such day and place at such time as specified.



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Section 48 : Application for performance to be made on a certain day

The promisee should apply for performance at a proper place within usual business hours

Section 49 : Where no application to be made and no place fixed for performance

The promisor should apply to the promisee to appoint a reasonable place for performance.

Section 50 : Performance in manner or at a time prescribed or sanctioned by promisee

To be performed in such manner or at such time as promisee prescribes or sanctions.

7. Performance of Reciprocal Promise

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

When a contract consists of reciprocal promises to be simultaneously performed,

no promisor needs to perform his promise

unless the promisee is ready and willing to perform his reciprocal promise.

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

Order of performance is expressly fixed by the contract

Perform in that order

Order is not expressly fixed -

Perform in that order which the nature of the transaction requires.

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

When a contract contains reciprocal promises, and one party to the contract prevents the other from performing his promise

Contract becomes voidable at the option of the party so prevented

And

He is entitled to compensation from the other party for any loss he may sustain in consequence of the non-performance of the contract



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(iv) Effect of default as to that promise which should be first performed in contract consisting of reciprocal promises - Section 54

- ❖ Section 54 applies when the promises are reciprocal and dependent.
- ❖ If the promisor who has to perform his promise before the performance of the other's promise fails to perform it, he cannot claim performance of the other's promise, and is also liable for compensation for his non-performance.

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

When a party to a contract promises to do certain thing at or before the specified time, and fails to do any such thing at or before the specified time,



the contract, or so much of it as has not been performed, **becomes voidable at the option of the promisee**, if the intention of the parties was that time should be of essence of the contract.

Effect of Such Failure when time is not essential

The contract does not become voidable by the failure to do such thing at or before the specified time,

but

The promisee is entitled to compensation from the promisor for any loss occasioned to him by such failure.

Effect of acceptance of performance at time other than agreed upon

The promisee cannot claim compensation for any loss occasioned by the non-performance of the promise at the time agreed, unless,
- at the time of acceptance, he gives notice to the promisor of his intention to do so.

(vi) Agreement to do Impossible Act - Section 56

The impossibility of performance may be of the two types, namely

a. Initial impossibility

b. Subsequent impossibility



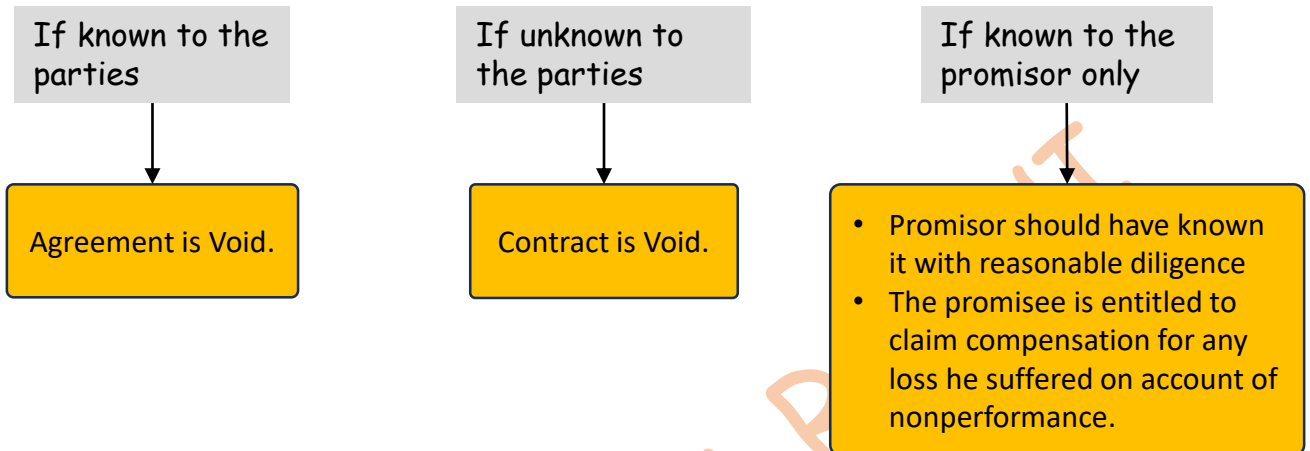
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a. Initial impossibility (Impossibility existing at the time of Contract)

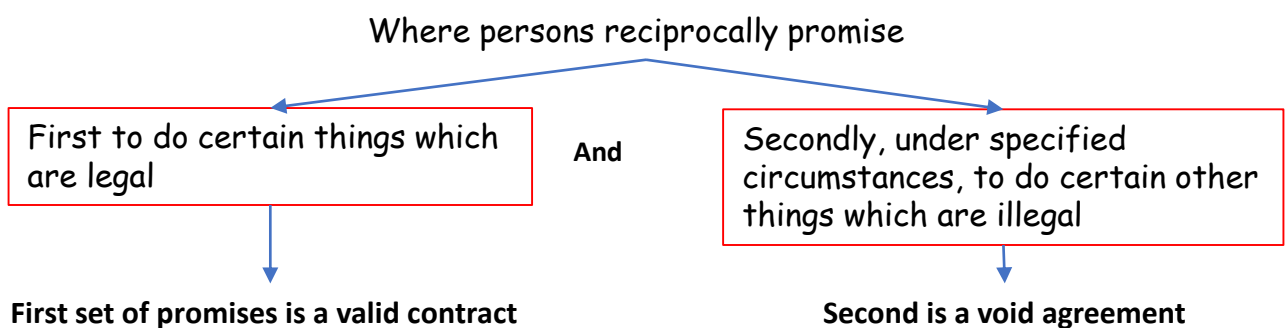
- ❖ When the parties agree upon doing of something which is obviously impossible in itself the agreement would be → void.
- ❖ Impossible in itself means impossible in the nature of things.
- ❖ The fact of impossibility may be and may not be known to the parties.



b. Subsequent or Supervening impossibility (Becomes impossible after entering into contract)

- When performance of promise becomes impossible or illegal by occurrence of an unexpected event or a change of circumstances beyond the contemplation of parties, the contract becomes → Void.
- The performance of a contract is quite possible when it is made. But subsequently, some event happens which renders the performance impossible or unlawful.
- **Such impossibility is called the subsequent or supervening.**
- **It is also called the post-contractual impossibility**

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





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(viii) "Alternative promise" One branch being illegal - Section 58

"In the case of the alternative promise, one branch of which is legal and the other illegal, the legal branch alone can be enforced"

8. Appropriation of Payments

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

If debt to be discharged is indicated (Section 59)

Payment should be applied to that debt indicated either by express intimation or under circumstances implying a particular debt.

If debt to be discharged is not indicated (Section 60)

- Creditor may apply it at his discretion to any lawful debt actually due and payable, where its recovery is or is not barred by law.
- However, the creditor shall not apply the payment to the disputed debt.

If neither part appropriates (Section 61)

- The payment shall be applied in discharge of the debts in the order of time, whether they are or are not barred by law.
- If all the debts are equal, payment shall be applied proportionately.

9. Contracts, Which need not be Performed with the consent of both the parties

i. Effect of Novation (Section 62)

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

a. Effect of Novation

- Parties to a contract may **substitute a new contract** for the old one.
- **Old contract is discharged** and **need not be performed**
- parties to the contract may be same or different
- It can take place only by mutual agreement between parties



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b. Effect of Rescission

- When the parties to a contract agree to rescind it, the contract need not be performed.
- only the old contract is cancelled and no new contract comes to exist in its place.
- It is needless to point out that novation also involves rescission
- The contract is discharge by mutual agreement

c. Effect of Alteration

- A contract is also discharged by alteration.
- The terms of contract may be so altered by mutual agreement that the alteration may have the effect of substituting a new contract for the old one.

Difference between Novation and Alteration

Novation	Alteration
1. There may be a change in the contracting parties in case of novation.	1. The contract is altered by mutual agreement, but the parties to the contract remain the same.
2. The old contract is substituted with a new one in case of novation.	2. In alteration, there may be some change in the terms and conditions of original contract.

ii. Promisee may waive or remit performance of promise (Section 63)

Every promisee may

- dispense with or remit, wholly or in part, the performance of the promise made to him, or
- may extend the time for such performance or
- may accept instead of it any satisfaction which he thinks fit".

A contract may be discharged by remission.

iii. Restoration of benefit under a voidable contract (Section 64)

- When a person at whose option a contract is voidable rescinds it, the other party thereto need not perform any promise therein contained in which he is the promisor
- If the party rescinding the contract has received any benefit under the contract, he must restore such benefit to the person from whom he has received it.



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

- When an agreement is discovered to be void or when a contract becomes void, any **person who has received any advantage** under such agreement or contract is **bound to restore it, or to make compensation for it** to the person from whom he received it.

v. - Communication of Rescission (Section 66)

- Rescission must be communicated to the other party in the same manner as a **proposal is communicated** under Section 4 of the Contract Act.
- Similarly, a rescission may be revoked in the same manner as a proposal is revoked.

vi. - Effects of neglect of promise to afford promisor reasonable facilities for performance (Section 67)

- If any promisee : → neglects or refuses to afford the promisor reasonable facilities for the performance of his promise,
- The promisor : → is excused by such neglect or refusal as to any non-performance caused thereby.

10. Discharge of Contract

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

i. Discharge by Performance

When the parties to a contract fulfil the obligations arising under the contract within the time and manner prescribed, then the **Contract** is discharged by performance.

Actual Performance

when each of the parties has done what he had agreed to do under the agreement.

Attempted Performance

When the promisor offers to perform his obligation, but the promisee refuses to accept the performance, it amounts to attempted performance or tender.



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ii. Discharge by Mutual Agreement (Section 62)

If all parties to a contract mutually agree to replace the contract with a new one or annul or remit or alter it, then it leads to a discharge of the original contract due to a mutual agreement.

iii. Discharge by impossibility of performance

- The impossibility may exist from the very start. In that case, it would be impossibility ab initio.
- Alternatively, impossibility may supervene. Supervening impossibility may take place owing to :

An unforeseen change in law

The destruction of the subject-matter essential to that performance

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

Declaration of a war.

iv. Discharge by lapse of time

- The Limitation Act, 1963 prescribes a specified period for performance of a contract.
- If the promisor fails to perform and the promisee fails to take action within this specified period, then the latter cannot seek remedy through law.
- It discharges the contract due to the lapse of time.

v. Discharge by operation of Law

A contract may be discharged by operation of law which includes by death of the promisor, by insolvency etc.



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vi. Discharge by breach of contract

- If a party to a contract fails to perform his obligation according to the time and place specified, then he is said to have committed a breach of contract.
- Breach can be of two types

1. Actual breach

2. Anticipatory breach

In both cases, the breach discharges the contract.

vii. Promisee may waive or remit performance of promise

- A promisee can waive or remit the performance of promise of a contract, wholly or in part.
- He can also extend the time agreed for the performance of the same.
- A contract may be discharged by remission. (Section 63)

viii. Effects of neglect of promisee to afford promisor reasonable facilities for performance

If any promisee neglects or refuses to afford the promisor reasonable facilities for the performance of his promise, the promisor is excused by such neglect or refusal as to any nonperformance caused thereby [Section 67].

ix. Merger of Rights

- In some situations, it is possible that inferior and superior right coincides in the same person.
- In such cases, both the rights combine leading to a discharge of the contract governing the inferior rights.

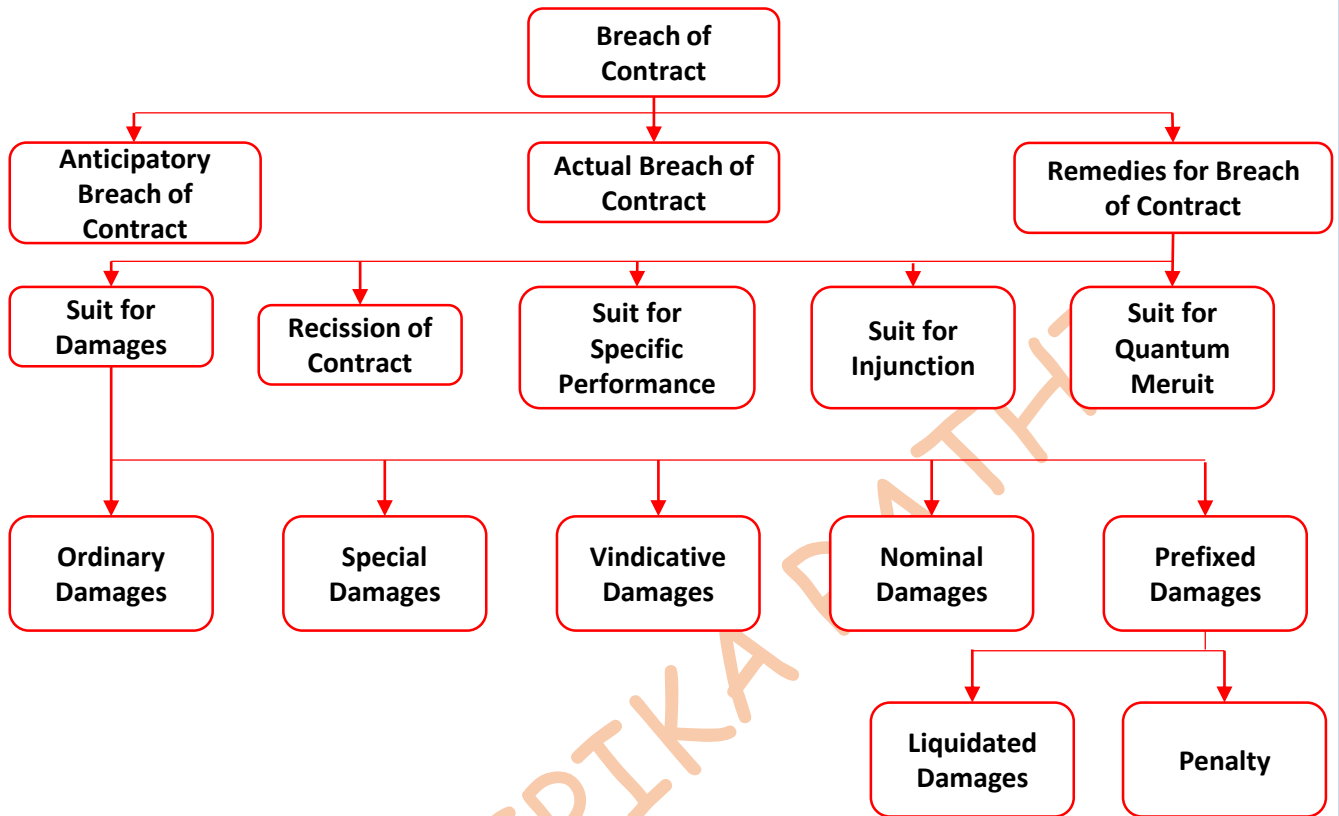


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Unit -5 : Breach Of Contract And Its Remedies



Meaning of Breach

- **Breach** means failure of a party to perform his or her obligation under a contract.
- Breach of contract may arise in two ways:
 1. Actual breach of contract
 2. Anticipatory breach of contract

1. Anticipatory Breach of Contract

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



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

A. Expressly by words spoken or written

B. Impliedly by the conduct of one of the parties

Effect of Anticipatory Breach

As per Section 39 of the Indian Contract Act, 1872 -

"When a party to a contract has refused to perform or disable himself from performing, his promise in its entirety, the promisee may put an end to the contract, unless he has signified, but words or conduct, his acquiescence in its continuance."

- The promisee is excused from performance or further performance of the contract.

He further has the following options

He can

- Rescind the contract **and**
- sue the other party for damages immediately without waiting till the due date of performance.

He may decide

- Not to rescind the contract **and**
- treat it as still operative and wait till the time of performance and then hold the other party responsible.

2. Actual Breach of Contract

- While an anticipatory breach is before the time of performance, an actual breach of contract is on the scheduled time of performance of the contract.

An actual breach of contract can be committed either

A. At the time when the performance of the contract is due

B. During the performance of the contract

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



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Remedies Available

Suit for
Damages

Rescission
of Contract

Suit for specific
performance

Suit for
Injunction

Suit upon
quantum meruit

3. Suit for Damages

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

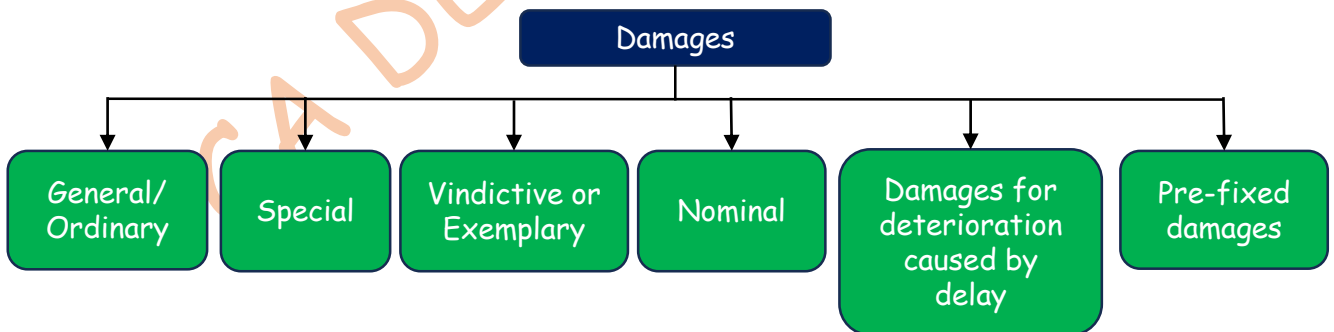
- On the breach of the contract, the party who suffers from such a breach is entitled to receive, from the party who has broken the contract, compensation for any loss or damage caused to him by breach.

- Compensation can be claimed for

Any loss or damage which naturally
arises in the usual course of events

Any loss or damage which the party
knew when they entered into the
contract, as likely to result from the
breach

- Special damages, if any, can be claimed only if the suffering party has given notice about it earlier.
- But the party suffering from the breach is bound to take reasonable steps to minimise the loss.
- No compensation is payable for any remote or indirect loss.



i. General / Ordinary Damages

When a contract has been broken,

- The party who suffers by such breach is entitled to receive, from the party who has broken the contract, compensation for any loss or damage 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.



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

Case Law: Hadley vs. Baxendale

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

Judgement: The court held that P was entitled only to ordinary damages and D was not liable for the loss of profits because the only information given by P to D was that the article to be carried was the broken shaft of a mill and it was not made known to them that the delay would result in loss of profits.

ii. Special Damages

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

iii. Vindictive or Exemplary Damages

These damages may be awarded only in two cases

i. For breach of promise to marry

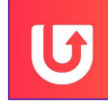
ii. For wrongful dishonour by a banker of his customer's cheque (*Gibbons v West Minister Bank*).

iv. Nominal Damages

- Nominal damages are awarded where the plaintiff has proved that there has been a breach of contract, but he has not in fact suffered any real damage.
- It is awarded just to establish the right to decree for the breach of contract.
- The amount may be a rupee or even 10 paise.



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v. Damages for deterioration caused by delay

- In the case of deterioration caused to goods by delay, damages can be recovered from carrier even without notice.
- The word 'deterioration' not only implies physical damages to the goods, but it may also mean loss of special opportunity for sale.

vi. Pre-Fixed Damages

- Sometimes, parties to a contract stipulate at the time of its formation that on a breach of contract by any of them, a certain amount will be payable as damage.
- It may amount to either or

liquidated damages (i.e., a reasonable estimate of the likely loss in case of breach)

OR

A penalty (i.e., an amount arbitrarily fixed as the damages payable).

Section 74 : If a sum is named in a contract as the amount to be paid in case of a breach, the aggrieved party is entitled to receive from the party at fault a reasonable compensation not exceeding the amount so named.

3. Penalty and Liquidated Damages (Section 74)

- ❖ English Law makes distinction between liquidated damages and penalty, whereas Indian Law does not make any distinction between the two.
- ❖ If the sum fixed in the contract represents a genuine pre-estimate by the parties of the loss, which would be caused by a future breach of the contract it is liquidated damages.
- ❖ **Penalty** : → Where the sum fixed in the contract is unreasonable and is used to force the other party to perform the contract, it is penalty.
- ❖ **Section 74** : → If the parties have fixed what the damages will be, the courts will never allow more. Thus, a person complaining of breach of contract is entitled to get reasonable compensation and is not entitled to realise anything by way of penalty.
- ❖ **Exception**: If a party enters into a contract with the State or Central government for the performance of an act in the interest of the general public, then a breach of such a contract makes the party liable to pay the entire amount mentioned in the contract.



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Distinction between liquidated damages and penalty

- If the sum payable is far in excess of the probable damage on breach of the contract, then it is a penalty.
- If a contract mentions an amount payable at a certain date and an additional amount if a default happens, then the additional sum is a penalty.
- Even if the contract specifies a sum as 'penalty' or 'damages', the Court needs to discern this from the facts of the case.
- In penalty, the payment intended to threaten (i.e., as a *terrorem* to) the offending party, whereas Liquidated damages is a genuine pre-estimate of the damage.
- The Indian Courts focus on awarding a reasonable compensation not exceeding the amount fixed in the contract and does not distinguish between the two.

Other remedies available for the breach of Contract, besides claiming damages

Rescission
of contract

Quantum
Meruit

Suit for specific
performance

Suit for
injunction

(i) Rescission of Contract

- When a contract is broken by one party, the other party may treat the contract as rescinded.
- In such a case he is free from all his obligations under the contract and is entitled to compensation for any damages that he might have suffered.

(ii) Quantum Meruit

- Where one person has rendered service to another in circumstances which indicate an understanding between them that it is to be paid for although no particular remuneration has been fixed, the law will infer a promise to pay.
- Quantum Meruit i.e. as much as the party doing the service has deserved.
- It covers a case where the party injured by the breach had at time of breach done part but not all of the work which he is bound to do under the contract and seeks to be compensated for the value of the work done.



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For the application of this doctrine, two conditions must be fulfilled:

It is only available if the original contract has been discharged

The claim must be brought by a party not in default

- Damages are compensatory in nature while quantum meruit is restitutory (i.e., seeking to restore the person to the position which he was in earlier).

The claim for quantum meruit arises in the following cases

- Agreement discovered to be void or when contract becomes void.
- Something done without intention of doing so gratuitously.
- Express or implied contract to render services but no agreement as to remuneration.
- Party refuses or abandons to perform contract.
- Divisible contract and party not in default has enjoyed benefit of part performance.
- When an indivisible contract for a lump sum is completely performed but badly the person who has performed the contract can claim the lump sum, but the other party can make a deduction for bad work.

(iii) Suit for Specific Performance

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

(iv) Suit for injunction

- Where a party to a contract is negating the terms of a contract, the court may by issuing an 'injunction orders', restrain him from doing what he promised not to do.

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

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



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Unit-6 : Contingent and Quasi Contracts

Contingent Contracts

Rules Relating to
Enforcement of
Contingent Contracts

Difference between
Contingent & Wagering
Contract

Quasi- Contracts

Cases deemed as
Quasi-Contracts

1. Contingent Contracts

Definition of 'Contingent Contract' (Section 31)

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

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

Meaning of collateral Event

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

Essential of a Contingent Contract

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

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

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

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



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2. Rules Relating to Enforcement

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

(a) Enforcement of Contracts contingent on an event happening (Section 32)

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

(b) Enforcement of Contracts contingent on an event not happening (Section 33)

- Where a contingent contract is made to do or not do anything if an uncertain future event does not happen, it can be enforced only when the happening of that event becomes impossible and not before.

(c) A contract would cease to be enforceable if it is contingent upon the conduct of a living person when that living person does something to make the 'event' or 'conduct' as impossible of happening. (Section 34)

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

Case Law: Frost V. Knight

Facts: The defendant promised to marry the plaintiff on the death of his father. While the father was still alive, he married another woman.

Judgement: It had become impossible that he should marry the plaintiff and she was entitled to sue him for the breach of the contract.

(d) Contingent on happening of specified event within the fixed time (Section 35)



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Contingent contracts to do or not to do anything, if a specified uncertain event happens within a fixed time, becomes void if

At the expiration of time fixed,
such event has not happened

Or

If, before the time fixed, such
event becomes impossible.

(e) Contingent on specified event not happening within fixed time: (Section 35)

Section 35 also says that -

"Contingent contracts to do or not to do anything, if a specified uncertain event does not happen within a fixed time, may be enforced by law when

- The time fixed has expired, and such event has not happened **or**
- Before the time fixed has expired, if it becomes certain that such event will not happen".

(f) Contingent on an impossible event (Section 36)

Contingent agreements to do or not to do anything, if an impossible event happens are void, whether the impossibility of the event is known or not to the parties to the agreement at the time when it is made.

Difference between a contingent contract and a wagering contract

Basis of difference	Contingent contract	Wagering contract
Meaning	A contingent contract is a contract to do or not to do something with reference to a collateralevent happening or not happening.	A wagering agreement is a promise to give moneyor money's worth with reference to an uncertainevent happening or not happening.
Reciprocal promises	Contingent contract maynot contain reciprocal promises.	A wagering agreement consists of reciprocalpromises.
Uncertain event	In a contingent contract,the event is collateral.	In a wagering contract, the uncertain event is the core factor.



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Nature of contract	Contingent contract may not be wagering in nature.	A wagering agreement is essentially contingent in nature.
Interest of contracting parties	Contracting parties have interest in the subject matter in contingent contract.	The contracting parties have no interest in the subject matter.
Doctrine of mutuality of lose and gain	Contingent contract is not based on doctrine of mutuality of lose and gain.	A wagering contract is a game, losing and gaining alone matters.
Effect of contract	Contingent contract is valid.	A wagering agreement is void.

3. Quasi Contracts

- Even in the absence of a contract, certain social relationships give rise to certain specific obligations to be performed by certain persons. These are known as quasi contracts as they create same obligations as in the case of regular contract.
- Such cases are not contract in the strict sense, but the Court recognises them as relations resembling those of contracts and enforces them as if they were contracts. Hence the term Quasi contracts (i.e. resembling a contract).
- Quasi contracts are based on principles of equity, justice and good conscience.
- A quasi or constructive contract rests upon the maxims, → **"No man must grow rich out of another person's loss"**

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

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

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



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Salient features of quasi contracts:

a. Such a right is always a right to money and generally, though not always, to a liquidated sum of money.

b. It does not arise from any agreement of the parties concerned, but is imposed by the law

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

Cases Deemed as Quasi -Contracts

Claims for necessities supplied
[Section 68]

Payment by an interested person
[Section 69]

Obligation of a person enjoying benefit of non gratuitous act
[Section 70]

Responsibility of finder of goods
[Section 71]

Money paid by mistake or under coercion
[Section 72]

A. Claim for necessities supplied to persons incapable of contracting (Section 68)

- If a person, incapable of entering into a contract, or anyone whom he is legally bound to support, is supplied by another person with necessities suited to his condition in life, the person who has furnished such supplies is entitled to be reimbursed from the property of such incapable person.
- To establish his claim, the supplier must prove that

The goods were supplied to the person who was minor or a lunatic

And

Also, that they were suitable to his actual requirements at the time of the sale and delivery

B. Payment by an interested person (Section 69)

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



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C. Obligation of person enjoying benefits of non-gratuitous act (Section 70)

- Where a person
 - lawfully does anything for another person, or delivers anything to him not intending to do so gratuitously and
 - Such other person enjoys the benefit thereof, the latter is bound to pay compensation to the former in respect of, or to restore, the thing so done or delivered.
- For a suit to succeed in this case, the plaintiff must prove:
 - That he had done the act or had delivered the thing lawfully
 - That he did not do so gratuitously and
 - That the other person enjoyed the benefit

Case Law: Shyam Lal vs. State of U.P.

Facts: 'K' a government servant was compulsorily retired by the government. He filed a writ petition and obtained an injunction against the order. He was reinstated and was paid salary but was given no work and in the meantime government went on appeal.

Judgement: Appeal was decided in favour of government and 'K' was directed to return the salary paid to him during period of reinstatement.

D. Responsibility of Finder of Goods (Section 71)

A person who finds goods belonging to another and takes them into his custody is subject to same responsibility as if he were a bailee.

Thus, a finder of lost goods has:

To take proper care of the property as man of ordinary prudence would take

No right to appropriate the goods

To restore the goods if the owner is found

Case Law: Hollins vs. Howler L. R. & H. L.

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

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



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E. Money paid by mistake or under coercion (Section 72)

A person to whom money has been paid or anything delivered by mistake or under coercion, must repay or return it.

- **Shivprasad Vs Sirish Chandra** - Every kind of payment of money or delivery of goods for every type of 'mistake' is recoverable.
- **Sales tax officer vs. Kanhaiyalal** - A payment of municipal tax made under mistaken belief or because of mis-understanding of the terms of lease can be recovered from municipal authorities.
- **Seth Khanjalek vs National Bank of India** - Any money paid by coercion is also recoverable. The word coercion is not necessarily governed by section 15 of the Act, rather, it is interpreted to mean and include oppression, extortion, or such other means.

Case Law: *Trikamdas vs. Bombay Municipal Corporation*

Facts: 'T' was traveling without ticket in a tram car and on checking he was asked to pay ₹5/- as penalty to compound transaction. T filed a suit against the corporation for recovery on the ground that it was extorted from him.

Judgement: The suit was decreed in T's favour.

Difference between quasi contracts and contracts

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



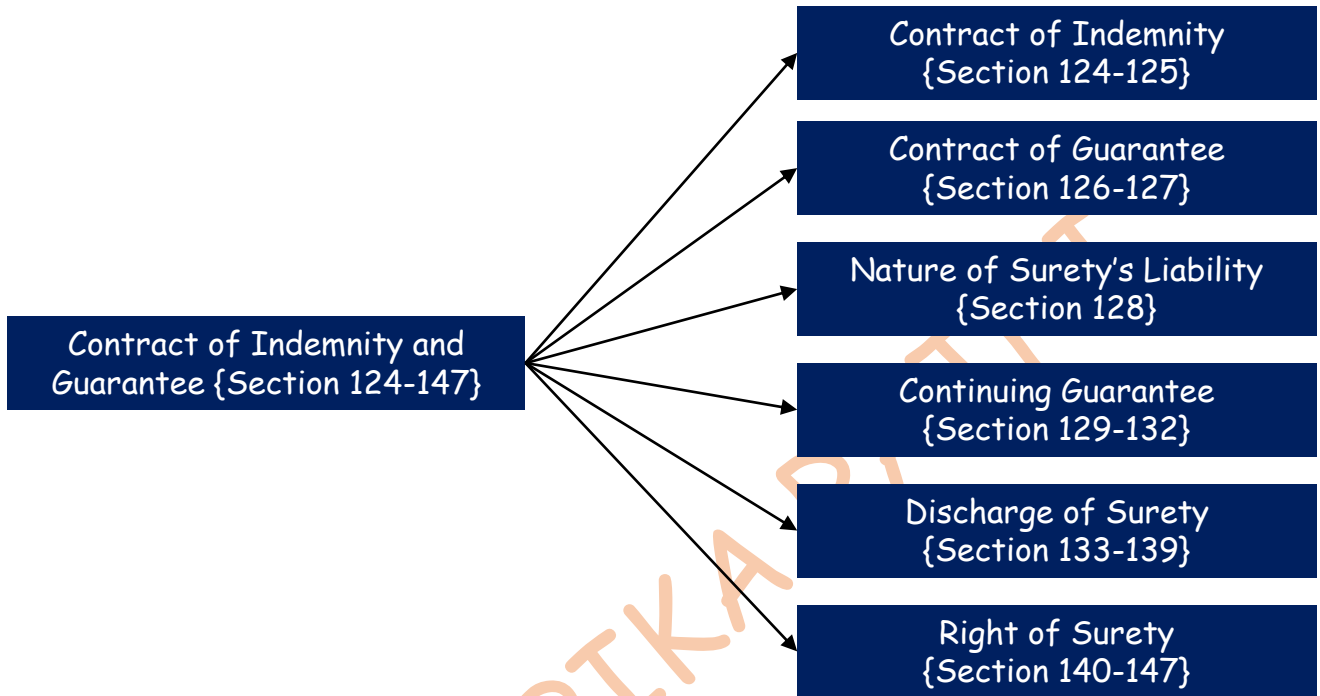
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Unit-7 : Contract of Indemnity and Guarantee

Overview



Introduction

- Contract of Indemnity and
- Guarantee

Are specific types of contracts

Provided under section 124 to 127 of the Indian Contract Act 1872.

- In addition to the specific provisions u/s Section 124 to Section 147 of the Indian Contract Act, 1872
- General principles of contracts are also applicable to such contracts which are

- a. Offer and Acceptance
- b. Intention to create legal obligation
- c. Consideration
- d. Competency to contract
- e. Free consent
- f. Lawful object
- g. The agreement must not be expressly declared to be void
- h. The terms of the agreement must not be vague or uncertain
- i. The agreement must be capable of performance
- j. Legal formalities.



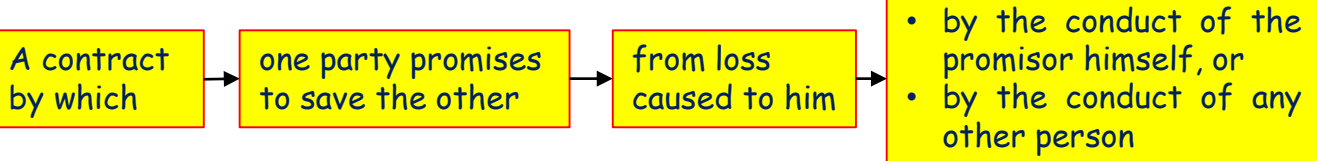
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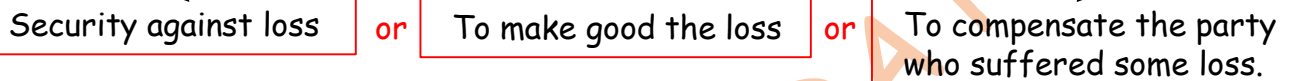
Contract of Indemnity

Definition u/s 124 of Indian Contract Act 1872



Meaning

Indemnity/ Indemnify means



As per English Law {*Gajanan Moreshwar v/s Moreshwar Madan (1942)*}

- Indemnity means → Promise to save another harmless from the loss.
- It covers every loss whether due to negligence of promisee or by natural calamity or by accident.

Basic Condition

- ❖ **Existence of loss** is essential
- ❖ Unless the promisee has suffered a loss he cannot be liable on the contract of indemnity.
- ❖ Such loss is caused by

Conduct of the promisor himself

Conduct of any other person

❖ Loss occasioned by

An accident not caused by any person

An act of God/ Natural event is not covered

Mode of Contract of Indemnity

Express : It is said to be express when a person expressly promises to compensate the other from loss.

Implied : It is said to be implied when it is to be inferred from the conduct of the parties or from the circumstances of the case.



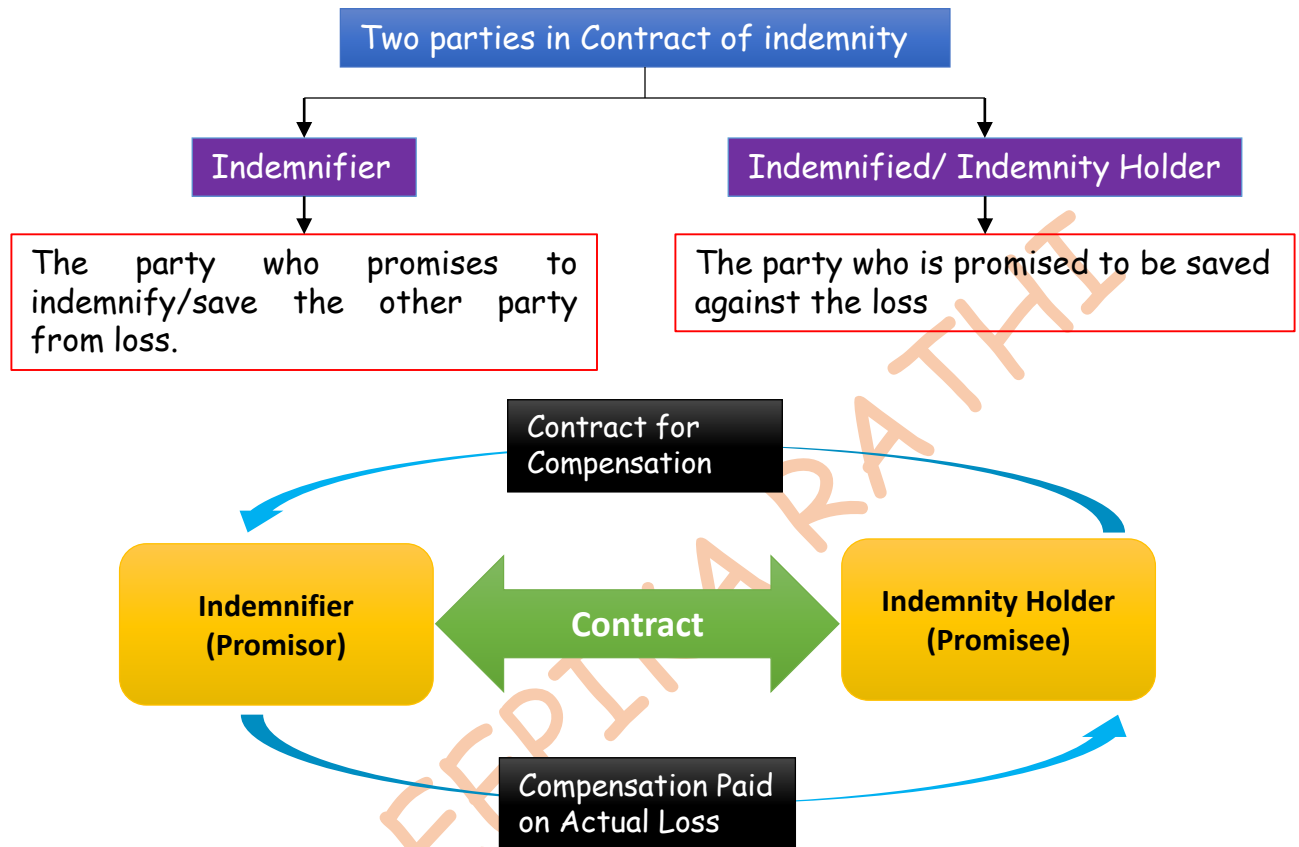
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Insurance Contracts

- Fire Insurance or Marine insurance → **Contract of Indemnity**
- Life Insurance → **Not a Contract of indemnity**



Right of Indemnity Holder (Section 125)

The promisee in a contract of indemnity, acting within the scope of his authority, is entitled to recover from the promisor/indemnifier

(a) All damages which he may be compelled to pay in any suit

(b) All costs which he may have been compelled to pay in bringing/ defending the suit

(c) All sums which he may have paid under the terms of any compromise of suit



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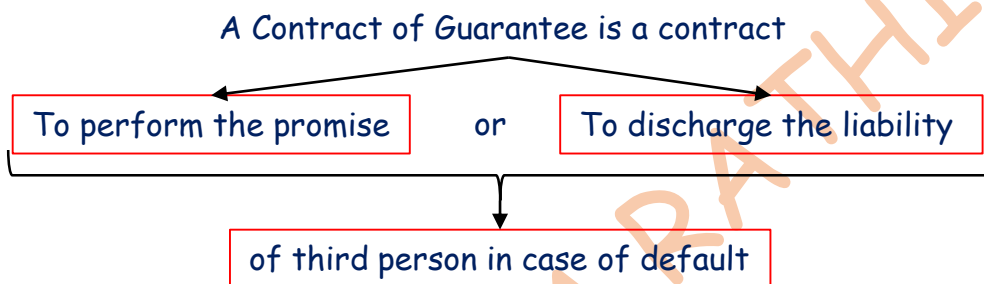
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When does the liability of an Indemnifier Commence?

- ❖ The Indian Contract Act, 1872, → is silent on the time of commencement of liability of indemnifier,
- ❖ As per judicial pronouncements → The liability of an indemnifier commences as soon as the liability of the indemnity-holder becomes absolute and certain.

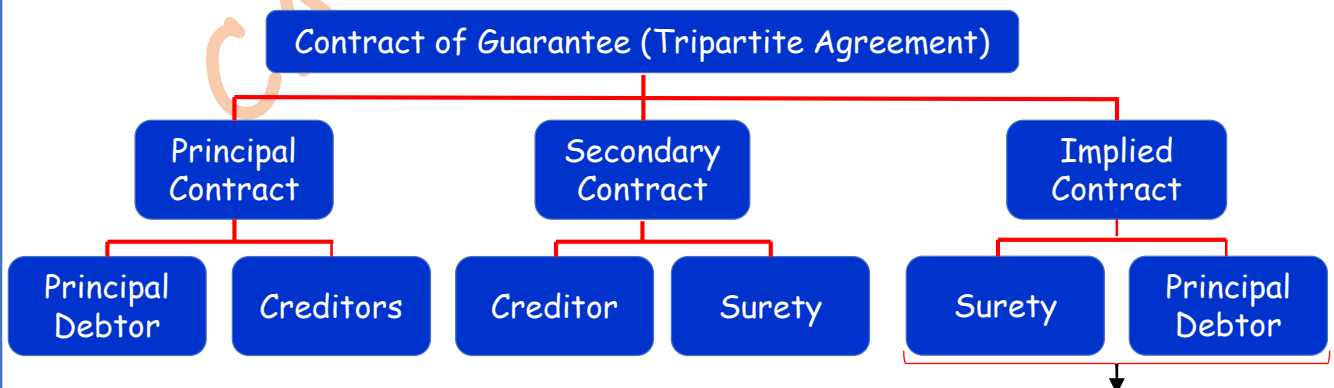
Contract of Guarantee

"Contract of guarantee", "surety", "principal debtor" and "creditor"[Section 126]



Three parties are involved in a contract of guarantee

- **Surety** :- Person who gives the guarantee
 - **Principal Debtor** :- Person in respect of whose default the guarantee is given
 - **Creditor** :- Person to whom the guarantee is given
- Guarantee is a promise to pay a debt owed by a third person in case the latter does not pay.
 - Guarantee: An Express contract → Given may be oral or written



Principal debtor is under an obligation to indemnify the surety if the surety is made to pay or perform.

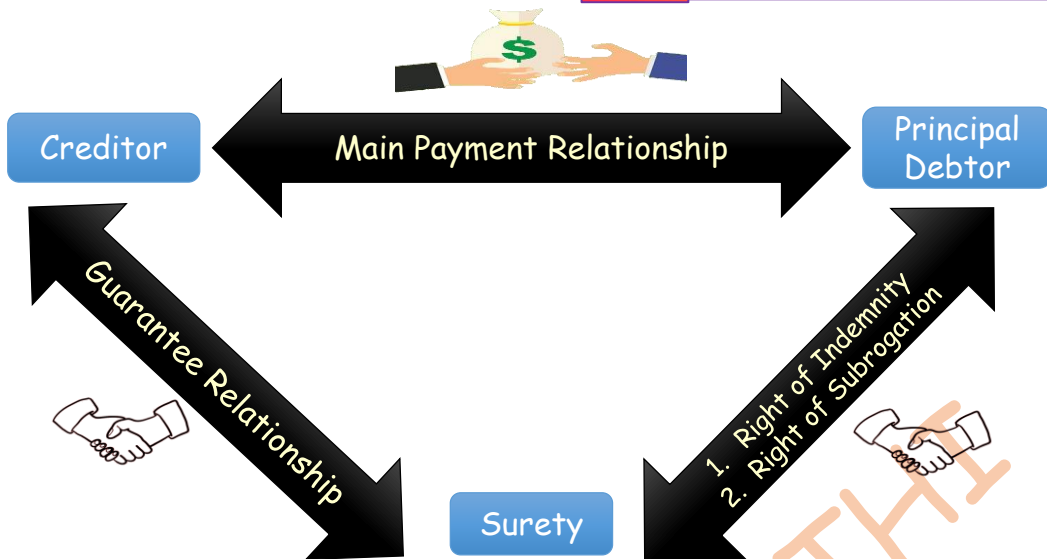
Note :-> The right of surety is not affected by the fact that the creditor has refused to sue the principal debtor or that he has not demanded the sum due from him.



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ESSENTIAL FEATURES OF A GUARANTEE

Purpose

To secure the payment of a debt

The existence of recoverable debt is necessary

If there is no principal debt, there can be no valid guarantee.

Consideration

Should be supported by some consideration

There is no need for a direct consideration between the surety and the creditor.

Section 127: Consideration received by the principal debtor is sufficient consideration to surety for giving the guarantee.

- **Principal Debtor incompetent to contract** :→ Guarantee is valid
- **Surety incompetent to contract** :→ Guarantee Void (Surety must be competent to contract)

Existence of a liability

There must be an existing liability or a promise whose performance is guaranteed.

Such liability or promise must be enforceable by law.

The liability must be legally enforceable and not time barred.



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No misrepresentation or Concealment (Section 142 and 143)

Section 142

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

Section 143

Any guarantee which the creditor has obtained by means of keeping silence as to material circumstances, is → **Invalid**

Writing not necessary

Section 126: → Guarantee may be either oral or written

Joining of the other co-sureties (Section 144)

- Where a person gives a guarantee upon a contract that the creditor shall not act upon it until another person has joined in it as co-surety, the guarantee is not valid if that other person does not join.
- The guarantee by a surety is not valid if a condition is imposed by a surety that some other person must also join as a co-surety, but such other person does not join as a co-surety.

Types of Guarantees

A. Specific Guarantee

- A guarantee which extends to a single debt/ specific transaction is called a specific guarantee.
- The surety's liability comes to an end when the guaranteed debt is duly discharged or the promise is duly performed.

B. Continuing Guarantee [Section 129]

- 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.



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DISTINCTION BETWEEN A CONTRACT OF INDEMNITY AND A CONTRACT OF GUARANTEE

Point of Distinction	Contract of Indemnity	Contract of Guarantee
Number of party/parties to the contract	There are only two parties namely the indemnifier [promisor] and the indemnified [promisee]	There are three parties - creditor, principal debtor and surety.
Nature of liability	The liability of the indemnifier is primary and unconditional	The liability of the surety is secondary and conditional as the primary liability is that of the principal debtor.
Time of liability	The liability of the indemnifier arises only on the happening of a contingency.	The liability arises only on the non-performance of an existing promise or non-payment of an existing debt.
Time to Act	The indemnifier need not act at the request of indemnity holder.	The surety acts at the request of principal debtor.
Right to sue third party	Indemnifier cannot sue a third party for loss in his own name as there is no privity of contract. Such a right would arise only if there is an assignment in his favour.	Surety can proceed against principal debtor in his own right because he gets all the right of a creditor after discharging the debts.
Purpose	Reimbursement of loss	For the security of the creditor
Competency to contract	All parties must be competent to contract	In the case of a contract of guarantee, where a minor is a principal debtor the contract is still valid.

Nature and extent of surety's liability [section -128]

- **Section 128** :→The **liability of the surety is co-extensive** with that of the **principal debtor** unless it is otherwise provided by the contract.
- **Liability of surety is of secondary nature** as he is liable only on default of principal debtor.
- Where a debtor cannot be held liable on account of any defect in the document, the liability of the surety also ceases.
- A creditor may choose to proceed against a surety first, unless there is an agreement to the contrary.



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Liability of two persons, primarily liable, not affected by arrangement between them that one shall be surety on other's default

Section 132 :-

- Where two persons contract with a third person to undertake a certain liability and
- also contract with each other
- that one of them shall be liable only on the default of the other,
- **the liability of each of such two persons to the third person under the first contract is not affected by the existence of the second contract,**
- although such third person may have been aware of its existence.

Discharge of a Surety

- ❖ A surety is said to be discharged when his liability as surety comes to an end.
- ❖ The various modes of discharge of surety are -

By Revocation of the contract of guarantee	By Conduct of the Creditor	By the invalidation of the contract of guarantee
<p>a.Revocation of continuing guarantee by notice (Section 130)</p> <p>b.Revocation of continuing guarantee by surety's death (Section 131)</p> <p>c.By Novation (Section 62)</p>	<p>a.By variance in terms of contract (Section 133) Exception : Variation which is not substantial or material or which is beneficial to surety will not discharge him of his liability</p> <p>b.By release or discharge of principal debtor (Section 134)</p> <p>c.Discharge of Surety when creditor compounds with, gives time to, or agree not to sue principal debtor (Section 135)</p> <ol style="list-style-type: none"> i. Composition ii. Promise to give time iii. Promise not to sue <p>Exception:</p> <p>(i) Surety not discharge when agreement made with third person to give time to principal debtor (Section- 136)</p> <p>(ii) Creditor's forbearance to sue does not discharge surety (Section- 137)</p> <p>d. Discharge of surety by creditor's act or omission impairing surety's eventual remedy (Section 139)</p>	<p>a. Guarantee obtained by misrepresentation invalid (Section 142)</p> <p>b. Guarantee obtained by concealment invalid (Section 143)</p> <p>c. Guarantee on contract that creditor shall not act on it until Co-Surety joins (Section 144)</p>



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By Revocation of the contract of guarantee

(a) Revocation of continuing guarantee by Notice (Section 130)

The **continuing guarantee** may at any time be revoked by the surety as to future transactions by notice to the creditors.

Once the guarantee is revoked, the surety is not liable for any future transaction however he is liable for all the transactions that happened before the notice was given.

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

(b) Revocation of continuing guarantee by surety's death (Section 131)

In the absence of any contract to the contrary, the **death of surety operates** as a revocation of a continuing guarantee as to the future transactions taking place after the death of surety.

However, the **surety's estate remains liable** for the past transactions which have already taken place before the death of the surety.

(c) By Novation (Section 62)

The **surety under original contract is discharged** if a fresh contract is entered into either between the same parties or between the other parties, the consideration being the mutual discharge of the old contract.

By Conduct of the Creditor

(a) By variance in terms of Contract (Section 133)

Where there is any variance in the terms of contract between the principal debtor and creditor without surety's consent,

it would discharge the surety in respect of all transactions taking place subsequent to such variance.

(b) By release or discharge of principal debtor (Section 134)

The surety is discharged if the creditor

(i) Enters into a fresh/ new contract with principal debtor; by which the principal debtor is released

(ii) Does any act or omission, the legal consequence of which is the discharge of the principal debtor.



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(c) Discharge of surety when creditor compounds with, gives time to, or agrees not to sue, principal debtor (Section 135)

A contract between the creditor and the principal debtor, by which the creditor makes

- A composition with, or
- Promises to give time to, or
- Promises not to sue, the principal debtor or,
- Discharges the surety,



unless the surety assents to such contract.

(i) Composition

If the creditor makes a composition with the principal debtor, without consulting the surety, → **The latter is discharged (Surety)**

Composition inevitably involves variation of the original contract, and, therefore, → **The surety is discharged.**

(ii) Promise to give time

- When the time for the payment of the guaranteed debt comes, the surety has the right to require the principal debtor to pay off the debt.
- Accordingly, it is one of the duties of the creditor towards the surety → **not to allow the principal debtor more time for payment.**

(iii) Promise not to Sue

- If the creditor under an agreement with the principal debtor promises not to sue him, the → **surety is discharged.**

Cases where surety not discharged

Surety not discharged when agreement made with third person to give time to principal debtor [Section 136]:

Where a contract to give time to the principal debtor is made by the creditor with a third person, and not with the principal debtor, → **The surety is not discharged.**

Creditor's forbearance to sue does not discharge surety [Section 137]

Mere forbearance on the part of the creditor to sue the principal debtor or to enforce any other remedy against him does not in the absence of any provision in the guarantee to the contrary, discharge the surety.



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(d) Discharge of surety by creditor's act or omission impairing surety's eventual remedy (Section 139)

If the creditor does any act/omits to do an act, which is inconsistent with the rights of the surety, then → **The surety is discharged.**

State bank of Saurashtra V Chitranjan Rangnath Raja (1980)

In a case before the Supreme Court of India,

"A bank granted a loan on the security of the stock in the godown. The loan was also guaranteed by the surety. The goods were lost from the godown on account of the negligence of the bank officials. The surety was discharged to the extent of the value of the stock so lost."

By invalidation of the contract of guarantee

A. Guarantee obtained by misrepresentation invalid (Section 142)

Any guarantee

- which has been obtained by means of misrepresentation made by the creditor **or**
- with his knowledge and assent, concerning a material part of the transaction

Invalid

B. Guarantee obtained by concealment invalid (Section 143)

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

C. Guarantee on contract that creditor shall not act it until co-surety joins (Section 144)

Where a person gives a guarantee upon a contract that the creditor shall not act upon it until another person has joined in it as co- surety, the guarantee is not valid if that other person does not join.



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Right of a Surety

Right against the principal debtor

Rights of subrogation [Section 140]

Surety, upon payment of all that he is liable for, is invested with all the rights which the creditor has against the principal debtor i.e., the surety steps into the shoes of the creditor

Right of indemnity [Section 145]

- In every contract of guarantee there is an implied promise by the principal debtor to indemnify the surety.
- The surety is entitled to recover from the principal debtor whatever sum he has rightfully paid under the guarantee, but not sums which he paid wrongfully.

Right against the Creditor

(a) Surety's right to benefit of creditor's securities [Section 141]

A surety is entitled to the benefit of every security which the creditor has against the principal debtor at the time when the contract of suretyship is entered into, whether the surety knows of the existence of such security or not; and, if the creditor loses, or, without the consent of the surety, parts with such security, the surety is discharged to the extent of the value of the security.

(b) Right to set off :

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

(c) Right to share reduction

The surety has right to claim proportionate reduction in his liability if the principal debtor becomes insolvent.

Right against the Co-Sureties

"When the same debt or duty is guaranteed by two or more persons, such persons are called co-sureties"



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(a) Co-sureties liable to contribute equally (Section 146):

Unless otherwise agreed, each surety is liable to contribute equally for discharge of whole debt or part of the debt remains unpaid by debtor.

(b) Liability of co-sureties bound in different sums (Section 147):

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

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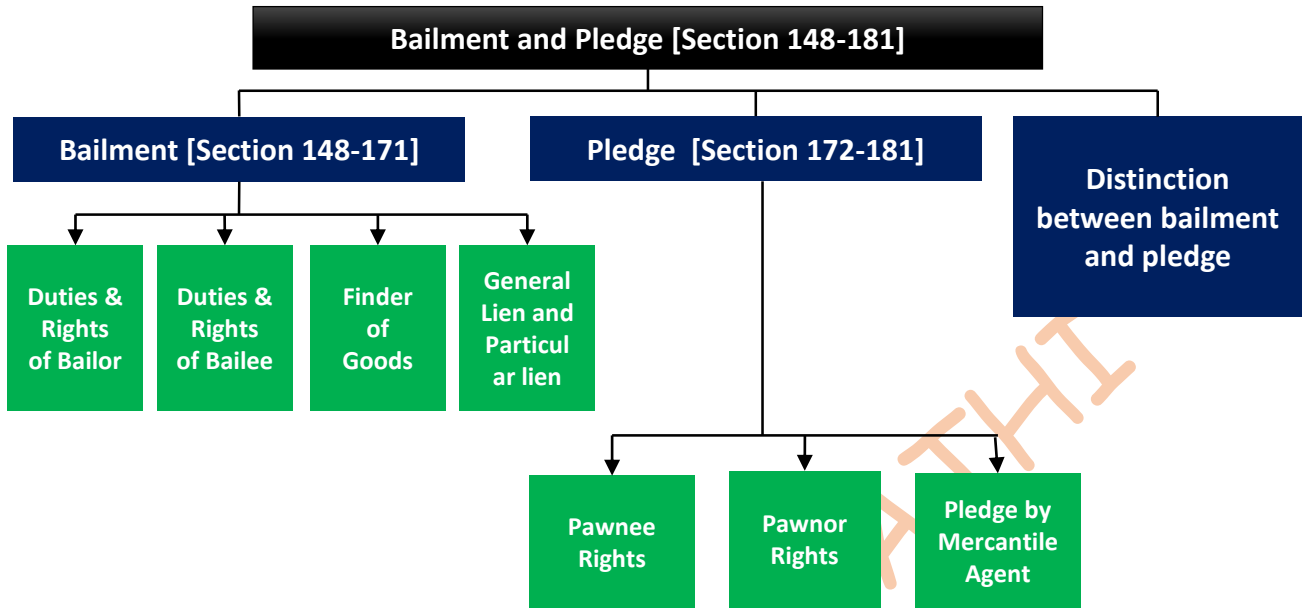


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Unit-8 : Bailment and Pledge



➤ **Question :** What is Bailment ?

➤ **Answer :**

- The word "**Bailment**" has been derived from the **French word "ballier"** which means "**to deliver**".
- Bailment etymologically means '**handing over**' or '**change of possession**'.
- As per **section 148** of the Act,
 - Bailment is the **delivery of goods** by one person to another for some purpose
 - **upon a contract**
 - that the goods shall, **when the purpose is accomplished**
 - be **returned or otherwise disposed** of according to the direction of the person delivering them.

➤ **Parties to bailment**

- Bailor** : The person delivering the goods.
- Bailee** : The person to whom the goods are delivered.

Essential Elements of a Contract of Bailment

a. Contract :

- Bailment is based upon a contract.
- The contract may be express or implied.
- **No consideration is necessary to create a valid contract of bailment.**



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b. Delivery of goods:

- It involves the delivery of goods from one person to another for some purposes.
- Bailment is only for moveable goods and never for immovable goods or money.

The delivery of the possession of goods is of the following kinds

Actual Delivery

Constructive Delivery

- When goods are physically handed over to the bailee by the bailor.
- E.g: Delivery of a car for repair to workshop.

- Where delivery is made by doing anything that has the effect of putting goods in the possession of the bailee or of any person authorized to hold them on his behalf.
- Eg: Delivery of the key of car to a workshop dealer for repair of the car.

c. Purpose :

The goods are delivered for some purpose. The purpose may be express or implied.

d. Possession :

- In bailment, possession of goods changes.
- Change of possession can happen by physical delivery or by any action which has the effect of placing the goods in the possession of bailee.
- The change of possession does not lead to change of ownership.
- In bailment bailor continues to be the owner of goods.
- Where a person is in custody without possession he does not become a bailee.

e. Return of goods :

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

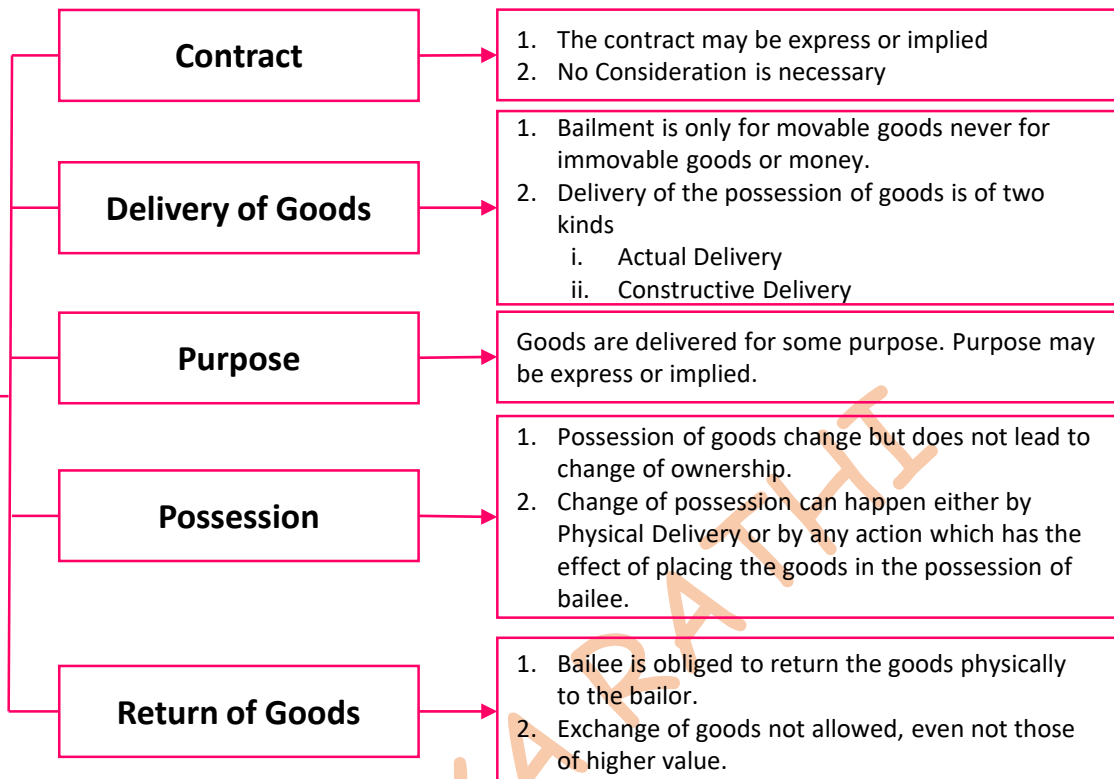


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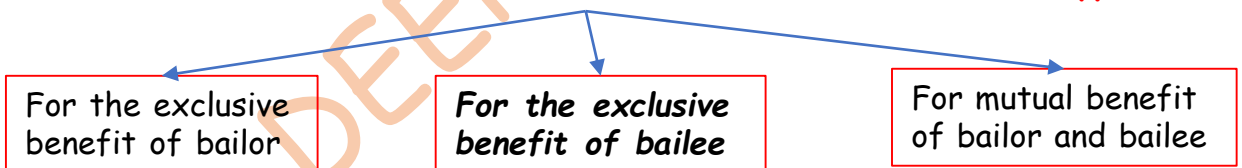
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Essentials of Bailment



Types of Bailment

1. On the basis of benefit, bailment can be classified into three types



2. On the basis of reward, bailment can be classified into two types

Gratuitous Bailment

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

Non- Gratuitous Bailment

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

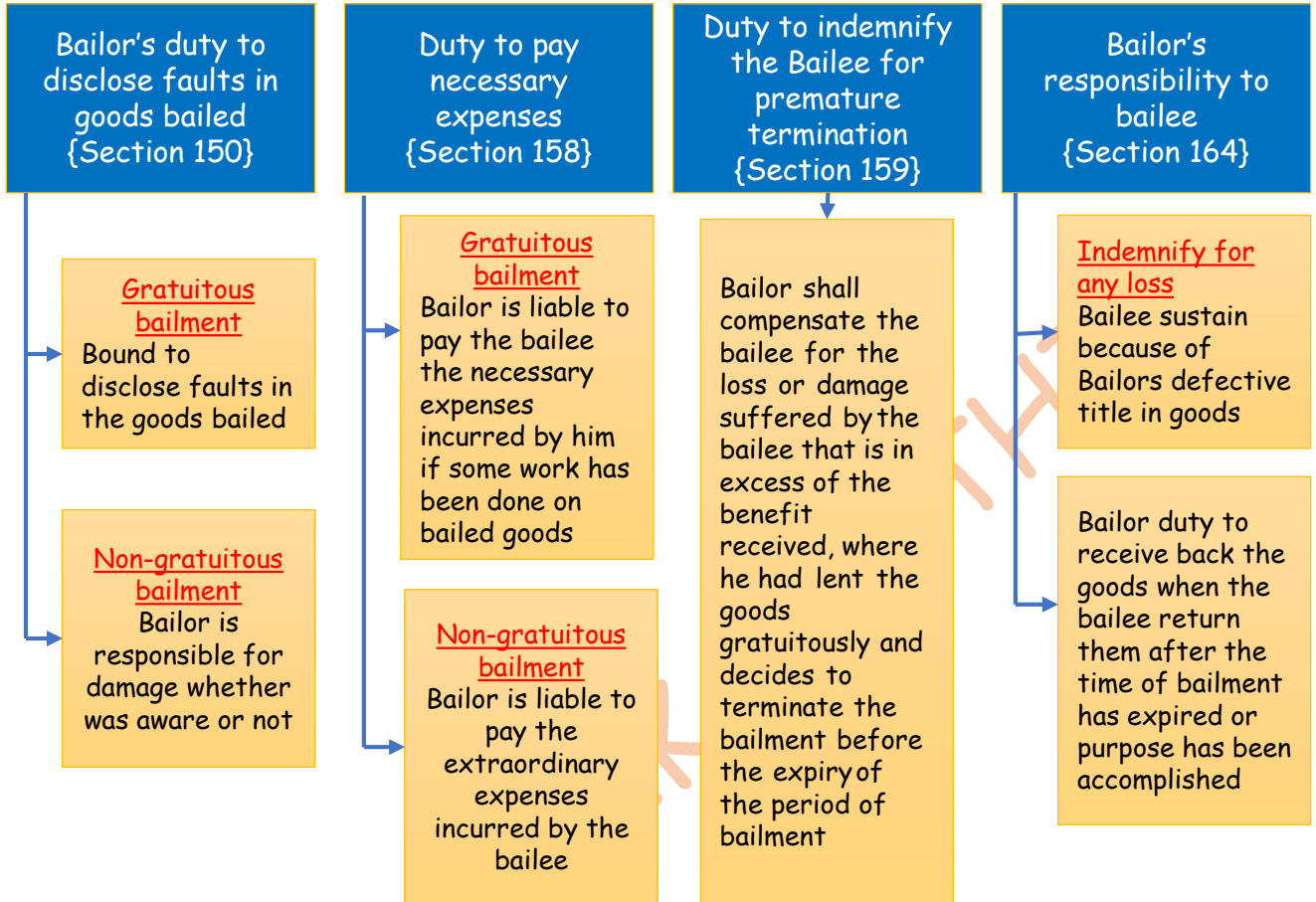


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Duties of a Bailor



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

a. In case of gratuitous bailment

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

b. In case of non-gratuitous bailment

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



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ii. Duty to pay necessary expenses [Section 158]

✓ In case of gratuitous bailment

- Where, by the conditions of the bailment, the goods are to be kept or to be carried, or to have work done upon them by the bailee for the bailor, and the bailee is to receive no remuneration (gratuitous bailment),
- **The bailor shall repay → to the bailee**
 - Necessary expenses incurred by him and
 - Any extraordinary expenses incurred by him for the purpose of the bailment.

✓ In case of non-gratuitous bailment

- The bailor is liable to pay the → **extraordinary expenses** incurred by the bailee.

iii. Duty to indemnify the Bailee for premature termination [Section 159]

- ✓ The bailor must compensate the bailee
 - for the loss or damage suffered by the bailee that is in excess of the benefit received, where he had lent the goods gratuitously and decides to terminate the bailment before the expiry of the period of bailment.

iv. Bailor's responsibility to bailee [Section 164]

The bailor is responsible to the bailee for following :

- Indemnify for any loss** which the bailee may sustain by reason that the bailor was not entitled to make the bailment, or to receive back the goods or to give directions, respecting them (**defective title in goods**).
- It is the duty of the bailor **to receive back the goods** when the bailee returns them after the time of bailment has expired or the purpose of bailment has been accomplished.

If the bailor refuses to take delivery of goods when it is offered at the proper time the bailee can claim compensation for all necessary expenses incurred for the safe custody.



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Duties of a Bailee

Take Reasonable
Care of the goods
(Section 151 & 152)

No Unauthorized
use of goods
(Section 153 & 154)

No mixing of bailor's
goods with his own
(Section 155, 156 & 154)

Return the good
(Section 160 & 161)

To Return any extra profit accruing from goods bailed
(Section 163)

Not to setup Adverse Title

i. Take reasonable care of the goods [Section 151 & 152]

- In all cases of bailment, the bailee is bound to take as much care of the goods bailed to him as a man of ordinary prudence would, under similar circumstances, take care of his own goods of the same bulk, quality and value, as the goods bailed.
- **Exception: Bailee when not liable for loss, etc., of thing bailed [Section 152]:** The bailee, in the absence of any special contract, is not responsible for the loss, destruction or deterioration of the thing bailed, if he has taken reasonable care as required under section 151.

ii. Not to make inconsistent use of goods [section 153 & 154]

- **Section 154 :** If the bailee makes any use of the goods bailed, which is not according to the terms and conditions of the bailment, he is liable to compensate the bailor for any loss or destruction of goods.
- **Section 153 :** A contract of bailment is voidable at the option of the bailor, if the bailee does not use the goods according to the terms and conditions of bailment.

iii. Not to mix the goods [Section 155, 156 & 157]

- Goods mix with consent of the bailor (Section 155) :** If the Bailee, mixes the goods bailed with his own goods, with the consent of the bailor, both the parties shall have an interest in proportion to their respective shares in the mixture thus produced.
- Goods mix without consent of the bailor & can be separated (Section 156) :** If the bailee, without the consent of the bailor, mixes the goods bailed with his own goods and the goods can be separated or divided, the property in the goods remains in the parties respectively; but the bailee is bound to bear the expense of separation or division and any damage arising from the mixture.
- Goods mix without consent of the bailor & cannot be separated (Section 157) :** If the bailee, without the consent of the bailor mixes the goods of the bailor with his own goods in such a manner that it is impossible to separate the goods bailed from the other goods and to deliver them back, the bailor is entitled to be compensated by the bailee for loss of the goods.



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iv. Return the goods [Section 160 & 161]

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

v. Return an accretion from the Goods [Section 163]

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

vi. Not to setup Adverse Title

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

Rights of a Bailor

i. Right to terminate the bailment [Section 153]

- A contract of bailment is **voidable at the option of the bailor**,
- if the **bailee does any act with regard to the goods bailed, inconsistent with the conditions of the bailment.**

ii. Right to demand back the goods [section 159]

- When the goods are lent gratuitously, the bailor can demand back the goods at any time even before the expiry of the time fixed or the achievement of the object.
- However, due to the premature return of the goods, if the bailee suffers any loss, which is more than the benefit actually obtained by him from the use of the goods bailed, the bailor has to compensate the bailee.

iii. Right to file a suit against a wrong doer [Section 180 & 181]

iv. Right to sue the bailee

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



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v. Right to compensation

- If any damage is caused to the goods bailed because of the unauthorized use of the goods or unauthorized mixing of the goods, the bailor has a right to claim compensation for the same.

Rights of a Bailee

i. Right to Deliver the Goods to any one of the joint bailors [Section 165]

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

ii. Right to indemnity [section 166]

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

iii. Right to claim compensation in case of faulty goods [Section 150]

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

iv. Right to claim necessary expenses [Section 158]

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

v. Right to Apply to court to decide the title to the goods [Section 167]

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

vi. Right to particular lien for payment of services [Section 170]

vii. Right to general lien [Section 171]



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RIGHTS OF A BAILOR AND BAILEE AGAINST ANY WRONG DOER (THIRD PARTY)

Suit by bailor & bailee against wrong doers [Section 180]

If a third person wrongfully deprives the bailee of the use or possession of the goods bailed, or does them any injury-

- The bailee is entitled to use such remedies as the owner might have used in the like case if no bailment had been made; and
- either the bailor or the bailee may bring a suit against a third person for such deprivation or injury.

Apportionment of relief or compensation obtained by such suits [Section 181]

Whatever is obtained by way of relief or compensation in any such suit shall, as between the bailor and the bailee, be dealt with according to their respective interests.

TERMINATION OF BAILMENT

Expiry of fixed period

Fulfilment of the purpose

By death of bailor or bailee

Inconsistent use of goods

Destruction/modification of the subject matter

A contract of bailment shall terminated in the following circumstances:

1. **On expiry of stipulated period** : If the goods were given for a stipulated period, the contract of bailment shall terminate → after the expiry of such period.
2. **On fulfillment of the purpose** : If the goods were delivered for a specific purpose, a bailment shall terminate → on the fulfillment of that purpose.
3. **By Notice** :

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

- A gratuitous bailment can be terminated by the bailor at any time by giving a notice to the bailee.
- However, the termination should not cause loss to the bailee in excess of the benefit derived by him.



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4. **By Death** : A gratuitous bailment terminates upon the death of either the bailor or the bailee.

5. **Destruction of the subject matter** : A bailment is terminated if

- the subject matter of the bailment is destroyed or
- there is a change in the nature of goods which makes it impossible to be used for the purpose of bailment.

Finder of Lost Goods

Right of finder of lost goods may sue for specific reward offered [Section 168]:

- The finder of goods has no right to sue the owner for compensation for trouble and expense voluntarily incurred by him to preserve the goods and to find out the owner.
- but he may retain the goods against the owner until he receives such compensation
- and, where the owner has offered a specific reward for the return of goods lost, the finder may sue for such reward, and may retain the goods until he receives it.

When finder of thing commonly on sale may sell it [Section 169]:

When a thing which is commonly the subject of sale is lost, if the owner cannot with reasonable diligence be found, or if he refuses, upon demand, to pay the lawful charges of the finder, the finder may sell it-

when the → thing is in danger of perishing or of losing the greater part of its value or

when the → lawful charges of the finder in respect of the thing found amount to two-thirds of its value

Right of Lien

Lien is the right of a person

- to retain the goods belonging to another
- until his claim is satisfied or
- some debt due to him is repaid.

Types of Lien: Lien may be of two types

Particular Lien

General Lien



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Particular Lien [Section 170]

It is a right to retain only the particular goods in respect of which the claim is due.

Section 170 provides,

- Where the bailee has, in accordance with the purpose of the bailment, **rendered any service involving the exercise of labour or skill in respect of the goods bailed.**
- He has, **in the absence of a contract to the contrary, a right to retain such goods until he receives due remuneration for the services he has rendered in respect of them.**

General Lien [Section 171]

- It is a right to retain the goods not only for demands arising out of the goods retained but for a general balance of account in favour of certain persons (in the absence of a contract to the contrary).
- Section 171 provides this right is available to Bankers, factors, wharfingers, policy brokers and attorneys of law.

Difference between Bailee's General and Particular Lien

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



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Pledge

"Pledge", "Pawnor" and "Pawnee" defined [Section 172]:

- **Meaning:** The bailment of goods as security for payment of a debt or performance of a promise is called "pledge".
- The bailor is in this case called the "pawnor". The bailee is called the "pawnee".

Section 172 to 182 of the Indian Contract Act, 1872 deal with the contract of pledge.

Essential of Contract of Pledge

Since pledge is a special kind of bailment, therefore all the essentials of bailment are also the essentials of the pledge.

There shall be a bailment for security against payment or performance of the promise,

The subject matter of pledge is goods,

Goods pledged for shall be in existence,

There shall be the delivery of goods from pledger to pledgee

Rights of a Pawnee/Pledgee

a. Right to retain the pledged goods [Section 173] :

The Pawnee may retain the goods pledged, not only for payment of the debt or the performance of the promise, but for the interest, of the debt, and all necessary expenses incurred by him in respect of the possession or for the preservation of the goods pledged.

b. Right to retention of subsequent debts [Section 174] :

- ✓ The Pawnee can retain the goods pledged for any debt or promise other than the debt or promise for which they are pledged.
- ✓ But he can exercise this right only when there is a contract to this effect. i.e. a right to retain goods for subsequent debts can be exercised only when it has been provided for in a contract to this effect.

c. Pawnee's right to extraordinary expenses incurred [Section 175] :

- ✓ The pawnee is entitled to receive from the pawnor extraordinary expenses incurred by him for the preservation of the goods pledged.
- ✓ For such expenses, however, he does not have the right to retain the goods, but he can sue the pawnor for such expenses.



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d. Pawnee's right where pawnor makes default [Section 176] :

- ✓ If the pawnor makes default in payment of the debt, or performance, at the stipulated time of the promise, in respect of which the goods were pledged, the pawnee has the following rights :
 - i. the pawnee may bring a suit against the pawnor upon the debt or promise, and retain the goods pledged as a collateral security or
 - ii. he may sell the thing pledged on giving the pawnor reasonable notice of the sale .
- ✓ If the proceeds of such sale are less than the amount due in respect of the debt or promise, the pawnor is still liable to pay the balance.
- ✓ If the proceeds of the sale are greater than the amount so due, the pawnee shall pay over the surplus to the pawnor.

Right of a Pawnor [Section 172]:

As the bailor of goods, pawnor has all the rights of the bailor. Along with that he also has the right of redemption to the pledged goods which is enumerated under section 177 of the Act.

Right to redeem [Section 177]:

- ✓ If a time is stipulated for the payment of the debt, or performance of the promise, for which the pledge is made, and the pawnor makes default in payment of the debt or performance of the promise at the stipulated time,
- ✓ he may redeem the goods pledged at any subsequent time before the actual sale of them
- ✓ But he must, in that case, pay, in addition, any expenses which have arisen from his default.

Duties of the Pawnee

- a. Duty to take reasonable care of the pledged goods.
- b. Duty not to make unauthorized use of pledged goods.
- c. Duty to return the goods when the debt has been repaid or the promise has been performed.
- d. Duty not to mix his own goods with goods pledged.
- e. Duty not to do any act which is inconsistent with the terms of the pledge.
- f. Duty to return accretion to the goods, if any.

Duties of the Pawnor

- a. The pawnor is liable to pay the debt or perform the promise as the case may be.
- b. It is the duty of the pawnor to compensate the pawnee for any extraordinary expenses incurred by him for preserving the goods pawned.
- c. It is the duty of the pawnor to disclose all the faults which may put the pawnee under extraordinary risks.



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- d. If loss occurs to the pawnee due to defect in pawnor's title to the goods, the pawnor must indemnify the pawnee.
- e. If the pawnee sells the good due to default by the pawnor, the pawnor must pay the deficit.

Pledge by Non -Owners

a. Pledge by mercantile agent [Section 178]:

- A mercantile agent, who is in the possession of goods or document of title, with the consent of owner, can pledge them while acting in the ordinary course of business as a Mercantile Agent.
- **Such Pledge shall be valid** as if were made with the authority of the owner of goods.
- Provided, Pawnee acted in good faith and had no notice that Pawnor has no authority to pledge.

b. Pledge by person in possession under voidable contract [Section 178A]:

- When the pawnor has obtained possession of the goods pledged by him under a contract voidable under section 19 or section 19A (contracts where consent has been obtained by fraud, coercion, misrepresentation, undue influence),
- but the contract has not been rescinded at the time of the pledge, the pawnee acquires a good title to the goods, provided he acts in good faith and without notice of the pawnor's defect of title.

c. Pledge where Pawnor has only a limited interest [Section 179]:

Where a person pledges goods in which he has only a limited interest i.e. pawnor is not the absolute owner of goods, the pledge is valid to the extent of that interest.

d. Pledge where Pawnor has only a limited interest:

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

e. Pledge by seller or buyer in possession:

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



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DISTINCTION BETWEEN BAILMENT AND PLEDGE

Basis of Distinction	Bailment	Pledge
Meaning	Transfer of goods by one person to another for some specific purpose is known as bailment.	Transfer of goods from one person to another as security for repayment of debt is known as the pledge.
Terms Applicable	<ul style="list-style-type: none">The person delivering the Goods under a contract of bailment is called as "Bailor"The person to whom the goods are delivered under a contract of bailment is called as "Bailee"	<ul style="list-style-type: none">The person who delivers the good as security is called the "Pawnor".The person to whom the goods are delivered as security is called the "pawnee"
Purpose	Bailment may be made for any purpose (as specified in the contract of bailment, eg: for safe custody, for repairs, for processing of goods).	Pledge is made for the purpose of delivering the goods as security for payment of a debt, or performance of a promise.
Consideration	The bailment may be made for consideration or without consideration.	Pledge is always made for a consideration.
Right to sell the goods	<ul style="list-style-type: none">The bailee has no right to sell the goods even if the charges of bailment are not paid to him.The bailee's rights are limited to suing the bailor for his dues or to exercise lien on the goods bailed.	The pawnee has right to sell the goods if the pawnor fails to redeem the goods.
Right to use of goods	Bailee can use the goods only for a purpose specified in the contract of bailment and not otherwise.	Pledgee or Pawnee cannot use the goods pledged.

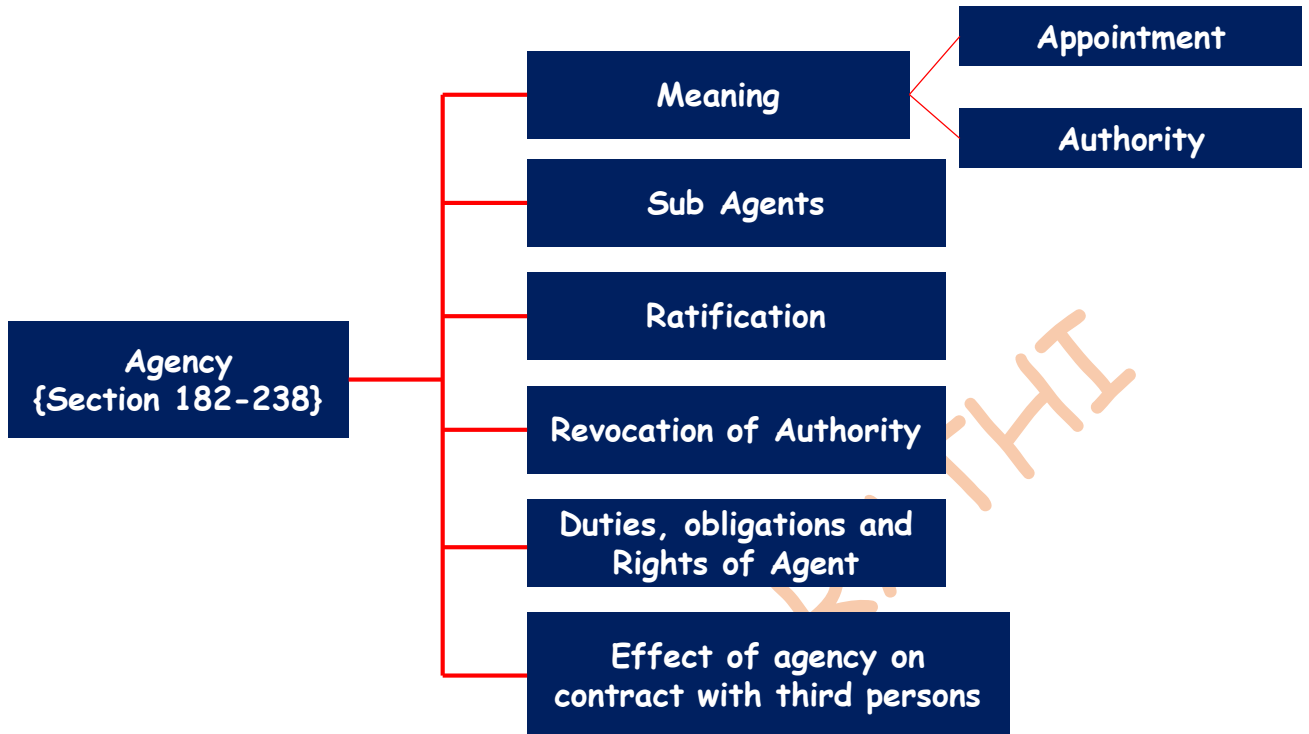


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Unit -9 : Agency



What is Agency ?

➤ **Question** : What is Agency ?

➤ **Answer** :

- ✓ The Indian Contract Act, 1872 does not define the word '**Agency**'.
- ✓ However, section 182 of the Indian Contract Act, 1872 defines Agent and Principal as :
 - **Agent**: means a person employed to do any act for another or to represent another in dealing with the third persons **and**
 - **The principal**: means a person for whom such act is done or who is so represented.

➤ **Test of Agency**

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

Question (b) : Whether he can establish privity of contract between the principal and third parties ?

Answer : If the answer to these questions is in affirmative (Yes), then there is a relationship of agency.

❖ '**Agency**' is a comprehensive word used to describe the relationship between one person and another, where the first mentioned person brings the second mentioned person into legal relation with others.



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- ❖ Thus, 'Agency' is a comprehensive word used to describe the relationship between one person and another,
 - where the first mentioned person brings the
 - second mentioned person into legal relation with others.
- ❖ The Rule of Agency is based on the maxim "*Qui facit per alium, facit per se*" i.e., **he who acts through an agent is himself acting.**

Appointment and Authority of Agents

Who may employ an agent ? [Section 183]

- A person who has attained majority according to the law (+18).
- Has sound mind.

Who may be an agent ? [Section 184]

- A person who has attained majority according to the law (+18) [to be responsible to his principal]
- Has sound mind.

Whether the consideration is necessary?

- ✓ As per Section 185
 - No consideration is necessary to create an agency?
 - Acceptance of the office of an agent is sufficient consideration.

Creation of Agency

In the words of Desai J, of the Supreme Court of India : → "The relation of agency arises whenever one person called the agent has the authority to act on behalf of another called the principal and consents to act. The relationship has genesis in a contract"

The relationship of the principal and the agent may be created in any of the following ways

The authority may be express or implied [Section 186]

Definitions of express and implied authority [Section 187]

1. Express Authority

An authority is said to be express when it is given by words, spoken or written.

2. Implied Authority

It is to be inferred from

- The circumstances of the case
- Things spoken or written
- Or in the ordinary course of dealing.



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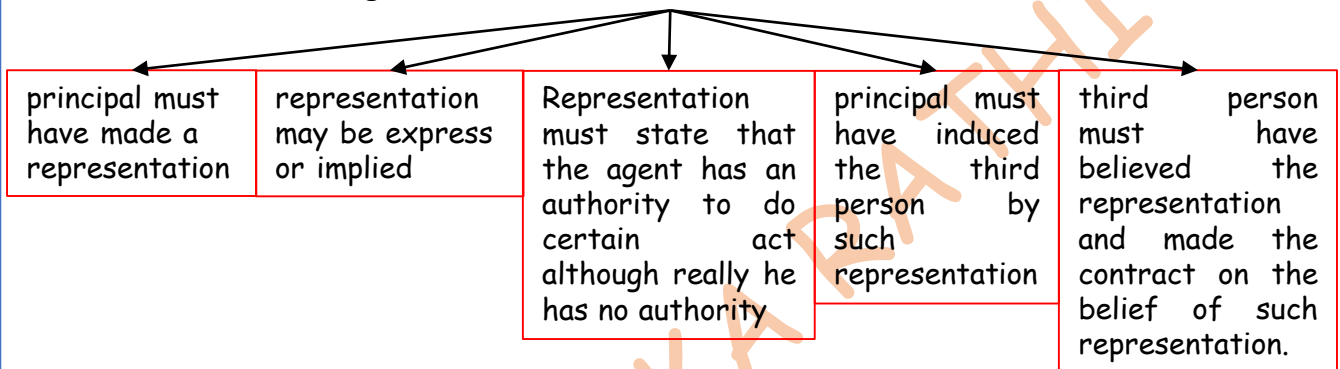
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Implied Agency includes

(a) Agency by Estoppel [Section 237]

Where the principal by his conduct or statement willfully induces another person to believe that a certain person is his agent, he is subsequently prevented or estopped from denying the fact of agency.

According to section 237 of the Contract Act, an agency by estoppel may be created when following essentials are fulfilled:



(b) Agency by Necessity

- An agency of necessity arises due to some emergent circumstances.
- where an agent is authorized to do certain act, and while doing such an act, an emergency arises, he acquires an extra-ordinary or special authority to prevent his principal from loss

3. Agency by Operation of Law

- When law treats one person as an agent of other.
- **For example** :-> A partner is the agent of the firm for the purposes of the business of the firm.

4. Rights of person as to acts done for him without his authority, Effect of ratification [Section 196]

- 'Ratification " means approving a previous act or transaction.
- Where acts are done by one person on behalf of another, but without his knowledge or authority he may elect to ratify it.
- This will make the agency valid.



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Essential of Valid Ratification

- a. **Ratification may be expressed or Implied [Section 197]:**
 - Ratification may be expressed or may be implied in the conduct of the person on whose behalf the acts are done.
- b. **Knowledge requisite for valid ratification [Section 198]:**
 - No valid ratification can be made by a person whose knowledge of the facts of the case is materially defective.
- c. **The whole transaction must be ratified [Section 199]:**
 - There can be ratification of an act in entirety or its rejection in entirety.
 - The principal cannot ratify a part of the transaction which is beneficial to him and reject the rest.
- d. **Ratification cannot injure third person [Section 200]:**
 - When the interest of third parties is affected, the principle of ratification does not apply.
 - Ratification cannot relate back to the date of contract if third party has in the intervening time acquired rights.
- e. **Ratification within reasonable time:**
 - Ratification must be made within a reasonable period of time.
- f. **Communication of Ratification:**
 - Ratification must be communicated to the other party.
- g. **Act to be ratified must be valid:**
 - Act to be ratified should not be void or illegal, for
 - e.g. payment of dividend out of capital, forgery of signatures, any other criminal offence, or anything which is not permitted under law

Extent of Agent's Authority

(A) Under Normal Circumstances (Section 188)

To do an act has authority to do every lawful thing which is necessary in order to do such act

To carry on a business has authority to do every lawful thing necessary for the purpose, or usually done in the course, of conducting such business.



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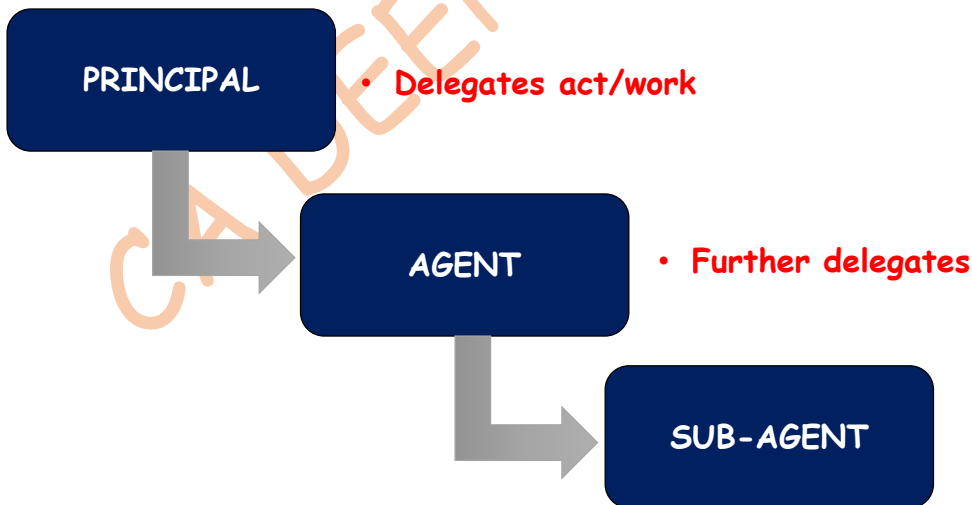


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(B) In Emergency (Section 189)

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

Sub-Agents



- **When agent cannot delegate [Section 190]** : An agent cannot lawfully employ another to perform acts which he has expressly or impliedly undertaken to perform personally, unless by the ordinary custom of trade a sub-agent may, or from the nature of the agency, a sub-agent must, be employed.



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- **"Sub-agent" defined [Section 191]** : A **"Sub-agent"** is a person employed by, and acting under the control of, the original agent in the business of the agency.

- The appointment of sub agent is not lawful, because the agent is a delegatee and a delegatee cannot further delegate.
- This is based on the Latin principle "**delegatus non potest delegare**".
- A contract of agency is of a fiduciary character.
- It is based on the confidence reposed by the principal in the agent and that is why a delegatee cannot further delegate.

Exception where an agent can appoint Sub-agent

The appointment of a sub agent would be valid if the terms of appointment originally contemplated it.

- Sometimes **customs of the trade** may provide for appointment of sub agents
- *In both these cases the sub agent would be treated as the agent of the principal.*

Where in the course of the agent's employment, **unforeseen emergency** arise making it necessary for him to delegate the authority that was given to him by the principal

Representation of principal by sub-agent properly appointed [Section 192]

Where a sub-agent is properly appointed

Principal is liable to third parties for the acts of the sub-agent

Agents responsibility for sub agents:

The agent is responsible to the principal for the acts of the sub-agent.

Sub-agents liability to principal:

The sub-agent is responsible for his acts to the agent, but not to the principal, except in case of fraud or willful wrong.



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Agent's responsibility for sub-agent appointed without authority [Section 193]

Where an agent, without having authority to do so, has appointed a person to act as a sub-agent

Agent is responsible for his acts both to the principal and to third persons

Principal is responsible for the acts of the sub agent

- Sub agent is not responsible to the principal at all.
- He is answerable only to the agent.

Substituted Agent

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

Relation between principal and person duly appointed by agent to act in business of agency [Section 194]:

Where an agent, holding an express or implied authority to name another person to act for the principal in the business of the agency, has named another person accordingly, such person is not a sub-agent, but an agent of the principal for such part of the business of the agency as is entrusted to him.

Agent's duty in naming such person [Section 195] :

- In selecting such agent for his principal, an agent is bound to exercise the same amount of discretion as a man of ordinary prudence would exercise in his own case **and**
- if he does this, he is not responsible to the principal for the acts or negligence of the agent so selected.



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DIFFERENCE BETWEEN A SUB-AGENT AND SUBSTITUED AGENT

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

DUTIES AND OBLIGATIONS OF AN AGENT

Duty to execute mandate

- Agent should perform the work which he has been appointed to do.
- Otherwise he shall be liable to compensate the principal.

Duty to follow instructions or customs (Section 211)

- Agent must conduct business as per the instructions of the principal.
- In absence of instructions, he must follow general customs of business.
- Otherwise, loss sustained/ undue profits made must be compensated back by agent to principal.

Duty to Reasonable care and skill (Section 212)

- Duty to reasonable care and skill to be used in exercising all his duties.
- Moreover, he is liable to compensate the principal for his negligence/misconduct



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**Agent duty to
communicate with
principal (Section 214)**

- Agent duty to communicate with principal and seeking his instructions in case of any difficulty in execution of his duties.

**Duty to Avoid Conflict of
Interest (Section 215)**

- a. Right of Principal when agent deals, on his own account, in business of agency without principals consent (Section 215)
The Principal may cancel the transaction if :
 - i. Material fact has been dishonestly concealed from him or
 - ii. Dealing have been disadvantageous to him.
- b. Principal's right to benefit gained by agent dealing on his account in business of agency (Section 216)
 - The principal is entitled to claim any benefit resulting from the transaction from the agent.

**Duty not to make secret
profits**

- An agent not to make any secret profit in the business of agency.
- His relationship with the principal is of fiduciary nature and this requires absolute good faith in the conduct of agency.

**Duty to render proper
accounts (Section 213)**

- Accounts supported with vouchers must be submitted whenever demanded by principal.

**Duty not to Delegate
(Section 190)**

- Acts which he is personally responsible to fulfil unless its required in ordinary course of trade.

**Agent's Duty to pay
sums received for
principal (Section 218)**

- Subject to such deductions, the agent is bound to pay to his principal all sums received on his account.

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



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RIGHT OF AN AGENT

Right of retain out of
sums received on
principal's account
(Section 217)

- a. All moneys due to himself
- b. Expenses properly incurred by him in conducting such business
- c. Remuneration

Right to remuneration
(Section 219)

- Remuneration may be as per contract or as per usual customary in business.
- **Section 120** : However an agent who is guilty of misconduct in the business of the agency is not entitled to any remuneration in respect of that part of the business which he has misconducted.

In the absence of any contract to the contrary an agent is entitled

- Retain the goods, papers and other property, whether movable or immovable of the principal.
- Until the amount due to himself for commission, disbursement and services in respect of the same has been paid or accounted for him.

Agent's lien on principal's
property
(Section 221)

Conditions :

- ✓ Agent should be lawfully entitled to receive remuneration /commission from the principal
- ✓ Property belongs to the principal
- ✓ Property has been received by the agent in his capacity and during the course of his ordinary duties as agent.
- ✓ Agent has only a particular/ specific lien.

The agent's right to lien is lost in the following cases:

- ✓ Possession of the property is lost.
- ✓ Agent waives his right expressly or impliedly.
- ✓ Contract does not allow lien.



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Right to indemnity

a. Right of indemnification for lawful acts (Section 222) :

Loss caused even after lawfully execution of authority shall be indemnified by principal

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

- Losses/ damages caused even though agent acted in good faith shall be indemnified by principal.
- Reimbursement cannot be claimed where the agent has contravened any laws and penalty is levied.

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

- Principal must make compensation to his agent any loss/damage caused to him due to principal's neglect or want of skill.

Right to compensation for injury caused by principal's neglect (Section 225)

- Principal must make compensation to his agent any loss/ damage caused to him due to principal's neglect or want of skill.

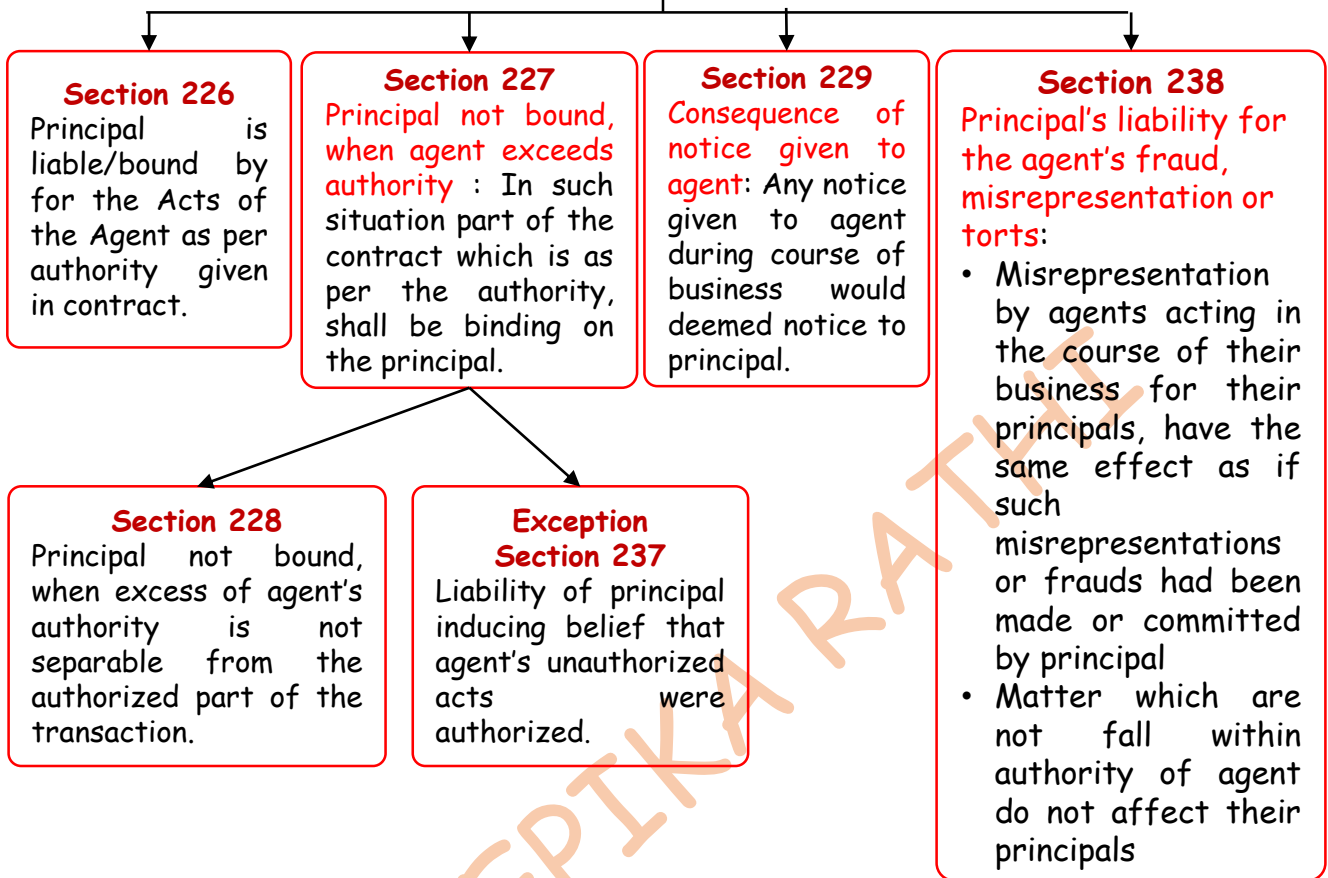


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Principal's Liability to Third Parties

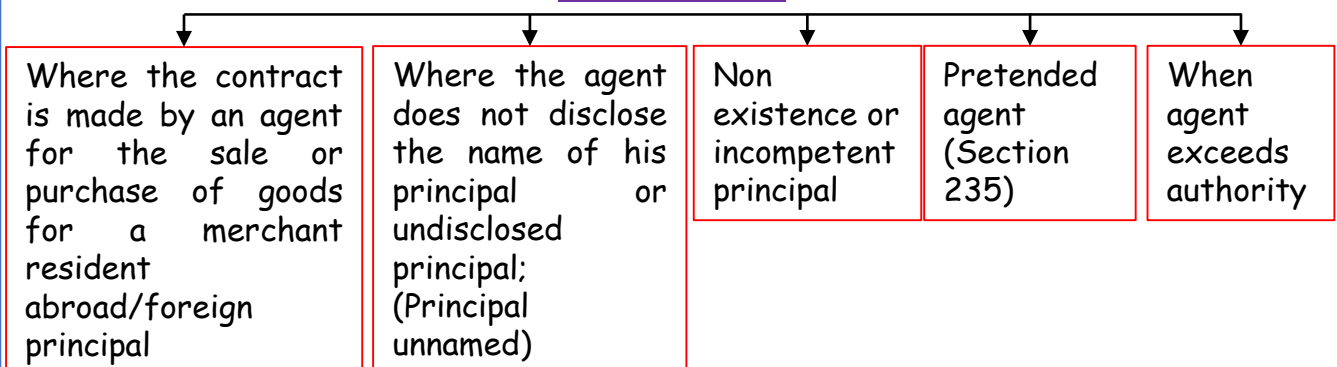


PERSONAL LIABILITY OF AGENT TO THIRD PARTIES

➤ **Agent cannot personally enforce nor be bound by, contract on behalf of principal [Section 230] :**

- In the absence of any contract to that effect, an agent cannot personally enforce contracts entered into by him on behalf of his principal, nor is he personally bound by them.
- He can neither sue nor be sued on contracts made by him on his principal's behalf.

Exceptions





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Agent cannot personally enforce, nor be bound by, contracts on behalf of principal (Section 230) : Agent can neither sue nor be sued on contracts made by him on his principal's behalf.

RIGHTS OF THIRD PARTIES

(i) Rights of parties to a contract made by undisclosed agent [Section 231]

- If an agent makes a contract with a person who neither knows, nor has reason to suspect, that he is an agent, his principal may require the performance of the contract; but the other contracting party has, as against the principal, the same right as he would have had as against the agent if the agent had been the principal.
- If the principal discloses himself before the contract is completed, the other contracting party may refuse to fulfill the contract, if he can show that, if he had known who was the principal in the contract, or if he had known that the agent was not a principal, he would not have entered into the contract.

(ii) Rights of parties to a contract made by undisclosed agent [Section 231]

- Where one man makes a contract with another, neither knowing nor having reasonable ground to suspect that the other is an agent, the principal,
- If he requires the performance of the contract, can only obtain such performance subject to the rights and obligations subsisting between the agent and the other party to the contract.

(iii) Option to Third Person -Sue the Agent or the Principal

a. Right of person dealing with agent personally liable [Section 233]:

In cases where the agent is personally liable, a person dealing with him may hold either him or his principal, or both of them, liable.

b. Consequence of inducing agent or principal to act on belief that principal or agent will be held exclusively liable [Section 234]:

- When a person who has made a contract with an agent induces the agent to act upon the belief that the principal only will be held liable or
- induces the principal to act upon the belief that the agent only will be held liable, he cannot afterwards hold liable the agent or principal respectively.



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REVOCATION OF AUTHORITY

Termination of Agency [Section 201]

Revocation

Renunciation
by agents

Completion of
business

Death of Principal or
the agent

Principal or agent
becoming of unsound mind

Insolvency of
principal

Expiry of time

i. Revocation

- **Section 203** : Principal may revoke the authority given to his agent at any time before the authority has been exercised so as to bind the principal .
- **Section 204** : However, the principal cannot revoke the authority given to his agent after the authority has been partly exercised so far as regards such acts and obligations as arise for acts already done in the agency.
- **Compensation for revocation by principal [Section 205]** : If there is premature revocation of agency without sufficient cause, the principal must compensate the agent, for such revocation.
- **Notice of revocation [Section 206]**: When the principal, having justification to do so, revokes the authority, he must give reasonable notice of such revocation to the agent, otherwise, he can be liable to pay compensation for any damage caused to the agent.
- **Revocation and renunciation may be expressed or implied [Section 207]**: Revocation of agency may be expressed or implied in the conduct of the principal.

ii. Renunciation by Agent [Section 206]

- An agent may renounce the business of agency in the same manner in which the principal has the right of revocation.
- **Section 205** : If the agency is for a fixed period, the agent would have to **compensate the principal** for any premature renunciation without sufficient cause.
- **Section 206** : A **reasonable notice of renunciation is necessary**. Length of notice is to be determined by the same principles which apply to revocation by the principal. If the agent renounces without proper notice, he shall have to make good any damage thereby resulting to the principal.



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iii. Completion of Business

- An agency is automatically and by operation of law terminated when its business is completed.
- Thus, for example, the authority of an agent appointed to sell goods ceases to be exercisable when the sale is completed.

iv. Death or Insanity

- An agency is determined automatically on the death or insanity of the principal or the agent. Winding up of a company or dissolution of partnership has the same effect.
- Act done by agent before death would remain binding.

v. Principal's Insolvency

An agency ends on the principal being adjudicated insolvent.

vi. On Expiry of Time

- Where an agent has been appointed for a fixed term, the expiration of the term puts an end to the agency, whether the purpose of agency has been accomplished or not.
- An agency comes to an automatic end on expiry of its term

When the Agency is Irrevocable ?

When the agent is personally interested in the subject matter of agency the agency becomes irrevocable.

Section 202 states that "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."

Effect of Termination [Section 208]

[When termination of agent's authority takes effect as to agent, and as to third persons Section 208]:

The termination of the authority of an agent does not, so far as regards the agent, take effect before it becomes known to him, or, so far as regards third persons, before it becomes known to them.



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Agent's duty on termination of agency by principal's death or insanity [Section 209]

When an agency is terminated by the principal dying or becoming of unsound mind, **the agent is bound to take, on behalf of the representatives of his late principal**, all reasonable steps for the protection and preservation of the interests entrusted to him.

Termination of sub-agent's authority [Section 210]

The termination of the authority of an agent causes the termination (subject to the rules herein contained regarding the termination of an agent's authority) of the authority of all sub-agents appointed by him.

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Chapter 3: The Sale of Goods Act, 1930



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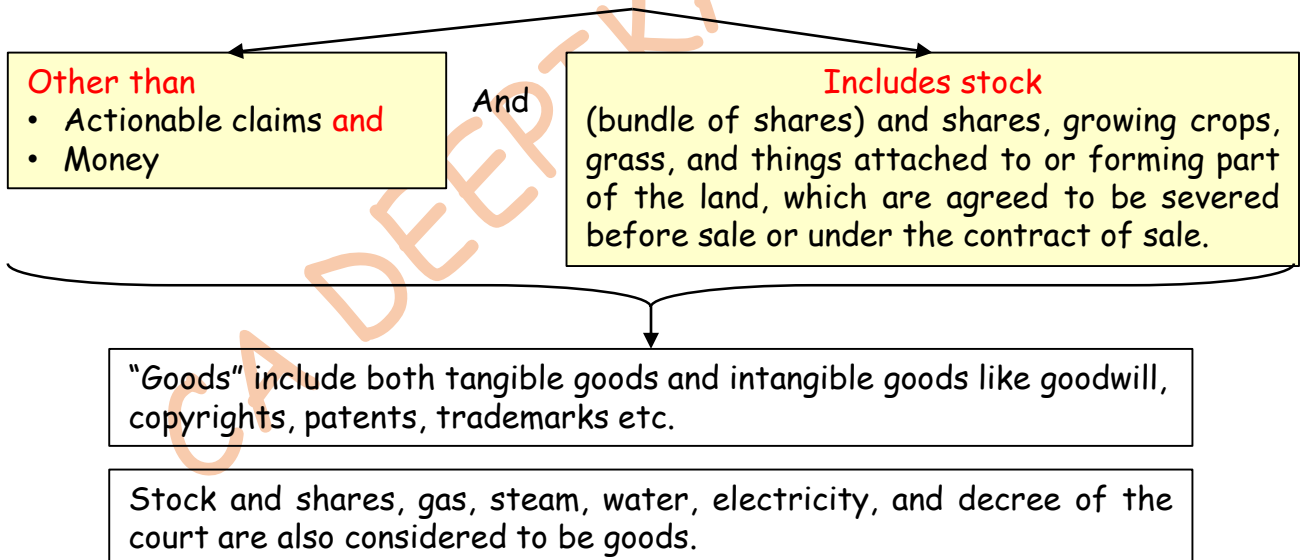
Unit -1 : Formation of Contract of Sale

Scope of the Act

- Sale of Goods Act, 1930 is an Act to define and amend the law relating to the sale of goods.
- It extends to the whole of India.
- It came into force on 1st July, 1930.
- Applicable to the contracts those Goods which are Movable Properties, not to Immovable Properties.

Definitions

- Buyer [Section 2(1)] : means a person who buys or agrees to buy goods .(Not only the person who buys but also the one who agrees to buy is a buyer).
- Seller [Section 2(13)] : means a person who sells or agrees to sell goods.(Not only a person who sells but also a person who agrees to sell).
- Goods [Section 2(7)] : "Goods" means every kind of movable property



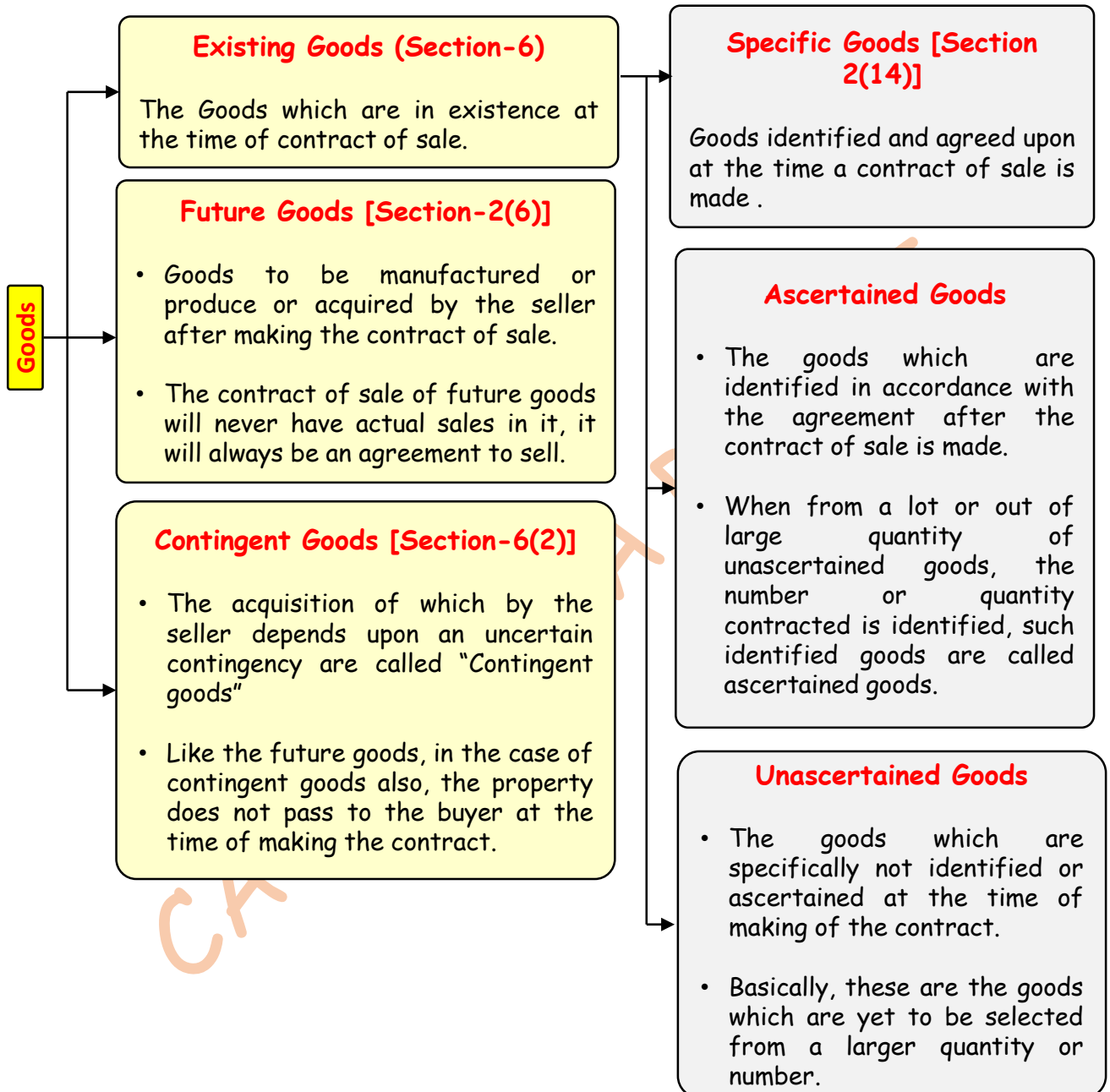


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Classification of Goods





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Delivery - Its Forms and Derivatives

Delivery [Section 2(2)]

- Delivery means voluntary transfer of possession from one person to another.
- The transfer of possession is the end result of the whole delivery process.
- The delivery could occur even when the goods are transferred to a person other than the buyer but who is authorized to hold goods on behalf of the buyer.

Deliverable state [Section 2(3)]

- Goods are said to be in deliverable state when they are in such a condition that the buyer would under a contract be bound to take delivery of them

Actual Delivery

- If the goods are physically given into the possession of the buyer, the delivery is actual delivery.

Constructive Delivery

- The transfer of goods can be done even when the transfer is effected without change in possession or custody of goods.
- A case of the delivery by attornment or acknowledgment will be a constructive delivery.
- If you pick up a parcel on behalf of your friend and agree to hold on to it for him, it is a constructive delivery.

Symbolic Delivery

- This kind of delivery involves the delivery of a thing in token of a transfer of some other thing.
- For instance, keys of a car, godown etc.



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Document of title of goods [Section 2(4)]

- It is a document used as a proof of the possession or control of goods.
- A document amounts to a document of title only where it shows an unconditional undertaking to deliver the goods to the holder of document.

Includes :

- bill of lading, dock-warrant, warehouse keeper's certificate, railway receipt, multimodal transport document, warrant or order for the delivery of goods and any other document.
- used in the ordinary course of business as proof of the possession or control of goods or authorizing or purporting to authorize, either by endorsement or by delivery, the possessor of the document to transfer or receive goods thereby represented."

Is Document to title and Document showing title same ?

- There is difference between 'Document Showing title ' and 'Document of Title'
- A document showing title merely shows that the person named in the document is its owner.
- It does not allow the person to transfer the ownership by mere endorsement of the document.

Mercantile Agent [Section 2(9)]

An agent who in the customary course of business has, as such agent, authority either to sell goods or to consign goods for the purpose of sale or to buy goods or to raise money on the security of the goods.

Property [Section 2(11)]

- ❖ 'Property' here means 'ownership' or general property.
- ❖ The property in the goods means the general property i.e., all ownership rights of the goods, and not just a special property

Insolvent [Section 2(8)]

A person is said to be insolvent when he ceases to pay his debts in the ordinary course of business, or cannot pay his debts as they become due, whether he has committed an act of insolvency or not.



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Price [Section 2(10)]

Price means the money consideration for a sale of goods.

Quality of goods [Section 2(12)]

Quality of goods includes their state or condition

SALE AND AGREEMENT TO SALE (SECTION-4)

Section 4(1)	<ul style="list-style-type: none">• "A contract of sale of goods is a contract whereby the seller transfers or agrees to transfer the property in goods to the buyer for a price".• There may be a contract of sale between one part-owner and another.
Section 4(2)	<ul style="list-style-type: none">• A contract of sale may be absolute or conditional.
Section 4(3) [PYQ MAY 2022]	<ul style="list-style-type: none">• Where under a contract of sale, the property in the goods is transferred from the seller to the buyer, the contract is called a sale.• Where the transfer of the property in the goods is to take place at a future time or subject to some condition thereafter to be fulfilled, it is called an agreement to sell.
Section 4(4)	<ul style="list-style-type: none">• An agreement to sell becomes a sale when the time elapses or the conditions are fulfilled subject to which the property in the goods is to be transferred.

Contract of sales

Sale

- ✓ There is immediate transfer of property from the seller to the buyer.
- ✓ Generally carried out on deliverable goods.

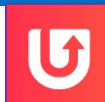
OR

Agreement to Sell

- ✓ The property in goods is not transferred immediately.
- ✓ The objective of the agreement is to **transfer the goods at a future date**, once some contingent clauses in the agreement or certain conditions are satisfied.
- ✓ Agreement to sell becomes a sale when the time elapses or the conditions are fulfilled subject to which the property in the goods is to be transferred.



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When agreement to sell becomes sale:

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

Elements must co-exist to constitute a contract of sale of goods

- 1 At least **two** parties. One shall be the seller and the other a buyer.
- 2 The **subject matter must be goods** (i.e) only **movable goods**. This "movable property" may constitute existing goods, goods in the possession or the ownership of the seller or future goods
- 3 A price in **money** should be paid or promised. The price consideration or the actual payment could be partly in kind and partly in money but **never in kind alone**.
- 4 A **transfer of property** in goods from seller to the buyer must take place.
- 5 A contract of sale may be **absolute or conditional**.
- 6 All other **essential elements of a valid contract** must be present in the contract of sale. The crucial elements of a contract like competency of parties, the legality of object and consideration etc. have to be present like in any other contract.

CONTRACT OF SALE HOW MADE (Section 5)

- ❖ **Section 5(1)** : A contract of sale is made by an offer to buy or sell goods for a price and the acceptance of such offer
- ❖ Modes of Delivery & Payment in Contract of Sale -
 - i. Immediate delivery of goods
 - ii. Immediate payment of price and delivery at future date
 - iii. Immediate delivery and immediate payment
 - iv. Delivery and payment both in instalments
 - v. Delivery or payment or both made at a future date

EXISTING & FUTURE GOODS (Section 6)

1. **Existing or Future goods** : The goods which form the subject matter of a contract of sale may be either existing goods that are acquired, owned or possessed by the seller, or future goods



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2. **Contingent Goods** : There may be a contract for the sale of goods the acquisition of which by the seller depends upon a contingency which may or may not happen.
3. **Agreement to Sell** : Where in a contract of sale the seller purports to affect a present sale of future goods, the contract operates as an agreement to sell the goods.

Goods perishing before making of contract (Section 7)

Where there is a contract for the sale of specific goods, if the goods without the knowledge of the seller have, at the time when the contract was made, perished or become so damaged as no longer to answer to their description contract -

The contract is void.

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

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

Agreement is thereby avoided or becomes void.

Perishing of future goods

If the future goods are specific, the destruction of such goods will amount to supervening impossibility and the contract shall become → Void.

ASCERTAINMENT OF PRICE (SECTION 9 & 10)

Ascertainment of Price [Section 9]

The price in the contract of sale may be-

- Fixed by the contract, or
- Agreed to be fixed in a manner provided by the contract
- Determined by the course of dealings between the parties.

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



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Agreement to Sell at Valuation [Section 10]

Section 10 provides for the determination of price by a third party.

Where there is an agreement to sell goods on the terms that price has to be fixed by the third party and he either does not or cannot make such valuation,

Agreement will be void.

In case the third party is prevented by the default of either party from fixing the price,

The party at fault will be liable to the damages to the other party who is not at fault.

A buyer who has received and appropriated the goods must pay a reasonable price for them in any eventuality.

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Unit -2 : Conditions & Warranties

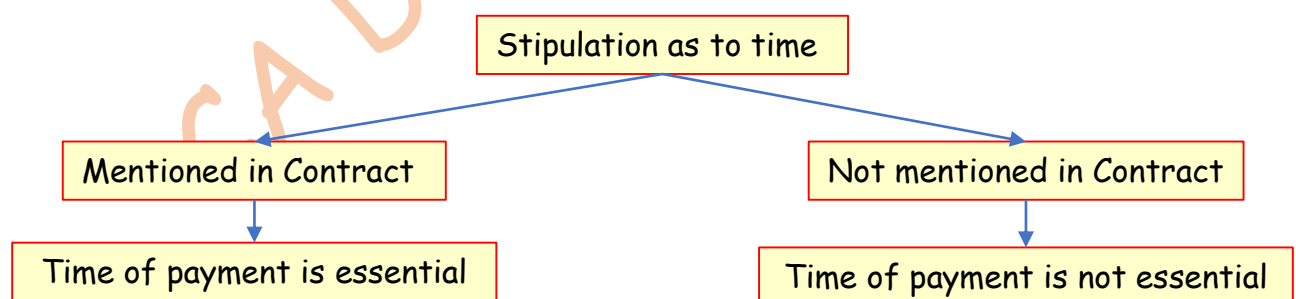
STIPULATION AS TO TIME [Section-11]

- ❖ As regard to time for the payment of price, unless a different intention appears from the terms of contract, stipulation as regard this, is not deemed to be of the essence of a contract of sale.
- ❖ But delivery of goods must be made without delay. Whether or not such a stipulation is of the essence of a contract depends on the terms agreed upon.
- ❖ Whether or not such a stipulation is of the essence of a contract depends on the terms agreed upon.
- ❖ Price for goods may be fixed by the contract or may be agreed to be fixed later on in a specific manner. Stipulation as to time of delivery are usually the essence of the contract.

Summary

Stipulation as to Time

Time for Payment of price	Time of Delivery	Any other stipulation as to Time
Not the essence of a contract of sale, unless mentioned in the Contract	Essence of a contract of sale	Essence or not depends on the terms of the contract



Condition and Warranty [Section-12]

1. A stipulation in a contract of sale with reference to goods which are the subject thereof may be a Condition or a Warranty.
2. A Condition is a stipulation essential to the main purpose of the contract, the breach of which gives rise to a right to treat the contract as repudiate.



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3. A Warranty is a stipulation collateral to the main purpose of the contract, the breach of which gives rise to a claim for damages but not to a right to reject the goods and treat the contract as repudiated.
4. Whether a stipulation in a contract of sale is a condition or a warranty depends in each case on the construction of the contract. A stipulation may be a condition, though called a warranty in the contract.

Stipulation

**Very essential / significant to the
Contract of Sale**

Condition

**Less essential / less significant to
the Contract of Sale**

Warranty

Difference between conditions and warranties:

S.No.	Condition	Warranty
1	Essential to main purpose	Collateral to main purpose
2	Aggrieved party can repudiate the contract and claim damages	Aggrieved party can claim only damages
3	A breach of condition may be treated as a breach of warranty	A breach of warranty cannot be treated as a breach of condition.

WHEN CONDITION TO BE TREATED AS WARRANTY (SECTION -13)

**Voluntary Waiver of a condition
[Section 13(1)] :**

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

**Compulsory waiver of a condition
[Section 13(2)] :**

- Where a contract of sale is not severable and the buyer has accepted the goods or part thereof,
 - ✓ The breach of any condition to be fulfilled by the seller can only be treated as a breach of warranty and
 - ✓ Not as a ground for rejecting the goods and treating the contract as repudiated, unless there is a term of the contract, express or implied, to that effect.



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

'Conditions' and 'Warranties' may be either express or implied.

Express Conditions

Agreed upon between the parties at the time of contract and are expressly provided in the contract.

Implied Conditions

Those which are presumed by law to be present in the contract. Implied conditions are incorporated by law in the contract of sale.

↓
Conditions which are implied in a contract of sale of goods unless the circumstances of the contract show a different intention.

Condition as to title [Section 14(a)]

In every contract of sale, the condition implied is that the seller has the right to sell the goods at the time when the property is to pass. i.e.,

In case of a sale, he has a right to sell the goods

And

In the case of an agreement to sell, he will have the right to sell the goods at the time when the property is to pass.

If Seller's title is defective - Then, buyer must return the goods to the true owner and recover the price from the seller.

Sale by description [Section 15]

- ❖ **Principle** : "if you contract to sell peas, you cannot compel the buyer to take beans."
- ❖ If there is a contract of sale of goods by description, a default implied condition is that these goods must correspond with this description.
- ❖ Description usually means the specifications / representations of product.
- ❖ The buyer is not bound to accept and pay for the goods which are not in accordance with the description of goods.
- ❖ The buyer is entitled to reject the goods whether the buyer is able to inspect them or not.



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The Act does not define 'description'. It could be

Where the class or kind to which the goods belong has been specified, e.g., 'Egyptian cotton', "java sugar", etc.,

and

Where the goods have been described by certain characteristics essential to their identification, e.g., jute bales of specified shipment, steel of specific dimension, etc.

- ❖ In these cases, description assumes the form of a statement or representation regarding the identity of particular goods by reference to the place of origin or mode of packing, etc.
- ❖ Whether or not such a statement or representation is essential depends, in each case, on the construction of the contract.

Sale by sample [Section 17]

When the goods are to be supplied on the basis of a sample the following conditions are implied:

The bulk supplied shall match with the sample in quality.

The buyer shall have a reasonable opportunity of comparing the bulk with the sample I.e. inspect the final goods.

The goods shall be free from any latent defect i.e. a hidden defect.

In case of latent defects, the buyer has the remedy of

Reject the goods

Recover the price

Claim damages

Sale by sample as well as by description [Section 15]

Where the goods are sold by sample as well as by description the implied condition is that the bulk of the goods supplied shall correspond both with the sample and the description.

Description	Not as per Description	As per Description	Not as per Description
Sample	As per Sample	Not as per Sample	Not as per Sample
Contract status	Buyer can repudiate	Buyer can repudiate	Buyer can repudiate



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Condition as to quality or fitness [Section 16(1)]

- ❖ Ordinarily, there is no implied condition as to the quality or fitness of the goods sold for any particular purpose.
- ❖ However, there is implied condition on the part of the seller that the goods supplied shall be reasonably fit for the purpose for which the buyer wants them, provided the following terms are fulfilled:

The buyer should have made known to the seller the particular purpose for which goods are required.

The buyer should rely on the skill and judgement of the seller.

The goods must be of a description dealt in by the seller, whether he be a manufacturer or not.

- ❖ Where the goods can be used for only one purpose, the buyer need not tell the seller the purpose for which he requires the goods.

Condition as to Merchantability [Section 16(2)]

- ❖ Where goods are bought by description from a seller who deals in goods of that description (whether he is the manufacturer or producer or not),
 - there is an implied condition that the goods shall be of merchantable quality.
- ❖ Essential requirements

Good should be sold by description

Seller should be dealing in those goods ordinarily

- ❖ if the buyer has examined the goods, there shall be no implied condition as regards defects which such examination ought to have revealed.
- ❖ **"Merchantable Quality"** - goods of such a quality and in such a condition a man of ordinary prudence would accept them as goods of that description.

Condition as to Wholesomeness

In the case of eatables and provisions, there is another implied condition that the goods shall be wholesome, in addition to the implied condition as to merchantability.



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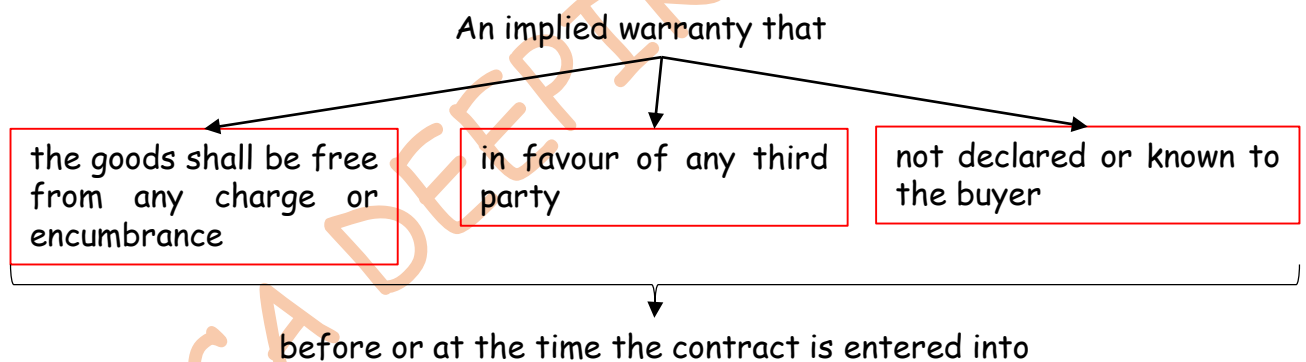
Implied Warranties

- ✓ Implied Warranty which the law implies into the contract of sale.
- ✓ It is a stipulation which has not been included in contract of sale in express words, but law presumes that the parties have incorporated it into their contract.
- ✓ Implied warranties may also be excluded by the course of dealings between the parties or by usage of trade [Section 62].

Warranty as to Undisturbed Possession [Section 14(b)]

- ❖ An implied warranty that the buyer shall have and enjoy quiet possession of the goods.
- ❖ If the buyer having got possession of the goods, is later on disturbed in his possession, → he is entitled to sue the seller for the breach of the warranty.

Warranty as to non-existence of encumbrances [Section 14(c)]



Warranty as to quality or fitness by usage of trade [Section 16(3)]

An implied warranty as to quality or fitness for a particular purpose may be annexed or attached by the usage of trade.

Disclosure of dangerous nature of goods

Where the goods are dangerous in nature and the buyer is ignorant of the danger,

- Seller must warn the buyer of the probable danger

If there is a breach of warranty,

- Seller may be liable in damages.



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Caveat Emptor

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

Rule of CEVEAT EMPTOR (Section -16)

- "subject to the provisions of this Act or of any other law for the time being in force, there is no implied warranty or condition as to the quality or fitness for any particular purpose of goods supplied under a contract of sale".
- Following are the conditions to be satisfied:
 - ✓ if the buyer had made known to the seller the purpose of his purchase, and
 - ✓ the buyer relied on the seller's skill and judgement, and
 - ✓ seller's business to supply goods of that description

Exceptions of the Rule

Fitness as to quality or use [Section 16(1)]

There is an implied condition that goods shall be reasonably fit for a particular purpose, if -

The buyer had made known to the seller the purpose of his purchase

The buyer relied on the seller's skill and judgement

Goods are of a description which is in the course of Seller's business to supply

Case Law: Priest vs. Last

Facts: P, a draper, purchased a hot water bottle from a retail chemist, P asked the chemist if it would stand boiling water. The Chemist told him that the bottle was meant to hold hot water.
The bottle burst when hot water was poured into it and injured his wife.

Judgement: It was held that the chemist shall be liable to pay damages to P, as he knew that the bottle was purchased for the purpose of being used as a hot water bottle.



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Case Law: Bombay Burma Trading Corporation Ltd. vs. Aga Muhammad

Facts: Timber was purchased for the express purpose of using it as railways sleepers and it was found to be unfit for the purpose.

Judgement: The Court held that the contract could be avoided.

Good purchased under patent or brand name [Section 16(1)]

In case where the goods are purchased under its patent name or brand name, there is no implied condition that the goods shall be fit for any particular purpose.

Goods sold by description [Section 15]

- Where the goods are sold by description there is an implied condition that the goods shall correspond with the description.
- If it is not so then the seller is responsible.

Goods of Merchantable Quality [Section 16(2)]

- Where the goods are bought by description from a seller who deals in goods of that description there is an implied condition that the goods shall be of merchantable quality.

- The rule of Caveat Emptor is not applicable.

But, where the buyer has examined the goods

→ This rule shall apply if the defects were such which ought to have not been revealed by ordinary examination.

Sale by sample [Section 17]

Where the goods are bought by sample,

- This rule of Caveat Emptor does not apply if the bulk does not correspond with the sample.

Goods by sample as well as description [Section 15]

Where the goods are bought by sample as well as description,

- The rule of Caveat Emptor is not applicable in case the goods do not correspond with both the sample and description or either of the conditions

Trade Usage [Section 16(3)]

An implied warranty or condition as to quality or fitness for a particular purpose may be annexed by the usage of trade and if the seller deviates from that,

- This rule of Caveat Emptor is not applicable.



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Seller actively conceals a defect or is guilty of fraud

The rule of Caveat Emptor will not apply

Where the seller sells the goods by making some misrepresentation or fraud and the buyer relies on it,

When the seller actively conceals some defect in the goods so that the same could not be discovered by the buyer on a reasonable examination.

In such a case the buyer has a right to avoid the contract and claim damages.

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Unit -3 : Transfer of Ownership & Delivery of Goods

A contract of sale of goods involves transfer of ownership in three stages



PASSING OF PROPERTY (Section 18-26)

- Passing of property implies passing of ownership.
- Once the property has passed to the buyer, the risk in the goods sold is that of the buyer and not of the seller, though the goods may still be in the seller's possession.

The rules regarding transfer of property in goods from the seller to the buyer depend on two basic factors

(A) Identification of Goods (Section 18)

- Where there is a **contract of sale for unascertained goods**, the **property in goods cannot pass to the buyer unless and until the goods are ascertained**.
- The buyer can get the ownership right on the goods only when the goods are specific and ascertained.

(B) Intentions of parties [Section 19(1)]

- The property in goods is transferred to the buyer at such time as the parties to the contract intend it to be transferred.
- **Section 19(2)** further provides that for the purpose of ascertaining the intention of the parties regard shall be:
 - i. **To the terms of the contract**
 - ii. **To the conduct of the parties and**
 - iii. **To the circumstances of the case**



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The primary rules determining the passing of property from seller to buyer

Passing of Property

Specific or Ascertained Goods

Passing of Unascertained Goods

Goods sent on approval or on sale or return

Transfer of property in case of reservation of right to disposal

A .Property (Specific or ascertained goods) passes when intended to pass [Section 19]

Section 19(1): Transfer of Property in case of a contract for sale of Specific or Ascertained Goods -

- The property in them is transferred to the buyer at such time as the parties to the contract intend it to be transferred.

Section 19(2): Ascertaining the Intention of Parties - The intention of the parties shall be ascertained with due regard to -

- The terms of the contract
- The conduct of the parties
- The circumstances of the case

Section 19(3): Unless a different intention appears, the rules contained in sections 20 to 24 are rules for ascertaining the intention of the parties as to the time at which the property in the goods is to pass to the buyer.

The stages of goods while passing of property are as follows

Specific goods in a deliverable state [Section 20]

Where there is an unconditional contract for the sale of specific goods in deliverable state

the property in goods passes to the buyer when the contract is made.

This rule holds true even if the time of payment of price, or the time for delivery of the goods, or both, is postponed.



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Specific goods to be put into a deliverable state (Section 21)

- Where there is a contract for the sale of specific goods
and
- The seller is bound to do something to put the goods in deliverable state

the property does not pass until such thing is done and buyer has notice thereof.

Specific goods in a deliverable state, when the seller has to do anything thereto in order to ascertain price [Section 22]

- Where there is a contract for the sale of specific goods in a deliverable state,
BUT
- seller is bound to weigh, measure, test or do some other act or thing with reference to the goods for the purpose of ascertaining the price,

the property does not pass until such act or thing is done and the buyer has notice thereof.

B. Goods must be ascertained

- **Section 18 :-** Where there is a contract for the sale of unascertained goods, no property in the goods is transferred to the buyer unless and until the goods are ascertained.
- The rules in respect of passing of property of unascertained goods are as follows -

Sale of unascertained goods by description [Section 23(1)]

- In case of contract of sale of unascertained/future goods by description and such goods are unconditionally appropriated to the contract, either by seller with the assent of the buyer or vice versa,

The property in goods passes to the buyer.

Delivery to the carrier [Section 23(2)]

When the seller delivers the goods to the buyer or to a carrier or other bailee for the purpose of transmission to the buyer and he does not reserve the right of disposal,

He is deemed to have unconditionally appropriated the goods.



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C. Goods sent on approval or 'On sale or return' [Section 24]

- A sale on approval, as applicable to the Sale of Goods Act, is a conditional sale of goods that is made on a trial basis. A buyer who enters into a sale of approval agreement receives the goods and has to decide whether to buy within a given time period.

When goods are sent on 'Sale or Approval' basis property in them passes to the buyer when -

Buyer signifies his approval to the seller

Or

Buyer does not signify his approval but retains the goods without giving a notice of rejection and

Buyer does something to the good which is equivalent to accepting the goods or does any act adopting the transaction.

If a time had been fixed for rejection - Such time has expired

If no time had been fixed for rejection - A reasonable time has expired,

Sale for cash only or Return

When goods are delivered by a person on 'Sale or return' on the condition that the goods will remain the property of the seller till they are paid -

Property in such goods does not pass to the buyer until the condition is complied with, i.e., cash is paid for.

D. Reservation of right of disposal (Section 25)

In certain cases, the seller may reserve the right of disposal of goods until certain conditions are fulfilled, in such a case

- irrespective of delivery of goods to a buyer the property in goods

Does not pass to the buyer until conditions imposed by seller are fulfilled.



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Circumstances under which the right to disposal may be reserved -

If the goods are shipped or delivered to a railway administration for carriage and by the bill of lading or railway receipt, the goods are deliverable to the order of the seller or his agent,

- then the seller is prima facie deemed to reserve the right of disposal.

- Where the seller draws a bill on the buyer for the price and sends to him the bill of exchange together with the bill of lading or the railway receipt, to secure acceptance or payment thereof, the buyer must return the bill of lading, if he does not accept or pay the bill.
- If he wrongfully retains the bill of lading or the railway receipt,
→ the property in the goods does not pass to him.

Risk Prima Facie Passes with Property [Section 26]

According to Section 26 of the Sale of Goods Act, 1930 -

- "Unless otherwise agreed, the goods remain at the seller's risk until the property therein is transferred to the buyer,
- but when the property therein is transferred to the buyer, the goods are at the buyer's risk whether delivery has been made or not".

Thus, in ordinary circumstances, risk is borne by the buyer only when the property in the goods passes over to him. However, the parties may, agree to the contrary.

Exception to the rule that 'Risk follows Ownership'

i. Where delivery of the goods has been delayed through the fault of either buyer or seller, the goods are at the risk of the party in fault as regards any loss which might not have occurred but for such fault.

ii. The duties and liabilities of the seller or the buyer as bailee of goods for the other party remain unaffected even when the risk has passed generally.



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TRANSFER OF TITLE BY NON OWNERS (Section 27-30)

Sale by person not the owner (Section 27)

"Subject to the provisions of this Act and of any other law for the time being in force, where goods are sold by a person who is not the owner thereof and who does not sell them under the authority or with the consent of the owner, the buyer acquires no better title to the goods than the seller had, unless the owner of the goods is by his conduct precluded from denying the seller's authority to sell".

- ❖ The general rule regarding the transfer of title is that the seller cannot transfer to the buyer of goods a better title than he himself has.
- ❖ If the seller is not the owner of goods, then the buyer also will not become the owner i.e. the title of the buyer shall be the same as that of the seller.

This rule is expressed in the Latin maxim 'Nemo dat quod non habet' which means 'No one can give what he has not got'.

Exceptions to the rule that Non-owner cannot convey a better Title to the Buyer

Sale by a Mercantile Agent {Section 27} :

The sale by a mercantile agent would pass a **good title** if

- he was in **possession** of the goods with **consent of the owner**,
- acting in **ordinary course** of business and
- the buyer has acted in **good faith**.

Sale by one of the joint owners {Section 28} :

If any **one of several joint owners** has the possession of the goods with the **permission** of the other co-owners, if

- person buys these goods in **good faith** and
- has **not noticed that the seller has no authority** to sell then the **property** in goods is **transferred** to the buyer.

Sale by a person in possession under the voidable contract {Section 29} :

When a seller who has obtained goods under a **voidable contract** sells the goods;

- the **buyer will get a good title** to the goods he has bought
- provided that the contract has not been rescinded until the time of sale.



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Sale by one who has already sold the goods but continues in possession thereof {Section 30(1)} :

- When even **after selling** the goods the seller **continues to be in possession** of goods; he may **sell them** to a **third person** and if such person obtains the delivery in **good faith** and without notice of previous sale, he would get a good title to the goods.
- A pledge or other disposition of the goods or documents of title by the seller in possession are equally valid

Sale by a buyer obtaining possession before the property in the goods has vested in him {Section 30(2)} :

- Where the buyer obtains possession of the goods he may sell, pledge or dispose the goods to a third person, and if such person obtains delivery in good faith and without notice of the lien or other right of the original seller, he would get a good title to the goods.
- A person in possession of goods under a 'hire-purchase' agreement which gives him only an option to buy is not covered within this section unless it amounts to a sale.

Effect of Estoppel : Where the owner is estopped by the conduct from denying the seller's authority to sell, the transferee will get a good title as against the true owner.

Sales by unpaid seller [Section 54(3)] : Where an unpaid seller who had exercised his right of lien or stoppage in transit resells the goods, the buyer acquires a good title to the goods as against the original buyer

Sale under the provisions of the other Acts :

- Sale by an Official Receiver or Liquidator of the Company will give the purchaser a valid title.
- Purchase of goods from a finder of goods will get a valid title under circumstances.
- A sale by pawnee can convey a good title to the buyer.

PERFORMANCE OF THE CONTRACT OF SALE (Section 31-44)

The performance of a contract of sale implies

- delivery of goods by the seller and
- acceptance of the delivery of goods and payment of price for them by the buyer

in accordance with the terms of the contract.



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Delivery Section 2(2)

- Delivery means voluntary transfer of possession from one person to another
- For delivery, physical possession is not important.
- If the possession is taken through unfair means, there is no delivery of the goods.
- Delivery of goods is of three types:
 - Actual Delivery
 - Symbolic delivery
 - Constructive Delivery

Duties of seller and buyer [Section 31]

- Duty of Seller - To deliver the goods
- Duty of the Buyer - To accept the goods and pay for them.
- Delivery, acceptance, and payment should be in accordance with the terms of the Contract of Sale.

Payment and Delivery are concurrent conditions [Section 32]

- Unless otherwise agreed, delivery of the goods and payment of the price are concurrent conditions.
- This means that,
 - **The seller**→ shall be ready and willing to give possession of the goods to the buyer in exchange for the price, and
 - **The buyer**→ shall be ready and willing to pay the price in exchange for possession of the goods.

Rules Regarding Delivery of goods

Delivery (Section 33)

Delivery of goods sold may be made by doing anything

Which the parties agree shall be treated as delivery or

Which has the effect of putting the goods in the possession of the buyer or of any person authorised to hold them on his behalf.



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Effect of part delivery (Section 34)

If a part-delivery of the goods is made in progress of the delivery of the whole, then it has the same effect for the purpose of passing the property in such goods as the delivery of the whole.

However, a part-delivery with an intention of severing it from the whole does not operate as a delivery of the remainder.

Buyer to apply for delivery (Section 35)

Apart from any express contract, the seller of goods is not bound to deliver them until the buyer applies for delivery.

Place of delivery [Section 36(1)]

Place of delivery

- Depends on the contract, express or implied : whether buyer to take possession of goods or seller to send them to the buyer
- Apart from such contract,

Goods sold:
Delivered at the place at which they are at the time of the sale.

Goods to be sold :
Delivered at the place at which they are at the time of agreement to sell

Goods not in existence at the time of agreement :
Delivered at place where they are manufactured or produced

Time of delivery [Section 36(2)]

Where under the contract of sale,

The seller is bound to send the goods to the buyer,

But no time for sending them is fixed, the seller is bound to send them within a reasonable time.

Goods in possession of a third party [Section 36(3)]

Where the goods at the time of sale are in possession of a third person,
→ There is no delivery unless and until such third person acknowledges to the buyer that he holds the goods on his behalf.

However, this shall not affect the operation of the issue or transfer of any document of title to goods.



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Time for tender of delivery [Section 36(4)]

- It is important that the demand or tender of delivery is made at a reasonable hour.
- If not, then it is rendered ineffectual. The reasonable hour will depend on the case.

Expenses for delivery [Section 36(5)]

The seller will bear all expenses pertaining to putting the goods in a deliverable state unless the parties agree to some other terms in the contract.

Delivery of wrong quantity (Section 37)

- **Sub-section 1 :**
 - ✓ If the seller delivers a **lesser quantity** of goods as compared to the contracted quantity, then the buyer may **reject** the delivery.
 - ✓ If he **accepts** it, then he shall **pay for them at the contracted rate**.
- **Sub-section 2 :**
 - ✓ If the seller delivers a **larger quantity** of goods as compared to the contracted quantity, then the buyer may **accept** the quantity included in the contract and **reject the rest**.
 - ✓ The buyer can also **reject the entire delivery**.
 - ✓ If he wants to accept the increased quantity, then he needs to pay at the contract rate.
- **Sub Section -3**
 - ✓ If the seller delivers a **mix of goods** where some part of the goods are mentioned in the contract and some are not, then the buyer **may accept the goods which are in accordance with the contract and reject the rest**.
 - ✓ He may also **reject the entire delivery**.
- **Sub Section -4**
 - ✓ The Provision of this section are subject to any usage of trade, special agreement or course of dealing between the parties.

Instalment deliveries (Section 38)

- The buyer does not have to accept delivery in installments unless he has agreed to do so in the contract.
- If such an agreement exists, then the parties are required to determine the rights and liabilities and payments themselves.



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Delivery to carrier [Section 39(1)]

- The delivery of goods to the carrier for transmission to the buyer is prima facie deemed to be 'delivery to the buyer' unless contrary terms exist in the contract.

Deterioration during transit (Section 40)

- If the goods are to be delivered at a distant place, then the liability of deterioration incidental to the course of the transit lies with the buyer even though the seller agrees to deliver at his own risk.

Buyer's right to examine the goods (Section 41)

- **Buyer** → has the right to ascertain that the goods delivered to him are in conformity with the contract.
- **Seller** → is bound to honor the buyer's request for a reasonable opportunity of examining the goods unless the contrary is specified in the contract.

Rule related to Acceptance of Delivery of Goods (Section - 42)

Acceptance is deemed to take place when the buyer

Intimates to the seller that he had accepted the goods;

or

Does any act to the goods, which is inconsistent with the ownership of the seller;

or

Retains the goods after the lapse of a reasonable time, without intimating to the seller that he has rejected them.

Buyer not bound to return rejected goods [Section 43]

Where goods are delivered to the buyer and he refuses to accept them, having the right so to do,

- he is not bound to return them to the seller,
- but it is sufficient if he intimates to the seller that he refuses to accept them.

Liability of buyer for neglecting or refusing delivery of goods [Section 44]

When the seller is

- Ready and willing to deliver the goods and
- Requests the buyer to take delivery, and
- Buyer does not within a reasonable time after such request take delivery of the goods,

- For any loss occasioned by his neglect or refusal to take delivery and
- Also for a reasonable charge for the care and custody of the goods.



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The provisions of this section shall not affect the rights of the seller where the neglect or refusal of the buyer to take delivery amounts to a repudiation of the contract.

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Unit -4 : Unpaid Seller

UNPAID SELLER

Unpaid Seller Right

- A contract comprises of reciprocal promises.
- In a contract of sale, if seller is under an obligation to deliver goods, buyer has to pay for it.
- In case buyer fails or refuses to pay, the seller, as an unpaid seller, shall have certain rights.

Definition[Section 45(1)]

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

The whole of the price has not been paid or tendered and the seller had an immediate right of action for the price.

When a bill of exchange or other negotiable instrument has been received as conditional payment, and the condition on which it was received has not been fulfilled by reason of the dishonour of the instrument or otherwise.

Seller Includes [Section 45(2)]

The term 'seller' here includes

any person who is in the position of a seller, as, for instance,

an agent of the seller to whom the bill of lading has been endorsed, or

a consignor or agent who has himself paid, or is directly responsible for, the price.

RIGHTS OF AN UNPAID SELLER

Unpaid Seller Right [Section 46(1)]

A lien on the goods for the price while he is in possession of them

in case of the insolvency of the buyer a right of stopping the goods in transit after he has parted with the possession of them;

A right of re-sale as limited by this Act.



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[Section 46(2)]

Where the **property in goods has not passed to the buyer**,

- the unpaid seller has, in addition to his other remedies,
- a right of **withholding delivery** similar to and **co-extensive with his rights of lien** and
- stoppage in transit where the property has passed to the buyer.

Rights of an unpaid seller against the Goods

Where the property in goods has passed to the buyer

Where the property in goods has not passed to the buyer

RIGHT OF UNPAID SELLER AGAINST THE GOODS

Sellers lien (Section 47)

- ✓ The unpaid seller of goods who is in possession of them is entitled to **retain possession** of them until payment in the following cases :
 - Goods sold without any stipulation as to credit
 - Goods sold on credit but the credit term has expired
 - Buyer becomes insolvent
- ✓ The unpaid seller can exercise his rights of lien while he is in possession of the goods by acting as an agent or bailee of the buyer.
- ✓ This is called **possessory lien** and can be exercised by the seller as long as he is in possession of the goods

Part Delivery (Section 48)

when an unpaid seller has made **part delivery** of the goods, he may exercise right of lien on the **remaining goods**.

Termination of Lien (Section 49)

Unpaid seller of Goods loses his lien in the following cases

- Delivery of goods to carrier for the purpose of transmission without reserving right of disposal
- By Waiver
- By Estoppel
- Buyer or agent lawfully obtains possession



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Right of stoppage in transit (Section 50)

MTP May 2024

- ✓ When the buyer of the goods becomes **insolvent**, and the unpaid seller who has **parted with possession** has the right of **stopping them in transit**.
- ✓ The right of stoppage in transit is lost when transit comes to an end.
- ✓ The Right of Stoppage in transit is exercised only when the following conditions are fulfilled:
 - The seller must be **Unpaid**.
 - He must have **parted with the possession** of goods.
 - The goods are in **Transit**.
 - The buyer has become **insolvent**.

Duration of transit (Section 51)

- ✓ **Goods are deemed to be in course of transit**
 - from the time delivered to carrier/ other bailee for purpose of transmission to the buyer, till the time buyer or his agent takes delivery from such carrier.
- ✓ **When goods are rejected by the buyer**
 - and the carrier or other bailee continues in possession of them, the transit is not deemed to be at an end, even if the seller has refused to receive them back.
- ✓ **Goods are delivered to a ship chartered by the buyer** → it is a question depending on the circumstances of the particular case, whether they are in the possession of the master as a carrier or as agent of the buyer.
- ✓ **Part delivery of the goods has been made to the buyer or his agent in that behalf**
 - the remainder of the goods may be stopped in transit, unless such part delivery has been given in such circumstances as to show an agreement to give up possession of the whole of the goods.

How stoppage in transit is effected (Section 52)

1. The unpaid seller may exercise his right of stoppage in transit either by taking actual possession of the goods, or by giving notice of his claim to the carrier or other bailee in whose possession the goods are.
 - Such notice may be given either to the person in actual possession of the goods or to his principal.
 - In the latter case, the notice, to be effectual, shall be given at such time and in such circumstances, that the principal, by the exercise of reasonable diligence, may communicate it to his servant or agent in time to prevent a delivery to the buyer.



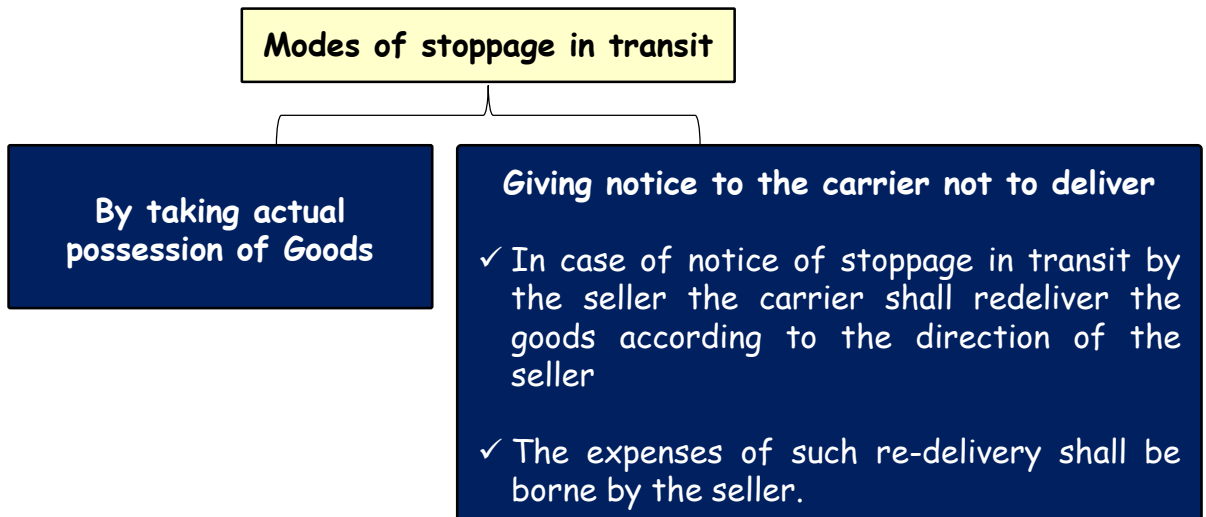
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2. When notice of stoppage in transit is given by the seller to the carrier or other bailee in possession of the goods, he shall re-deliver the goods to, or according to the directions of, the seller.

The expenses of such re-delivery shall be borne by the seller.



Section 53 : Effects of sub-sale or pledge by buyer

- The right of lien or stoppage in transit is **not affected** by the buyer selling or pledging the goods unless the **seller has assented to it**. Based on principle second buyer cannot stand in a better position than his seller
- The right of stoppage is **defeated** if the buyer has **transferred the document of title** or pledges the goods to a sub-buyer in **good faith and for consideration**.

Exceptions

- a. When the seller has assented to the sale, mortgage or other disposition of the goods made by the buyer. (*Mount D.F. Ltd. vs Jay & Jay (Provisions) Co. Ltd*)
- b. When a document of title to goods has been transferred to the buyer and the buyer transfers the documents to a person who has bought goods in good faith and for value i.e. for price, then, the proviso of sub-section (1) stipulates as follows:
 - i. If the last-mentioned transfer is by way of sale, right of lien or stoppage in transit is defeated, **or**
 - ii. If the last mentioned transfer is by way of pledge, unpaid seller's right of lien or stoppage only be exercised, subject to the rights of the pledgee.



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Section 54 : Right of re-sale

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

- i. **Where the goods are of a perishable nature** :→ the buyer need not be informed of the intention of resale.
- ii. **Where he gives notice to the buyer of his intention to re-sell the goods** : → If after the receipt of such notice the buyer fails within a reasonable time to pay or tender the price, the seller may resell the goods.
 - a. Recover the difference between the contract price and resale price, from the original buyer, as damages.
 - b. Retain the profit if the resale price is higher than the contract price.
 - ✓ The seller can **recover damages and retain the profits** only when the goods are resold after giving the **notice of resale** to the buyer.
 - ✓ In case **no notice** is given to the buyer **before reselling** the goods, the **seller cannot recover the loss on resale** and above this he must **return the profit on resale** to the original buyer.
- iii. **Where an unpaid seller who has exercised his right to lien or stoppage in transit, resells the goods**: → the new buyer gets a good title to the goods as against the original buyer.
- iv. **A re-sale by the seller where a right of re-sale is expressly reserved in a contract of sale** :→ the seller is not required to give notice of resale to the original buyer.
- v. **Where the property in goods has not passed to the buyer**: → The unpaid seller in addition to his remedies has a right to withhold the delivery of the goods. It is similar to right of lien and is called "**Quasi Lien**".



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RIGHT OF UNPAID SELLER AGAINST THE BUYER (Section 55-61)

Rights of unpaid seller against the buyer personally

- ✓ Can enforce certain rights against the goods as well as against the buyer personally.
- ✓ Rights of unpaid seller against the buyer are otherwise known as seller's remedies for breach of contract of sale.
- ✓ The rights of the seller against the buyer personally are called rights in personam and are in addition to his rights against the goods.

Suit for Price (Section 55)

Section -55(1) :- Where under a contract of sale, the property in the goods has passed to the buyer and the buyer wrongfully neglects or refuses to pay for the goods according to the terms of the contract,

- seller may sue him for the price of the goods.

Section -55 (2) :- Where under a contract of sale, the price is payable on a certain day irrespective of delivery and the buyer wrongfully neglects or refuses to pay such price,

- seller may sue him for the price although the property in the goods has not passed and
- the goods have not been appropriated to the contract.

Suit for damages for non acceptance (Section 56)

Where the buyer wrongfully neglects or refuses to accept and pay for the goods, the
➤ seller may sue him for damages for non-acceptance.

Repudiation of contract before due date (Section 60)

- ✓ Where the buyer repudiates the contract before the date of delivery,
 - The seller may
 - treat the contract as rescinded and
 - sue damages for the breach.
- ✓ This is known as the '**rule of anticipatory breach of contract**'.



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Suit for Interest (Section 61)

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

- The seller may recover interest from the buyer.

If, however, there is no specific agreement to this effect,

The seller may charge interest on the price when it becomes due from such day as he may notify to the buyer.

In the absence of a contract to the contrary, the Court may award interest to the seller in a suit by him at such rate as it thinks fit on the amount of the price from the date of the tender of the goods or from the date on which the price was payable.

REMEDIES OF BUYER AGAINST THE SELLER

Breach of contract by seller

Breach of contract by seller where he-

Fails to deliver the goods at the time or in manner prescribed

Breach of contract by seller where he-

Repudiates the contract

Breach of contract by seller where he-

Delivery non-conforming goods and buyer rejects and revokes acceptance

If the seller commits a breach of contract, the buyer gets the following rights against the seller

Damages for non-delivery [Section 57]

Suit for specific performance (Section 58)

Suit for breach of warranty (Section 59)

Repudiation of contract before due date (Section 60)

1. Suit for interest



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Damages for non-delivery [Section 57]

Where the seller wrongfully neglects or refuses to deliver the goods to the buyer,
➤ The buyer may sue the seller for damages for non-delivery.

Suit for Specific performance [Section 58]

- ✓ Where the seller commits of breach of the contract of sale,
 - The buyer can appeal to the court for specific performance.
- ✓ The court can order for specific performance only when the goods are ascertained or specific.
- ✓ This remedy is allowed by the court subject to these conditions
 - a. The contract must be for the sale of specific and ascertained goods.
 - b. The power of the court to order specific performance is subject to provisions of Specific Relief Act of 1963.
 - c. It empowers the court to order specific performance where damages would not be an adequate remedy.
 - d. It will be granted as remedy if goods are of special nature or are unique.

Suit for breach of warranty [Section 59]

- ✓ Where there is breach of warranty on the part of the seller, or where the buyer elects to treat breach of condition as breach of warranty,
 - The buyer is not entitled to reject the goods only on the basis of such breach of warranty.
- ✓ But he may -
 - i. set up against the seller the breach of warranty in diminution or extinction of the price; or
 - ii. sue the seller for damages for breach of warranty.

Repudiation of contract before due [Section 60]

Where either party to a contract of sale repudiates the contract before the date of delivery, the other

- May either treat the contract as subsisting and wait till the date of delivery, or
- May treat the contract as rescinded and sue for damages for the breach.



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Suit for Interest

1. Nothing in this Act shall affect the right of the seller or the buyer to recover interest or special damages, in any case where by law interest or special damages may be recoverable, or to recover the money paid where the consideration for the payment of it has failed.
2. In the absence of a contract to the contrary, the court may award interest at such rate as it thinks fit on the amount of the price to the buyer in a suit by him for the refund of the price in a case of a breach of the contract on the part of the seller from the date on which the payment was made.

AUCTION SALE (Section 64)

- ✓ **Auction sale** : - An 'Auction Sale' is a mode of selling property by inviting bids publicly and the property is sold to the highest bidder.
- ✓ **Auctioneer** : -
 - An auctioneer is an agent governed by the Law of Agency
 - When he sells, he is only the agent of the seller.
 - He may, however, sell his own property as the principal and need not disclose the fact that he is so selling.

Legal Rules of Auction sale: *Section 64 of the Sale of Goods Act, 1930* provides following rules to regulate the sale by auction:

- a. Where goods are sold in lots:** Where goods are put up for sale in lots, each lot is *prima facie* deemed to be subject of a separate contract of sale.
- b. Completion of the contract of sale:** The sale is complete when the auctioneer announces its completion by the fall of hammer or in any other customary manner and until such announcement is made, any bidder may retract from his bid.
- c. Right to bid may be reserved:** Right to bid may be reserved expressly by or on behalf of the seller and where such a right is expressly reserved, but not otherwise, the seller or any one person on his behalf may bid at the auction.
- d. Where the sale is not notified by the seller:** Where the sale is not notified to be subject to a right to bid on behalf of the seller, it shall not be lawful for the seller to bid himself or to employ any person to bid at such sale, or for the auctioneer knowingly to take any bid from the seller or any such person; and any sale contravening this rule may be treated as fraudulent by the buyer.
- e. Reserved price:** The sale may be notified to be subject to a reserve or upset price.



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f. **Pretended bidding:** If the seller makes use of pretended bidding to raise the price, the sale is voidable at the option of the buyer.

INCLUSION OF INCREASED OR DECREASED TAXES IN CONTRACT OF SALE (Section 64A)

- Where after a contract has been made but before it has been performed, tax revision takes place.
- Where tax is being imposed, increased, decreased or remitted in respect of any goods without any stipulations to the payment of tax, the parties would become entitled to read just the price of the goods accordingly.

CA DEEPIKA RATHI

Chapter 4: Indian Partnership Act, 1932



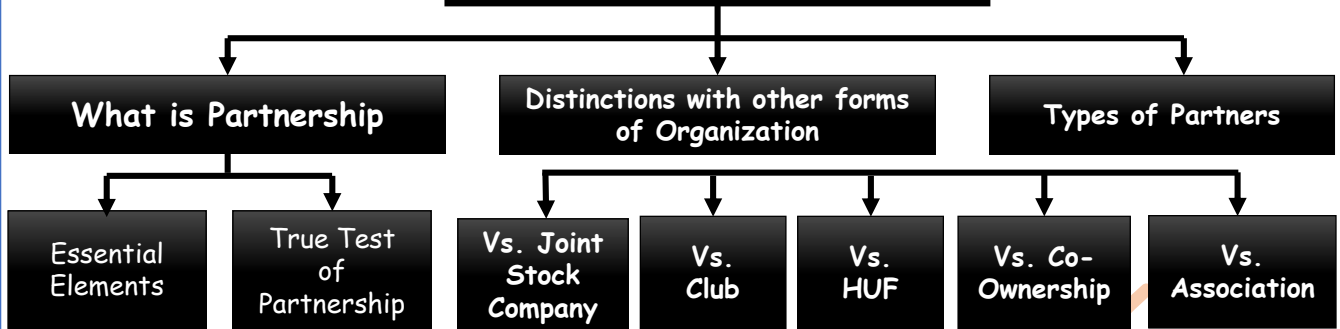
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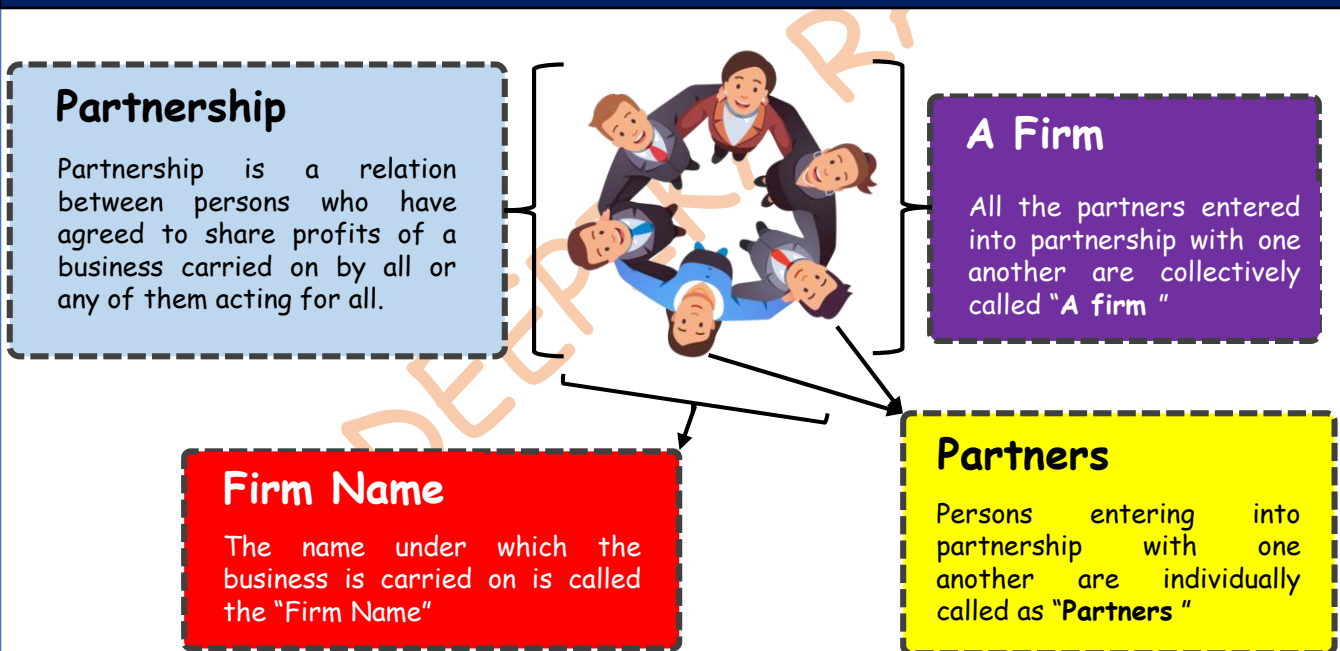
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UNIT-1 GENERAL NATURE OF PARTNERSHIP

General Nature of Partnership



DEFINATION OF PARTNERSHIP PARTNER FIRM & FIRM NAME



ELEMENTS OF PARTNERSHIP

1. Association of two or more persons

- Partnership is an **association of 2 or more persons**, only the persons recognized by law can enter into an agreement of partnership.
- A firm cannot be a partner as it is not recognized as a person in the eyes of law.
- The limit on maximum number of partners is put by section 464 of Companies Act 2013 i.e. 50 Partners



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2. Agreement

There must be an agreement **entered into by all persons concerned.**

The nature of the partnership is **Voluntary** and **Contractual.**

The Agreement from which relationship of partnership arises may be **express.**

It may be **oral** or **in writing.**

3. Business

- The term business includes every trade, occupation and profession.
- Two propositions must be kept in mind,
 - i. There must exist a business and
 - ii. The motive of the business is acquisition of gains.

4. Agreement to share profits

- There can be no partnership where only one of the partners is entitled to the whole of the profits of the business.
- Partners must agree to share the profits in any manner they choose.
- **Agreement to share losses** - An agreement to share losses is not an essential element.
 - It is open to one or more partners to agree to share all the losses.
 - However, in the event of losses, unless agreed otherwise, these must be borne in the profit-sharing ratio.

5. Business carried on by all or any of them acting for all

- The business must be carried on by all the partners or by anyone or more of the partners acting for all.

→ This is the cardinal principle of the Partnership Law.

- There should be a **binding contract of mutual agency** between the partners.
- An act of one partner in the course of the business of the firm is an act of all partners.
- Each partner carrying on the business is the principal as well as the agent for all the other partners.



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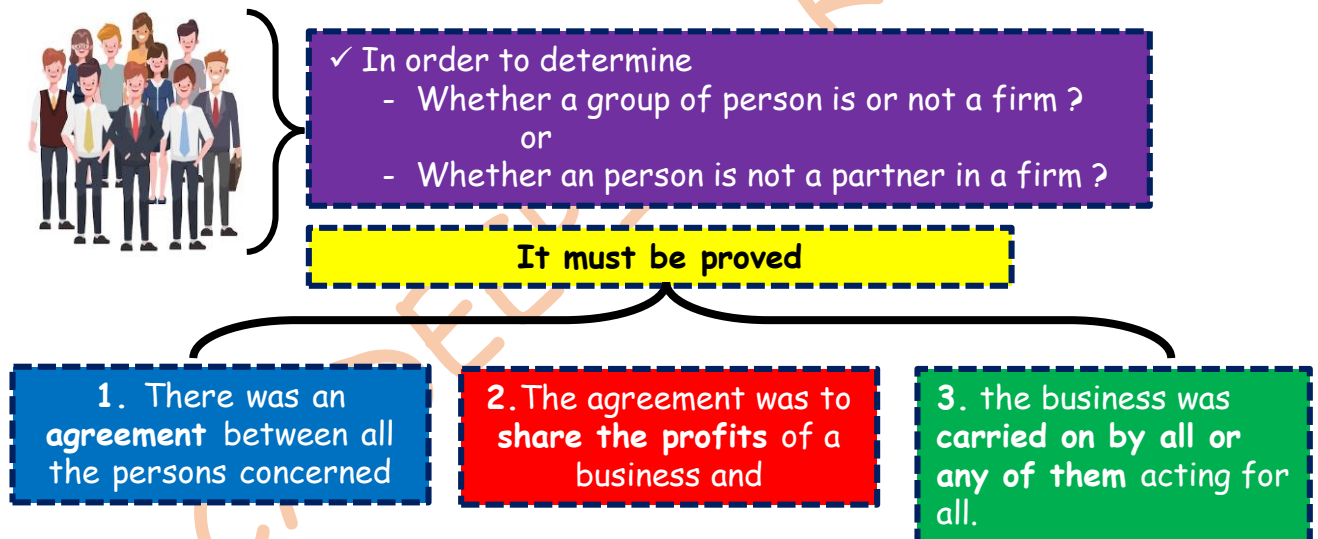
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Case Law : KD Kamath & Co.

- ✓ The Supreme Court has held that two essential conditions to be satisfied are that:
 1. There should be **an agreement to share the profits as well as the losses of business** and
 2. The **business must be carried on by all or any of them acting for all.**
- ✓ The fact that **exclusive power and control**, by agreement of the parties, is **vested in one partner** or the further circumstance that only one partner can operate bank account or borrow on behalf of the firm are not destructive of the theory of partnership provided the two essential conditions are satisfied.

Note:- The 'Partnership Agreement' is also known as 'Partnership Deed'.

TRUE TEST OF PARTNERSHIP



1. Agreement

Partnership is Created by agreement and not by status [Section 5]

2. Sharing of Profit

- ❖ The sharing of profits or of gross returns arising from property by persons holding a joint or common interest in that property

does not of itself make such person partners.



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The receipt by a person of a share of the profits of a business, or of a payment contingent upon the earning of profits or varying with the profits earned by a business,

Does not of itself make him a partner with the persons carrying on the business;

The receipt of such share or payment-

1. By a lender of money to persons engaged or about to engage in any business
2. By a servant or agent as remuneration,
3. By a widow or child of a deceased partner, as annuity or
4. By a previous owner or part owner of the business, as consideration for the sale of the goodwill or share thereof,

Does not of itself make the receiver a partner with the persons carrying on the business.

- Sharing of profit is an essential element to constitute a partnership.
- But it is only a prima facie evidence and not conclusive evidence, in that regard.

- ❖ To share the profit of a business and the business is being carried on by all or any of them acting for all, if there is -

Express agreement between partners

There is no difficulty in determining the existence or otherwise of partnership.

No specific agreement

For testing the existence or otherwise of partnership relation, Sec 6 has to be referred.

- ❖ According to Section 6, regard must be had to the real relation between the parties as shown by all relevant facts taken together.
- ❖ Cumulative effect of all relevant facts such as written or verbal agreement, real intention and conduct of the parties, other surrounding circumstances etc., are to be considered while deciding the relationship between the parties and ascertaining the existence of partnership.



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3. Agency

- Each partner carrying on the business is the principal as well as an agent of other partners. So, the act of one partner done on behalf of firm, binds all the partners.
- If the elements of mutual agency relationship exist between the parties constituting a group formed with a view to earn profits by running a business, a partnership may be deemed to exist.

Case Law: Santiranjn Das Gupta Vs. Dasyran Murzamull (SC)

In this case, the following factors weighed upon the Supreme Court to reach the conclusion that there is no partnership between the parties:

- Parties have not retained any record of terms and conditions of partnership.
- Partnership business has maintained no accounts of its own, which would be open to inspection by both parties.
- No account of the partnership was opened with any bank.
- No written intimation was conveyed to the Deputy Director of Procurement with respect to the newly created partnership.

PARTNERSHIP DISTINGUISHED FROM OTHER FORM OF ORGANISATION

Partnership Vs. Joint Stock Company

Basis	Partnership	Joint Stock Company
Legal Status	No legal personality distinct its constituent members.	Separate legal entity distinct from its members
Agency	Every partner is an agent of the other partners as well as of the firm.	A member is not an agent of the other members or of the company.
Distribution of profits	Distributed among the partners according to terms of partnership deed.	There is no such compulsion to distribute its profits among its members.
Extent of liability	Liability of the partners is unlimited.	Limited liability - limited by shares or limited by guarantee.
Property	The firm's property is the 'joint estate' of all the partners.	In a company, its property is separate from that of its members.



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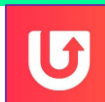
Management	In the absence of an express agreement to the contrary, all the partners are entitled to participate in the management.	<ul style="list-style-type: none"> Members of a company are not entitled to take part in the management unless they are appointed as directors, in which case they may participate. Members, however, enjoy the right of attending general meeting and voting where they can decide certain questions such as election of directors, appointment of auditors, etc.
Registration	Not compulsory	Comes into existence only after it is registered under the Companies Act, 2013.
Winding up	Can be dissolved at any time if all the partners agree.	Either wound up by the NCLT or its name is struck off by the ROC.
Number of members	Restricted by the Companies Act, 2013 and Rules thereon to 50.	<ul style="list-style-type: none"> Public Co. - May have any number of members but not less than 2. Private Co. - Minimum 2 members and maximum 200. Can also be formed as One Person Company.
Duration of existence	Death, retirement, or insolvency of a partner results in the dissolution of the firm.	Perpetual succession

Partnership Vs. Club

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



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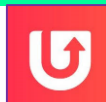
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Partnership Vs. Hindu Undivided Family

Basis	Partnership	Hindu Undivided Family
Mode of creation	By an agreement.	Right in business is created by birth in the family.
Death of member	Leads to the dissolution of partnership.	Does not give rise to dissolution of the family business.
Management	All the partners are equally entitled to take part in the partnership business.	The right of management of joint family business generally vests in the Karta, the governing male member or female member of the family.
Authority to bind	Every partner can, by his act, bind the firm.	The Karta or the manager, has the authority to contract for the family business and the other members in the family.
Liability	In a partnership, the liability of a partner is unlimited.	In a Hindu undivided family, only the liability of the Karta is unlimited, and the other coparcener are liable only to the extent of their share in the profits of the family business.
Calling for accounts on closure	A partner can bring a suit against the firm for accounts, provided he also seeks the dissolution of the firm.	On the separation of the joint family, a member is not entitled to ask for account of the family business.
Governing Law	Indian Partnership Act, 1932	The Hindu Law.
Minor's capacity	A minor cannot become a partner, though he can be admitted to benefits of partnership.	A minor becomes a member of the ancestral business by the incidence of birth.
Continuity	A firm gets dissolved by death or insolvency of a partner.	A Joint Hindu family has continuity till it is divided.
Number of Members	Should not exceed 50.	Members may be unlimited in number.
Shares in Business	Each partner has a defined share by agreement between the partners.	In a HUF, no coparceners have a definite share. The share fluctuate.



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Partnership Vs. Co-ownership /Joint Ownership

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

Partnership Vs. Association

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

KINDS OF PARTNERSHIP





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Based on Duration

Partnership at will

- ✓ Section 7 of the Act Partnership at will is a partnership when -
 - a. No fixed period has been agreed upon for duration of the partnership
 - b. There is no provision made as to determination of the partnership
- ✓ If there is an agreement between the partners about the duration or the determination of the firm, this will not be a partnership at will.
- ✓ A partnership at will may be dissolved by any partner by giving notice in writing to all other partners of his intention to dissolve the same.

Partnership for a fixed period

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

Based on Extent of Business

Particular Partnership

- ✓ Where a person becomes a partner with another person in any particular adventure or undertaking, the partnership is called 'particular partnership'.
- ✓ Particular partnership is, subject to any agreement, dissolved by the completion of the adventure or undertaking.

General Partnership

- ✓ Where a partnership is constituted with respect to the business in general, it is called a general partnership.
- ✓ Unlike a particular partnership in a general partnership the scope of business to be carried out is not defined.
- ✓ So, all partners will be liable for all the actions of the partnership.

PARTNERSHIP DEED

- ✓ *No particular formalities are required for an agreement of partnership.*
- ✓ It may be in **writing** or formed **verbally**.



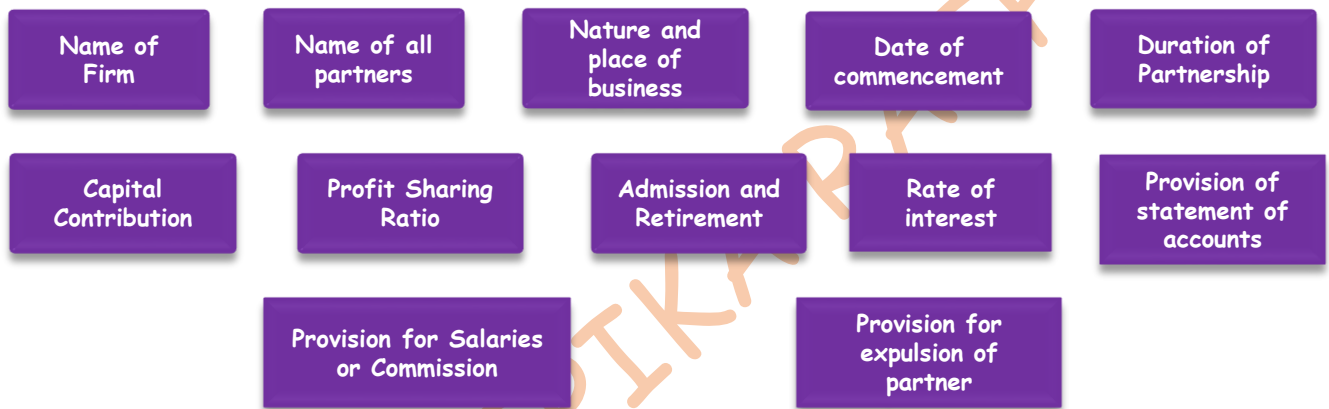
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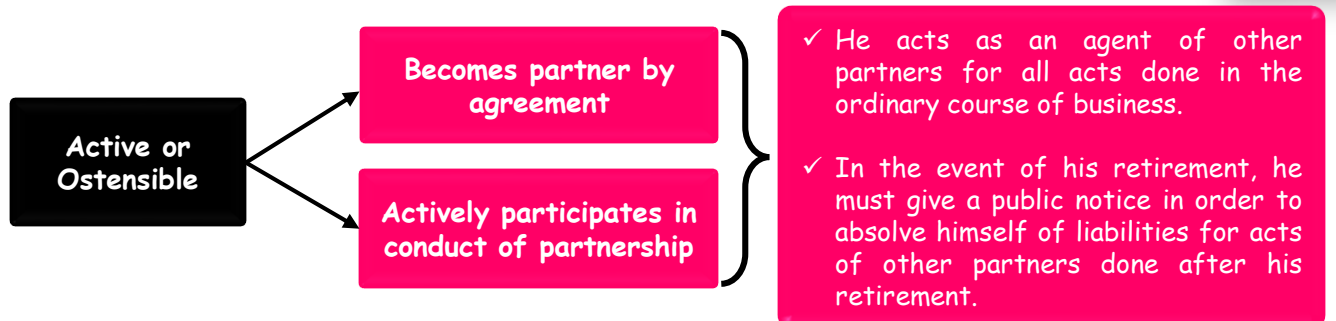
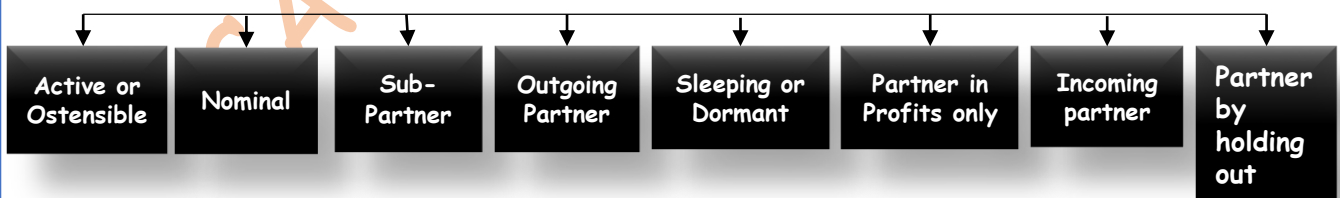
- ✓ The document in writing containing various terms and conditions as to the relationship of the partners to each other is called the '**Partnership Deed**'.
- ✓ Where the partnership comprises immovable property, the instrument of partnership must be in writing, stamped and registered under Registration Act.
- ✓ Partnership deed should be drafted with care and be stamped according to the provisions of the Stamp Act, 1899.

Content of Partnership deed



Note : A partnership firm may add or delete any provision according to the needs of the firm.

TYPES OF PARTNERS

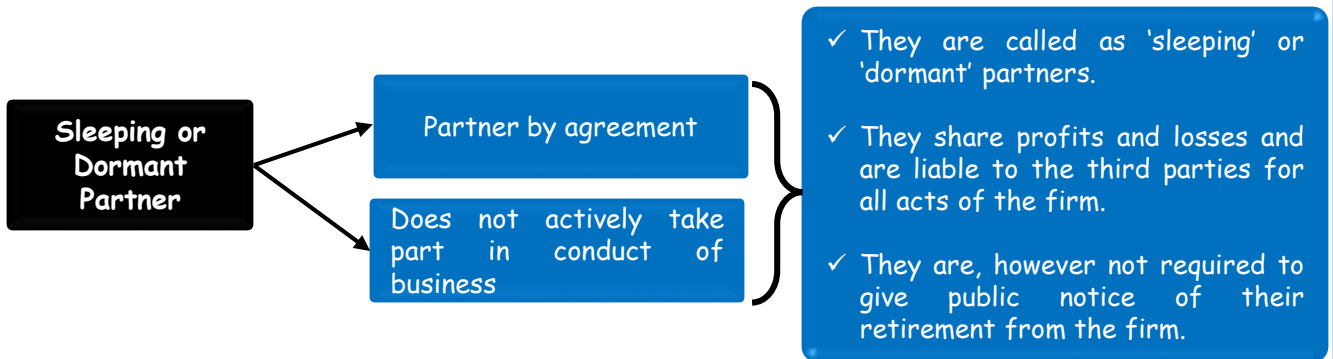




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Nominal Partner



Partner in Profits only



Incoming Partner

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

Such a partner is **not liable** for any act of the firm done before his admission as a partner.

Outgoing Partner

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

Such a partner **remains liable** to third parties for all acts of the firm until public notice is given of his retirement.



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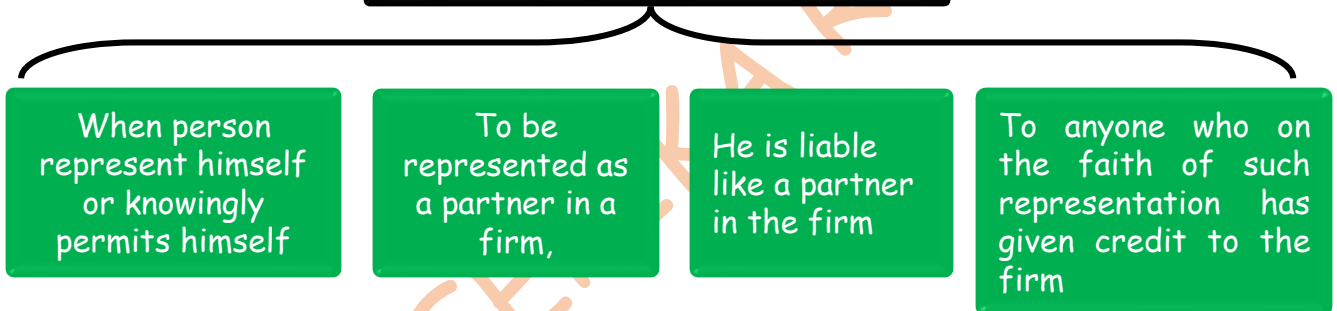


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Partner by holding out (Section-28)

- ❖ Where a man holds (represents) himself out as a partner, or allows others to do it, he is then stopped from denying the character assumed and upon the faith of which creditors may be presumed to have acted.
- ❖ Partnership by holding out is also known as partnership by estoppel.
- ❖ It is only the person to whom the representation has been made and who has acted thereon that has right to enforce liability arising out of 'holding out'.
- ❖ For fixing liability on a person who has, by representation, led another to act, it is not necessary to show that he was actuated by a fraudulent intention.

Partner by holding out (Section-28)





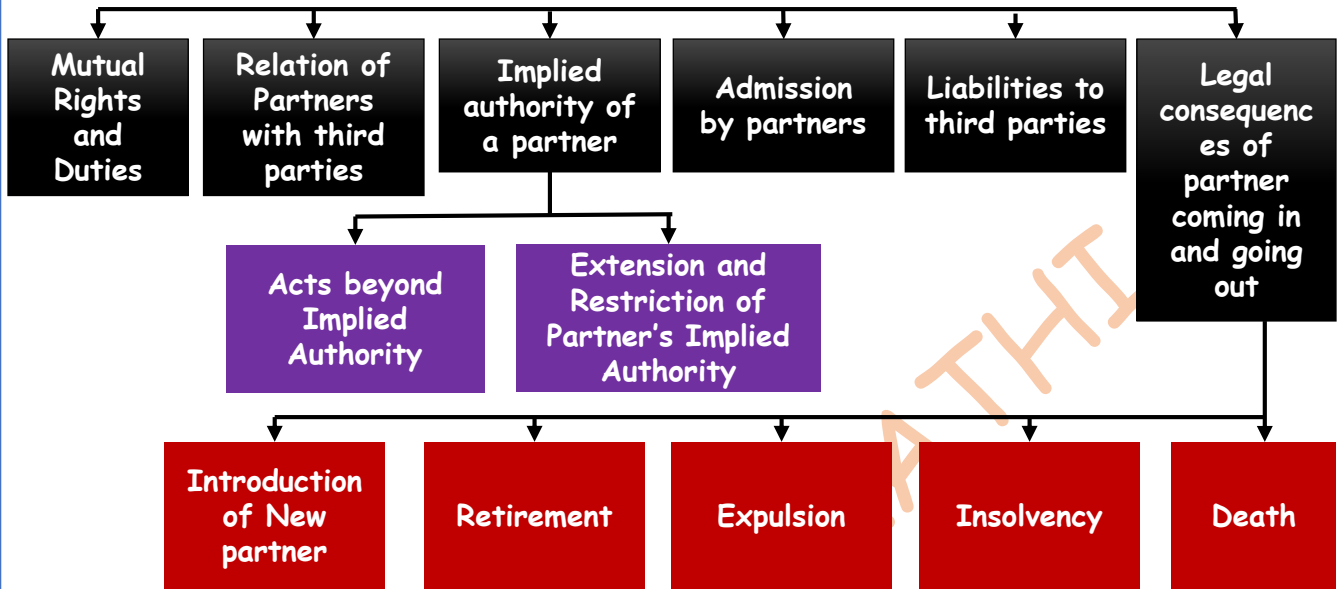
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UNIT-2 RELATION OF PARTNERS

Relation of Partners



RELATION OF PARTNERS TO ONE ANOTHER

GENERAL DUTIES OF PARTNERS (SECTION 9)

To carry on the business of the firm to the greatest common advantage of the firm and its partners.

To observe utmost good faith in his dealings with the other partners.

To render to any partner or his legal representatives full information of all things affecting the firm.

Where some of the accounts are kept by one of the partners, prima facie he would be the proper person to explain and give full information about them.

DUTY TO INDEMNIFY FOR LOSS CAUSED BY FRAUD (SECTION 10)

❖ Every partner shall → indemnify the firm for any loss caused to it by his fraud in the conduct of the business of the firm.

The amount so brought in the partnership should be divided between the partners.

❖ An act of a partner imputable (i.e., chargeable) to the firm or the principles of agency, which is a fraud on his co-partners, entitles the co-partners as between themselves, to make the partner responsible for consequences.



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DETERMINATION OF RIGHTS AND DUTIES OF PARTNERS BY CONTRACT BETWEEN THE PARTNERS (SECTION 11)

a. The rights and duties of the partners may be determined by contract between the partners, whether express or implied.

Such contract may be varied by consent of all the partners, which may also be express or implied.

b. Agreements in restraint of trade

The contract of partnership may provide that a partner shall not carry on any business other than that of the firm while he is a partner.

THE CONDUCT OF THE BUSINESS (SECTION 12)

Rights of the Partners in relation to Conduct of the Business

Every partner has the right

→ To take part in the conduct of the business

→ To have access to and inspect the books of the firm

→ To express opinion on difference arising as to ordinary matters

Every partner is bound

→ to attend diligently to his duties in the conduct of the business

In the event of death of any partners, legal representative or heir or authorised agents shall have right to access and inspect the books.

Right to take part in the conduct of the Business [Section 12(a)]

- ❖ Every partner has the right to take part in the business of the firm, provided there is no contract to the contrary between the partners.
- ❖ Partnership business is a business of the partners, and their management powers are generally coextensive
- ❖ In case of partnership agreements which

gives only limited power of management to a partner

or

contains a term that the management of the partnership will remain with one or more of the partners to the exclusion of others



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The Court will normally be unwilling to intervene in the management with such partner or partners, unless it is clearly made out that something was done illegally or in breach of the trust reposed in such partners.

Right to be consulted [section 12(c)]

- Where any difference arises between the partners with regard to the business of the firm, it shall be determined by the views of the majority of them, and every partner shall have the right to express his opinion before the matter is decided.
- However, no change in the nature of the business of the firm can be made without the consent of all the partners. In such a case, the unanimous consent of the partners is needed.
- In routine matters, the opinion of the majority of the partners will prevail.

Right of access to books [Section 12(d)]

- ✓ Every partner is entitled to have access to any of the books of the firm and to inspect or take out a copy thereof.
- ✓ This right is applicable equally to active and dormant partners.

Right of legal heirs/ representatives/ their duly authorized agents [Section 12(e)]

In the event of death of a partner, his heirs or legal representatives or their duly authorized agents shall have a

→ Right of access to and to inspect and copy of any books of the firm.

MUTUAL RIGHTS AND LIABILITIES (SECTION 13)

Right to remuneration [Section 13(a)]

- No partner is entitled to receive any remuneration in addition to his share in the profits of the firm for taking part in the business of the firm.
- However, this rule can always be varied by an express agreement, or by a course of dealings, in which event the partner will be entitled to remuneration.
- Where it is customary to pay remuneration to a partner for conducting the business of the firm he can claim it even in the absence of a contract for the payment of the same.



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Right to share Profits [Section 13 (b)]

- Partners are entitled to share in the profits earned and so also to contribute to the losses sustained by the firm.
- The amount of a partner's share must be ascertained by enquiring whether there is any agreement in that behalf between the partners.
- The profits and losses are shared equally in absence of an agreement.
- There is no connection between the proportion in which the partners shall share the profits and the proportion in which they have contributed towards the capital of the firm.

Interest on Capital [Section 13 (c)]

The partners of a firm shall be entitled to interest on moneys brought by him in the partnership business, provided, there is -

An express agreement to that effect, or practice of the particular partnership

or

Any trade custom to that effect

or

A statutory provision which entitles him to such interest

In the absence of any agreement, no interest on capital is payable.

Interest on advances [Section 13(d)]

- ✓ In case where a partner gives an advance to the firm in addition to the amount of capital contributed by him, the partner is entitled to claim interest @6% per annum.
- ✓ The interest on advances keep running even after dissolution upto the date of payment.

Right to be indemnified [Section 13 (e)]



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Every partner has the right to be indemnified by the firm in respect of

Payments made and liabilities incurred by him in the ordinary and proper conduct of the business of the firm,

Payment made in the performance of an act in an emergency for protecting the firm from any loss, if the payments, liability, and act are such as a prudent man would make, incur, or perform in his own case, under similar circumstances

Right to indemnify the firm [Section 13(f)]

A partner must indemnify the firm for any loss caused to it by wilful neglect in the conduct of the business of the firm.

PARTNERSHIP PROPERTY (SECTION 14)

- ❖ Property of the firm is also referred to as 'partnership property', 'partnership assets', 'joint stock', 'common stock' or 'joint estate'.
- ❖ The property of the firm, in the absence of any agreement between the partners showing contrary intention, is comprised of the following items:

All property, rights, and interests which partners may have brought into the common stock as their contribution to the common business

All the property, rights and interest acquired or purchased by or for the firm, or for the purposes and in the course of the business of the firm,

Goodwill of the business.

- ❖ The determination of the question whether a particular property is or is not 'property' of the firm ultimately depends on the real intention or agreement of the partners.
- ❖ Mere fact that property of a partner is being used for purposes of the firm shall not by itself make it partnership property, unless it is intended to be treated as such.
- ❖ Partners may, by an agreement at any time, convert the property of any partner or partners or the separate property of any partner into a partnership property.



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- ❖ Partners may, by an agreement at any time, convert the property of any partner or partners or the separate property of any partner into a partnership property.

Such conversion, if made in good faith, would be effectual between partners and against creditors of firm.

Goodwill

- Defined as value of the reputation of a business house in respect of profits expected in future over and above normal level of profits earned by undertaking belonging to the same class of business.
- Goodwill is a part of the property of the firm.
- It can be sold separately or along with the other properties of the firm.
- Any partner may upon the sale of the goodwill of a firm, make an agreement with the buyer that such partner will not carry on any business similar to that of the firm within a specified period or within specified local limits.

APPLICATION OF THE PROPERTY OF THE FIRM [SECTION 15]

- Subject to contract between partners, the property of the firm shall be held and used exclusively for the purpose of the firm.
- During the subsistence of the partnership, a particular partner does not have any proprietary interest in the assets of the firm.

PERSONAL PROFIT EARNED BY PARTNERS (SECTION 16)

According to section 16, subject to contract between the partners :

If a partner derives any profit for himself from any transaction of the firm, or from the use of the property or business connection of the firm or the firm name,

He shall account for that profit and pay it to the firm.

If a partner carries on any business of the same nature as and competing with that of the firm,

He shall account for and pay to the firm all profits made by him in that business.



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RIGHTS & DUTIES OF PARTNERS AFTER CHANGE IN THE FIRM (SECTION 17)

Following are the situations when there is a change in the constitution of the firm

- 1 Admission of new partner
- 2 Death or retirement of a partner
- 3 Partnership carries on business other than original one
- 4 Fixed period partnership carried on even after expiry of fixed period

According to section 17, subject to contract between the partners-

- a. **After a change in the firm:** Where a change occurs in the constitution of a firm, the mutual rights and duties of the partners in the reconstituted firm **remain the same as they were immediately before the change**, as far as may be.
- b. **After the expiry of the term of the firm:** Where a firm constituted for a fixed term continues to carry on business after the expiry of that term, the mutual rights and duties of the **partners remain the same as they were before the expiry**, so far as they may be consistent with the incidents of partnership at will
- c. **Where additional undertakings are carried out:** where a firm constituted to carry out one or more adventures or undertakings carries out other adventures or undertakings are the **same as those in respect of the original adventures or undertakings**.

RELATION OF PARTNERS TO THIRD PARTIES

Partner to be Agent of the Firm [Section 18]

- Subject to the provisions of the Act, a partner is the agent of the firm for the purpose of the business of the firm.
- The rule that a partner is the agent of the firm for the purpose of the business of the firm cannot be applied to all transactions and dealings between the partners themselves.
- It is applicable only to the act done by partners for the purpose of the business of the firm.



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Implied Authority of Partner as Agent of the Firm [Section 19]

- Subject to the provisions of section 22, the act of a partner which is done to carry on, in the usual way, business of the kind carried on by the firm, → binds the firm.
- The authority of a partner to bind the firm conferred by this section is called his "implied authority".
- **MODE OF DOING ACT TO BIND FIRM Section 22:** In order to bind a firm, an act or instrument done or executed by a partner or other person on behalf of the firm shall be **done or executed in the firm name, or in any other manner expressing or implying an intention to bind the firm**
- **Section 19(2)** In the absence of any usage or custom of trade to the contrary, the implied authority of a partner does not empower him to-
 - a. Submit dispute to arbitration
 - b. Open bank account of firm in his own name
 - c. compromise or relinquish any claim or portion
 - d. withdraw a suit or proceedings filed
 - e. admit any liability in a suit or proceedings
 - f. acquire immovable property on behalf of firm
 - g. transfer immovable property
 - h. enter into partnership on behalf of the firm
- If partnership be of a general commercial nature, any partner may
 - Pledge or sell the partnership property,
 - Buy goods on account of the partnership
 - Borrow money, contract debts and pay debts on account of the partnership
 - Draw, make, sign, endorse, transfer, negotiate and procure to be discounted, Promissory notes, bills of exchange, cheques and other negotiable papers in the name and on account of the partnership

Extension and Restriction of Partners' Implied Authority [Section 20]

- The implied authority of a partner may be extended or restricted by contract between the partners.



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- Under the following conditions, restrictions imposed on the implied authority of a partner by agreement shall be effective against third party -

The third party knows
about the restrictions

And

The third party does not know that
he is dealing with a partner in a firm.

- However, such extension or restriction is only possible with the consent of all the partners.
- Any one partner, or even a majority of the partners, cannot restrict or extend the implied authority.

Partner's Authority in an Emergency [Section 21]

In case of an emergency, a partner has authority

to do all such acts for the purpose of protecting the firm from loss as would be done by a person of ordinary prudence, in his own case, acting under similar circumstances,

Such acts bind the firm.

Effect of Admissions by a Partner [Section 23]

- An admission or representation made by a partner **concerning the affairs of the firm is evidence against the firm** if it is made in the **ordinary course of business**.
- However, an admission or representation by a partner will not bind the firm if his authority on the point is limited and the other party knows of the restriction.

Effect of Notice to Acting Partner [Section 24]

- Notice to a partner who habitually acts in the business of the firm of any **matter relating to the affairs of the firm** operates as **notice to the firm**.
- The only **exception** is in the case of a **fraud on the firm committed by or with the consent of that partner**.
- Notice to one is equivalent to the notice to the rest of the partners of the firm, just as a notice to an agent is notice to his principal



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- Notice must be actual and not constructive.
- It must be received by a working partner and not by a sleeping partner.

LIABILITY TO THIRD PARTIES (SECTION 25 TO 27)

Liability of a Partner for acts of the Firm [Section 25]

- Every partner is liable, **jointly** with all the other partners and **also severally**, for all acts of the firm done while he is a partner.
- The expression 'act of firm' connotes any act or omission by all the partners or by any partner or agent of the firm, which gives rise to a right enforceable by or against the firm.
- To bring a case under Section 25, it is necessary that the act of the firm, in respect of which liability is brought to be enforced against a party, must have been done while he was a partner.

Liability of the Firm for Wrongful Acts of a Partner [Section 26]

- ❖ The firm is liable to the same extent as the partner for any loss or injury caused to a third party by the wrongful acts of a partner, if they are done by the partner while acting:

in the ordinary course of the business of the firm

with the authority of the partners

- ❖ If act fall within these 2 categories, fact that method employed by partner in doing it was unauthorized/wrongful, doesn't matter.
- ❖ Furthermore, all the partners in a firm are liable to a third party for loss or injury caused to him by the negligent act of a partner acting in the ordinary course of the business.

Liability of Firm for Misapplication by Partners [Section 27]

Where

a. A firm in the course of its business receives money or property from a third party, and the money or property is misapplied by any of the partners while it is in the custody of the firm,

b. A partner acting within his apparent authority receives money or property from a third party and misapplies it,

The firm is liable to make good the loss



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- If receipt of money by one partner is not within the scope of his apparent authority, his receipt cannot be regarded as a receipt by the firm and the other partners will not be liable, unless the money received comes into their possession or under their control.

RIGHTS OF TRANSFeree OF A PARTNER'S INTEREST (SECTION 29)

- A share in a partnership is → transferable like any other property,
- But as the partnership relationship is based on mutual confidence, the assignee of a partner's interest by sale, mortgage or otherwise cannot enjoy the same rights and privileges as the original partner.

The rights of such a transferee are as follows

During the Continuance of Partnership

- To interfere with the conduct of the business
- To require accounts or
- To inspect books of the firm

He is only entitled to receive the share of the profits of the transferring partner and he is bound to accept the profits as agreed to by the partners, i.e., he cannot challenge the accounts.

On Dissolution of the firm/ Retirement of transferring partner

- Entitled to receive the share of the assets of the firm, and
- for this purpose, to an account as from the date of the dissolution.

Note :→ A partner cannot by transferring his own interest, make anybody else a partner in his place, unless the other partners agree to accept that person as a partner.

MINORS ADMITTED TO THE BENEFITS OF PARTNERSHIP (SECTION 30)

- A minor cannot become a partner in a firm; however, he can be admitted to the benefits of partnership under Section 30 of the Act, with the consent of all the partners for the time being.
- He can be validly given a share in the partnership profits.



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Rights of the Minor

- i. A minor partner has a right to his agreed share of the profits and of the firm.
- ii. He can have access to, inspect and copy the accounts of the firm.
- iii. He can sue the partners for accounts or for payment of his share but only when severing his connection with the firm, and not otherwise.
- iv. On attaining majority he may within 6 months elect to become a partner or not to become a partner.
 - **If he elects to become a partner** → , then he is entitled to the share to which he was entitled as a minor.
 - **If he does not**, → then his share is not liable for any acts of the firm after the date of the public notice served to that effect.

Liabilities of the Minor

Before attaining majority

- Confined to the extent of his share in the profit
- No personal liability for debts of the firm
- Cannot be declared insolvent

After attaining majority

When he becomes partner

Becomes personally liable to third parties

Share in profits and property remains the same

When he elects not to become a partner

His **rights and liabilities continue** to be those of a minor up to the **date of giving public notice**.

Not liable for the acts of the firm

Entitled to sue the partners



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LEGAL CONSEQUENCES OF PARTNER COMING IN AND GOING OUT (SECTION 31-35)

Introduction of a Partner [Section 31]

- Subject to a contract between partners and to the provisions regarding minors, no person shall be introduced as a partner into a firm without the consent of all the existing partners.
- **Rights and liabilities of new partner**
 - The liabilities of the new partner ordinarily commence from the date when he is admitted as a partner, unless he agrees to be liable for obligations incurred by the firm prior to the date
 - The new firm, including the new partner who joins it, may agree to assume liability for the existing debts of the old firm, and creditors may agree to accept the new firm as their debtor and discharge the old partners.
 - The creditor's consent is necessary in every case to make the transaction operative.
 - An agreement between the partners and the incoming partner that he shall be liable for existing debts will not ipso facto give creditors of the firm any right against him.

Note : This section does not apply to a partnership of two partners which is automatically dissolved by the death of one of them.

Retirement of a Partner [Section 32]

➤ A partner may Retire

With the consent of
all the other parties

In accordance with
express agreement by
the partners

In case of Partnership
at Will - by giving
notice in writing of all
the other partners

- A retiring partner may be discharged from any liability to any third party for acts of the firm done before his retirement by an agreement made by him with such third party and the partners of the reconstituted firm, and such agreement may be implied by a course of dealing between the third party and the reconstituted firm after he had knowledge of the retirement.



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- Notwithstanding the retirement of a partner from a firm
 - he and the partners continue to be liable as partners to third parties for any act done by any of them which would have been an act of the firm if done before the retirement until public notice is given of the retirement
 - Provided that a retired partner is **not liable to any third party who deals with the firm without knowing that he was a partner.**
- Notices under sub-section (3) may be given by the retired partner or by any partner of the reconstituted firm

Case Law: Vishnu Chandra Vs. Chandrika Prasad (SC)

The Supreme Court held that the expression 'if any partner wants to dissociate from the partnership business', in a clause of the partnership deed which was being construed, comprehends a situation where a partner wants to retire from the partnership. The expression clearly indicated that in the event of retirement, the partnership business will not come to an end.

EXPULSION OF A PARTNER (SECTION 33)

The expulsion is not deemed to be in bona fide interest of the business of the firm, unless all the following conditions are present -

The power of expulsion must have existed in a contract between the partners

The power has been exercised by a majority of the partners

It has been exercised in good faith

The test of good faith as required u/s 33(1) includes 3 things

Expulsion is in the interest of the partnership

Partner to be expelled is served with a notice

He is given an opportunity of being heard

Note : If a partner is otherwise expelled, the expulsion is null and void.

Note : The expulsion of partners does not necessarily result in dissolution of the firm. The invalid expulsion of a partner does not put an end to the partnership even if the partnership is at will and it will be deemed to continue as before.



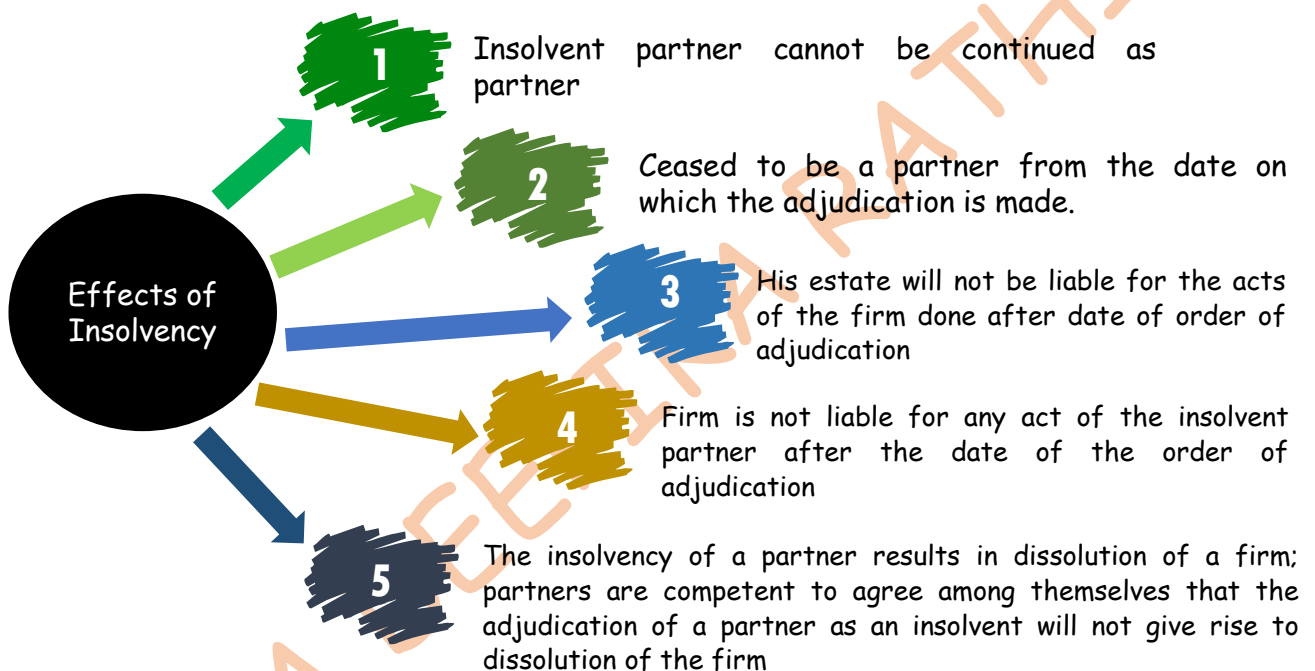
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Insolvency of a Partner [Section 34]

1. Where a partner in a firm is adjudicated as an insolvent
 - he ceases to be a partner on the date on which the order of adjudication is made, whether or not the firm is hereby dissolved.
2. Where under a contract between the partners the firm is not dissolved by the adjudication of a partner as an insolvent, the estate of a partner so adjudicated
 - is not liable for any act of the firm and
 - the firm is not liable for any act of the insolvent,
 - done after the date on which the order of adjudication is made



Liability of Estate of Deceased Partner [Section 35]

Where under a contract between the partners, the firm is not dissolved by the death of a partner, the estate of a deceased partner is not liable for any act of the firm done after his death.

RIGHTS OF OUTGOING PARTNER TO CARRY ON COMPETING BUSINESS (SECTION 36)

- ✓ An outgoing partner may carry on business competing with that of the firm and he may advertise such business, but subject to contract to the contrary, he may not,-
- a. use the firm name
 - b. represent himself as carrying on the business of the firm or
 - c. solicit the custom of persons who were dealing with the firm before he ceased to be a partner.



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- ✓ **Agreement in restraint of trade-** (2) A partner may make an agreement with his partners that on ceasing to be a partner
- he will not carry on any business similar to that of the firm within a specified period or within specified local limits and,
 - notwithstanding anything contained in section 27 of the Indian Contract Act, 1872, such agreement shall be valid if the restrictions imposed are reasonable.

RIGHTS OF OUTGOING PARTNER IN CERTAIN CASES TO SHARE SUBSEQUENT PROFITS (SECTION 37)

- Where any person ceases to be a partner because of his death or retirement, and the other partners continue the business of the firm without final settlement of accounts, in such a situation the outgoing partner or his representatives are entitled to either -
 - i. Share in the profits of the firm made since he ceased to be a partner as attributable to the use of his share of property of the firm
 - or
 - i. Interest at the rate of 6% per annum on the amount of his share in the property of the firm.
- Where, by a contract between the partners, an option is given to surviving or continuing partners to purchase the interest of a deceased or outgoing partner, and that option is duly exercised, the estate of the deceased partner/ outgoing partner/ his estate, is not entitled to any further or other share of profits.

REVOCATION OF CONTINUING GUARANTEE BY CHANGE IN FIRM (SECTION 38)

According to section 38,

- A continuing guarantee given to a firm or to third party in respect of the transaction of a firm is, in the absence of an agreement to the contrary, revoked as to future transactions from the date of any change in the constitution of the firm.

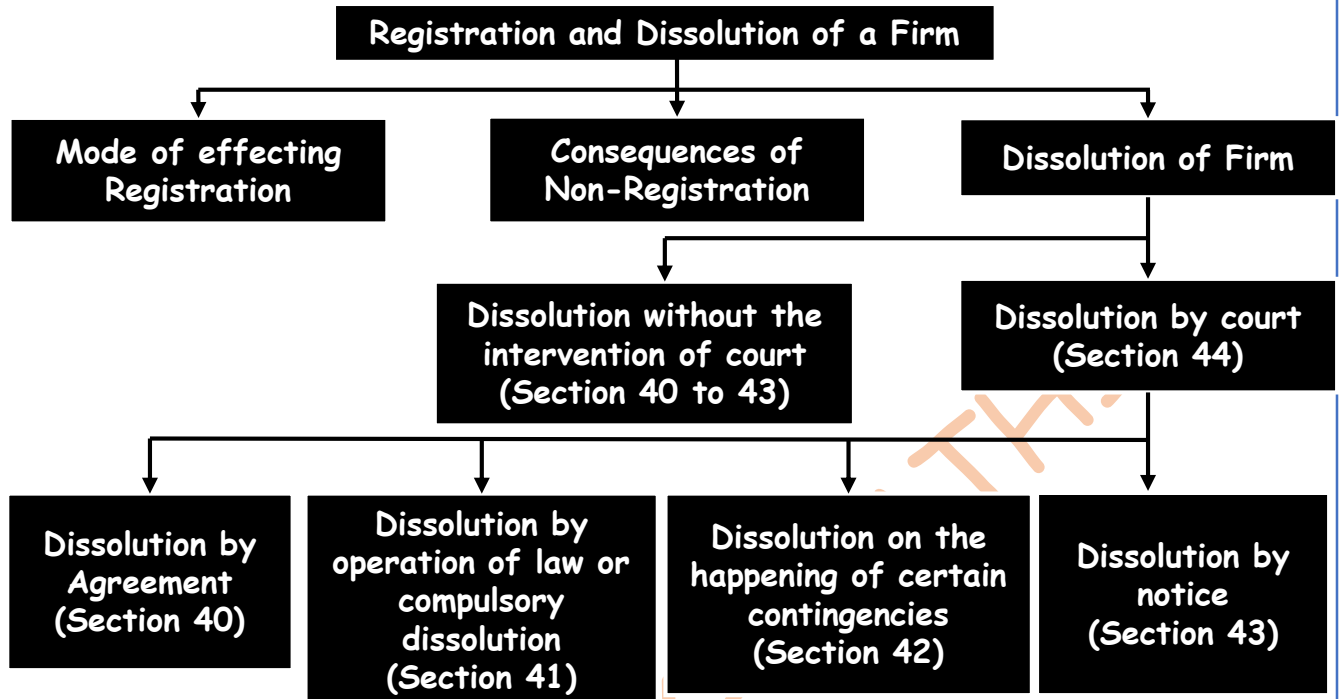


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UNIT-3 REGISTRATION AND DISSOLUTION OF FIRM



REGISTRATION OF FIRMS

- The registration of a partnership is optional, and one partner cannot compel another partner to join in the registration of the firm.
- It is not essential that the firm should be registered from the very beginning.
- When the partners decide to get the firm registered as per the provisions of Section 58 of the Indian Partnership Act, 1932, they have to file the statement in the prescribed form.

Application For Registration (Section 58)

The registration of a firm may be effected at any time by sending by post or delivering to the Registrar of the area in which any place of business of the firm is situated or proposed to be situated, a statement in the prescribed form and accompanied by the prescribed fee, stating :-

- a. The firm's name
- b. The place or principal place of business of the firm
- c. The names of any other places where the firm carries on business,
- d. the date when each partner joined the firm
- e. the names in full and permanent addresses of the partners, and
- f. the duration of the firm.



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The statement shall be signed by all the partners, or by their agents specially authorized in this behalf.

- (1) Each person signing the statement shall also verify it in the manner prescribed
- (2) A firm name shall not contain any of the following words, namely:-Crown', Emperor', 'Empress', 'Empire', 'Imperial', 'King', 'Queen', 'Royal', or words expressing or implying the sanction, approval or patronage of Government except when the State Government signifies its consent to the use of such words as part of the firm-name by order in writing.



Note : **Subsequent alterations** in the name, place, constitution, etc., of the firm that may occur during its continuance **should also be registered.**

Registration [Section 59]





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Late Registration on Payment of Penalty [Section 59A-1]

In case of failure to send and deliver the statement within a time specified in sub-section (1A) of Section 58,

- The firm may get registration on payment → of ₹ 100/- per year of delay or part thereof as penalty to the Registrar of Firms.

CONSEQUENCES OF NON-REGISTRATION (Section 69)

- The Indian Partnership Act does not make the registration of firms compulsory nor does it impose any penalty for non-registration.
- However, u/s 69 non-registration of partnership gives rise to a number of disabilities which are as follows

a. No suit in a civil court by firm or other co-partners against third party

The firm or any other person on its behalf cannot bring an action against the third party for breach of contract entered into by the firm, unless -

The firm is registered

and

The persons suing are or have been shown in the register of firms as partners in the firm.

b. No relief to partners to set-off of claim

If an action is brought against the firm by a third party, then

Neither firm nor the partner can claim any set-off

If the suit be valued for more than Rs. 100 or pursue other proceedings to enforce the rights arising from any contract.

c. Aggrieved partner cannot bring legal action against other partner or the firm

A partner of an unregistered firm (or any other person on his behalf) cannot bring any legal action against the firm or any other partner.



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d. Third party can sue the firm

Even if the firm is unregistered, a third party may bring an action against the firm.

Exceptions - Rights not affected by non-registration of a firm

1. The right of third parties to sue the firm or any partner
2. The right of partners to sue for the dissolution of the firm or for the settlement of the accounts of a dissolved firm, or for realization of the property of a dissolved firm.
3. The power of an Official Assignees, Receiver of Court to release the property of the insolvent partner and to bring an action.
4. The right to sue or claim a set-off if the value of suit does not exceed ₹ 100 in value.
5. The right to suit and proceeding instituted by legal representatives or heirs of the deceased partner of a firm for accounts of the firm or to realise the property of the firm.

DISSOLUTION OF FIRM (Section 39-47)

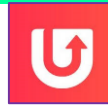
Meaning of 'Dissolution of the Firm' [Section 39]

The dissolution of partnership between all partners of a firm is called the 'dissolution of the firm'

- Thus, the dissolution of firm means → the discontinuation of the legal relation existing between all the partners of the firm.
- But, when only one or more partners retires or becomes incapacitated from acting as a partner due to death, insolvency or insanity, the partnership, i.e. the relationship between such a partner and other is dissolved, but the rest may decide to continue.
 - In such cases, there is in practice, no dissolution of the firm.



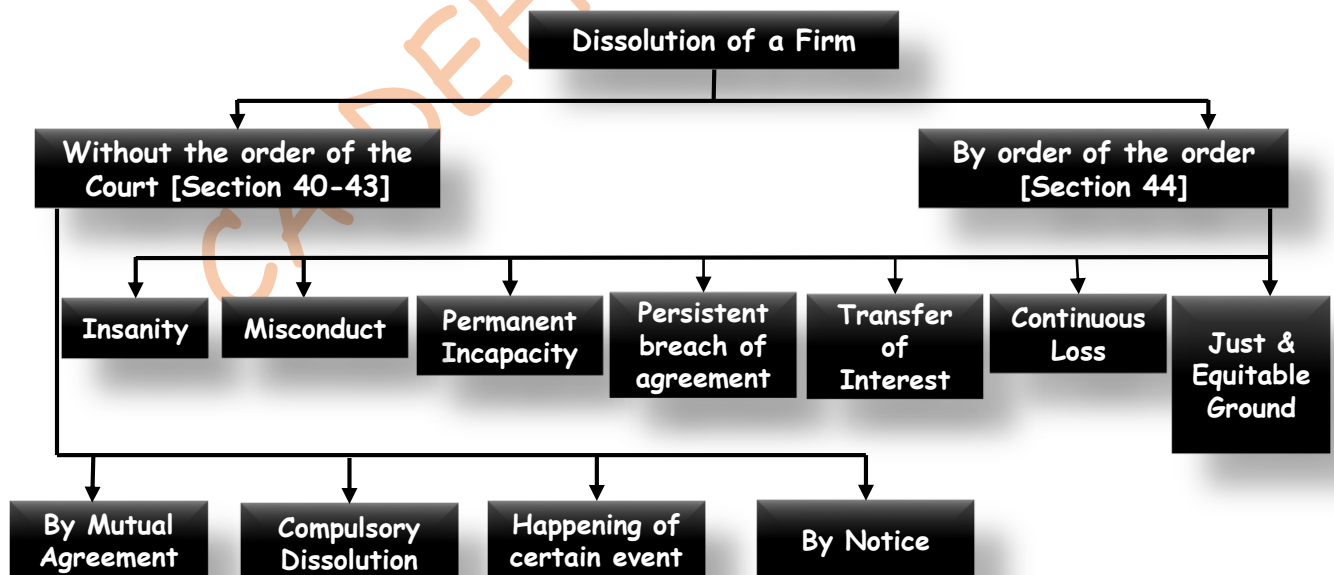
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Dissolution of Firm Vs. Dissolution of Partnership

S. No.	Basis of Difference	Dissolution of Firm	Dissolution of Partnership
1	Continuation of business	It involves discontinuation of business in partnership.	It does not affect continuation of business. It involves only reconstitution of the firm.
2	Winding up	It involves winding up of the firm and requires realization of assets and settlement of liabilities.	It involves only reconstitution and requires only revaluation of assets and liabilities of the firm.
3	Order of court	A firm may be dissolved by the order of the court.	Dissolution of partnership is not ordered by the court.
4	Scope	It necessarily involves dissolution of partnership.	It may or may not involve dissolution of firm.
5	Final closure of books	It involves final closure of books of the firm.	It does not involve final closure of the books of the firm.





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1. DISSOLUTION WITHOUT THE ORDER OF THE COURT OR VOLUNTARY DISSOLUTION

A. Dissolution by Agreement (Section 40)

A firm may be dissolved

- With the consent of all the partners or
- In accordance with a contract between the partners.

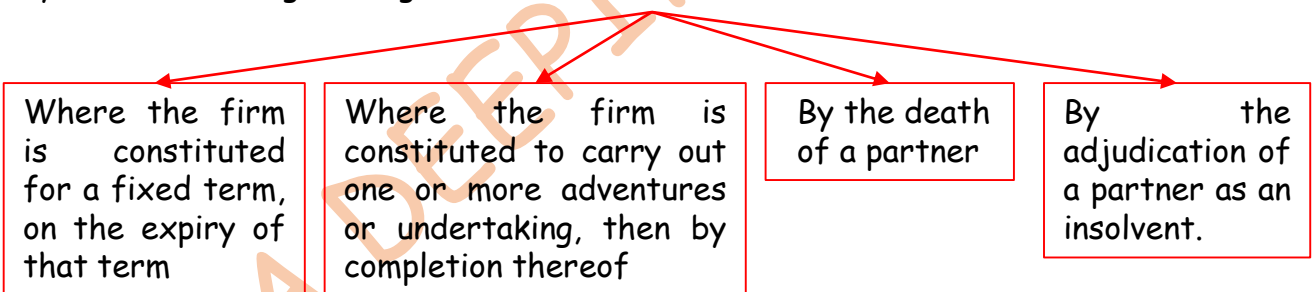
B. Compulsory Dissolution (Section 41)

A firm is compulsorily dissolved -

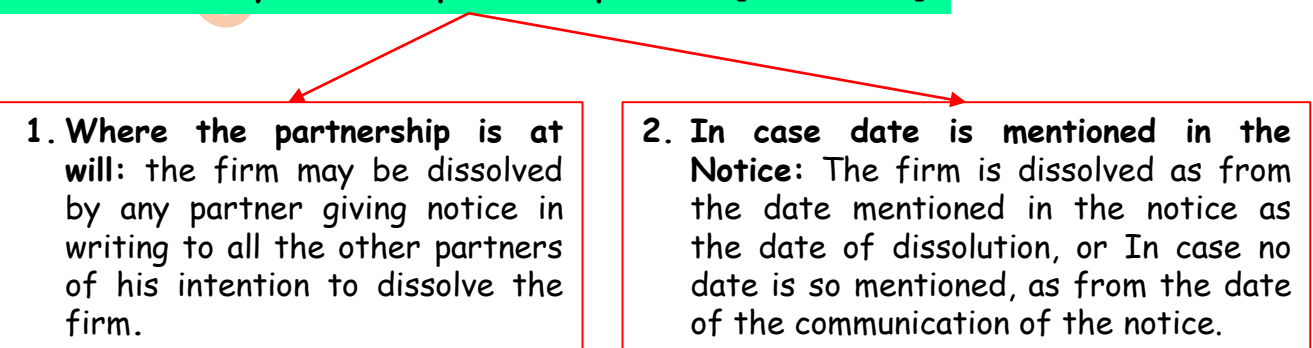
- By the adjudication of all the partners or of all the partners but one as insolvent,
Or
- By the happening of any event which makes it unlawful for the business of the firm to be carried on or for the partners to carry it on in partnership.

C. Dissolution on the happening of certain contingencies [Section 42]

Subject to contract between the partners, a firm can be dissolved on the happening of any of the following contingencies:



D. Dissolution by notice of partnership at will [Section 43]





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2. DISSOLUTION BY THE COURT (SECTION 44)

Court may, at the suit of the partner, dissolve a firm on any of the following ground

- a. **Insanity/Unsound Mind:** When a partner other than a sleeping partner has become of unsound mind, other partners or next friend of insane partner may file a suit to dissolve the firm. The courts may dissolve the firm on the basis of such suit.
- b. **Permanent incapacity:** When a partner, other than the partner filing the suit, has become permanently incapable of performing his duties as a partner, then the court may dissolve the firm.
- c. **Misconduct:** Where a partner, other than the partner filing the suit, is guilty of conduct which unreasonably affects the business of the firm, the courts may order dissolution of the firm, giving regard to the nature of the business.
- d. **Persistent breach of agreement:** When a partner wilfully or continuously commits breach of agreements relating to the management of the affairs of the firm or conduct of the business, then the courts may dissolve the firm at the instance of any of the partners.

Following comes into the category of breach of contract:

- ✓ Embezzlement
- ✓ Keeping erroneous accounts
- ✓ Holding more cash than allowed
- ✓ Refusal to show accounts despite repeated requests.

- e. **Transfer of interest:** Where a partner has transferred whole of his interest to a third party or has allowed his share to be charged or sold by the court for recovery of arrears of land revenue due by him, the courts may dissolve the firm at the instance of any other partner.
- f. **Continuous/Perpetual losses:** Where the business of the firm cannot be carried on except at a loss in future also, the court may order its dissolution.
- g. **Just and Equitable grounds:** Where the court considers any other ground just and equitable for dissolution of the firm, it may dissolve the firm. The following are the cases of just and equitable grounds :
 - i. Deadlock in the management
 - ii. Where the partners are not in talking terms between them
 - iii. Loss of substratum
 - iv. Gambling by a partner on a stock exchange.



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CONSEQUENCES OF DISSOLUTION (Section 45-55)

Liability for acts of partners done after dissolution [Section 45]

This provision has two objectives

It seeks to protect third parties dealing with the firm who had no notice of priordissolution

It also seeks to protect partners of a dissolved firm from liability towards thirdparties

Exceptions - Even where notice of dissolution has not been given, there will be no liability for subsequent acts in the case of-

- The estate of a deceased partner
- An insolvent partner, or
- A dormant partner

Right of partners to have business wound up after dissolution [Section 46]

On the dissolution of a firm every partner or his representative is entitled, as against all the other partners or their representative -

To have the property of the firm applied in payment of the debts and liabilities of thefirm,

And

To have the surplus distributed among the partners or their representatives according to their rights

Continuing authority of partners for purposes of winding up [Section 47]

After the dissolution of a firm the authority of each partner to bind the firm, and the other mutual rights and obligations of the partners, continue so far as may be necessary

- To wind up the affairs of the firm and
- To complete transactions begun but unfinished at the time of the dissolution, but not otherwise.

However, the firm is in no case bound by the acts of a partner who has been adjudicated insolvent.



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Mode of Settlement of partnership accounts [Section 48]

In settling the accounts of a firm after dissolution, the following rules shall, subject to agreement by the partners, be observed:-

- i. Losses, including deficiencies of capital, shall be
 - paid first out of profits,
 - next out of capital, and,
 - lastly, if necessary, by the partners individually in the proportions in which they were entitled to share profits
- ii. The assets of the firm, including any sums contributed by the partners to make up deficiencies of capital, must be applied in the following manner and order :
 - a. paying the debts of the firm to third parties
 - b. paying to each partner rateably what is due to him from capital
 - c. paying to each partner rateably what is due to him on account of capital
 - d. the residue, if any, shall be divided among the partners in the proportions in which they were entitled to share profits.

Mode of Settlement of partnership accounts [Section 48]

Where there are joint debts due from the firm and also separate debts due from any partner:

Property of the Firm

- **First** : Applied in the first instance in payment of the debts of the firm
- **Any Surplus** : Each partner's share applied to payment of his separate debt or paid to him.

Separate property of any partner

- **First** : Applied in payment of his separate debts
- **Any Surplus** : Applied in the payment of debts of the firm.



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Chapter-5 : THE LIMITED LIABILITY PARTNERSHIP ACT, 2008

Introduction

Short Title ,Extent, Commencement & Application

Commencement of the Act

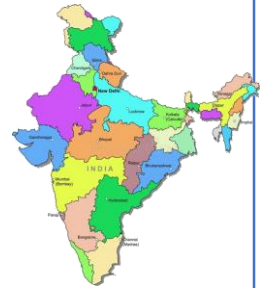
- The Ministry of Law and Justice on 9th January 2007 notified the Limited Liability Partnership Act, 2008.
- The **Parliament** passed the Limited Liability Partnership **Bill** on **12th December 2008** and the **President** of India has **assented** the Bill on **7th January 2009**.

Short title of the Act

- **The** Limited Liability Partnership Act, 2008 (the "LLP Act, 2008").

Extent to the applicability of the Act

- The Act shall be extend to the whole India



Purpose of the Act

- Act has been enacted to make provisions for the formation and regulation of Limited Liability Partnerships and for matters connected there with or incidental thereto.

Structure of the Act

The LLP Act, 2008 has 81 sections and 4 schedules (section 81 is now omitted with effect from 1st April 2022)

First Schedule	Deals with mutual rights and duties of partners and limited liability partnership and its partners where there is absence of a formal agreement amongst them.
Second Schedule	Deals with conversion of a firm into LLP.
Third Schedule	Deals with conversion of a private company into LLP.
Fourth Schedule	Deals with conversion of unlisted public company into LLP.

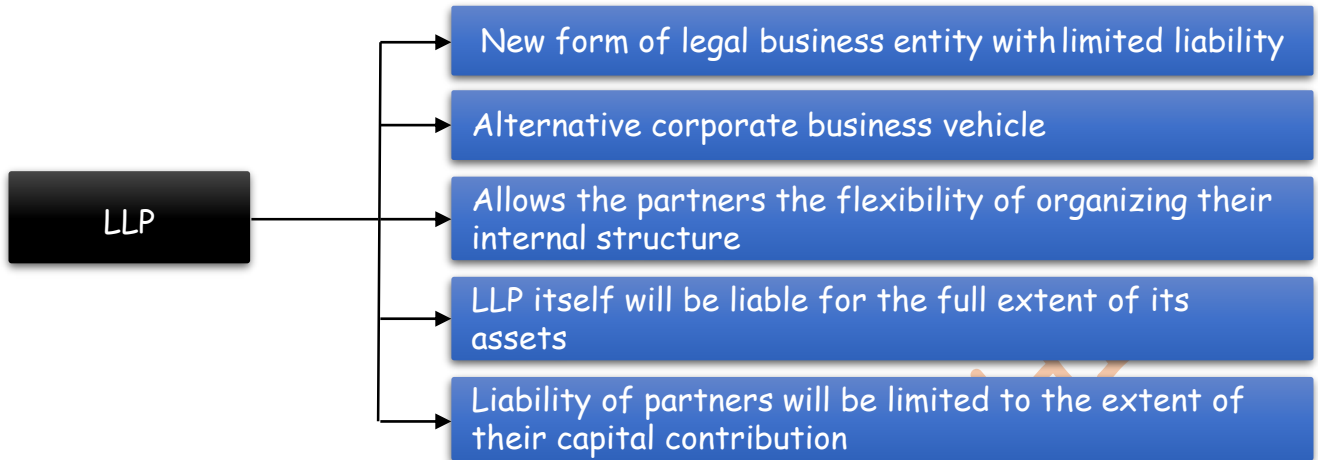


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Limited Liability Partnership Meaning and Concept



Section 2(d)

Body Corporate

It means a company as defined in section 3 of the Companies Act, 1956 (now Companies Act, 2013) and includes

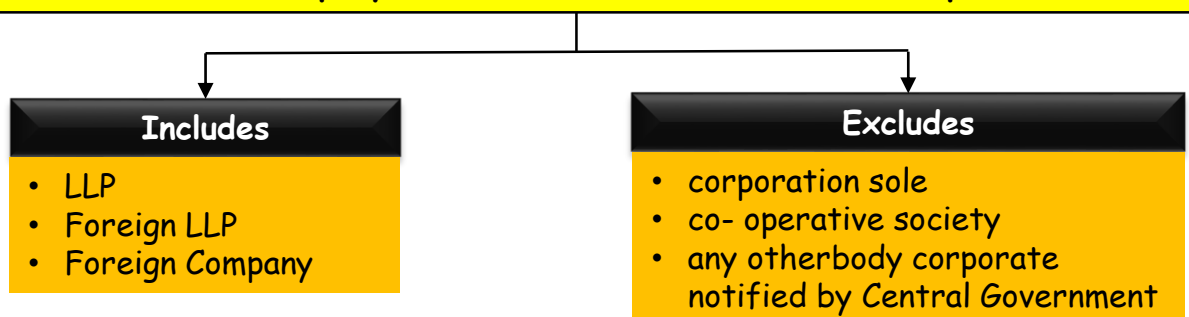
- a LLP registered under this Act;
- a LLP incorporated outside India; and
- a company incorporated outside India,

but does not include—

- a corporation sole;
- a co-operative society registered under any law for the time being in force; and
- any other body corporate (not being a company as defined in **clause (20) of section 2 of the Companies Act, 2013** or a limited liability partnership as defined in this Act), which the Central Government may, by notification in the Official Gazette, specify in this behalf.

Body Corporate

Means : It means a company as defined in section 3 of the Companies Act, 2013





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**Section
2(1)(e)**

Business

"Business" includes every trade, profession, service and occupation except any activity which the Central Government may, by notification, exclude.

**Section
2(1)(j)**

Designated Partner

"Designated partner" means any partner designated as such pursuant to section 7

**Section
2(1)(k)**

Entity

"Entity" means any body corporate and includes, for the purposes of sections 18, 46, 47, 48, 49, 50, 52 and 53, a firm setup under the Indian Partnership Act, 1932.

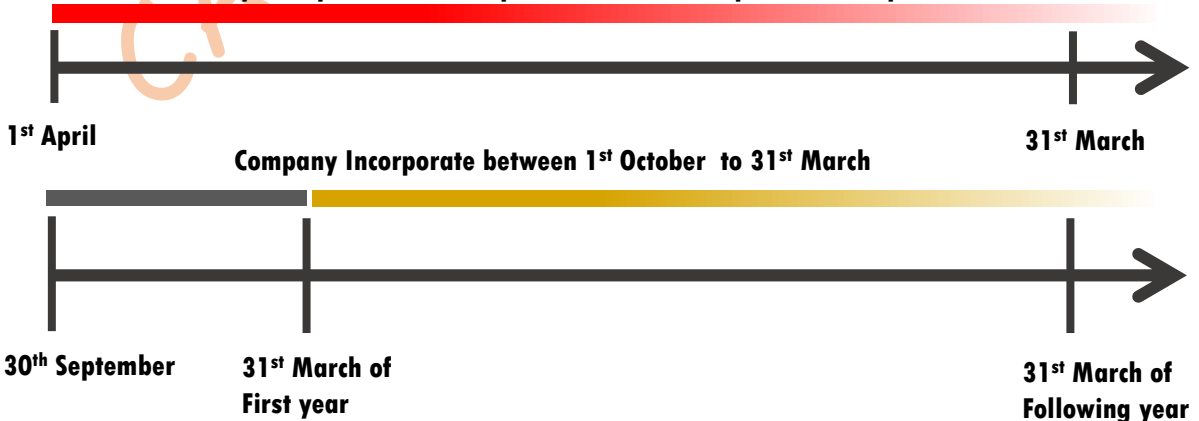
**Section
2(1)(l)**

Financial Year

- ✓ "Financial year", in relation to a LLP, means the period from the 1st day of April of a year to the 31st day of March of the following year.
- ✓ However, in the case of a LLP incorporated after the 30th day of September of a year, the financial year may end on the 31st day of March of the year next following that year.

Analysis of Section 2(1)(l)

LLP Already Incorporated or Incorporate between 1st April to 30th September



Financial Year



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**Section
2(1)(m)**

Foreign LLP

It means a LLP formed, incorporated or registered outside India which establishes a place of business within India.

**Section
2(1)(n)**

Limited Liability Partnership

Limited Liability Partnership means a partnership formed and registered under this Act.

**Section
2(1)(o)**

Limited Liability Partnership Agreement

- ✓ It means any written agreement between the partners of the LLP or between the LLP and its partners which determines the mutual rights and duties of the partners and their rights and duties in relation to that LLP.
- ✓ The First Schedule shall be applicable for all matters not covered by the Agreement w.r.t the mutual rights and duties of the partners and their rights and duties in relation to the LLP.

**Section
2(1)(q)**

Partner

Partner, in relation to a LLP, means any person who becomes a partner in the LLP in accordance with the LLP agreement.

**Section
2(1)(ta)**

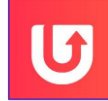
Small Limited Liability Partnership

It means a limited liability partnership-

- i. the contribution of which, does not exceed ₹ 25 Lakhs or such higher amount, not exceeding ₹ 5 crore, as may be prescribed; and
- ii. the turnover of which, as per the Statement of Accounts and Solvency for the immediately preceding financial year, does not exceed ₹ 40 lakh rupees or such higher amount, not exceeding ₹ 50 crore, as may be prescribed or
- iii. which meets such other requirements as may be prescribed, and fulfils such terms and conditions as may be prescribed



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Small Limited Liability Partnership [Section 2(ta)]

Contribution of which does not exceed ₹ 25 lakhs or such higher amount but not exceeding ₹ 5 Crore

And

Turnover of which does not exceed ₹40 lakhs or such higher amount but not exceeding ₹ 50 Crore

Or

Meets such other requirements as may be prescribed, and fulfils such terms and conditions as may be prescribed

Non-applicability of the Indian Partnership Act, 1932 (Section 4): Save as otherwise provided, the provisions of the Indian Partnership Act, 1932 shall not apply to a LLP.

Partners [Section -5]

- Any **individual** or **body corporate** may be a partner in a LLP.
- However, an individual shall not be capable of becoming a partner of a LLP if
 - a. he has been found to be of **unsound mind** by a Court of competent jurisdiction and the finding is in force or
 - b. he is an **undischarged insolvent**
 - c. he has applied to be **adjudicated as an insolvent** and his application is pending.

Following persons can become partner in LLP



i. Individuals (Resident Indians including Non Resident Indians & Overseas Citizen of India as well as foreign nationals)

ii. Limited Liability Partnerships

iii. Companies (including foreign companies)

iv. Foreign Limited Liability Partnerships

v. Limited Liability Partnership incorporated outside India

vi. Foreign Companies



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Minimum Member of Partners [Section -6]

LLP shall have at least 2 partners

Is number of
Partners fall
below 2 ?

Yes

LLP carries on
business more than
6 months with such
reduced number of
partners

Consequences

person who is only partner of the LLP during that time
shall be **personally liable** for the **payment of the
whole obligations** LLP during that time period.

Designated Partners [Section -7]

LLP shall have at least
2 designated partners
at least one of them
shall be Resident in
India

If all the partners are
bodies corporate / One or
more individuals and bodies
corporate

least **two individuals** who **are
partners of such LLP or
nominees of such bodies
corporate**

act as designated partners

'resident of India' means
a person who has stayed
in India
for a period of not less
than 120 days during the
immediately preceding
one year.

CHARACTERISTIC OF LLP

Body
Corporate

Perpetual
Succession

Separate legal
entity

Mutual
Agency

LLP
Agreement

Artificial
Legal Person

Common Seal

Limited
Liability

Management
of Business

Minimum and
maximum
number of
members

Business for
Profit only

Investigation

Compromise
or Agreement

Conversion
into LLP

Foreign LLPs

E-filing of
documents



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Characteristic of LLP

LLP is a Body corporate [Section 2(1)(d) & 3]

- LLP is a **body corporate** formed and incorporated under this Act and is a **legal entity separate from that of its partners** and shall have **perpetual succession**.
- Therefore, any change in the partners of a LLP shall not affect the existence, rights or liabilities of the LLP.
- **Section 3** :- LLP is a body corporate formed and incorporated under this Act and is a legal entity separate from that of its partners.

Perpetual Succession

- The LLP can continue its existence irrespective of changes in partners.
- **Death, insanity, retirement or insolvency of partners has no impact on the existence of LLP**
- **It is capable of entering into contracts and holding property in its own name.**

Separate Legal Entity

- The LLP as a separate legal entity, is liable to the full extent of its assets but liability of the partners is limited to their agreed contribution in the LLP
- In other words, creditors of LLP shall be the creditors of LLP alone.

Mutual Agency

- No partner is liable on account of the independent or un-authorized actions of other partners, thus individual partners are shielded from joint liability created by another partner's wrongful business decisions or misconduct.
- All partners will be the agents of the LLP alone
- No one partner can bind the other partner by his acts.

LLP Agreement

- Mutual rights and duties of the partners within a LLP are governed by an agreement between the partners.
- The Act provides flexibility to partners to make the agreement as per their choice.
- In absence of such agreement the rights and duties of partners are governed by The First Schedule of the LLP Act, 2008.



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Artificial Legal Person	<ul style="list-style-type: none"> • A LLP is an artificial person because it is created by a legal process and is clothed with all rights of an individual • It can enter into contracts in its own name, hold property in its name, open a bank account etc. • A LLP is invisible, intangible, immortal but not fictitious because it really exists.
Common Seal	<ul style="list-style-type: none"> • A LLP being an artificial person can act through its partners and designated partners. LLP may have a common seal, if it decides to have one. • Thus, it is not mandatory for a LLP to have a common seal. • It shall remain under the custody of some responsible official and it shall be affixed in the presence of at least 2 designated partners of LLP.
Limited Liability	<ul style="list-style-type: none"> • Section 26 :- The liability of partners will be limited to their agreed contribution in the LLP, • unlike a normal partnership firm where the liability of the partners is unlimited and extends to their personal assets.
Management of Business	<ul style="list-style-type: none"> • The partners in the LLP are entitled to manage the business of LLP. But only the designated partners are responsible for legal compliances.
Minimum and Maximum number of Partners	<p>Minimum</p> <ul style="list-style-type: none"> • Every LLP shall have least two(2) partners and • shall also have at least 2 individuals as designated partners of whom at least one shall be resident in India. <p>Maximum</p> <ul style="list-style-type: none"> • There is no maximum limit on the partners in LLP.
Business for Profit Only	<ul style="list-style-type: none"> • The essential requirement for forming LLP is carrying on a lawful business with a view to earn profit. • Thus, LLP cannot be formed for charitable or non-economic purpose.
Investigation	<ul style="list-style-type: none"> • The Central Government shall have powers to investigate the affairs of an LLP by appointment of competence authority for the purpose.
Compromise or Arrangement	<ul style="list-style-type: none"> • Any compromise or agreements including merger and amalgamation of LLPs shall be in accordance with the provisions of the LLP Act, 2008.



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Conversion into LLP	<ul style="list-style-type: none"> A firm, private company or an unlisted public company would be allowed to be converted into LLP in accordance with the provisions of LLP Act, 2008.
E-Filing of Documents	<ul style="list-style-type: none"> Every form or application of document required to be filed or delivered under the act and rules made thereunder, shall be filed in computer readable electronic form on its website www.mca.gov.in and authenticated by a partner or designated partner of LLP by the use of electronic or digital signature.
Foreign LLPs [Section 2(1)(m)]	<ul style="list-style-type: none"> A limited liability partnership formed, incorporated, or registered outside India which established as place of business within India". Foreign LLP can become a partner in an Indian LLP.

Advantage of LLP FORM

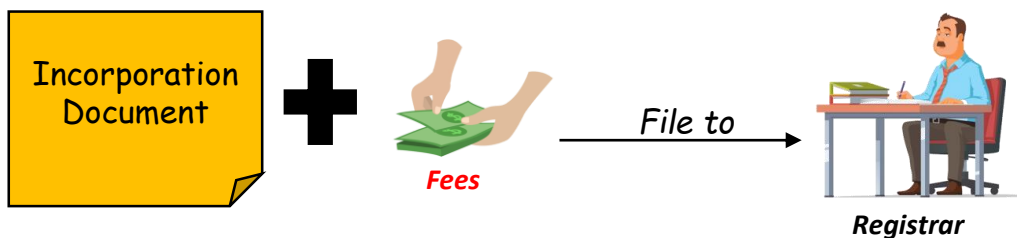
- LLP form is a form of business model which
 - is organized and operates on the basis of an agreement.
 - Provides flexibility without imposing detailed legal and procedural requirements.
- Easy to form
- All partners enjoy limited liability
- Flexible capital structure
- Easy to dissolve

Incorporation Document [Section -11]

Step -1

Two or more persons associated for carrying on a **lawful business** with a view to profit shall subscribe their names to an incorporation document

Step -2





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Statement to be filed

Step -3

- ✓ A statement, in a prescribed format, must be provided by either an advocate, a Company Secretary, a Chartered Accountant, or a Cost Accountant who is involved in forming the LLP, as well as by any individual who has signed the incorporation document.
- ✓ This statement affirms that all obligations outlined in this Act and the associated rules have been fulfilled concerning the LLP's incorporation and related processes.

Incorporation Documents

- Be in a Prescribed Form
- Shall state
 - ✓ Name of LLP
 - ✓ Proposed business of LLP
 - ✓ Address of Registered office of LLP
 - ✓ **name and address of each of the persons** who are to be partners of the LLP on incorporation
 - ✓ **name and address** of the persons who are to be **designated partners** of the LLP on incorporation
 - ✓ such other information concerning the proposed LLP as may be prescribed.

Penalty on False Statement

If a person makes a statement as discussed above which he-

(a) **Knows to be false;** or

(b) **Does not believe to be true,** shall be punishable with

- Imprisonment for a term which may extend to 2 years and
- Fine which shall not be less than Rs. 10,000 but which may extend to Rs. 5,00,000.

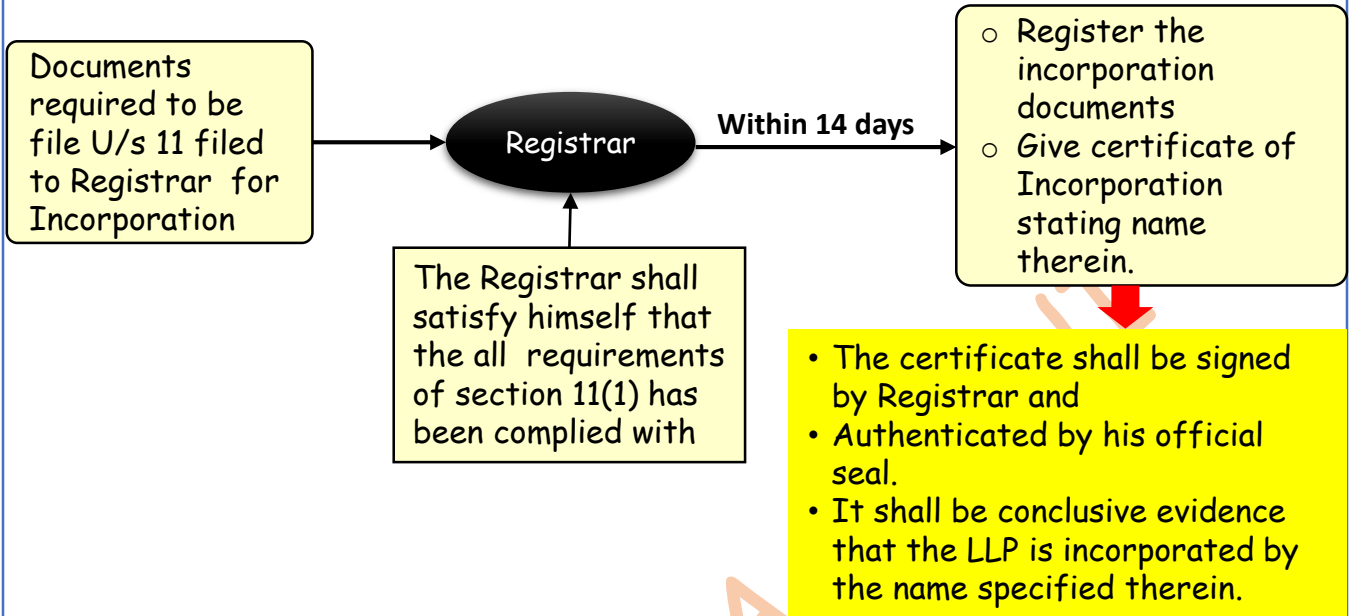


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Incorporation of Registration [Section -12]



Registered Office of LLP & Change Therein [Section -13]

1. Every (LLP) is required to maintain a registered office. This is the designated address for receiving all official communications and notices related to the LLP.

2. A document can be delivered to LLP/Partner/ Designated Partner through

- Post under a certificate of posting or
- Registered Post
- Any other manner(as prescribed)

At registered office



3. LLP may change its registered office and file a notice to Registrar for such change.

4. Penalty on contravention of section 13:

LLP and every partner → ₹ 500 per day subject to maximum ₹50000/-



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Effect of Registration [Section -14]

On Registration, LLP shall by its name, be capable of

I . Suing and being sued



III . Having a common seal, if it decides to have one

II . Acquiring, owning, holding and developing or disposing of property, whether movable or immovable, tangible or intangible

IV . Doing and suffering other acts and things as bodies corporate may lawfully do and suffer

Name [Section -15]

1. Every limited liability partnership shall have either the words "limited liability partnership" or the acronym "LLP" as the last words of its name.

2. No LLP shall be registered by a name which, in the opinion of the Central Government is-

a. undesirable

b. identical or too nearly resembles to that of any other LLP or a company or a registered trademark of any other person under the Trade Marks Act, 1999.

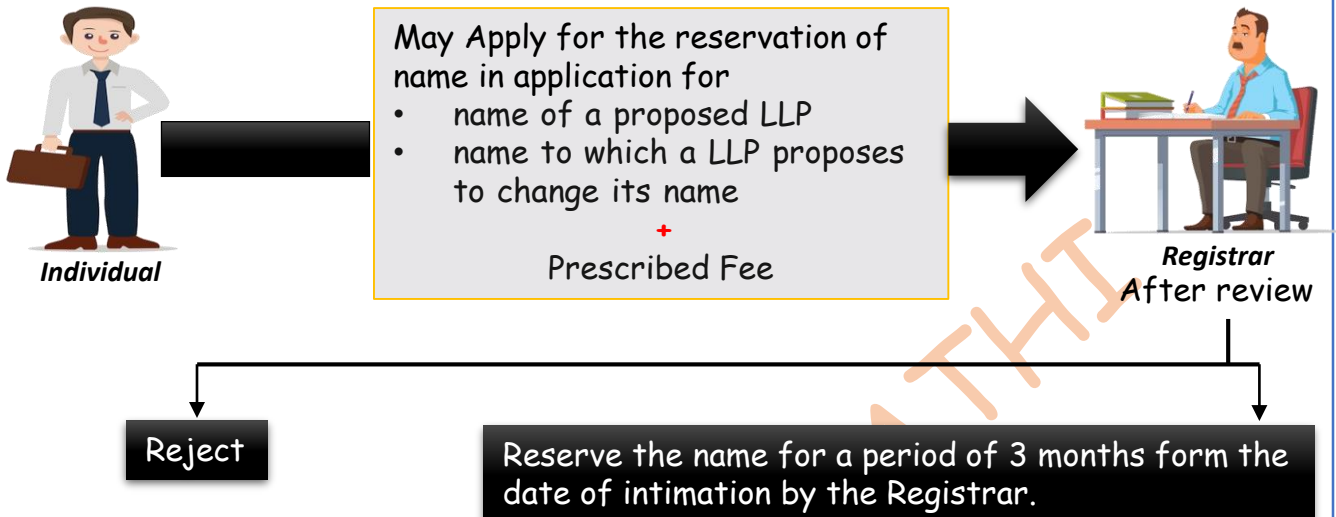


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Reservation of Name [Section -16]



Rectification of Name of LLP [Section -17]

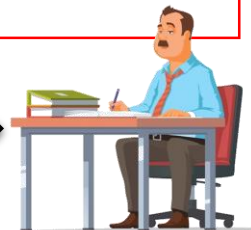
1. If through inadvertence, or otherwise the **name is identical or too nearly resembling** an existing company or LLP name, then Central Government may order the company to change name **within 3 months**

Or

2. If Application is made to Central Government from registered proprietor of Trade Mark(Registered Under Trade Mark Act 1999) , within 3 years of incorporation or change of name or registration, stating that name of a LLP is identical or nearly resembling their trademark, then Central Government may order the LLP to change name **within 3 months**.

If LLP changes its name or obtain a new name, it shall notify the such changes + Order of Central Government

Within 15 days to



Registrar

Of change in the certificate of incorporation, such LLP shall change its name in the LLP agreement.

within 30 days

Shall carry out necessary changes in Certificate of Incorporation



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If LLP is in default in complying with any direction given under sub-section (1),

- The Central Government shall allot a new name to the company in such manner as may be prescribed and
- The Registrar shall enter the new name in the register of companies in place of the old name and issue a fresh certificate of incorporation with the new name, which the company shall use thereafter.

Note : Provided that nothing in this sub-section shall prevent a LLP from subsequently changing its name.

Difference with Other Forms of Organization

	Basis	LLP	Partnership firm
1.	Regulating Act	The Limited Liability Partnership Act, 2008.	The Indian Partnership Act, 1932.
2.	Body corporate	It is a body corporate.	It is not a body corporate,
3.	Separate legal entity	It is a legal entity separate from its members.	It is a group of persons with no separate legal entity.
4.	Creation	It is created by a legal process called registration under the LLP Act, 2008.	It is created by an agreement between the partners.
5.	Registration	Registration is mandatory. LLP can sue and be sued in its own name.	Registration is voluntary. Only the registered partnership firm can sue the third parties.
6.	Perpetual succession	The death, insanity, retirement or insolvency of the partner(s) does not affect its existence of LLP. Members may join or leave but its existence continues forever.	The death, insanity, retirement or insolvency of the partner(s) may affect its existence. It has no perpetual succession.
7.	Name	Name of the LLP to contain the word limited liability partners (LLP) as suffix.	No guidelines. The partners can have any name as per their choice.
8.	Liability	Liability of each partner limited to the extent to agreed contribution except in case of willful fraud.	Liability of each partner is unlimited. It can be extended up to the personal assets of the partners.



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9.	Mutual agency	Each partner can bind the LLP by his own acts but not the other partners.	Each partner can bind the firm as well as other partners by his own acts.
10.	Designated partners	At least two designated partners and at least one of them shall be resident in India.	There is no provision for such partners under the Partnership Act, 1932.
11.	Common seal	It may have its common seal as its official signatures.	There is no such concept in partnership
12.	Legal compliances	Only designated partners are responsible for all the compliances and penalties under this Act.	All partners are responsible for all the compliances and penalties under the Act.
13.	Annual filing of documents	LLP is required to file: (i) Annual statement of accounts (ii) Statement of solvency (iii) Annual return with the registration of LLP every year.	Partnership firm is not required to file any annual document with the registrar of firms.
14.	Foreign partnership	Foreign nationals can become a partner in a LLP.	Foreign nationals cannot become a partner in a partnership firm.
15.	Minor as partner	Minor cannot be admitted to the benefits of LLP.	Minor can be admitted to the benefits of the partnership with the prior consent of the existing partners.

Distinction between LLP and Limited Liability Company

	Basis	LLP	Limited Liability Company
1.	Regulating Act	The LLP Act, 2008.	The Companies Act, 2013.
2.	Members/Partners	The persons who contribute to LLP are known as partners of the LLP.	The persons who invest the money in the shares are known as members of the company.
3.	Internal governance structure	The internal governance structure of a LLP is governed by contract agreement between the partners.	The internal governance structure of a company is regulated by statute (i.e., Companies Act, 2013).



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4.	Name	Name of the LLP to contain the word "Limited Liability partnership" or "LLP" as suffix.	Name of the public company to contain the word "limited" and Pvt. Co. to contain the word "Private limited" as suffix.
5.	No. of members/partners	Minimum – 2 members Maximum – No such limit on the members in the Act. The members of the LLP can be individuals/or body corporate through the nominees.	Private company: Minimum – 2 members Maximum 200 members Public company: Minimum – 7 members Maximum – No such limit on the members. Members can be organizations, trusts, another business form or individuals.
6.	Liability of members/partners	Liability of a partners is limited to the extent of agreed contribution in case of intention is fraud.	Liability of a member is limited to the amount unpaid on the shares held by them.
7.	Management	The business of the company managed by the partners including the designated partners authorized in the agreement.	The affairs of the company are managed by board of directors elected by the shareholders.
8.	Minimum number of directors/designated partners	Minimum 2 designated partners.	Pvt. Co. – 2 directors Public co. – 3 directors



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Chapter 6 : Companies Act 2013

The Companies Act 2013

was enacted to consolidate and amend the law relating to the companies

was preceded by the Companies Act, 1956

contains 470 sections and seven schedules.

has been divided into 29 chapters.

aims to improve corporate governance, simplify regulations, strengthen the interests of minority investors and for the first time legislates the role of whistle-blowers

Company : Applicability of the Companies Act 2013

The Provisions of this Act shall apply to :-

- **Companies Registered under this act or earlier Act**
- **Insurance Companies** (except in so far as the said provisions are inconsistent with the provisions of the Insurance Act, 1938 or the Insurance Regulatory and Development Authority Act, 1999)
- **Banking Companies** (except in so far as the said provisions are inconsistent with the provisions of the Banking Regulation Act, 1949)
- **Companies producing/supplying electricity** (except in so far as the said provisions are inconsistent with the provisions of the Electricity Act, 2003)
- **Company regulated by special Act**, for the time being in force, (except in so far as the said provisions are inconsistent with the provisions of such special Act,)

and

- **Such body corporate, incorporated by any Act for the time being in force, as the Central Government may, by notification, specify in this behalf, subject to such exceptions, modifications or adaptation, as may be specified in the notification. Example:** Food Corporation of India (FCI), National Highway Authority of India (NHAI) etc.



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Company : Meaning and Its Features

According to Chief Justice Marshall

- "A corporation is an artificial being, invisible, intangible, existing only in contemplation of law.
- Being a mere creation of law, it possesses only those properties which the charter of its creation confers upon it, either expressly or as accidental to its very existence".

According to Professor Haney

"A company is an incorporated association, which is an artificial person created by law, having a separate entity, with a perpetual succession and a common seal."

Section 2(20) of Companies Act 2013

"Company means a company incorporated under this Act or under any previous company law".

Features of Company

1. Separate Legal Entity

- When a company is registered, it is clothed with a legal personality.
- It comes to have almost the same rights and powers as a human being.
- Its existence is distinct and separate from that of its members.
- A company can own property, have bank account, raise loans, incur liabilities and enter into contracts.

• It is at law, a person which is different from the subscribers to the memorandum of association.

• Even members can contract with company, acquire right against it or incur liability to it.
• **For the debts of the company, only its creditors can sue it and not its members.**

A member does not even have an insurable interest in the property of the company {Case : Macaura Vs. Northern Assurance Co. Limited (1925)}:

- ✓ **Fact of the Case :-** Macaura (M) was the holder of nearly all (except one) shares of a timber company. He was also a major creditor of the company. M insured the company's timber in his own name. The timber was lost in a fire. M claimed insurance compensation.
- ✓ **Held :-** The insurance company was not liable to him as no shareholder has any right to any item of property owned by the company, for he has no legal or equitable interest in them.



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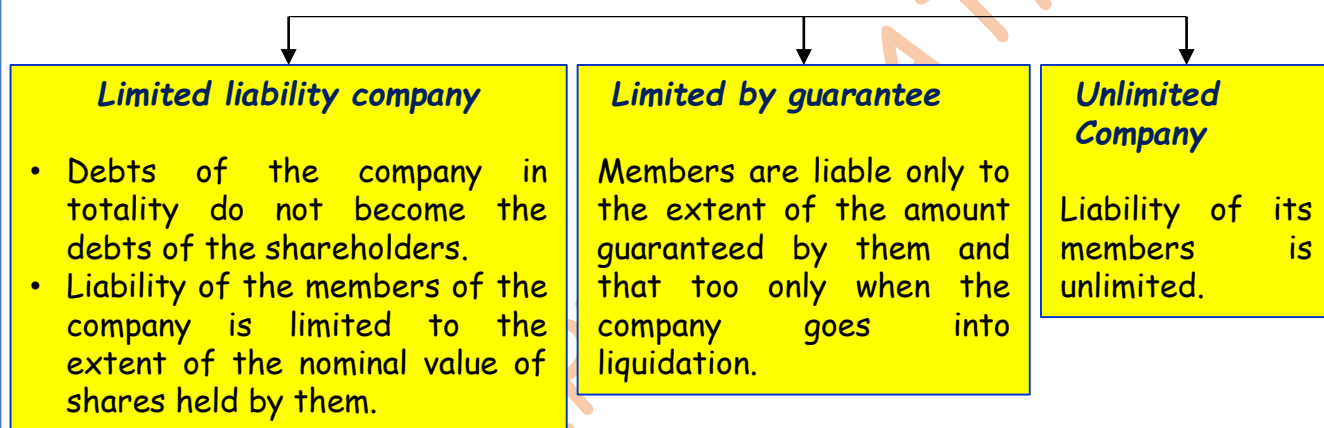
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2. Perpetual Secession

- Members may die or change, but the company goes on till it is wound up on the grounds specified by the Act.
- The shares of the company may change hands infinitely but that does not affect the existence of the company.
- Its existence is not affected by the death or insolvency of its members.

3. Limited Liability

The liability of a member depends upon the kind of company of which he is a member.



4. Artificial Legal Person

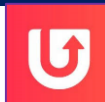
1. A company is an artificial person as it is created by a process other than natural birth. It is legal or judicial as it is created by law. It is a person since it is clothed with all the rights of an individual.
2. Further, the company being a separate legal entity can own property, have banking account, raise loans, incur liabilities and enter into contracts.
3. As the company is an *artificial person*, it can act only through some human agency, viz., directors.
4. Thus, a company is called an artificial legal person.

5. Common Seal

- Common seal is the official signature of a company, which is affixed by the officers and employees of the company on its every document.



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- The common seal is a seal used by a corporation as the symbol of its incorporation.
- However, the Companies Amendment Act, 2015 has made the common seal optional.

Corporate Veil Theory

- ❖ Members of a company are shielded from liability connected to the company's actions.
- ❖ If the company incurs any debts or contravenes any laws, the corporate veil concept implies that members should not be liable for those errors. In other words, they enjoy corporate insulation.
- ❖ Shareholders are protected from the acts of the company.

Salomon Vs. Salomon and Co Ltd. laid down the foundation of the concept of corporate veil or independent corporate personality.

Case Law: Salomon Vs. Salomon and Co Ltd.

Facts: Salomon incorporated a company named 'Salomon & Co. Ltd.', with seven subscribers consisting of himself, his wife, four sons and one daughter. This company took over the personal business assets of Salomon for £38,782 and in turn, Salomon took 20,000 shares of £1 each, debentures worth £10,000 of the company with charge on the company's assets and the balance in cash. His wife, daughter and four sons took up one £1 share each. Subsequently, the company went into liquidation due to general trade depression. The unsecured creditors to the tune of £7,000 contended that Salomon could not be treated as a secured creditor of the company, in respect of the debentures held by him, as he was the managing director of one-man company, which was not different from Salomon and the cloak of the company was a mere sham and fraud.

Judgement: It was held that upon incorporation; a company gets legality of its own and manage it. Even though the hands receiving the profits may be the same and the same person manage the company. The company in the eyes of law is not an agent of the people who own it or manage it therefore Salomon & Co. are separate person.

Hence, Salomon being a secured debenture holder is entitled to a repayment prior to other creditors.



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Lifting of Corporate Veil

- ❖ **Meaning of "Lifting the Veil"** :→ Looking behind the company as a legal person, i.e., disregarding the corporate entity and paying regard, instead, to the realities behind the legal facade.
- ❖ Where the *Courts ignore the company and concern themselves directly with the members or managers*, the corporate veil may be said to have been lifted.

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

1. To determine the character of the company [enemy or friend]

- Company does not have mind or conscience; therefore it cannot be a friend or a foe.
- It may be characterized as an enemy company if its affairs are under control of people of an enemy country.
- For this purpose, the court may determine the character of persons who are in charge of the affairs of the company.
- *Daimler Co. Ltd. vs. Continental Tyre & Rubber Co.*

2. To protect revenue/tax

- Where corporate entity is used to evade or circumvent tax, the Court can disregard the corporate entity.

Case Law: Dinshaw Maneckjee Petit

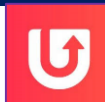
Facts: The assessee earned huge income by way of dividends and interest. So, he opened some companies and purchased their shares in exchange of his income by way of dividend and interest. This income was transferred back to assessee by way of loan.

Judgement: It was held that the company was not a genuine company at all but merely the assessee himself disguised under the legal entity of a limited company. Court decided that the private companies were a sham and the corporate veil was lifted to decide the real owner of the income.

Other Case Laws : Juggilal vs. Commissioner of Income Tax, S. Berendsen Ltd. vs. Commissioner of Inland Revenue



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3. To avoid a legal obligation

Where the courts find that there is avoidance of welfare legislation, it will be free to lift the corporate veil.

Case Law: Workmen of Associated Rubber Industry Ltd., v. Associated Rubber Industry Ltd.

Facts: 'A Limited' purchased shares of 'B Limited' by investing a sum of ₹4,50,000. The dividend in respect of these shares was shown in the profit and loss account of the company, year after year.

It was considered for the purpose of calculating the bonus payable to workmen of the company.

Sometime in 1968, the company transferred the shares of 'B Limited', to 'C Limited' a subsidiary, wholly owned by it. Thus, the dividend income did not find place in the Profit & Loss Account of 'A Limited', with the result that the surplus available for the purpose for payment of bonus to the workmen got reduced.

Judgement: 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. Thus, the Supreme Court brushed aside the separate existence of the subsidiary company.

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.

Case Law : Merchandise Transport Limited vs. British Transport Commission (1982)

Fact of the Case :

- ✓ A transport company wanted to obtain licenses for its vehicles, but could not do so if applied in its own name.
- ✓ It therefore formed a subsidiary company, and the application for license was made in the name of subsidiary.
- ✓ The vehicles were to be transferred to the subsidiary company.

Held : The parent and the subsidiary were one commercial unit and the application for licences was rejected.



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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.
- ✓ **Case Law: Gilford Motor Co. vs. Horne**

Classes of Companies Under The Act

Company Limited by shares {Section 2(22)}

- ❖ When the liability of the members of a company is limited by its memorandum of association to the amount (if any) unpaid on the shares held by them, it is known as a company limited by shares [Section 2(22)].
- ❖ For meeting the debts of the company, the shareholder may be called upon to contribute only to the extent of the amount, which remains unpaid on his shareholdings.
- ❖ His separate personal property cannot be used to meet the company's debt.

Company Limited by guarantee {Section 2(21)}

- ❖ The company having the liability of its members limited by the memorandum to such amount as the members may respectively undertake by the memorandum to contribute to the assets of the company in the event of its being wound up [Section 2(21)].
- ❖ The liability of the member of a company limited by guarantee is limited up to a stipulated sum mentioned in the memorandum. Members cannot be called upon to contribute beyond that stipulated sum.

Difference between both the Companies

In the case of company limited by guarantee : Members may be called upon to discharge their liability only after commencement of the winding up and only subject to certain conditions.

In the case of company limited by shares : members may be called upon to do so at any time, either during the company's life-time or during its winding up.



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The right of a guarantee company to refuse to accept the transfer by a member of his interest in the company is on a different footing than that of a company limited by shares.

The membership of a guarantee company may carry privileges much different from those of ordinary shareholders [Narendra Kumar Agarwal vs. Saroj Maloo (SC)].

Unlimited Company {Section 2(92)}

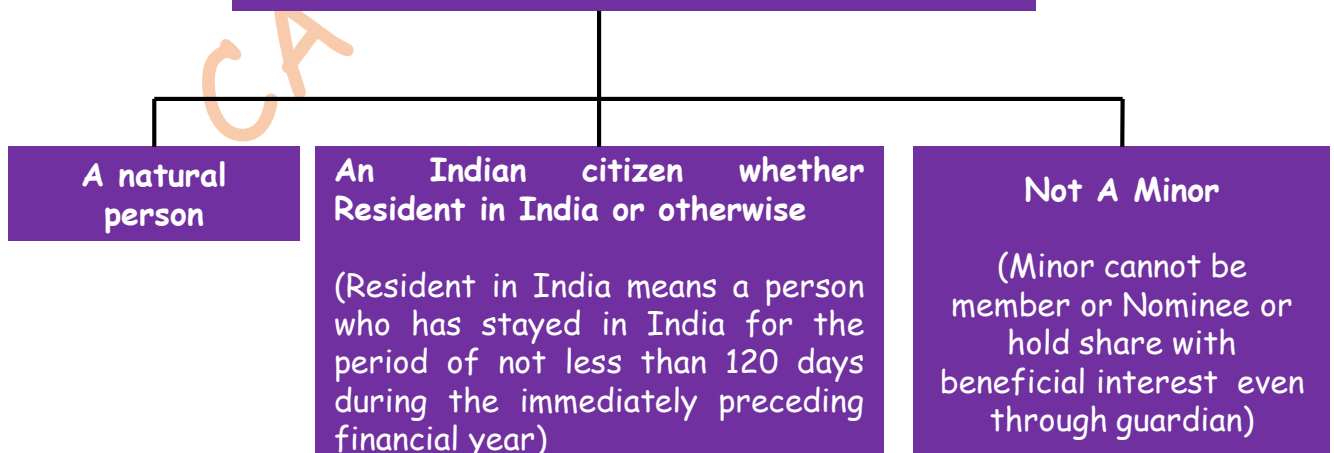
- A company not having any limit on the liability of its members [Section 2(92)].
- A company, the liability of a member ceases when he ceases to be a member.
- Liability of each member extends to the whole amount of the company's debts and liabilities, but he will be entitled to claim contribution from other members.
- In case the company has share capital, as long as the company is a going concern the liability on the shares is the only liability which can be enforced by the company.
- Member can be called upon to contribute only in the event of winding up of the Company.

One Person Company

PYQ May 2021, MTP May 2023, RTP Dec. 2023

- **Section 2(62)** : One Person Company (OPC) as a company which has only one person as a member.
- Such companies are permitted to be formed by The Companies Act, 2013 to encourage entrepreneurship and corporatization of business.
- It is formed as a Private Company [Section 3(1)(C)].

Qualification of Member/Nominee of OPC





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Name of Nominee shall be stated in memorandum

Written Consent of the Nominee shall be obtained

Nominee has a right to withdraw his consent

Member may change the nominee by giving notice

Natural person
Indian Citizen
Whether Resident* of India or not

Member and Nominee in only one OPC

No incorporation or conversion into Sec 8 Co.

No Non-Banking Financial Investment activities

Can be converted into Private or Public Company anytime after its incorporation

Private Company {Section 2(68)}

PYQ June 2019, MTP May 2024, RTP May 2022

Private Company

A company having a minimum paid-up share capital as may be prescribed

its Articles of Association
- Restricts transferability of shares
- Limits the number of members to 200

Prohibits invitation to public to subscribe to securities of the company.

Note : Nothing has been prescribed

In calculation of number of members the following things must be considered:

- Employees** who are also members are not to be considered
- Ex-employees** are not to be considered provided they had acquired shares while in employment.
- Joint Holders** are considered as **one**.

Small Company {Section 2(85)}

MTP May 2024, RTP 2024, PYQ June 2021, Nov 2022, May 2023.



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Means a Company, other than a Public Company-

Paid Up Share Capital

of which does not exceed **50 Lakhs Rupees** Or such higher amount as may be prescribed*, which shall not be more than 10 Crore Rupees

And

Turnover

of which as per Profit and Loss account for the immediately preceding financial year does not exceed **2 Crore Rupees** or Such higher amount as may be prescribed*, which shall not be more than 100 Crore Rupees.

*As per Rule 2(1)(t) of Companies (Specification of Definitions Details) Rules, 2014 **Paid up Capital** and **Turnover** of the **Small company** shall not exceed **Rupees 4 crores** and **Rupees 40 crores** respectively.

Provided that nothing in this clause shall apply to-

- A holding company or a subsidiary company
- A company registered under section 8
- A company or body corporate governed by any special Act.

Public Company {Section 2(71)}

- "Public company" means a company which—
 - is not a private company; and
 - has a minimum paid-up share capital, as may be prescribed:
- **Provided** that a company which is a subsidiary of a company, not being a private company, shall be deemed to be public company for the purposes of this Act even where such subsidiary company continues to be a private company in its articles
- According to section 3(1)(a), a company may be formed for any lawful purpose by seven or more persons, where the company to be formed is to be a public company.
- Is not a private company (Articles do not have the restricting clauses).
- Shares freely transferable.
- No minimum paid up capital requirement.
- Minimum number of members - 7.
- Maximum numbers of members - No limit.



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Holding Companies {Section 2(46)}

- A company is a holding company in relation to one or more other companies, means a company of which such companies are subsidiary companies.
- For the purposes of this clause, the expression "company" includes any body corporate.

Subsidiary Company {Section 2(87)}

Subsidiary company in relation to any other 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 [Section 2(87)].

Provided that such class or classes of holding companies as may be prescribed shall not have layers of subsidiaries beyond such numbers as may be prescribed.

- a. A company shall be deemed to be a subsidiary company of the holding company even if the control is of another subsidiary company of the holding company.
- b. The composition of a company's Board of Directors shall be deemed to be controlled by another company if that other company by exercise of some power can appoint or remove all or a majority of the directors.

Associate Company {Section 2(6)}

In relation to another company, means

- A company in which that other company has a significant influence, but which is not a subsidiary company of the company having such influence and includes a joint venture company.

Significant Influence

Means

control of at least twenty (21%) per cent of

- total voting power, or
- control of or
- participation in business decisions under an agreement

Joint Venture

Means

- a joint arrangement
- whereby the parties that have joint control of the arrangement
- have rights to the net assets of the arrangement



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"Total Share Capital"

Means

the aggregate of the -

- a. Paid-up equity share capital; and
- b. Convertible preference share capital.

Listed Company {Section 2(46)}

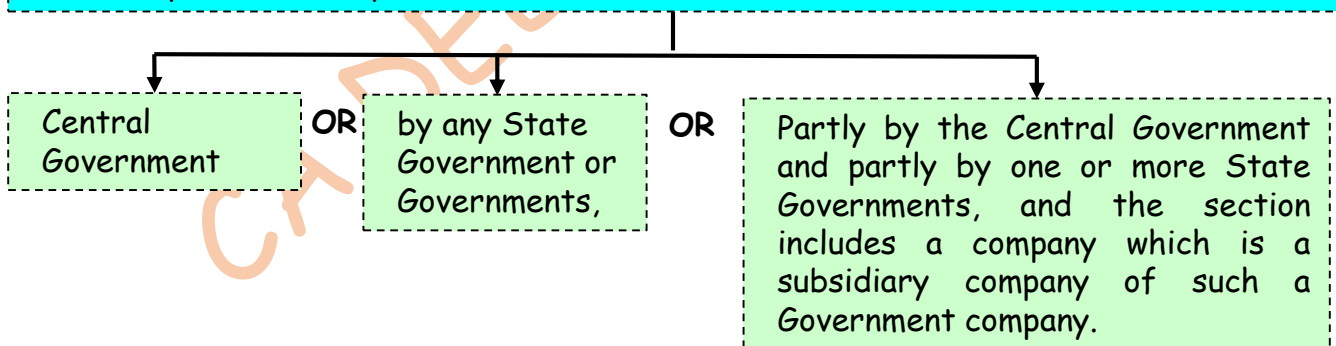
- it is a company which has any of its securities listed on any recognised stock exchange.
- Provided that such class of companies, which have listed or intend to list such class of securities, as may be prescribed in consultation with the Securities and Exchange Board, shall not be considered as listed companies.

Unlisted Company

Unlisted company means company other than listed company

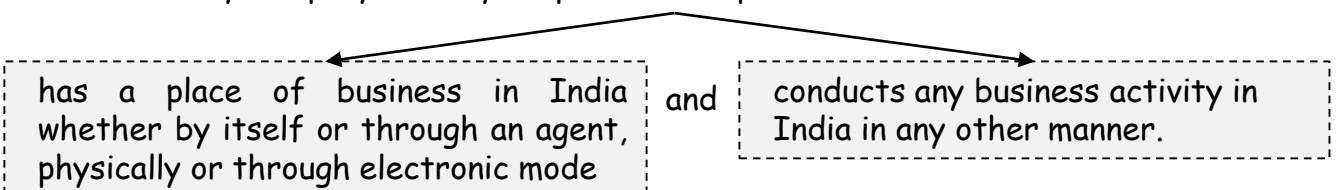
Government Company {Section 2(45)}

Government Company means any company in which not less than 51% of the paid-up share capital is held by-



Foreign Company {Section 2(42)}

It means any company or body corporate incorporated outside India which





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Formation of Companies with Charitable Objects etc. (Section 8 Company)

Objective of Formation

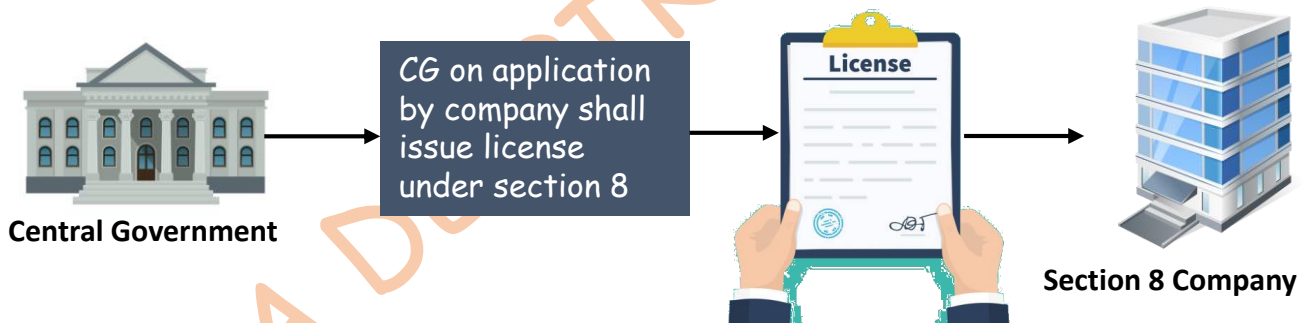
To promote the charitable objects of commerce, art, science, sports, education, research, social welfare, religion, charity, protection of environment etc.

Intends to apply its profit in
✓ promoting its objects
and
✓ prohibiting the payment of any dividend to its members.

Section 8 companies are

FICCI,
ASSOCHAM,
National Sports

Where these conditions specified above are satisfied, the Central Government may register such person or association of persons as a company with limited liability without the addition of words 'Limited' or 'Private limited' to its name, by issuing licence on such conditions as it deems fit.



Revocation of License by Central Government may be done if

Section 8 Conditions Contravened

License conditions contravened

Affairs of the company conducted fraudulently against public policy or against the objects



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Where a licence is revoked the Central Government shall direct to company

Convert its status and change its name (Put 'Limited' or 'Private Limited' after its name)

Wind Up

Amalgamate with any other company having similar objective.

Punishment for Contravention of section 8

Company

Not less than Rs.10 lakhs which may extend to RS.1 Crore

Officer in default

- Not less than Rs.25 thousand which may be extend to RS.25 lakhs
- Provided that when it is proved that the affairs of the company were conducted fraudulently, every officer in default shall be liable for action under section 447.

Dormant Company (Section-455)

Where a company is formed and registered under this Act for

- ✓ A future project or
- ✓ To hold an asset or
- ✓ Intellectual property and
- ✓ Has no significant accounting transaction,

such a company or an inactive company may make an application to the Registrar in such manner as may be prescribed for obtaining the status of a dormant company.

Dormant Company Formed & Registered under this act



Future Project



Hold an Asset



Intellectual Property



Has no significant accounting transaction



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Inactive Company

Inactive Company Means

- a) A company which has **not been carrying on any business or operation** or
- b) A company which has **not made any significant accounting transaction during the last 2 financial years;** or
- c) A company which has **not filed financial statements and annual returns during the last 2 financial years.**

Nidhi Company

Company which has been **incorporated as a nidhi** with the object of

- **Cultivating the habit of thrift (Cost Cutting) and**
- **Saving amongst its members, receiving deposits from and lending to**
- **Its members only for their mutual benefit and which complies with such rules as are prescribed by the Central Government for regulation of such class of companies.**

Public Financial Institutions (PFI)

Section 2(72)

Following institutions are to be regarded as Public Financial Institutions

The life Insurance Corporation of India established under the Life Insurance Corporation Act 1956

The Infrastructure Development Finance Company Limited

Specified company referred to in the Unit Trust of India (Transfer of Undertaking and Repeal Act 2002)

Institutions notified by the Central Government under section 4A(2) of the Companies Act 1956 so repealed under section 465 of the Act

Such Other institutions as may be notified by the Central Government in consultation with the Reserve Bank of India



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Conditions for an institution to be notified as PFI

1. Established or constituted by or under any Central or State Act or other than this act or the previous Companies Law ; or

2. At least 51% of the paid up share capital is held by the CG or by SG or partly by CG and partly by one or more SG.

Mode of Registration/ Incorporation of Company



Promoters
Section 2(69)

A

Who has been named as such in a prospectus

Or

Is identified by the company in the annual return referred to in section 92

B

Who has control over the affairs of the company directly or indirectly

C

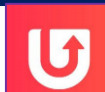
On whose advice, direction or instructions the Board of Directors is accustomed to act.

Basic requirements with respect to the constitution of Company(Section-3)

Difference	Private Company	Public Company	One Person Company
Minimum shareholders	2	7	1
Maximum shareholders	200	Unlimited	1
Minimum Directors	2	3	1
Maximum Directors	15 (Can be exceeded by Passing special resolution)	15 (Can be exceeded by passing special resolution)	15 (Can be exceeded by passing special resolution)
Transferability of Shares	Restricted	Freely Transferable	Restricted



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FORMATION OF COMPANY



Seven to form
Public Company



Two to form
Private Company



One to form One Person Company + A nominee

The above companies can either be

- Limited by shares
- Limited by Guarantee
- Unlimited liability companies

Incorporation of a Company (Section -7)

1. Filing of Documents to Registrar of company

- Signed MOA & AOA by all subscriber
- Declaration that all requirements of the act & rules have been satisfied by
 - Person named in AOA (i.e. Director, Manager)
 - Persons engaged in formation of company (i.e. Advocate, CA/CS/Cost Accountant)
- Declaration from subscriber to MOA & first Directors stating that:
 - They are not convicted of any offence in connection with formation of company
 - Not guilty of misfeasance/ breach under this or previous Companies Act during last five years
 - All documents & information contained in term are correct as per their knowledge and belief.
- Address for correspondence till registered office is established.
- Particulars and identity proof of subscribers to MOA, first Directors of AOA.
- Particulars of the interests of first Directors in AOA in other firms/ bodies corporate along with consent to act as directors of the company
- Prescribed Fees



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2. On the basis of documents and information filed the Registrar shall issue a **Certificate of Incorporation** in prescribed form and allot a **Corporate Identity Number (CIN)** to the Company which shall be included in Certificate of Incorporation.

3. The company shall maintain and preserve at its registered office copies of all documents and information as originally filed till its dissolution under this Act.

4. If any person knowingly provides false information or suppress any material fact liability U/S 447 attracted.

5. If a company is already incorporated by furnishing any false or incorrect information or representation or by suppressing any material fact application may be filed to Tribunal.



After giving reasonable opportunity of being heard the Tribunal shall pass such order

Direct Removal of name of the company from the register of companies

Pass an order for the winding up of the company

Direct that liability of the members shall be unlimited

Change MOA/AOA in the interest of Public, creditors and member

Pass such other orders as it may deem fit

Steps of Incorporation

- 1 • Reservation of name by filing e-application
- 2 • Drafting & signing of MOA & AOA and its submission to ROC. These documents have to be e-filled and e-stamped.
- 3 • Consent of person nominated as directors to act as directors to be submitted electronically
- 4 • Submission of statutory declaration of compliance and other declarations
- 5 • Pay fees & amount of stamp duty electronically
- 6 • Obtain certificate of incorporation digitally signed by ROC
- 7 • File declaration about address of Registered office.



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Effect of Registration (Section -9)

MTP June 2020



Company XYZ Ltd.



Incorporation
Certificate

Company after
getting certificate
of incorporation

capable of
exercising all the
functions of an
incorporated
company under this
Act

Having perpetual succession with
power to acquire, hold and
dispose of property, both
movable and immovable, tangible
and intangible, to contract and to
sue and be sued, by the said
name.

All other persons, who may
from time to time become
members of the company,
shall be a
- **body corporate by
the name contained in
the memorandum.**

Effect of Memorandum and Articles (Section-10)

Where the memorandum and articles when registered, shall bind

The company

The members thereof

All monies payable by any member to the company under the memorandum or articles shall be a debt due from him to the company.

Classification of Capital

PYQ Dec 2021 6 Marks

- The word capital means share capital, i.e., the capital or figure in terms of so many rupees divided into shares of fixed amount.
- The proportion of the capital to which each member is entitled is his share.



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Nominal or Authorized or Registered Capital	Issued Capital	Subscribed Capital	Called up Capital	Paid-up capital
Section 2(8) Authorized or Nominal Capital means such capital as is authorized by the memorandum of a company to be the maximum amount of share capital of the company.	Section 2(50) <ul style="list-style-type: none"> Issued Capital means such capital as the company issues from time to time for subscription. It is that part of the authorized capital which is offered by the company for subscription. 	Section 2(86) Subscribed capital is that part of capital which is subscribed by the members of company	Section 2(15) <ul style="list-style-type: none"> Called-up capital is that part of the capital, which has been called for payment, it is the total amount called up on the shares issued. 	It is the total amount paid or credited as paid up on shares issued, it is equal to called-up capital less calls in arrears.

Shares

- ❖ **Section 2(84) of the Companies Act, 2013 'share' means** :→ A share in the share capital of a company and includes stock.
- ❖ Share is an interest in the company [**Borland Trustees vs. Steel Bors. & Co. Ltd.**]
- ❖ It represents such proportion of the interest of the shareholders as the amount paid up thereon bears to the total capital payable to the company.
- ❖ It is a measure of the interest in the company's assets to which a person holding a share is entitled.
- ❖ The shares or debentures or other interests of any member in a company shall be movable property transferable in the manner provided by the articles of the company [**Section 44**]
- ❖ Every share in a company having a share capital, shall be distinguished by its distinctive number [**Section 45**].



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Kinds of Share Capital (Section 43)

Equity Share Capital

Equity share capital with reference to a company limited by shares, means all share capital which is not preference share capital.

Preference Share Capital

With reference to any company limited by shares, means that part of the issued share capital of the company which carries or would carry a preferential right with respect to-

Equity Share with
Uniform Voting
Rights

Equity Share
with Differential
Voting Rights

a. **Payment of dividend**, either as a fixed amount or an amount calculated as a fixed rate

b. **Repayment**, in case of winding up or repayment of capital of the amount of the share capital paid up or deemed to have been paid up.

Memorandum of Association

- Memorandum of Association of company is in fact its charter: → it defines its constitution and the scope of the powers of the company with which it has been established under the Act.
- A company cannot depart from the provisions contained in the memorandum however imperative may be the necessity for the departure.
- It is the very foundation on which the whole edifice of the company is built.
- Section 399 : It is a public document. Consequently, every person entering into a contract with the company is presumed to have the knowledge of the conditions specified therein.
- A company cannot enter into a contract or engage in any trade or business, which is beyond the power conferred on it by the memorandum. If it does so, it would be ultra vires the company and void.



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As per Section 4, Memorandum of a company shall be drawn up in such form as is given in Tables A, B, C, D and E in Schedule I of the Companies Act, 2013

Table A

Table A is a form for MOA of a company limited by shares.

Table B

Table B is a form for MOA of a company limited by guarantee and not having a share capital.

Table C

Table C is a form for MOA of a company limited by guarantee and having a share capital.

Table D

Table D is a form for MOA of an unlimited company.

Table E

Table E is a form for MOA of an unlimited company and having share capital.

Name Clause

❖ The memorandum of the company shall state, in relation to the name clause, the name of the company with the last word

- 'Limited' in the case of a public limited company, or
- 'Private Limited' in case of a private limited company.

❖ **Section 8 company**

- This clause is not applicable to Section 8 company.
- In case of Section 8 company formed in accordance with the Electoral Trusts Scheme, 2013 notified by the Central Board of Direct Taxes (CBDT), the name including phrase 'Electoral Trust' may be allowed.
- Also, for the Companies under section 8 of the Act, the name shall include the words foundation, Forum, Association, Federation, Chambers, Confederation, council, Electoral trust, and the like etc.

❖ **Government Company** - A Government company's name must end with the word 'Limited'.

❖ **One Person Company** - In the case of One Person Company, the words 'One Person Company', should be included below its name.

Registered Office Clause

The State in which the registered office of the company is to be situated.

Object Clause

❖ Objects for which the company is proposed to be incorporated and any matter considered necessary in furtherance thereof.



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- ❖ If Company has changed its activities which are not reflected in its name - It shall change its name in line with its activities within a period of 6 months from the change of activities after complying with all the provisions as applicable to change of name.

Liability Clause

This clause covers details on liability of members of a company, whether limited or unlimited,

Capital Clause

- Amount of authorized share capital and also details about the number of shares the capital is divided into along with the value of each share.
- A company not having share capital need not have the Capital Clause.

Association Clause

Every subscriber to the memorandum shall take atleast one share and shall write against his name the number of shares taken by him.

Nomination Clause

In the case of OPC, the name of the person who, in the event of death of the subscriber, shall become the member of the company.

Memorandum must be

Printed

Divided into
paragraphs

Numbered
consecutively

Signed by at least seven persons (two in the case of a private company and one in the case of One Person Company) in the presence of at least one witness, who will attest the signatures

- A company being a legal person can through its agent, subscribe to the memorandum.
- However, a minor cannot be a signatory to the memorandum as he is not competent to contract.
- The guardian of a minor, who subscribes to the memorandum on his behalf, will be deemed to have subscribed in his personal capacity



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Doctrine of Ultra Vires

- ❖ The term ultra vires means 'beyond (their) powers'. The legal phrase "ultra vires" is applicable only to acts done in excess of the legal powers of the doers.
- ❖ When an act is performed, which though legal in itself, is not authorized by the object clause of the memorandum, or by the statute, it is said to be ultra vires the company, and hence null and void.
- ❖ An act which is ultra vires (i.e., beyond the powers of) is void and does not bind the company. Neither the company nor the contracting party can sue on it.
- ❖ An act which is ultra vires the company being void, cannot be ratified by the shareholders of the company.
- ❖ An ultra vires contract can never be made binding on the company. It cannot become "Intra vires" by reasons of estoppel, acquiescence, lapse of time, delay, or ratification.

Case Law: **Ashbury Railway Carriage and Iron Company Limited v. Riche**

Facts: The main objects of a company were:

- To make, sell or lend on hire, railway carriages and wagons.
- To carry on the business of mechanical engineers and general contractors.
- To purchase, lease, sell and work mines.
- To purchase and sell as merchants or agents, coal, timber, metals etc.

Directors of the company entered a contract with Riche, for financing the construction of a railway line in Belgium, and the company further ratified this act of the directors by passing a special resolution. The company however, repudiated the contract as being ultra-vires. And Riche brought an action for damages for breach of contract. His contention was that the contract was well within the meaning of the word general contractors and hence within its powers. Moreover, it had been ratified by a majority of share-holders.

Judgement: It was held that the contract was null and void. The Court held that the word 'general contractors' had to be given a restricted meaning. Only such contracts could be covered in the term 'general contractors' as are in some way related or connected with mechanical engineering. Therefore, the company could not finance the construction of a railway line by alleging that such a business falls under the business of general contractors.



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Article of Association

- ❖ The articles of association (AOA) of a company are its rules and regulations, which are framed to manage its internal affairs.
- ❖ Just as the memorandum contains the fundamental conditions upon which the company is allowed to be incorporated, so also the articles are the internal regulations of the company [*Guinness vs. Land Corporation of Ireland*].
- ❖ It regulates domestic management of a company and creates certain rights and obligations between the members and the company [*S.S. Rajkumar vs. Perfect Castings (P) Ltd.*].
- ❖ AOA are the bye-laws of the company according to which director and other officers are required to perform their functions as regards the management of the company, its accounts and audit

Contents of the Articles [Section 5]

- ❖ The articles of a company shall contain the regulations for management of the company.
- ❖ The articles shall also contain such matters, as are prescribed under the rules.
- ❖ However, a company may also include such additional matters in its articles as may be considered necessary for its management.
- ❖ **Entrenchment Provision :**
 - ✓ The articles may contain provisions for entrenchment (to protect something). It is such provision in AOA that makes certain amendments either more difficult or impossible to pass, making such amendments inadmissible.
 - ✓ The provision for entrenchment may be made
 - at the time of formation of the company or
 - by an amendment to the articles
 - with the consent of all members, in case of a private company
 - by passing a special resolution, in case of a public company.
- ❖ Where the articles contain provisions for entrenchment, the company shall give notice to the Registrar of such provisions in such form and manner as may be prescribed.



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❖ Forms of Articles

- The articles of a company shall be in respective forms specified in Tables, F, G, H, I and J in Schedule I as may be applicable to such company.
- A company may adopt all or any of the regulations contained in the model articles applicable to such company.
- Where the registered articles of a company registered after the commencement of this Act do not exclude or modify the regulations contained in the model articles applicable to such company, those regulations shall, so far as applicable, be the regulations of that company as if they were contained in the duly registered articles of the company.

Doctrine of Constructive Notice

- ❖ The memorandum and articles of association of a company when registered with Registrar of Companies, become public documents, and they are available for inspection to any person, on the payment of a nominal fees.
- ❖ It is, therefore, the duty of every person dealing with a company to inspect its documents and make sure that his contract is in conformity with their provisions but whether a person reads them or not, it will be presumed that he knows the contents of the documents.
- ❖ This kind of presumed/implied notice is called constructive notice.

The doctrine of Constructive Notice means that

- Whether a person reads the documents or not, he is presumed to have knowledge of the contents of the documents.
- He is not only presumed to have read the documents but also understood them in their true perspective,

Every person dealing with the company not only has the constructive notice of

- the memorandum and articles, but also of
- all the other related documents, such as Special Resolutions etc., which are required to be registered with the Registrar.

Thus, if a person enters into a contract which is beyond the powers of the company as defined in the memorandum, or outside the authority of directors as per memorandum or articles, he cannot acquire any rights under the contract against the company.



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Doctrine of Indoor Management

- The Doctrine of Indoor Management is the exception to the doctrine of constructive notice.
- This can be explained with the help of a landmark case ***The Royal British Bank vs. Turquand***. This is the doctrine of indoor management popularly known as ***Turquand Rule***.

FACTS of the Royal British Bank vs. Turquand

Mr. Turquand was the official manager (liquidator) of the insolvent Cameron's Coalbrook Steam, Coal and Swansea and Loughor Railway Company.

The company board of directors took loan from bank beyond their borrowing power.

Later on company went into liquidation, and liquidator denied money to bank saying the bank was deemed to be aware that the directors could borrow only up to the amount resolutions allowed

The court however directed the company to repay loan to bank as the bank being an outsider cannot be expected to know about internal irregularities of company.

Exceptions to the doctrine of Indoor Management

- 1) **Actual or constructive knowledge of irregularity:** The rule does not protect any person when the person dealing with the company has notice, whether actual or constructive, of the irregularity.

In ***Howard vs. Patent Ivory Manufacturing Co.*** where the directors could not defend the issue of debentures to themselves because they should have known that the extent to which they were lending money to the company required the assent of the general meeting which they had not obtained.

- 2) **Suspicion of Irregularity:** The doctrine in no way, rewards those who behave negligently. Where the person dealing with the company is put upon an inquiry, for example, where the transaction is unusual or not in the ordinary course of business, it is the duty of the outsider to make the necessary enquiry.

Where, for example, as in the case of ***Anand Bihari Lal vs. Dinshaw & Co.*** the plaintiff accepted a transfer of a company's property from its accountant, the transfer was held void. The plaintiff could not have supposed, in absence of a power of attorney that the accountant had authority to effect transfer of the company's property.



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3) Forgery: The rule does not apply where a person relies upon a document that turns out to be forged since nothing can validate forgery.

Ruben v Great Fingall Consolidated

In this case the plaintiff was the transferee of a share certificate issued under the seal of the defendant's company. The company's secretary, who had affixed the seal of the company and forged the signature of the two directors, issued the certificate.

The plaintiff contended that whether the signature were genuine or forged was apart of the internal management, and therefore, the company should be estopped from denying genuineness of the document

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THE NEGOTIABLE INSTRUMENT ACT, 1881

Chapter Overview

Notes, Bills & Cheques- Types classification and its Characteristics

Modes of Negotiation

Presentment of Instruments

Modes of Negotiation

Meaning of Negotiable Instruments

- Negotiable Instruments is an instrument which is
 - freely transferable from one person to another by mere delivery or
 - by indorsement and delivery.
- The property in such an instrument passes to a bonafide transferee for value.

Types of Negotiable Instrument

Promissory Note

Bill of Exchange

Cheque

A negotiable instrument is payable to order when

a. It is expressed to be so payable

b. When it is expressed to be payable to a specified person and does not contain words prohibiting its transfer

A negotiable instrument is payable to bearer when

a. It is expressed to be so payable

b. When the only or last indorsement (indorsement means signing of the instrument) on the instrument is an indorsement in blank i.e., the person who possesses it can demand payment.



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Essential Characteristic of Negotiable Instruments

1. Necessarily in writing.
2. It should be signed.
3. It is freely transferable from one person to another.
4. Holder's title is free from defects.
5. It can be transferred any number of times till its satisfaction.
6. Every negotiable instrument must contain an unconditional promise or order to pay money. The promise or order to pay must consist of money only.
7. The sum payable, the time of payment, the payee, must be certain.
8. The instrument should be delivered. Mere drawing of instrument does not create liability.

Written

Signed

Transferable

Title free from
defects

Can transferred
number of times

Unconditional promise/
order to pay

Certainty of sum payable time
of payment and the payee

Delivered

Promissory Note

Meaning

Section 4 of Negotiable Instrument Act 1881

"A 'promissory note' is

an instrument in writing
(not being a bank-note
or a currency-note)
containing an
unconditional undertaking

signed by
the maker

to pay a certain
sum of money
only to, or

to the order of,
a certain person,
or to the bearer
of the instrument

Parties to promissory note

1. **Maker:** The person who makes the promise to pay is called the Maker. He is the debtor and must sign the instrument.
2. **Payee:** Payee is the person to whom the amount on the note is payable.

Customer

Supplier

DRAWER
(Maker/ Debtor /Payer)

Supply of goods /services

Issue promissory note

DRAWEE
(Bearer/ Creditor/Payee)



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Essential Characteristics of a Promissory Note

1. Written
2. Promise to pay
3. Definite and unconditional promise
4. Promise to pay certain sum of money
5. The maker and payee must be certain person
6. Signature by maker
7. Promise in money only
8. stamping

Bills of Exchange

Meaning

A "bill of exchange" is

An instrument in writing containing an unconditional order

signed by the maker

directing a certain person to pay a certain sum of money

only to, or to the order of, a certain person or to the bearer of the instrument.

Parties to the Bill of Exchange

Drawer

Maker of bill of exchange

Drawee

Person directed by the drawer to pay

He is liable for payment of the bill

Payee

Person named in the instrument to whom, or to whose order the money is, by the instrument, directed to be paid.

Essential characteristics of Bill of Exchange

- Must be in writing
- Contain an express order to pay
- Order must be definite and unconditional
- Drawer, drawee, and payee must be certain

- Drawer must sign the instrument
- Sum must be certain
- Order must be to pay money only
- It must be stamped

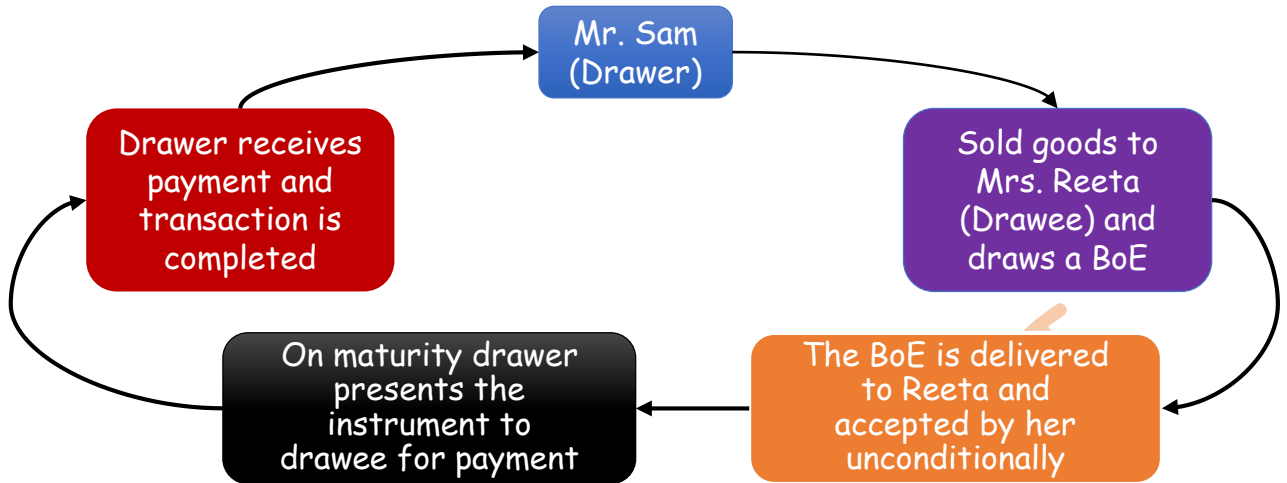


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Process of Bill of Exchange



Difference between promissory note and bill of exchange

S.no.	Basis	Promissory Note	Bill of Exchange
1.	Definition	"A Promissory Note" is an instrument in writing (not being a banknote or a currency-note) containing an unconditional undertaking signed by the maker, to pay a certain sum of money only to, or to the order of, a certain person, or to the bearer of the instrument.	"A bill of exchange" is an instrument in writing containing an unconditional order, signed by the maker, directing a certain person to pay a certain sum of money only to, or to the order of a certain person or to the bearer of the instrument.
2	Nature of Instrument	In a promissory note, there is a promise to pay money.	In a bill of exchange, there is an order for making payment.
3	Parties	In a promissory note, there are only 2 parties namely: i. the maker and ii. the payee	In a bill of exchange, there are 3 parties which are as under: i. the drawer ii. the drawee iii. the payee
4	Acceptance	A promissory note does not require any acceptance, as it is signed by the person who is liable to pay.	A bills of exchange needs acceptance from the drawee.



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Payable to bearer

A promissory note cannot be made payable to bearer.

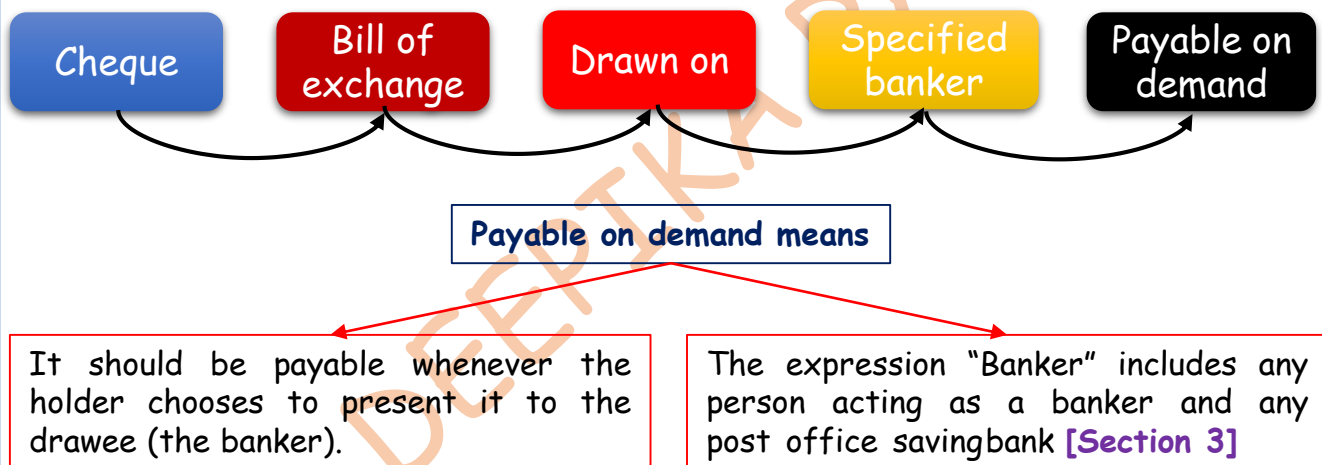
On the other hand, a bill of exchange can be drawn payable to bearer. However, it cannot be payable to bearer on demand.

Cheque

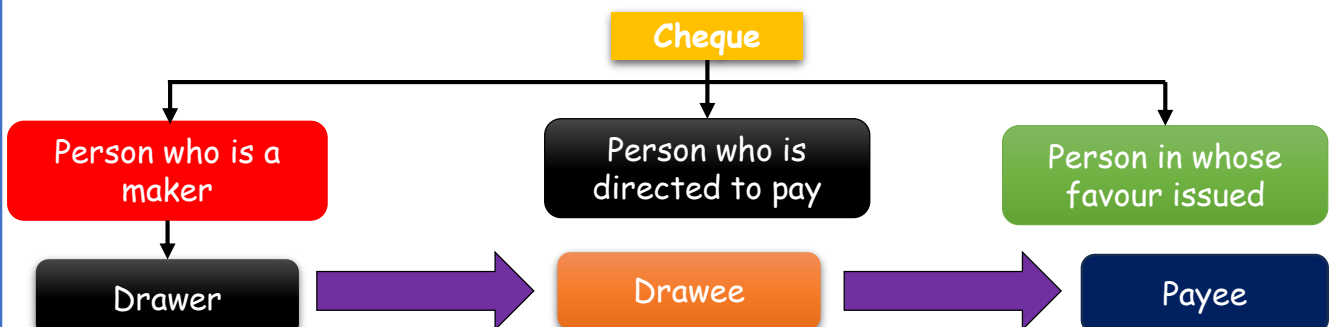
Meaning

A "cheque" is

- A bill of exchange
- drawn on a specified banker and not expressed to be payable otherwise than on demand and
- it includes the electronic image of a truncated cheque and a cheque in the electronic form



- **Cheque in the electronic Form** :→ The cheque is drawn and signed electronically by the use of digital signature.
- **Truncated cheque** :→ It means the cheque whose electronic image has been created during the course of clearing cycle, to substitute the further physical movement.





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Essential Characteristics of a Cheque

According to the definition of cheque under section 6, a cheque is a species of bill of exchange. Thus, it should fulfil.

- All the essential characteristics of a bill of exchange
- Must be drawn on a specified banker
- It must be payable on demand.

Note: These two additional features distinguish a cheque from bill. Thus, all cheques are bills while all bills are not cheques.

CLASSIFICATION OF NEGOTIABLE INSTRUMENTS

"Bearer instrument" and "order instrument" [Section 13]

Bearer Instrument

An instrument where the name of the payee is blank or specified with the words "or bearer" or where the last indorsement is blank.

Such instrument can be negotiated by mere delivery.

Order Instrument

It is an instrument which is payable to a person or his order or where the last indorsement is in full, such instrument can be negotiated by indorsement and delivery.

"Inland instrument" and "Foreign instrument" [Sections 11 & 12]

Inland Instrument

A promissory note, bill of exchange or cheque

drawn or made in India

made payable in, or drawn upon any person resident in India

shall be deemed to be an inland instrument



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Place where Instrument is Drawn and made payable	Residence of Person on whom Instrument is Drawn	Nature of Instrument
P/N, BOE, Cheque drawn/ made in India	+ Payable in India OR	Are Inland Instruments
	+ Drawn upon a person resident in India.	

Foreign Instrument

A foreign instrument is one which is not an inland instrument.

Place where bill is Drawn	Residence of Person on whom Drawn and place where made payable	Nature of Instrument
P/N, BOE, Cheque drawn/ made outside India	On a person resident in or outside India + made payable in India	Are Foreign Instruments
	On a person residing outside India + payable outside India.	
	On a person residing in India + Payable outside India	

Inland instrument – When BOE/ P/N / Cheque

Drawn/made in India

Made payable in /Drawn upon person resident in India

Foreign instrument – When BOE/ P/N / Cheque is not

Drawn in India

Made in India

Made payable in India

Liability of maker/ drawer of foreign bill

The liability of the maker or drawer of a foreign promissory note or bill of exchange or cheque

- Is regulated in all essential matters by the law of the place where he made the instrument, and
- The respective liabilities of the acceptor and indorser by the law of the place where the instrument is made payable.



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"Inchoate and Ambiguous Instruments

Inchoate Instrument

It means an instrument that is **incomplete in certain respects**.

The drawer/ maker/ acceptor/ indorser of a negotiable instrument may sign and deliver the instrument to another person in his capacity leaving the instrument, either wholly blank or having written on it the word incomplete.

- Such an instrument is called an inchoate instrument
and
- This gives a power to its holder to make it complete by writing any amount either within limits specified therein or within the limits specified by the stamp's affixed on it.

➤ Inchoate Instrument is based on the principle of estoppel.

Liability on drawing inchoate instrument

The person signing and delivering the inchoate instrument is liable both to

Holder

Rights

The holder of such an instrument cannot recover the amount in excess of the amount intended to be paid by the signor.

Holder in due course

Rights

The holder in due course can, however, recover any amount on such instrument provided it is covered by the stamp affixed on the instrument.

Ambiguous Instrument [Section 7]

- An instrument which is **vague** and **cannot be clearly identified either** as a **bill of exchange**, or as a **promissory note**, is an **ambiguous instrument**.
- An instrument **may be construed either as promissory note, or as a bill of exchange**.
- Section 17 provides that the **holder may, at his discretion, treat it as either and the instrument shall thereafter be treated accordingly**.



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- Thus, after exercising his option, the holder cannot change that it is the other kind of instrument.

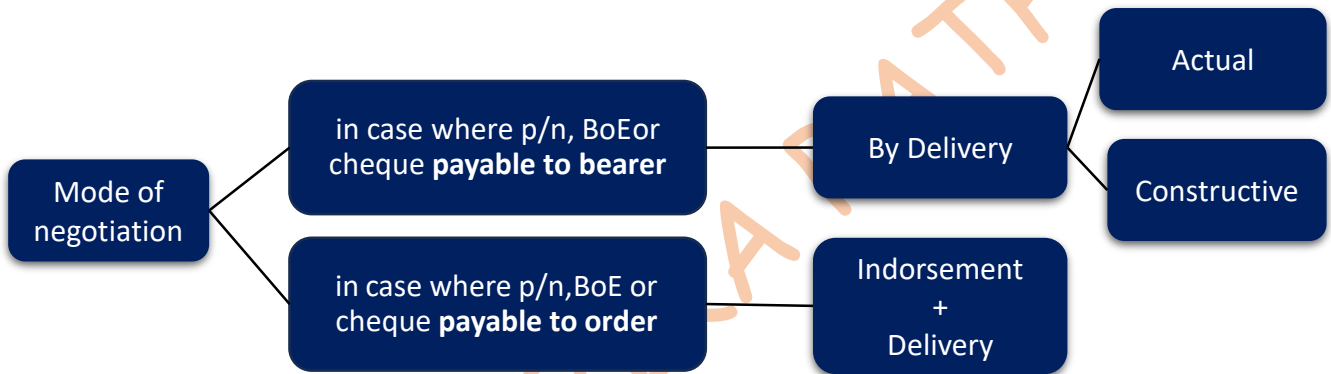
NEGOTIATION (TRANSFER) OF NEGOTIABLE INSTRUMENTS

Section 14 of N.I. Act

When a negotiable instrument is transferred to any person with a view to constitute the person holder thereof,

→ the instrument is deemed to have been negotiated.

Modes of Negotiation



Negotiation by Delivery [Section 47]

- **Subject to the provisions of section 58 :** [Instrument obtained by unlawful means or for unlawful consideration], a promissory note, bill of exchange or cheque payable to bearer is negotiable by delivery thereof.
- **Exception:** A promissory note, bill of exchange or cheque delivered on condition that it is not to take effect except in a certain event is not negotiable (except in the hands of a holder for value without notice of the condition) unless such event happens.

Negotiation by indorsement [Section 48]

Subject to the provisions of section 58,

- A promissory note, bill of exchange or cheque payable to order, is negotiable by the holder by indorsement and delivery thereof.



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Importance of Delivery in Negotiation [Section 46]

- **Delivery of an instrument is essential** whether the instrument is payable to bearer or order for effecting the negotiation.
- The delivery must be
 - Voluntary, and
 - Object of delivery should be to pass the property in the instrument to the person to whom it is delivered.
- Delivery can be
 - **Actual** : → Actual delivery takes place when the instrument changes hand physically.
 - **Constructive** : → Takes place when the instrument is delivered to the agent, clerk or servant of the indorsee on his behalf or when the indorser, after indorsement, holds the instrument as an agent of the indorsee.
- **Section 46** :→ When an instrument is conditionally or for a special purpose only, the property in it does not pass to the transferee, even though it is indorsed to him, unless the instrument is negotiated to a holder in due course.
- The delivery is essential not only at the time of negotiation but also at the time of making or drawing of negotiable instrument.
- The rights in the instrument are not transferred to the indorsee unless after the indorsement the same has been delivered.
- **Section 57** : → If a person makes the indorsement of instrument but before the same could be delivered to the indorsee the indorser dies, the legal representatives of the deceased person cannot negotiate the same by mere delivery thereof.

Note

- According to section 57, the legal representative of a deceased person cannot negotiate by delivery only, a promissory note, bill of exchange or cheque payable to order and indorsed by the deceased but not delivered.
- A legal representative is not an agent of the deceased. Therefore, a legal representative cannot complete the instrument if the instrument was executed by the deceased but could not be delivered because of his death.



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Delivery when effective between the parties

Negotiation of instruments between the parties

As between parties standing in immediate relation



How delivery is to be made

Delivery to be effectual must be made by the party making, accepting, or endorsing the instrument, or by a person authorized by him in that behalf.

As between such parties and any holder of the instrument other than a holder in due course



It may be shown that the instrument was delivered conditionally or for a special purpose only, and not for the purpose of transferring absolutely the property therein.

DISHONOUR OF CHEQUES FOR INSUFFICIENCY OF FUNDS IN THE ACCOUNTS [SECTION 138 TO 142]

DISHONOR OF CHEQUE FOR INSUFFICIENCY, ETC., OF FUNDS IN THE ACCOUNTS [SECTION 138]

Where any cheque drawn by a person on an account maintained by him with a banker

for the payment of any amount of money

to another person from that account

for the discharge, in whole or in part, of any debt or other liability

is returned by the bank unpaid

Either because of –

- amount of money standing to the credit of that account is insufficient,
or
- that it exceeds the amount arranged to be paid from that account by an agreement made with that bank,

such person shall be deemed to have committed an offence

shall be punished with

- imprisonment for a term which may extend to 2 years, or
- fine which may extend to twice the amount of the cheque or
- both



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When section 138 shall be not apply : Conditions for levy of penalty

Cheque must be presented within 3 months from the date on which it is drawn or within the period of its validity, whichever is earlier

Payee/holder in due courses notifies in writing to the drawer within 30 days of receipt of information by him from the bank regarding dishonour and asks for payment.

The drawer of such cheque fails to make the payment within 15 days of receipt of such notice.

- For the purpose of this section, "debt or other liability" means a legally enforceable debt or other liability.
- Compliant can be filed after 45 days of dishonor of the cheque (i.e., 30 days of notice period + 15 days of the receipt of the said notice.)

PRESUMPTION IN FAVOR OF HOLDER [SECTION 139]

When a cheque is dishonored, it shall be presumed, unless the contrary is proved, that the

- holder of a cheque received the cheque of the nature referred to in section 138 for the discharge in whole or in part, or any debt or other liability
- The effect of this presumption is that the evidential burden rests on the accused.

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

It shall not be a defence in a prosecution of an offence under section 138 that

→ Drawer had no reason to believe when he issued the cheque that the cheque may be dishonoured on presentment for the reasons stated in that section.



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PRESENTMENT OF INSTRUMENTS

Presentment for acceptance [Section 61]

A bill of exchange payable after sight must [if no time or place is specified therein for presentment] be presented

to the drawee thereof for acceptance [if he can, after reasonable search, be found] by a person entitled to demand acceptance

within a reasonable time after it is drawn, and in business hours on a business day.

- In default of such presentment, no party thereto is liable thereon to the person making such default.
- If the drawee cannot, after reasonable search, be found, → **Bill is dishonoured.**
- If the bill is directed to the drawee at a particular place
 - it must be presented at that place, and
 - if at the due date for presentment he cannot, after reasonable search, be found there, → **Bill is dishonoured.**
- Where authorized by agreement or usage, a presentment through the post office by means of a registered letter is sufficient.

Presentment of promissory note for sight [Section 62]

- ✓ A promissory note, payable at a certain period after sight, must be presented to the maker thereof for sight (if he can after reasonable search be found) by a person entitled to demand payment, within a reasonable time after it is made and in business hours on a business day
- ✓ In default of such presentment, no party thereto is liable thereon to the person making such default.

Drawee's time for deliberation [Section 63]

The holder must, if so required by the drawee of a bill of exchange presented to him for acceptance, allow the drawee 48 hours (exclusive of public holidays) to consider whether he will accept it.



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Presentment for payment [Section 64]

- ✓ Promissory notes, bill of exchange and cheques must be presented for payment to the maker, acceptor or drawee thereof respectively, by or on behalf of the holder as hereinafter provided.
- ✓ In default of such presentment, the other parties thereto are not liable thereon to such holder.
- ✓ Where authorised by agreement or usage, a presentment through the post office by means of a registered letter is sufficient.
- ✓ **Exception:** Where a promissory note is payable on demand and is not payable at a specified place, no presentment is necessary in order to charge the maker thereof.
- ✓ Notwithstanding anything contained in section 6, where an electronic image of a truncated cheque is presented for payment, the drawee bank is entitled to demand any further information regarding the truncated cheque from the bank holding the truncated cheque in case of any reasonable suspicion about the genuineness of the apparent tenor of instrument, and if the suspicion is that of any fraud, forgery, tampering or destruction of the instrument, it is entitled to further demand the presentment of the truncated cheque itself for verification:
- ✓ Provided that the truncated cheque so demanded by the drawee bank shall be retained by it, if the payment is made accordingly.

Hours for presentment (Section 65)

- Presentment for payment must be made during the usual hours of business, and, if at a banker's within banking hours.

Presentment for payment of instrument payable after date or sight (Section 66)

A promissory note or bill of exchange, made payable at a specified period after date or sight thereof, must be presented for payment at maturity.

Presentment for payment of promissory note payable by instalments (Section 67)

A promissory note payable by instalments must be presented for payment on the third day after the date fixed for payment of each instalment; and non-payment on such presentment has the same effect as non-payment of a note at maturity.



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Presentment for payment of instrument payable at specified place and not elsewhere (Section 68)

A promissory note, bill of exchange or cheque made, drawn or accepted payable at a specified place and not elsewhere must, in order to charge any party thereto, be presented for payment at that place.

Instrument payable at specified place (Section 69)

A promissory note or bill of exchange made, drawn or accepted payable at a specified place must, in order to charge the maker or drawer thereof, be presented for payment at that place.

Presentment where no exclusive place specified (Section 70)

A promissory note or bill of exchange, not made payable as mentioned in sections 68 and 69, must be presented for payment at the place of business (if any) or at the usual residence, of the maker, drawee or acceptor thereof, as the case may be.

Presentment when maker, etc., has no known place of business or residence (Section 71)

If the maker, drawee or acceptor of a negotiable instrument has no known place of business or fixed residence, and no place is specified in the instrument for presentment for acceptance or payment, such presentment may be made to him in person wherever he can be found.

Presentment of cheque to charge drawer (Section 72)

Subject to the provisions of section 84, a cheque must, in order to charge the drawer, be presented at the bank upon which it is drawn before the relation between the drawer and his banker has been altered to the prejudice of the drawer.

Presentment of cheque to charge any other person (Section 73)

A cheque must, in order to charge any person except the drawer, be presented within a reasonable time after delivery thereof by such person.

Presentment of instrument payable on demand (Section 74)

Subject to the provisions of section 31, a negotiable instrument payable on demand must be presented for payment within a reasonable time after it is received by the holder.



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Presentment by or to agent, representative of deceased, or assignee of insolvent (Section 75)

Presentment for acceptance or payment may be made to the duly authorised agent of the drawee, maker or acceptor, as the case may be, or, where the drawee, maker or acceptor has died, to his legal representative, or, where he has been declared an insolvent, to his assignee.

Excuse for delay in presentment for acceptance or payment (Section 75A)

- ✓ Delay in presentment for acceptance or payment is excused if the delay is caused by circumstances beyond the control of the holder, and not imputable to his default, misconduct or negligence.
- ✓ When the cause of the delay ceases to operate, presentment must be made within a reasonable time.

When presentment unnecessary (Section 76)

No presentment for payment is necessary, and the instrument is dishonoured at the due date for presentment, in any of the following cases:

- a. (i) If the maker, drawee or acceptor intentionally prevents the presentment of the instrument, or
- (ii) if the instrument being payable at his place of business, he closes such place on a business day during the usual business hours, or
- (iii) if the instrument being payable at some other specified place, neither he nor any person authorised to pay it attends at such place during the usual business hours, or
- (iv) if the instrument not being payable at any specified place, he cannot after due search be found
- b. As against any party sought to be charged therewith, if he has engaged to pay notwithstanding non-presentment.
- c. As against any party if, after maturity, with knowledge that the instrument has not been presented-
 - he makes a part payment on account of the amount due on the instrument,
 - or promises to pay the amount due thereon in whole or in part,
 - or otherwise waives his right to take advantage of any default in presentment for payment;



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- d. As against the drawer, if the drawer could not suffer damage from the want of such presentment.

Liability of banker for negligently dealing with bill presented for payment (Section 77)

When a bill of exchange, accepted payable at a specified bank, has been duly presented there for payment and dishonoured, if the banker so negligently or improperly keeps, deals with or delivers back such bill as to cause loss to the holder, he must compensate the holder for such loss.

PRESENTMENT OF INSTRUMENTS

Rules as to compensation (Section 117)

The compensation payable in case of dishonour of promissory note, bill of exchange or cheque, by any party liable to the holder or any endorsee, shall be determined by the following rules:

- a. The holder is entitled to the amount due upon the instrument, together with the expenses properly incurred in presenting, noting and protesting it;
- b. When the person charged resides at a place different from that at which the instrument was payable, the holder is entitled to receive such sum at the current rate of exchange between the two places
- c. An endorser who, being liable, has paid the amount due on the same is entitled to the amount so paid with interest at 18% per annum from the date of payment until tender or realisation thereof, together with all expenses caused by the dishonour and payment;
- d. When the person charged and such endorser reside at different places, the endorser is entitled to receive such sum at the current rate of exchange between the two places;
- e. The party entitled to compensation may draw a bill upon the party liable to compensate him, payable at sight or on demand, for the amount due to him, together with all expenses properly incurred by him.
Such bill must be
 - Accompanied by the instrument dishonoured and the protest thereof (if any).
 - If such bill is dishonoured, the party dishonouring the same is liable to make compensation thereof in the same manner as in the case of the original bill.