

TOP THE SEMESTER

by

ADV. MOHIT TANWR

ADV. SHIVANG VERMA

DISCLAIMER AND LIMITATION OF LIABILITY

This book has been prepared and published solely for academic purposes and provides general information regarding the law of contracts as applicable under the Indian law. The content herein reflects the authors' understanding and interpretation of the law at the time of writing. Every effort has been made to ensure the accuracy of the material, however, laws and legal interpretations are subject to change and errors may occur despite the authors' best efforts.

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UNIT 1

INDEMNITY, GUARANTEE AND AGENCY

1.1 DISTINCTION BETWEEN INDEMNITY AND GUARANTEE

INTRODUCTION TO INDEMNITY AND GUARANTEE

The Indian Contract Act, 1872 regulates various aspects of contract law in India. The Act provides a legal framework for business transactions and covers various types of contracts. Sections 124 to 147 of the Act deal specifically with the laws pertaining to Contracts of Indemnity and Guarantee.

Contract of Indemnity

Section 124 of the Indian Contract Act, 1872, defines a contract of indemnity as a contract by which one party promises to save the other from loss caused to him by the conduct of the promisor himself, or by the conduct of any other person.

A contract of indemnity typically involves two parties,

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the indemnifier (the person who promises to compensate for the loss) and the indemnified (the person whose loss is to be compensated). An example of this would be an insurance policy where the insurer promises to compensate the insured for any damage or loss suffered due to certain specified events.

The scope of indemnity under Indian law is quite broad and may cover losses resulting from lawsuits, damages, or financial loss. The nature and extent of the indemnity provided are based on the terms of the contract.

The main rights of the indemnity holder are:

- a. To claim damages from the indemnifier for all losses, irrespective of whether the indemnity contract specifically provides for it, provided that the losses were a direct consequence of the circumstances stated in the contract.
- b. To claim all costs reasonably incurred in any proceedings.

The scope of the indemnity obligation would be determined by the construction of the contract of indemnity, including the surrounding circumstances known to both parties.

Contract of Guarantee

A contract of guarantee is defined in Section 126 of the

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Indian Contract Act, 1872 as a contract to perform the promise or discharge the liability of a third person in case of his default. The parties involved are the creditor (the person to whom the guarantee is given), the principal debtor (the person on whose default the guarantee is given), and the surety/guarantor (the person who gives the guarantee).

A contract of guarantee involves three contracts:

- Contract between the principal debtor and the creditor
- Contract between the principal debtor and the surety
- Contract between the surety and the creditor

A contract of guarantee can be oral or written. Its primary purpose is to provide security for the performance of an obligation.

The rights of the surety include:

- Rights against the Creditor: The right of indemnity, the right to securities, and the right of set-off.
- Rights against the Principal Debtor: The right of subrogation, the right of indemnity, and the right to proceed concurrently against the debtor.
- Rights against Co-sureties: The right of contribution, the right of subrogation, and the right of exoneration.

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In **Bank of Bihar v. Damodar Prasad** (AIR 1969 SC 297), it was held that the surety is discharged if there is any act of the creditor or the principal debtor that is inconsistent with the rights of the surety, or any agreement between the principal debtor and creditor by which the contract is altered, unless the surety consents to such act or agreement.

The Indian Contract Act, 1872, provides a clear framework for contracts of indemnity and guarantee, outlining the rights and obligations of parties. While the Act sets the foundational principles, the specific terms of each contract require careful drafting and, often, legal expertise to avoid disputes. Judicial interpretations further emphasize the need for precision, making a thorough understanding of these provisions essential for effective application.

INDEMNITY AND GUARANTEE IN ENGLISH LAW TO INDIAN LAW

In both Indian and English law, the principles of indemnity and guarantee are recognized and operate to ensure that parties are protected from financial loss. However, there are a few key differences in how these concepts are applied and interpreted in each jurisdiction.

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Contract of Indemnity

In English law, the concept of indemnity is used more broadly than in Indian law. English law recognizes two types of indemnity contracts: contracts of specific indemnity and contracts of general indemnity.

- **Specific indemnity:** These contracts arise when a specific contract expressly stipulates the liability. They're similar to Indian law indemnity contracts.
- **General indemnity:** These contracts are derived from tortuous liability rather than specific contracts. In such cases, the principle of subrogation does not apply.

However, in Indian law, the scope of indemnity is generally confined to contracts, where one party promises to save the other from the loss caused either by the conduct of the promisor or by the conduct of any other person.

Contract of Guarantee

Both English and Indian law recognize the contract of guarantee, which involves three parties: the creditor, the principal debtor, and the guarantor. However, there are some differences:

- **Revocation:** Under Indian law, a continuing guarantee can be revoked at any time, concerning

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future transactions, by the surety giving notice to the creditor. In contrast, English law allows revocation of a continuing guarantee only on the occurrence of a certain event or expiry of a certain period.

- **Nature of Liability:** In English law, the liability of the guarantor is secondary, and he becomes liable only upon the default of the principal debtor. Conversely, under Indian law, the surety's liability can be co-extensive with the principal debtor unless it is otherwise provided by the contract.
- **Rights of Surety:** Under English law, a surety is entitled to the benefit of every security that the creditor has against the principal debtor. This right arises immediately when the contract of guarantee is entered into and does not depend on the surety having paid anything. However, under Indian law, the surety is entitled to the benefit of the creditor's securities only after he has paid under the guarantee.

While the principles of indemnity and guarantee share common roots in English and Indian law, key differences arise due to distinct legal traditions and statutory frameworks in each jurisdiction. A nuanced understanding of these variations is essential for practitioners drafting or interpreting contracts across these legal systems, ensuring compliance and mitigating potential disputes

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1.2 RIGHT AND DUTIES OF INDEMNIFIER AND DISCHARGE

RIGHTS AND DUTIES OF INDEMNIFIER

The contract of indemnity, as outlined in Section 124 of the Indian Contract Act, 1872, has at its core two main parties: the indemnifier and the indemnity-holder. The indemnifier is the party who promises to make good any loss suffered by the indemnity-holder. This promise could be due to the conduct of the promisor or any other person. To understand the contract of indemnity, we need to delve into the rights and duties of the indemnifier, as provided under the Act.

Duties of the Indemnifier

The primary duty of the indemnifier is to indemnify or compensate the indemnity-holder against the loss, damage, or liability that was agreed upon in the contract. The scope of the indemnifier's liability is generally determined by the terms of the contract.

The indemnifier's liability can be invoked when the indemnity-holder has suffered an actual loss. The liability is not dependent on whether the indemnity-holder has sued the third party for the loss or whether the third party is solvent or not. If the indemnity-holder has incurred an actual loss, the indemnifier is duty-bound to make good

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on his promise to indemnify the loss.

Rights of the Indemnity Holder (Section 125)

Section 125 of the Indian Contract Act, 1872, provides for the rights of the indemnity holder. According to Section 125, the indemnity-holder has the following rights:

- a. **All Damages:** The indemnity holder, when sued, has the right to recover from the promisor all damages which he may be compelled to pay in any suit in respect of any matter to which the promise to indemnify applies.
- b. **All Costs:** The indemnity holder has the right to recover all costs. These are costs that he may be compelled to pay in bringing or defending such suit if, in bringing or defending it, he did not contravene the orders of the promisor and acted as it would have been prudent for him to do in the absence of any contract of indemnity, or if the promisor authorized him to bring or defend the suit.
- c. **All Sums:** The indemnity holder has the right to recover all the sums which he may have paid under the terms of any compromise of any such suit, provided the compromise was not contrary to the orders of the promisor, and was one which it would have been prudent for the promisee to make in the absence of any contract of indemnity, or if the promisor authorized him to compromise the suit.

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In the case of General Assurance Society Ltd. vs Chandumull Jain & Anr (AIR 1966 SC 1644), it was held by the Supreme Court that under Section 125 of the Contract Act, the indemnity-holder, in the absence of a contract to the contrary, is entitled to recover from the indemnifier: (1) any damages he may be compelled to pay in a lawsuit; (2) all costs; and (3) all sums paid under the terms of a compromise, if it would have been prudent for the indemnity-holder to make such a compromise.

These rights aim to make the indemnity holder whole and compensate him for any loss suffered due to the acts of the promisor or any other person, in line with the promise made in the contract of indemnity. They are an essential part of the broader framework of rights and obligations under contracts of indemnity.

Examples of Duties and Rights of the Indemnifier

Let's illustrate the duties and rights of the indemnifier with examples:

Example 1 (Duty):

Suppose a person, Mr. A, is a civil contractor. He enters into a contract with Mr. B for a construction project. In the agreement, there is an indemnity clause where Mr. A promises to indemnify Mr. B for any loss or damage caused to the property during the construction process.

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During the construction, one of Mr. A's employees accidentally damages a part of the existing structure, resulting in substantial repair costs. Here, as per the indemnity clause, it's the duty of Mr. A (indemnifier) to compensate Mr. B (indemnity-holder) for the loss incurred.

Example 2 (Right):

Continuing with the above example, let's say Mr. A, as part of his duty, compensates Mr. B for the damages. Now, Mr. A can exercise his right of subrogation. He can recover the amount paid to Mr. B from his employee or his employee's insurance company, if applicable. Here, the employee or the insurer becomes the third party from whom the indemnifier recovers the compensation paid to the indemnity holder.

Example 3 (Right of Recoupment):

Assume Mr. A had clearly instructed his employee regarding the safety precautions to avoid any damage, but the employee disregarded those instructions, leading to the damage. In this case, after compensating Mr. B, Mr. A can claim the loss from his employee exercising the right of recoupment as the loss was due to the employee's fault.

These examples give practical insights into how the duties

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and rights of the indemnifier come into play during the course of contractual obligations and how they help ensure fair practices and justice.

DISCHARGE OF SURETY

The role of a surety or guarantor in a contract of guarantee is pivotal in ensuring the performance of a promise or obligation by a third party, known as the principal debtor. The surety acts as a secondary party, assuring the creditor that the principal debtor will fulfill their obligations. However, specific circumstances outlined in Sections 130 to 139 of the Indian Contract Act, 1872, provide for the discharge of the surety from liability. These provisions aim to safeguard the surety from undue or unforeseen liabilities, ensuring fairness and balance in the contract of guarantee.

Circumstances of Discharge of Surety

1. Revocation by Surety (Section 130)

A continuing guarantee can be revoked by the surety concerning future transactions by giving notice to the creditor.

- **Effect of Revocation:** Revocation does not impact obligations or liabilities already incurred before the notice. Transactions executed before the revocation remain binding on the surety.

2. Death of Surety (Section 131)

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The death of the surety operates as a revocation of a continuing guarantee concerning future transactions unless a contract to the contrary exists.

- **Estate of the Surety:** While future liabilities are revoked, the surety's estate remains liable for obligations incurred before their death.

3. Variation in Terms of Contract (Section 133)

A surety is discharged if there is any **variation in the terms of the contract** between the creditor and the principal debtor without the surety's consent.

- **Reason for Discharge:** A surety's liability arises based on the specific terms of the guarantee contract. Any unilateral alteration in these terms without the surety's approval nullifies their liability for future obligations.

4. Release or Discharge of the Principal Debtor (Section 134)

The release or discharge of the **principal debtor** from liability by the creditor results in the discharge of the surety.

- **Co-extensive Nature of Liability:** The liability of the surety is co-extensive with that of the principal debtor. If the principal debtor is no longer liable, the surety cannot be held accountable independently.

5. Arrangement Between Creditor and Principal

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Debtor (Section 135)

If the creditor enters into a composition, promises to give time, or agrees not to sue the principal debtor without the surety's consent, the surety is discharged.

- **Exceptions:**

The surety remains bound if they have expressly consented to such arrangements.

6. Creditor's Act or Omission Impairing Surety's Rights (Section 139)

If the creditor performs any act inconsistent with the rights of the surety or fails to perform an act that is the creditor's duty to the surety, the surety is discharged.

- **Impact on Surety's Remedy:** Actions or omissions that impair the surety's eventual remedies against the principal debtor render the surety discharged from liability.

Judicial Interpretations on Discharge of Surety

Bank of Bihar v. Damodar Prasad (AIR 1969 SC 297)

The Supreme Court ruled that creditor acts or omissions inconsistent with the rights of the surety or prejudicial to them would discharge the surety. This case highlighted the importance of safeguarding the surety's rights throughout the guarantee contract.

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State of Madhya Pradesh v. Kaluram (AIR 1967 SC 1073)

This case reaffirmed the principle that any act or omission of the creditor, which impairs the surety's right of recourse or remedies against the principal debtor, would lead to the discharge of the surety.

ESSENTIALS OF A VALID GUARANTEE

A contract of guarantee, defined in Section 126 of the Indian Contract Act, 1872, is a contract to perform the promise or discharge the liability of a third person in case of his default. It involves three parties – the creditor, the principal debtor, and the surety or guarantor. However, for such a contract to be considered valid, certain key elements must be present:

1. **Existence of a debt or duty:** There must be a valid and enforceable debt or duty that exists or is contemplated. The surety is liable only if the principal debtor is liable. A guarantee cannot exist in a vacuum; it is accessory to a principal liability and can't exist without it.
2. **Surety's Consent:** According to Section 126, a guarantee may be either oral or written, but what matters is that it must be based on the consent of the surety. The surety should be competent to contract as per the general principles of contract law (Section 11), and his consent should not be

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obtained by misrepresentation, fraud, undue influence or coercion (Sections 15-22).

- 3. Consideration (Section 127):** An essential of any contract is the existence of consideration. However, for a contract of guarantee, consideration for the surety is the consideration received by the principal debtor. In other words, the guarantor does not necessarily need to receive a benefit for the guarantee to be valid.
- 4. Three Parties:** There must be three separate and distinct parties to the contract of guarantee i.e., the creditor, the principal debtor, and the surety or guarantor. Each must be clearly identifiable.
- 5. Principal Debt Must be Enforceable:** The guarantee is only as good as the principal debt. The principal debt must be a legally enforceable debt. If the principal debt is not enforceable (due to illegality or otherwise), the guarantee cannot be enforced.
- 6. Specificity:** A guarantee must be specific in terms. It should specify the exact extent of the surety's liability. A vague or ambiguous guarantee that doesn't clearly outline the extent of the surety's liability may not be enforceable.

These requirements form a critical framework for individuals entering into contracts of guarantee. A clear

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grasp of these essentials enables parties to safeguard their interests and navigate the complexities of guarantee agreements effectively, ensuring both compliance and protection under the law

EFFECT OF FRAUD, MISREPRESENTATION OR CONCEALMENT ON GUARANTEE

Just as with any contract, a contract of guarantee is based on the principles of good faith and fair dealing. The implications of fraud, misrepresentation, or concealment on such a contract are covered under Sections 142 and 143 of the Indian Contract Act, 1872.

1. **Fraud (Section 142):** According to this section, any guarantee obtained by means of misrepresentation made by the creditor, or with his knowledge and assent concerning a material part of the transaction, is invalid. A material part of the transaction is any information that might significantly affect the decision of the surety to enter into the guarantee. If the creditor has engaged in fraudulent practices to secure the guarantee, the surety is not bound by the agreement.
2. **Concealment (Section 143):** This section states that any guarantee which the creditor has obtained by concealing any material circumstance is invalid. If the creditor purposefully hides a

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material fact that could have influenced the surety's decision to provide the guarantee, then the contract of guarantee is not enforceable.

As per the principles laid down by the Act, the guarantor must be privy to all material facts related to the transaction. Any form of concealment or fraud vitiates the contract. This aligns with the fundamental principle of "*uberrimae fidei*" which denotes utmost good faith. The aim is to prevent exploitation and to ensure that the surety's rights are protected.

In the landmark case of **Maharashtra State Electricity Board, Bombay v. Official Liquidator, High Court, Ernakulam and Ors** (AIR 1982 SC 1497), it was held by the Supreme Court that a surety is entitled to be informed about all the facts which might affect his interests and the creditor is duty-bound to inform him, failing which the surety can revoke the guarantee.

These provisions protect the surety from being bound by a guarantee that was obtained by fraudulent means, thereby safeguarding their interests and upholding the principles of equity and fairness in contractual dealings.

COMMENCEMENT OF LIABILITY OF INDEMNIFIER

The liability of an indemnifier arises from a contract of indemnity, which is a distinct form of contract defined

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under the Indian Contract Act, 1872. As per Section 124 of the Act, "a contract by which one party promises to save the other from loss caused to him by the conduct of the promisor himself, or by the conduct of any other person, is called a contract of indemnity."

Under a contract of indemnity, the indemnifier promises to compensate the indemnity holder for any losses or damages suffered by them due to the actions of the indemnifier or a third party. The commencement of liability of the indemnifier arises from the occurrence of the specified event or conduct that results in a loss to the indemnity holder.

However, the Indian Contract Act, unlike English law, does not explicitly discuss when the liability of the indemnifier begins. Under English law, the indemnity holder first needs to suffer the loss before the indemnifier becomes liable.

By implication and from judicial interpretations, the following points may be inferred about the commencement of the indemnifier's liability under Indian law:

1. **Promise to Indemnify:** The indemnifier's liability commences with the promise to indemnify. However, the indemnifier is only liable to make good the loss once the loss has actually been suffered by the indemnity holder.
2. **Performance of Promise:** The indemnifier is

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not liable until the indemnity holder has performed his part of the contract or has suffered the promised loss.

- 3. Actual Loss:** The indemnity holder must prove the actual loss or damage incurred. The indemnifier is not liable for any prospective or assumed loss.

In **Gajanan Moreshwar Parelkar v. Moreshwar Madan Mantri** (AIR 1942 Bom 302), the court held that the Indian law on indemnity is not identical to the English law. Under Indian law, the indemnity holder is entitled to recover from the indemnifier even before actual loss is suffered, under certain circumstances.

However, as the Indian Contract Act doesn't clearly specify the commencement of liability of the indemnifier, it is generally subject to the terms of the contract of indemnity and dependent on the factual situation of each case.

RIGHTS OF SURETY

The Indian Contract Act, 1872, outlines several rights that the surety is entitled to in a contract of guarantee. These rights are divided into two main categories: rights against the creditor, and rights against the principal debtor and co-sureties.

Rights Against the Creditor

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1. **Right of Subrogation (Section 140):** Once the surety has discharged the debt or performed all that he is obligated to perform, he steps into the shoes of the creditor. The surety has the right to benefit from all the securities which the creditor had against the principal debtor, whether the surety was aware of them or not at the time when he entered into the contract of guarantee.
2. **Right to Indemnity (Section 145):** The surety is entitled to recover from the principal debtor any sum which he has rightly paid under the guarantee, but he cannot recover any sum which he has paid wrongfully.

Rights Against the Principal Debtor

3. **Right to Require the Principal Debtor to Discharge Debt (Section 140):** When a surety has guaranteed the performance of a contract on behalf of a principal debtor, he can compel the principal debtor to perform the contract and thus prevent any further liability.

Rights Against Co-Sureties

4. **Rights in Case of Co-Sureties (Section 141-143):** Where there are co-sureties for the same debt, they are, as between themselves, each liable for an equal share of the debt or performance, irrespective of the amount for which they signed as sureties. If any co-surety pays more than his

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share, he has a right of contribution from his co-sureties.

In the case of **Bank of Bihar v. Damodar Prasad** (AIR 1969 SC 297), the Supreme Court held that the liability of the surety is co-extensive with that of the principal debtor unless it is otherwise provided by the contract. However, if the creditor makes any composition with the principal debtor, which varies the terms of the principal contract, it discharges the surety.

RIGHT OF SURETY AGAINST THE CREDITOR

A surety, or a guarantor, as part of a contract of guarantee, takes on significant financial liability. However, to safeguard the surety's interests and ensure fair dealings, the Indian Contract Act, 1872 provides several rights to the surety against the creditor. These rights ensure that the surety isn't unduly burdened and the liability is limited to what's fair and agreed upon. Let's explore these rights in detail:

1. **Right of Subrogation (Section 140):** Upon honouring the guarantee obligation, the surety steps into the shoes of the creditor. This means that the surety gains the right to all remedies, securities, and claims that the creditor held against the principal debtor. This is known as the right of subrogation. In other words, the surety can enforce every right of the creditor against the

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debtor to recover the amount paid under the guarantee. This right is inherent and arises immediately when the surety pays the guaranteed debt.

2. **Right to Securities (Section 141):** If the creditor holds any security regarding the debt (like a mortgage or lien), and if the surety discharges the debt without knowing about the security, the surety is still entitled to benefit from the security, just as much as the creditor. This is a crucial aspect that provides a safety net for the surety and mitigates the risk associated with the suretyship.

In the landmark case of **State of Madhya Pradesh v. Kaluram** (AIR 1967 SC 1073), it was reiterated by the Supreme Court of India that the surety, after satisfying the guarantee, is entitled to the benefit of all securities which the creditor has against the principal debtor at the time when the contract of suretyship was entered into, whether the surety knew of the existence of such securities or not.

These rights against the creditor protect the surety's interests by allowing the surety to recover amounts paid under the contract of guarantee. They ensure that the surety is not unduly burdened by the guarantee obligation and maintains the balance of fairness in the transaction.

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DISTINCTION BETWEEN INDEMNITY AND GUARANTEE

While both indemnity and guarantee are forms of contingent contracts under the Indian Contract Act, 1872, they serve different purposes and have distinctive characteristics. Let's delve into the differences between the two:

1. Number of Parties:

a. Indemnity (Section 124): An indemnity involves two parties - the indemnifier (the person promising to compensate for the loss) and the indemnity-holder (the person whose loss is to be compensated).

b. Guarantee (Section 126): A guarantee involves three parties - the principal debtor (the person in respect of whose default the guarantee is given), the creditor (the person to whom the guarantee is given), and the surety/guarantor (the person who gives the guarantee).

2. Number of Contracts:

a. Indemnity: There is only one contract, which is between the indemnifier and the indemnity-holder.

b. Guarantee: There are two contracts - one between the principal debtor and the creditor,

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and the other between the surety and the creditor.

3. Liability:

- a. **Indemnity:** The liability of the indemnifier is primary and independent. The indemnifier is obliged to compensate the indemnity-holder only if the latter suffers some loss.
- b. **Guarantee:** The liability of the surety is secondary and contingent on the default of the principal debtor. The surety's obligation to pay arises when the principal debtor defaults on his obligation to the creditor.

4. Purpose:

- a. **Indemnity:** The purpose of an indemnity contract is to protect the indemnity-holder against loss promised in the contract.
- b. **Guarantee:** The purpose of a contract of guarantee is to provide an assurance to the creditor that his debt or other obligation will be fulfilled.

5. Extent of Liability:

- a. **Indemnity:** The indemnifier's liability arises only when the loss occurs. Until the loss occurs, the indemnifier has no liability.
- b. **Guarantee:** The surety's liability is co-

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extensive with that of the principal debtor from the very beginning. This means that the surety is liable for the debt or duty of the principal debtor even if the debtor fails to perform it.

In the case of Gajanan **Moreshwar Parelkar v. Moreshwar Madan Mantri** (AIR 1942 Bom 302), it was observed that under Indian law, the indemnity holder is entitled to recover from the indemnifier even before the actual loss is suffered, under certain circumstances, which is not the case with a contract of guarantee.

1.3 RIGHTS AND DUTIES OF BAILOR/BAILEE, LIEN, ETC

Introduction to Bailment

Bailment is a distinctive type of contractual arrangement, explicitly discussed under the Indian Contract Act, 1872, Sections 148 to 181. A bailment is a type of arrangement in which the physical possession of goods is transferred from one person to another for a particular purpose under a contract.

- **Section 148:** "A bailment is the delivery of goods by one person to another for some purpose, upon a contract that they shall, when the purpose is

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accomplished, be returned or otherwise disposed of according to the directions of the person delivering them."

Here are the parties involved in a bailment:

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

This delivery of goods is made on the condition that the goods will be returned to the bailor, or disposed of as per the bailor's directions, once the purpose of the bailment has been fulfilled. The bailee holds a responsibility to return the goods in a designated condition and time.

Bailment contracts can arise in various scenarios, including:

- The lending of goods for use by a friend.
- The delivery of goods for repair.
- Storage of goods with a warehouse.
- Parking a car in a garage.

The law of bailment outlines the duties and rights of both the bailor and the bailee. The bailee has a responsibility to take care of the goods and return them according to the agreement. Simultaneously, the bailor has the responsibility not to unnecessarily interfere with the bailee's use of goods.

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A prominent example of bailment in case law is the decision of the Supreme Court of India in **State of Gujarat vs. Memon Mahomed Haji Hasam** (AIR 1967 SC 1885). In this case, the Court held that in the case of bailment, the burden of proving negligence is on the bailor, and it is not enough to show that the bailee did not take enough care of the goods as they themselves would have done.

ESSENTIAL FEATURES OF BAILMENT

Bailment, as defined in the Indian Contract Act, 1872, has a set of specific characteristics that differentiate it from other forms of contractual agreements. The essential features of bailment, as stated in Section 148, are as follows:

1. **Delivery of Goods:** The foremost requirement of bailment is the delivery of goods from one person to another. Delivery could be actual, where the physical possession is transferred, or constructive, where the means of control and possession are transferred. The goods may be all kinds of movable properties excluding money.
2. **Two Parties:** There must be two parties in a contract of bailment - the bailor (who delivers the goods) and the bailee (who receives the goods).
3. **Specific Purpose:** The delivery of goods is done

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for a specific purpose. This could be for safekeeping, repair, transportation, etc. The purpose must be lawful and agreed upon by both parties.

4. **Return or Disposal of Goods:** Once the purpose is accomplished, the goods should be returned to the bailor or disposed of as per the bailor's directions. The return of the exact goods is a requirement in the case of a specific bailment, whereas in the case of non-specific bailment, goods of the same kind and quality must be returned.
5. **Contractual Relationship:** The delivery of goods must be based on a contract. The parties involved should have the intention to enter into a legal relationship. The contract can be either express or implied.
6. **Change in Form:** There may be a change in the form or substance of the goods bailed. For example, when wood is given to a carpenter to make furniture, the goods will be returned in a changed form.
7. **No Transfer of Ownership:** In a contract of bailment, only possession of goods is transferred, not the ownership. The bailee is expected to return the exact goods or goods in an altered form after the purpose is fulfilled.

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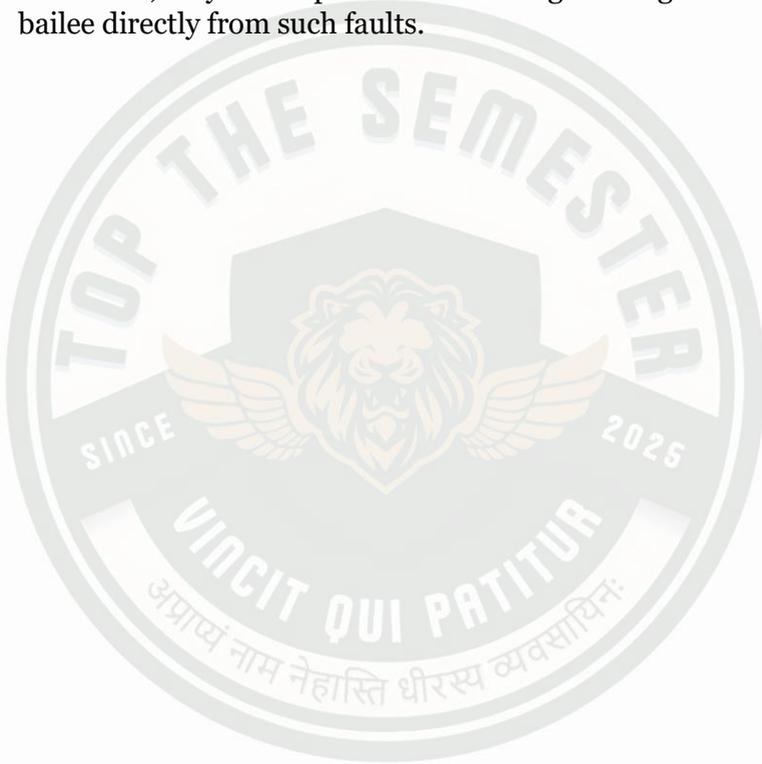
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Section 149 further adds that the bailor is responsible for disclosing all the faults in the goods bailed that would interfere with the use of them, or expose the bailee to extraordinary risks; if the bailor does not make such disclosure, they are responsible for damage arising to the bailee directly from such faults.



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DUTY OF BAILOR

The Indian Contract Act, 1872, explicitly outlines the duties of a bailor under a contract of bailment. It is vital for the bailor, who is the party delivering the goods, to abide by these duties to maintain a fair and equitable relationship with the bailee. These duties are stipulated in Sections 150 to 153 of the Act.

- 1. Duty to Disclose Known Faults (Section 150):** It is the bailor's duty to disclose all the faults in the goods bailed that are known to him, which could interfere with the use of the goods or expose the bailee to extraordinary risks. If the bailor fails to disclose such faults, he is responsible for damage arising to the bailee directly from such faults.
- 2. Duty to Bear Extraordinary Expenses (Section 151):** The bailor has the duty to bear all extraordinary expenses incurred by the bailee for the preservation of goods bailed.
- 3. Duty to Indemnify the Bailee (Section 152 and 153):** The bailor is bound to indemnify the bailee for any loss that the bailee may have incurred due to any defect in the title of the goods bailed. Additionally, if the bailee is not at fault and incurs a loss in respect of the goods bailed, the bailor is bound to indemnify the bailee.
- 4. Duty to Receive Back the Goods (Section**

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160): When the time period or purpose of bailment has ended, the bailor is obliged to receive the goods back from the bailee.

- 5. Duty to Pay Agreed Remuneration (Section 158):** If there is an agreement between the bailor and the bailee for any payment in respect of the bailment, the bailor is obliged to make such payment.

In the case of **Kaliaperumal vs. Visalakshi** (AIR 1962 Mad 44), it was ruled that a bailor's duty to disclose known faults to the bailee cannot be ignored. The court held that if a bailor knowingly lends a defective car to someone, which results in an accident, the bailor will be held responsible for the damage.

DUTIES OF BAILEE

Under a contract of bailment, the party receiving the goods, or the bailee, has certain obligations that need to be fulfilled. These duties are explicitly outlined in Sections 151 to 161 of the Indian Contract Act, 1872, which safeguard the interest of the bailor and ensure the bailee's accountability.

- 1. Duty to Take Care of Goods (Section 151):** The bailee is obliged to take as much care of the bailed goods as a person of ordinary prudence would take care of their own goods. This level of care is necessary to prevent any loss, destruction,

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or damage to the goods.

- 2. Duty Not to Make Unauthorized Use (Section 154):** The bailee should use the goods only for the purpose stipulated in the contract. Any unauthorized use of the goods which is inconsistent with the conditions of the bailment could make the bailee responsible for any damage arising from such use.
- 3. Duty Not to Mix Bailor's Goods (Section 155, 156, 157):** If the bailee, without the bailor's consent, mixes the goods with his own or goods of others, he is bound to bear the loss. Depending on whether the goods can be separated or not, the bailee might have to deliver an equivalent of the goods or compensate for the goods.
- 4. Duty to Return the Goods (Section 160):** The bailee is obliged 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. If the bailee fails to do this, he is responsible to the bailor for any loss, destruction, or deterioration of the goods from that time.
- 5. Duty to Return any Accretion to the Goods (Section 163):** The bailee is bound to deliver to the bailor, or according to his directions, any increase or profit (excluding the bailee's

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expenses) which may have accrued from the goods bailed.

A noteworthy case regarding the duties of a bailee is the Supreme Court's decision in **Moran Mar Basselios Catholicos and Another vs. Most Rev. Mar Poulouse Athanasius and Others** (AIR 1954 SC 526). In this case, the Court held that a bailee in possession of goods could resist their return to the bailor if the latter is in debt to the bailee in respect of those goods, reiterating the obligation of the bailor towards the bailee.

These duties ensure that the bailee acts in a responsible and lawful manner, respecting the bailor's rights and the terms of the bailment contract. Failure to adhere to these duties can result in legal repercussions and potentially damage the relationship between the bailor and the bailee.

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RIGHTS OF BAILOR

The Indian Contract Act, 1872, under Sections 153, 161, 163, and 166, delineates the rights of a bailor in a contract of bailment. These rights are designed to protect the interests of the bailor and ensure that the bailee fulfils their obligations:

- 1. Right to Demand Return of Goods (Section 161):** The bailor has the right to demand the return of goods as soon as the time period or purpose for which they were bailed has elapsed. If the bailee fails to return the goods, they may be liable for any loss, destruction, or deterioration of the goods.
- 2. Right to Receive Increase or Profit from Goods (Section 163):** Any accretion or profit (excluding the bailee's necessary expenses) derived from the goods bailed should be delivered to the bailor. This could be in the form of interest, dividend, etc.
- 3. Right to Terminate Bailment (Section 153):** If the bailee uses the bailed goods in a manner inconsistent with the conditions of the bailment, the bailor has the right to terminate the contract.
- 4. Right to Compensation (Section 166):** If the bailee does anything with the goods bailed inconsistent with the conditions of the bailment, the bailor has a right to compensation for any

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damage, loss, or destruction of the goods.

In the case of **Smt. Sugra Begum vs. Haji Kummua Mia Sahib** (AIR 1969 SC 878), it was held that the bailor's right to sue for redelivery of possession extends to all who wrongfully detain the goods, and not merely to the bailee.

These rights ensure that the bailor's interests are safeguarded, and they allow for proper recourse in the event that the bailee fails to meet their obligations under the contract of bailment. This balance of rights and duties between the bailor and bailee helps maintain the fairness of the bailment agreement.

RIGHTS OF BAILEE

The Indian Contract Act, 1872, in Sections 158, 159, 164, 165, 167, and 170-173, stipulates the rights of the bailee in a contract of bailment. These rights are designed to protect the bailee's interests and offer a degree of security against any undue claim by the bailor.

1. **Right to Recover Expenses (Section 158):** The bailee is entitled to recover any necessary expenses incurred for the preservation of the goods bailed.
2. **Right to Lien (Section 170, 171):** The bailee has a right to retain the goods until they receive due remuneration for the services they have rendered under the terms of the bailment. This can be a general lien (available to specific people)

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or a particular lien (available to all, only on goods for which the dues are pending).

- 3. Right to Indemnification (Section 164, 167):** The bailee has the right to receive damage from the bailor for any harm incurred due to the faults in the goods bailed. Also, if any loss occurs to a third person by the use of goods, and the bailee was not aware of the faults, the bailor is responsible to indemnify the bailee.
- 4. Right to Compensation (Section 159):** If the bailor wrongfully deprives the bailee of the use of the goods bailed, the bailee is entitled to receive compensation from the bailor.
- 5. Right to Sue (Section 180):** The bailee can sue third parties who wrongfully deprive them of the use or possession of the goods bailed or who cause them any injury.

In the case of Bank of India vs. Grains and Gunny Agencies (AIR 1971 SC 793), it was held that a bailee has the right to lien even against the true owner in respect of lawful charges for preservation of goods.

These rights of the bailee provide a level of security and protection against any undue claim by the bailor and ensure that the bailee's interests are safeguarded under the contract of bailment. The equilibrium maintained between the rights and duties of the bailee and bailor is crucial for a harmonious bailment agreement.

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LIEN AND RIGHT OF LIEN

A lien is a right that a person has over the goods of another, which entitles them to retain possession of such goods until certain legal claims are satisfied. It serves as a security interest over the property until the debt or duty is discharged. In the context of bailment, both the bailor and the bailee can have lien rights, although it is more commonly associated with the rights of the bailee.

The Indian Contract Act, 1872, explicitly provides for two types of liens in the context of bailment: Particular and General, described in Sections 170-171:

- 1. Particular Lien (Section 170):** A bailee has the right to retain specific goods until payment is made for the due amount. This amount could be due for the services rendered for those specific goods. This right is available to every bailee, irrespective of any contractual agreement.
- 2. General Lien (Section 171):** Unlike the particular lien, the general lien gives the bailee the right to retain any goods as security for a general balance of account. It could be for the amount due in respect of several different items. However, this right is not available to all bailees; only certain categories of bailees like bankers, factors, wharfingers, attorneys of a High Court, and policy brokers can exercise this right, as per the law unless it is agreed upon in a contract.

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In the case of **J.K. Synthetics Ltd vs. Collector of Central Excise, Jaipur** (1996 10 SCC 387), it was held that a banker's right of general lien is not an absolute right and can be restricted by a contractual agreement between the parties.

However, it is crucial to remember that these rights of lien do not permit the bailee to sell the goods if the bailor fails to pay his debt or perform his promise. The bailee must maintain the goods in the condition they were received, and once the dues are paid, they must return the goods to the bailor. Only under specific circumstances, such as under the terms of a contract, or if the law permits the sale of goods, can the bailee sell the goods to recover their due.

The concept of lien plays a pivotal role in bailment contracts, offering the bailee security against the bailor's default in payment or performance. By balancing the rights and obligations of both parties, it ensures equitable protection of their interests, reinforcing the integrity of contractual relationships.

INTRODUCTION TO PLEDGE

A pledge is a particular type of bailment where goods are delivered as security for payment of a debt or performance of a promise. This concept is elaborately covered under Sections 172 to 176 of the Indian Contract Act, 1872.

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The parties involved in a contract of pledge are the 'pawnor' (the person pledging the goods, equivalent to the bailor) and the 'pawnee' (the person to whom the goods are pledged, equivalent to the bailee).

Key features of a pledge are:

- 1. Delivery of Goods:** The goods must be delivered by the pawnor to the pawnee, either physically or constructively, to constitute a pledge. Constructive delivery occurs when the possession of goods is transferred without physically moving the goods, as in giving the key to a locked warehouse containing the goods.
- 2. Security for Debt or Performance:** The goods delivered act as security for the payment of a debt or the performance of a promise. If the pawnor defaults, the pawnee has the right to sell the goods to recover the amount due.
- 3. Pawnor's Title:** The pawnor must have a legal title to the goods, and he should have the authority to make a valid pledge of the goods. If he does not have clear title, he can still pledge the goods, but he will be responsible for any defects in the title.
- 4. Return of Goods:** Upon payment or satisfaction of the debt or promise, the pawnee must return the goods to the pawnor. If the pawnee fails to do so, he can be held liable for the non-return of the

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goods.

The leading case on the law of pledge is **Morvi Mercantile Bank Ltd. vs. Union of India** (1965 AIR 195). The Supreme Court held that the pledgee is entitled to file a suit for sale of the pledged goods in case of default by the pledgor and recover the balance due after deducting the sale proceeds.

The concept of pledge serves as a vital mechanism for securing debt repayment or obligation performance. It assures creditors of their interests while enabling debtors to access necessary funds or security, thereby fostering trust and efficiency in financial transactions

ESSENTIAL INGREDIENTS OR CHARACTERISTICS OF PLEDGE

A pledge, as defined under Section 172 of the Indian Contract Act, 1872, refers to a bailment of goods as security for payment of a debt or performance of a promise. There are several essential ingredients or characteristics which constitute a valid pledge:

1. **Bailment of Goods:** The first and foremost characteristic is that there must be a bailment, or delivery of goods. This delivery could be actual (physical transfer) or constructive (transfer of means of possession, such as keys to a warehouse), from the pawnor (the person pledging the goods) to the pawnee (the person to

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whom goods are pledged).

- 2. Delivery as Security:** The goods bailed must serve as security for the repayment of a debt or the performance of a promise. The delivery of goods must be made with this explicit understanding.
- 3. Presence of a Debt or Obligation:** A pledge is created to provide assurance for the payment of a debt or fulfillment of an obligation. Without such debt or promise, there can be no pledge.
- 4. Moveable Property:** The subject of a pledge must be a movable property. Immovable property cannot be pledged.
- 5. Rightful Ownership or Possession:** The pawnor must either be the owner of the goods or have the authority to pledge them. If the pawnor does not have a good title but still pledges the goods, he will be liable for any defects in the title and any resulting damages.
- 6. Possession of the Pawnee:** Upon the completion of the pledge, the goods must be in the possession of the pawnee, either actually or constructively.
- 7. Return of Goods:** Once the debt is repaid or the obligation is fulfilled, the goods must be returned to the pawnor. The pawnee only has a special property right – the right to retain and eventually

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sell the goods if the pawnor defaults. The general property, or ownership, remains with the pawnor.

- 8. Right to Sell on Default:** If the pawnor defaults on his obligation, the pawnee has the right to sell the pledged goods to recoup the debt or obligation. However, this must be done following the rules laid down in the Act (Sections 176).

In the landmark case **Kapildeo Prasad Singh vs. The State of Bihar & Ors** (1981 AIR 684), it was noted that the key test to establish a contract of pledge is the actual or constructive delivery of possession for the purpose of providing a security.



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RIGHTS OF PAWNEE

The rights of the pawnee, the party to whom goods are pledged, are provided under Sections 173-176 of the Indian Contract Act, 1872. These rights serve to protect the pawnee's interest and ensure that they are fairly compensated or repaid for their debt or promise.

1. **Right of Retainer (Section 173):** The pawnee has the right to retain the goods pledged until the payment has been made not only in respect of the debt or promise but also of the interest thereof and all necessary expenses incurred by the pawnee for the preservation of the goods pledged.
2. **Right of Sale (Section 176):** If the pawnor makes a 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 right to sell the goods. However, the pawnee must give the pawnor reasonable notice of the sale. If the proceeds of such sale are less than the amount due, the pawnor is still liable to pay the balance. If the proceeds of the sale are greater than the amount due, the pawnee must return the surplus to the pawnor.
3. **Right to sue for the debt or promise (Section 174):** If the pawnee chooses not to exercise the right to sell the goods, they can instead sue the pawnor for the amount due.

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4. **Right to Extraordinary Expenses (Section 175):** The pawnee is entitled to receive from the pawnor extraordinary expenses incurred for the preservation of the goods pledged.

In the case of **Lallan Prasad vs Rahmat Ali & Anr** (1967 AIR 1322), the Supreme Court held that it is a rule of universal application that pledgee has only a special property while the general property remains in the pledgor and wholly reverts to him when the debt is discharged.

These rights of the pawnee are significant in maintaining the balance of security and fairness in a pledge agreement, ensuring that the pawnee can recover their debt or promise effectively and efficiently.

COMPETENCY TO PLEDGE

The competency to pledge, which is essentially the legal capacity to make a valid pledge, is defined under Sections 178 and 178A of the Indian Contract Act, 1872.

According to Section 178A, if a pawnor has possession of goods or documents of title under a voidable contract, but the contract has not been rescinded at the time of the pledge, the pawnee acquires a good title to the goods, provided they act in good faith and without notice of the pawnor's defect of title.

However, in cases where goods are pledged by a person

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who is not the owner but who is in possession under a void agreement, such pledge is not valid.

Section 178 of the Act addresses pledges made by mercantile agents. It says that where a mercantile agent is, with the consent of the owner, in possession of goods or the document of title to goods, any pledge made by him, when acting in the ordinary course of business of a mercantile agent, shall be as valid as if he were expressly authorised by the owner of the goods to make the same; provided that the pawnee acts in good faith and has not at the time of the pledge notice that the pawnor has no authority to pledge.

Section 179 states that a person in possession of goods, having a mere right to use them, cannot create a pledge on these goods. It stipulates: "Where a person pledges goods in which he has only a limited interest, the pledge is valid to the extent of that interest."

Thus, the person competent to pledge is one who is either the owner of the goods or a mercantile agent who is in possession of the goods with the owner's consent and acts in good faith in the ordinary course of business.

In essence, the person pledging the goods should either be the owner or should have the authority to pledge the goods. This principle is particularly crucial in mercantile and commercial transactions.

The case of **Bank of Bihar Ltd. vs State of Bihar & Ors** (1971 AIR 1210) provides a valuable explanation in

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this context. Here, the Supreme Court held that if the pawnor is in possession of the goods or documents of title under a voidable contract and the contract is not rescinded at the time of the pledge, the pawnee acquires a good title.

Competency to pledge is based on the principle that you cannot give what you do not have, commonly known as "nemo dat quod non habet". Consequently, a non-owner cannot pass a good title unless they fall within the exceptions specified by the law. The legitimacy of the pawnee's title to the goods is, therefore, directly contingent on the pawnor's competency to pledge.

HYPOTHECATION

Hypothecation is a legal transaction where a debtor pledges collateral to secure a debt while retaining the ownership of the goods. The debtor possesses the goods, but the creditor has the right to seize the goods if the debtor fails to repay the debt.

In simple terms, hypothecation is a credit facility provided by the banks or financial institutions against the security of movable assets, mostly vehicles. The borrower remains in possession of the movable property, but the lender has the right to sell the property to recover the dues if the borrower defaults.

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Comparison with Pledge and Mortgage:

Hypothecation is often compared with concepts like "pledge" and "mortgage". The main difference lies in the possession of the collateral. In a pledge (as per Section 172 of the Indian Contract Act, 1872), the possession of the goods is transferred to the lender, whereas, in hypothecation, the borrower retains the possession.

A mortgage, on the other hand, pertains to immovable property (as defined under Section 58 of the Transfer of Property Act, 1882), while hypothecation deals with movable assets.

Legal Framework for Hypothecation in India:

The concept of hypothecation is provided under the Indian Companies Act, 2013 (Section 2(59)), and its enforcement is governed by the SARFAESI Act, 2002. The term is described in various rules and forms under the Companies (Creation and Modification of Charges) Rules, 2014. The SARFAESI Act, 2002, empowers the creditor to enforce the security interest without the intervention of the court.

Rights and Obligations in Hypothecation:

The debtor and the creditor in a hypothecation agreement have specific rights and obligations. The debtor, or the owner of the goods, retains the right of possession and can use the goods. However, the debtor is obligated to repay the debt according to the agreement. If they fail to repay, the creditor has the right to seize and sell the goods

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to recover the dues. The creditor is obliged to return the goods if the debtor repays the entire debt.

Key Features of Hypothecation

The concept of hypothecation is not directly defined in the Indian Contract Act, 1872, but it is governed under the provisions of the Sarfaesi Act, 2002 (Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002) and the Companies Act, 2013.

In the case of hypothecation, the lender holds a right to sell the property pledged as collateral upon default by the borrower. However, the lender must first take possession of the property before it can be sold.

Key features of hypothecation include:

1. **Ownership:** The borrower retains ownership of the goods and can use them while the loan remains outstanding. This is one of the primary differences between a pledge and hypothecation.
2. **Possession:** In a hypothecation agreement, the possession of goods is not transferred to the lender. The borrower retains both ownership and possession.
3. **Collateral:** Any movable property can be hypothecated. This is typically seen with vehicles and inventory.

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- Legal Action:** Unlike in the case of a pledge, in hypothecation, the lender must obtain a decree from the court to take possession of the collateral in case of default by the borrower.
- Floating Charge:** Hypothecation often results in a 'floating charge'. This means the borrower can sell the hypothecated goods in the ordinary course of business. The charge becomes 'fixed' only when the loan becomes due or in case of a default.

The landmark case **Bank of India vs Custodian & Ors** (1997 AIR 2208) underlined the rights of a creditor in cases of hypothecation. It confirmed that a creditor has a right to sell hypothecated goods only after taking possession and that until then, the debtor remains in possession of the goods.

Hypothecation is a key concept in banking and finance, particularly for loans secured against movable property. It offers flexibility by allowing debtors to retain asset usage while providing creditors with security for repayment, balancing the interests of both parties effectively.

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1.4 DEFINITIONS OF AGENT AND PRINCIPAL, CREATION OF AGENCY AND ITS TERMINATION

Introduction to Agency

In legal terms, an agency is a fiduciary relationship established when one person (the principal) authorizes another person (the agent) to act on their behalf. The agent represents the principal in business transactions or other dealings, creating a legal relationship between the principal, the agent, and third parties.

The concept of agency is elaborated in Chapter X (Sections 182-238) of the Indian Contract Act, 1872. Section 182 defines an "agent" as a person employed to do any act for another, or to represent another in dealings with third persons. The person for whom such act is done, or who is so represented, is called the "principal".

Key aspects of agency include:

1. **Formation of Agency:** An agency can be created by express or implied agreement, necessity, ratification, or operation of law.
2. **Capacity:** A minor or an incompetent person cannot be a principal, but they can be an agent because the agent does not need contractual capacity. The principal must have the capacity as they are the ones who will be bound by the

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contract.

- Duties and Rights:** The agent owes various duties to the principal, such as the duty to carry out the work undertaken, duty to follow principal's directions, duty of care and skill, duty of integrity, etc. In return, the agent has the right to receive agreed remuneration, right of lien on principal's goods, right of indemnity and compensation, among others.
- Liability of Parties:** In general, an agent is not personally liable to the third party as the contract is between the principal and the third party. However, the agent may become personally liable under certain conditions, such as when acting for an undisclosed principal.
- Termination of Agency:** Agency may be terminated by act of parties, by operation of law, or due to certain changes in circumstances.

In the landmark case of **Harpum vs. Neville** (1848), the Court recognized that an agent owes a fiduciary duty to the principal to act loyally and in good faith for the principal's benefit.

The concept of agency is foundational in legal practice, with wide-ranging applications in business, personal affairs, and litigation. Agents act on behalf of principals in diverse scenarios, from real estate transactions to commercial negotiations, making a thorough

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understanding of this relationship indispensable

Essentials of Agency

Agency is a crucial concept in law and commerce. To establish an agency relationship, certain essential elements must be present. The Indian Contract Act, 1872, in Chapter X (Sections 182-238), offers comprehensive coverage of the concept of agency.

Here are the essential elements or conditions for a valid agency:

- 1. Agreement between Principal and Agent:** The very first requirement is the agreement between the agent and the principal. This agreement could be express (clearly stated in words) or implied (understood from the circumstances, conduct, or relationship of the parties). Express agency agreements can be oral or written.
- 2. Intention to Act as Agent and Principal:** The individual agreeing to act as the agent should intend to represent the principal. Similarly, the principal must intend the agent to work on their behalf.
- 3. Competency of Principal:** The principal must be competent to contract. According to the Indian Contract Act, Section 183, any person who is of

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the age of majority and of sound mind, or is not disqualified from contracting by any law to which he is subject, may employ an agent. A minor or mentally unstable person can't be a principal.

- 4. No Formal Consideration Required:** Consideration is not required to create an agency relationship. An agency can be established without payment to the agent.
- 5. Legal Purpose:** The agent's role should be for a legal purpose. Any agency relationship formed for an illegal act or purpose will be considered void.
- 6. Fiduciary Relationship:** The relationship between a principal and an agent is fiduciary, which means it is based on trust and confidence. The agent must act in the best interest of the principal.
- 7. Control of the Principal:** The principal has the right to control the actions of the agent. The agent is bound to act according to the directions or instructions given by the principal.

Agency can be established by express agreement or through implication, and the intention to act on behalf of the principal is crucial.

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Agent and Servant

The terms 'agent' and 'servant' are often used interchangeably, but they have different legal connotations. While both roles involve acting on behalf of another, they differ in the degree of control the employer (or principal) has over the actions of the individual involved.

1. **Agent:** According to Section 182 of the Indian Contract Act, 1872, an agent is a person employed to do any act for another (the principal) or to represent another in dealings with third parties. The person for whom such act is done or who is represented is called the 'principal'. The agent can bind the principal by his actions, creating a contractual relationship between the principal and the third party.
2. **Servant:** A servant, on the other hand, is an individual hired to perform services for another, usually referred to as the 'employer'. A servant is not authorised to act on behalf of the employer in dealings with third parties. They work under the direct control and supervision of the employer and their actions do not create contractual obligations for the employer with third parties.

Key differences between an agent and a servant:

1. **Creation of Contractual Rights:** An agent can create contractual rights and obligations between

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the principal and third parties. A servant cannot do this – they merely perform tasks as directed by the employer.

2. **Control:** The principal has less control over the actions of the agent, as the agent exercises discretion and independent judgement within the scope of their authority. In contrast, a servant works under the direct control and supervision of the employer.
3. **Scope of Work:** The agent's role is typically more expansive and involves decision-making authority. A servant's role is more narrow, often involving specific tasks as directed by the employer.
4. **Legal Representation:** An agent legally represents the principal in transactions with third parties, whereas a servant does not represent the employer in this way.

The Supreme Court, in the case of **Dharangadhara Chemical Works Ltd. Vs. State of Saurashtra** (AIR 1957 SC 264), distinguished between a contract of service (servant) and a contract for service (independent contractor, similar to an agent). The control test was introduced where the nature of control the employer has over the worker is significant.

Distinguishing between an agent and a servant is vital, as it determines the extent of the principal's or employer's

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liability for wrongdoing or breach of duty. This distinction also shapes third-party interactions and obligations, making it a critical consideration in business and legal contexts

Competency of Agent and Principal

The competency of both the agent and the principal is a fundamental aspect of agency law. It dictates the validity and enforceability of the actions carried out by the agent on behalf of the principal.

According to the Indian Contract Act, 1872, the rules for the competency of an agent and principal are covered under Sections 183 and 184.

Competency of Principal (Section 183):

Any person who is of the age of majority according to the law to which he is subject, and who is of sound mind, may employ an agent. Thus, to be a principal, a person must be:

1. Of the age of majority
2. Of sound mind
3. Not disqualified from contracting by any law

It means that minors, persons of unsound mind, and people disqualified by law from entering into a contract cannot appoint agents. If such persons do appoint agents,

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any contract formed by the agent on behalf of the principal will be void.

Competency of Agent (Section 184):

As per Section 184 of the Indian Contract Act, any person can become an agent. But for the purpose of being an agent:

1. No consideration is necessary to create an agency
2. The agent must be competent to contract (in the sense of being able to understand the nature of the contract)
3. It is not necessary for a person to be competent to contract to be an agent, i.e., even a minor or a person of unsound mind can become an agent. However, the agent must not be a person who is disqualified from contracting by any law.

Thus, while the agent needs to understand the implications of the actions being carried out, they do not necessarily need to be capable of entering into a contract themselves. This rule is especially important because it allows businesses to employ people who might otherwise be unable to form contracts, such as minors, as agents.

It's also important to note that an agent who is not competent to contract cannot personally enforce, or be bound by, contracts they have entered into on behalf of their principal.

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Section 185 further states that no consideration is necessary to create an agency. This means the act of appointing an agent does not need to involve any form of payment or compensation. A principal can appoint an agent without paying them any consideration, and the agency contract would still be valid.

In the case of **Tan Kim Choo v. Caledonian Insurance Co. Ltd.**, 5 W.R. 507, the court held that a minor can act as an agent, but the minor agent cannot be held personally liable for the contracts they enter into on behalf of the principal.

Creation of Agency

The creation of agency refers to the establishment of a relationship where one person (the agent) is authorized to act on behalf of another person (the principal). The Indian Contract Act, 1872 provides for the creation of agency in several ways, as set out in Sections 186 to 191:

1. **Express Appointment (Section 186):** An agency can be expressly created by the principal. This occurs when the principal explicitly appoints someone as their agent. This can be done orally or in writing. There is no legal requirement that the appointment must be in writing, except in certain cases (such as in the appointment of agents for the sale or purchase of immovable property, which must be done in writing).
2. **Implied Appointment (Section 187):** Agency

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can also be created by implication, i.e., from the circumstances of the case, the conduct of the parties, or the nature of the situation or transaction. For example, a wife has implied authority to pledge her husband's credit for necessaries suitable to their lifestyle.

- 3. Agency by Ratification (Section 196 to 200):** Ratification refers to the approval or confirmation of an act performed on behalf of another without authority. If a person, without being authorized, does an act or enters into a contract on behalf of another, and if the latter, after knowing about it, approves it, then it results in an agency by ratification.
- 4. Agency by Necessity (Section 189):** This type of agency arises in situations where an agent is compelled to act beyond their authority in an emergency to protect the interest of the principal. This requires that the agent cannot communicate with the principal, and the agent's action is necessary to prevent loss to the principal with respect to the property committed to the agent's care.
- 5. Agency by Estoppel (Section 237):** If a person, by his words or conduct, leads another person to believe that a certain person is his agent, then he is stopped from denying the agency later. This principle is based on the equitable doctrine

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of estoppel.

- 6. Agency by Holding Out:** This is a type of implied agency. Here, the principal leads others to believe that a person is acting as their agent, even if they have not expressly appointed them as such.

The principal must have full knowledge of all material circumstances for valid ratification.

It's essential to note that, irrespective of how an agency is created, the agent must always act within the scope of their authority and in the best interests of the principal. If they fail to do so, they may be held liable for any loss or damage caused due to their actions.

Definitions of Agent and Principal

In the context of contract law, an "agent" and a "principal" are two key roles in a contractual relationship. The definitions of both terms, as provided by the Indian Contract Act of 1872, clarify their roles and responsibilities.

- 1. Agent (Section 182):** An agent, according to the Act, is a person employed to do any act for another or to represent another in dealings with third persons. The individual for whom such act is done or who is so represented is called the 'principal'. The agent's primary responsibility is to represent the principal in various transactions or activities

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and can bind the principal with his or her actions. This representative relationship is based on trust and confidence.

- 2. Principal (Section 182):** A principal, as per the Act, is the person who employs another person (the agent) to act on his behalf. The principal gives the agent authority to perform certain acts or functions on their behalf. The principal is responsible for the acts of the agent performed within the scope of the authority given.

In simple terms, the agent is the one authorized to act, and the principal is the one on whose behalf the agent acts. The relationship between the principal and the agent should be direct and immediate.

The crucial test of an agency is the right to exercise authority and to do the act in a particular way, which was under the control of the principal.

While there are different types of agents and principals, the fundamental principle remains the same: the agent has the power to affect the principal's legal status by their acts and the principal has the right to control the agent's actions. The creation of the agent-principal relationship is based on the consent of both parties, and both parties have duties and rights towards each other.

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Rights of an Agent

The Indian Contract Act, 1872 sets out the rights and duties of an agent in relation to the principal.

Here are the main rights an agent has under the Act:

1. **Right to Remuneration (Section 219):** An agent has the right to receive the agreed-upon remuneration for his services. If no specific remuneration is agreed upon, the agent is entitled to a reasonable commission or fee.
2. **Right of Retainer (Section 217):** The agent has the right to retain any money received on behalf of the principal until any dues or debts owed to the agent by the principal have been cleared. This essentially is the right to set-off the amount due to him by the principal.
3. **Right of Indemnity (lawful acts) (Section 222):** The principal must indemnify the agent against the consequences of all lawful acts done by the agent in exercise of the authority conferred upon him. This includes all losses and liabilities the agent incurs while carrying out his duties.
4. **Right of Compensation (Section 225):** The agent has the right to be compensated for any injury suffered due to the principal's neglect or lack of skill.
5. **Right of Lien (Section 221):** An agent has a

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right to retain goods, papers, and other property, whether movable or immovable, of the principal received by him, until the amount due to himself for commission, disbursements, and services in respect of the same has been paid or accounted for to him. This is known as the right of "particular lien" and not a "general lien".

- 6. Right to Indemnity (Good faith) (Section 223):** Section 223 provides that the agent has a right to be indemnified against the consequences of acts done in good faith, even if it causes injury to the rights of third persons. This holds true unless the agent acted negligently or without exercising reasonable diligence.

Remember that these rights coexist with the responsibilities of the agent. Agents are obliged to conduct the business of their principal according to the directions given by the principal. The principal is also entitled to compensation for any breach of duty by the agent.

The relationship between principal and agent is primarily a fiduciary relationship, and the agent is bound to protect the interests of the principal. This implies that while an agent enjoys several rights, these rights come with the duty to serve the principal's interests with utmost integrity and loyalty.

Section 220 of the Indian Contract Act, 1872, stipulates that "An agent who is guilty of misconduct in the business

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of the agency is not entitled to any remuneration in respect of that part of the business which he has misconducted."

Section 220 highlights a limitation to an agent's right to remuneration, whereby they can lose their right to remuneration if they are found to be guilty of misconduct in their agency-related activities.

Duties of an Agent

The duties of an agent are clearly outlined in the Indian Contract Act, 1872. Here are the key duties of an agent as prescribed in the Act:

- 1. Duty to Follow Principal's Directions or Custom (Section 211):** The agent must act according to the principal's directions or, in the absence of any such directions, according to the custom which prevails in doing the kind of business he is engaged in.
- 2. Duty to Carry Out Work with Skill and Diligence (Section 212):** An agent is bound to conduct the business of the agency with as much skill as is generally possessed by persons engaged in similar business unless the principal has notice of his want of skill. The agent must also make compensation to his principal in respect of direct consequences of his own neglect, default or want of skill.

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3. **Duty to Render Proper Accounts (Section 213):** An agent is bound to render proper accounts to his principal on demand.
4. **Duty to Communicate (Section 214):** It is the duty of an agent, in cases of difficulty, to use all reasonable diligence in communicating with his principal and in seeking to obtain his instructions.
5. **Duty Not to Deal on His Own Account (Section 215):** Without the consent of the principal, an agent must not deal on his own account in the business of the agency; that is, he must not make any profit out of his agency apart from his remuneration.
6. **Duty to Pay Sums Received for Principal (Section 218):** Subject to such deductions, the agent is duty-bound to pay to his principal all sums received on his account.
7. **Duty not to Delegate (Section 190):** An agent, being entrusted with specific functions, must perform those functions personally and should not delegate his duties to another person unless by the nature of the agency, a delegation is necessary.
8. **Duty to Not to Make Secret Profits (Section 216):** The agent has a duty not to make a secret profit out of his agency. Any secret profit made is recoverable by the principal.

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- 9. 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.

These duties illustrate that the relationship between the agent and the principal is fiduciary in nature. This means that the agent must act in the best interests of the principal, maintain good faith, trust, confidence and a duty to act with the utmost honesty and loyalty.

Where the agent acts in the name of the principal, the latter becomes bound by the act of his agent and he is responsible for his acts. This binds the agent to perform in the best interests of the principal.

An agent owes a duty to the principal to act with utmost good faith, integrity, loyalty, and fidelity. It was also stated that he should not make any profit out of his agency other than his usual remuneration, unless agreed otherwise by the principal.

Remember, a breach of duty by the agent can lead to the termination of the agency and also the agent becoming liable for any loss caused to the principal due to the breach.

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Rights of a Principal

In the agency relationship, not only does the agent have certain rights, but the principal also has several rights outlined by the Indian Contract Act, 1872. Here are the principal's key rights:

- 1. Right to Revoke the Agency (Section 203):** The principal has the right to revoke the agent's authority at any time, either from the completion of the agency or before the time the agent was appointed to act.
- 2. Right to Instruct:** The principal has the right to give instructions to the agent, and it is the agent's duty to act in accordance with these instructions as long as they are lawful and reasonable.
- 3. Right to Remuneration:** If the agent has breached the terms of the contract, the principal has the right to withhold the agent's remuneration.
- 4. Right to Resist Agent's Unlawful Act:** If an agent acts unlawfully and against the instructions of the principal, the principal has the right to resist any claim made by the agent for indemnity.
- 5. Right against the agent in case of direct conflict of interest (Section 210):** If an agent deals in the business of the agency on his own account without first obtaining the consent of the

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principal and acquainting him with all material circumstances which have come to his own knowledge on the subject, the principal may repudiate the transaction.

6. **Right to claim damage (Section 225):** Where the agent has acted without authority or has exceeded the given authority, the principal has a right to claim any damages that may have resulted from the agent's actions.
7. **Right to Benefit from Agency (Section 215 and 216):** A principal is entitled to all the benefits which the agent has acquired while acting as an agent. If an agent takes any secret profit or bribe in connection with the agency, the principal has a right to claim it from the agent.
8. **Right to Receive Accounts (Section 213):** A principal has the right to receive a complete set of accounts from his agent at any time during the course of the agency.

Remember, these rights also come with certain duties. The principal is required to indemnify the agent for any losses incurred due to the actions of the agent carried out on behalf of the principal, and to pay the agreed remuneration to the agent.

In general, the principal can revoke the agent's authority at any time, even if the agent has incurred expenses or suffered loss on the assumption that the agency would

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continue for a certain period of time. However, this right is not absolute and can be subject to conditions in the contract of agency.

Duties of a Principal

The Indian Contract Act, 1872 also outlines the duties of the principal towards the agent. Here are the main duties of a principal as per the Act:

- 1. Duty to Indemnify the Agent (Section 222):** The principal is obligated to indemnify the agent against the consequences of all lawful acts done by such agent in exercise of the authority conferred upon him. This means that the principal must make good any loss the agent might have incurred while acting lawfully under the agency agreement.
- 2. Duty to Pay Agreed Remuneration (Section 219):** The principal must pay to the agent the agreed-upon remuneration for his services. If no specific remuneration is agreed upon, the principal must pay the agent a reasonable commission or fee for his services.
- 3. Duty to Indemnify Agent against Consequences of Acts Done in Good Faith (Section 223):** When an agent does an act in good faith, and it causes injury to the rights of third persons, the principal must indemnify the

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agent against the consequences of that act, though it causes an injury to such rights.

- 4. Duty to Compensate the Agent in Respect of Injury Caused by Principal's Neglect (Section 225):** The principal must make compensation to his agent in respect of injury caused to such agent by the principal's neglect or lack of skill.
- 5. Principal's Duty where Agent's Authority is Partially Revoked (Section 207):** If a principal revokes the agent's authority before it has been fully exercised, he must make compensation to the agent, and to third parties, for any resulting loss.

The duties of a principal emphasise the fiduciary nature of the relationship between the principal and agent. The principal must act in good faith, not cause harm to the agent and fulfill all obligations to the agent in order for the agency relationship to be effective.

Agent's Authority

The authority of an agent is the power which he has to affect the legal relations of his principal by acts done in accordance with the principal's manifestation of consent.

Extent of Agent's Authority (Section 188):

According to Section 188, an agent, having an authority

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to do an act, has the right to do every lawful thing necessary in order to complete such an act.

The agent's authority can be broadly classified into two types as per the Indian Contract Act, 1872: Actual Authority and Ostensible or Apparent Authority.

1. Actual Authority (Sections 186 and 187):

Actual Authority is when the principal has expressly or impliedly granted permission to the agent to act on his behalf. It can be further divided into:

- **Express Authority:** This is the authority given by the principal to the agent in clear, direct, and definite terms. It may be given orally or in writing. For example, a principal telling his agent to sell a particular item is giving express authority.
- **Implied Authority:** This refers to an agent having the authority to do a certain act or series of acts that, in the ordinary course of business, would be seen as incidental or ancillary to the act the agent is directed to do. For example, a manager in a shop has the implied authority to sell items in the shop.

2. Ostensible or Apparent Authority (Section 237):

Apparent or ostensible authority is the authority of an agent as it appears to others. This can occur if the principal's behavior would lead a reasonable person to

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believe that the agent had authority, even if no actual authority was granted. In this case, the principal is estopped from denying the grant of such authority if third parties have acted in reliance on the apparent authority of the agent.

It is important to note Section 238 of the Act which states that an agent having authority to do an act has authority to do every lawful thing necessary to complete the act.

Moreover, an agent cannot personally enforce, nor be bound by, contracts on behalf of his principal, unless he has either an express or implied authority to that effect as per Section 230.

Landmark cases like **Freeman & Lockyer v Buckhurst Park Properties (Mangal) Ltd** [1964] 2 QB 480 have clearly emphasized that if a principal represents that an agent is carrying on his business, he is liable for the debts contracted by the agent in the name of his business.

The scope of an agent's authority is pivotal, as it governs the validity of contracts executed by the agent and the principal's liability for those actions. A principal is legally bound by acts performed within the agent's authority, underscoring the importance of clearly defining such limits.

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Agent's Authority in Emergency

The Indian Contract Act, 1872 provides for a special provision where an agent gets certain authority during an emergency. Section 189 of the Act states:

"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."

This provision gives the agent the power to act beyond his ordinary authority to prevent a loss to the principal during an emergency situation. The agent can perform any act which a reasonable person would do to safeguard his own interests under the same circumstances.

An agent has the authority to take all reasonable steps to protect his principal in an emergency, where the principal cannot be contacted in time.

This implies that, if a situation arises that requires immediate action to prevent harm or loss to the principal's property, and the agent is unable to communicate with the principal due to the urgent nature of the situation, the agent can take the necessary action to protect the principal's interests, even if the action falls outside the scope of the agent's ordinary authority.

However, the agent must exercise this power in good faith and the actions taken must be justifiable under the given circumstances.

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Examples/Scenarios of Exercising Emergency Powers

1. **Existence of an Emergency:** The emergency must be real and imminent. A mere possibility or apprehension of an emergency is not enough.
2. **Inability to Communicate with the Principal:** The agent must have attempted to communicate with the principal, and it must be established that it was not possible to get the instructions of the principal in time.
3. **Protection of Principal's Interest:** The agent's actions should aim at protecting the principal's interests from loss.
4. **Prudent Action:** The action taken by the agent must be what a person of ordinary prudence would do in his own case under similar circumstances.
5. **Consistent with the Principal's Interests:** The action taken must not be in conflict with the express or implied instructions of the principal, or the principal's known wishes.

For example, if a consignment of perishable goods has been sent to an agent for sale, and the market conditions change suddenly making the goods likely to spoil or drastically reduce in value, the agent could sell the goods immediately, even if he was originally instructed to hold them for a specific period.

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However, it's worth noting that the agent's actions during an emergency are open to scrutiny. The agent's decision must be reasonable given the circumstances and the principal is within his rights to question the agent's decision if he believes that the agent acted unreasonably or irresponsibly.

The right of the agent to act during an emergency does not give him a *carte blanche* to act in any way he chooses, rather it gives him the discretion to take reasonable and necessary steps to protect the interests of the principal. The determination of what constitutes an 'emergency' and what actions are 'reasonable' under such circumstances would be made based on the facts and circumstances of each case.

Effect of Misrepresentation and Fraud on Agency

The law surrounding misrepresentation and fraud is vital in the context of agency. If an agency relationship is created under conditions of fraud or misrepresentation, it can have serious implications. The Indian Contract Act, 1872 addresses this issue in Section 238 and Section 17.

1. Misrepresentation (Section 238):

Misrepresentation, as defined by the Act, refers to a positive assertion that is not warranted by the information of the person making it. If an agency is created by the agent falsely claiming that they have the authority to act as an agent, the principal is not bound by

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the acts of the agent. However, such acts may bind the agent towards the third party.

The implications are as follows:

- The agent may be required to compensate the third party for any losses incurred due to reliance on the agent's misrepresentation of his authority.
- The principal may be able to claim damages against the agent for any loss caused by the agent's misrepresentation of his authority.

2. Fraud (Section 17):

Fraud occurs when false representations are made knowingly, or without belief in their truth, or recklessly without caring whether they are true or false. If an agent fraudulently makes a contract on behalf of the principal, the contract can be voidable at the option of the principal. This is provided under Section 19 of the Indian Contract Act, 1872.

If the agent's act is fraudulent, or facts are concealed by the agent, or if the agent acts beyond his authority, the principal is not bound by such acts. However, the agent would be personally liable for such acts.

Case Law:

A notable case on this matter is Satgur Prasad v. Har Narain Das (AIR 1932 All 141). In this case, the court ruled that the principal is not liable if the agency was

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created due to fraud by the agent.

It is evident that the establishment and operation of agency is significantly impacted by instances of fraud and misrepresentation. If an agent acts fraudulently or misrepresents his authority, this can result in the agent being personally liable and the principal having the right to repudiate the contract.

Termination of Agency

An agency can come to an end in a variety of ways as per the provisions of the Indian Contract Act, 1872. The following sections detail the circumstances under which an agency may be terminated:

1. By the Act of the Parties (Section 201):

An agency is terminated by the principal revoking the agency, or by the agent renouncing the business of the agency. However, this revocation or renouncement must be done in accordance with the terms of the contract of agency, and it may not prejudice any rights acquired by third parties in good faith prior to the notice of revocation or renouncement.

2. By the Principal or Agent's Death or Mental Incapacity (Section 201):

The agency is terminated when the principal or agent dies or becomes of unsound mind. The principal's representatives in case of death, and the agent, must

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make the termination known to the other party.

3. By Business Being Completed:

If an agency was created for a specific purpose or for a defined period, it will automatically terminate once that purpose is achieved or that period is over.

4. By Insolvency of the Principal:

If the principal is declared insolvent, the agency may be terminated.

5. By Destruction of Subject Matter:

If the subject matter of the agency is destroyed or rendered non-existent, the agency is automatically terminated.

6. By Principal becoming an Alien Enemy:

If the principal becomes an alien enemy, the agency may be terminated.

7. By Dissolution of Company or Insolvency of Principal:

If the principal (if a company) is dissolved or becomes insolvent, the agency terminates.

8. By the Agent's Misconduct:

If the agent breaches his duties or acts in a way that is detrimental to the principal's interest, the principal may choose to terminate the agency.

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9. By the Agent's Incapacity to Act:

If the agent becomes incapable of performing his duties, the principal can terminate the agency.

10. Section 203 – When principal may revoke the authority:

As per Section 203, the principal may revoke the authority of the agent at any time before it has been exercised to complete the business of the agency. However, the principal must compensate the agent for any loss or damage caused by such a revocation. This might be the case if the agent had already incurred expenses or had taken steps to act on the agency agreement before the revocation.

11. Section 206 – Revocation where authority has been partly exercised:

Section 206 provides that 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 from acts already done in the agency. This provision means that if the agent has partly exercised his authority, the principal cannot revoke the agent's authority regarding actions that have already been taken. Therefore, the principal is obligated to allow the agent to complete those transactions.

While termination of agency relieves the agent of his/her duties towards the principal, it's essential to note that certain obligations may continue post-termination. For

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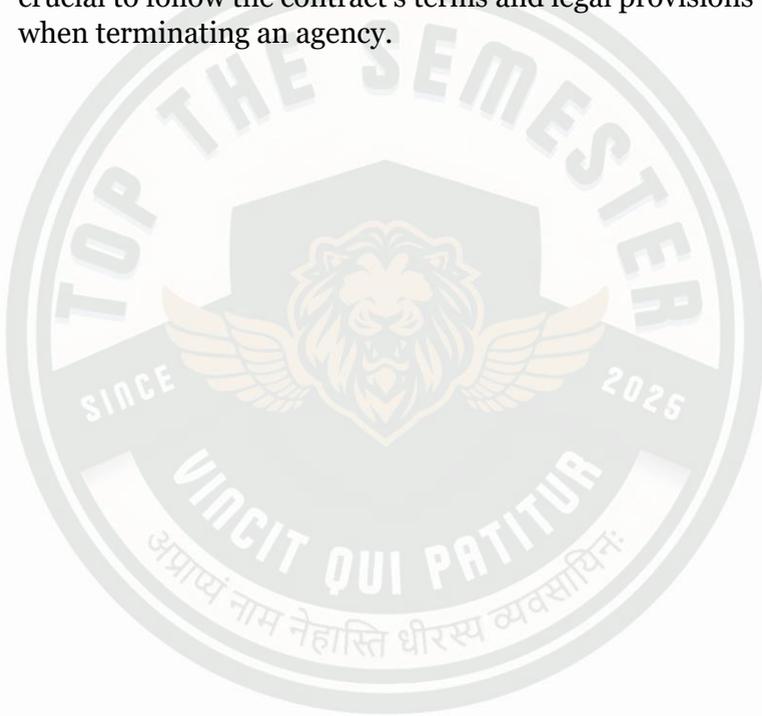
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instance, the duty of confidentiality generally continues even after the termination of the agency.

Remember, the termination of an agency may have significant legal implications, affecting the rights, duties, and obligations of all parties involved. Therefore, it's crucial to follow the contract's terms and legal provisions when terminating an agency.



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UNIT 2

THE INDIAN PARTNERSHIP ACT, 1932

INTRODUCTION AND OVERVIEW OF THE INDIAN PARTNERSHIP ACT, 1932

The Indian Partnership Act, of 1932, is an act enacted by the Parliament of India to regulate the formation, functioning, rights, and duties of partners and partnerships in the country. It provides a legal and systematic framework for partnerships, which are one of the most common types of business entities operating in India.

The Act came into force on 1st October 1932 and is applicable to the whole of India except the State of Jammu and Kashmir. A partnership under the Act is defined as “the relation between persons who have agreed to share the profits of a business carried on by all or any of them acting for all”. This definition stresses three fundamental aspects of a partnership:

1. There must be an agreement entered into orally or in writing by the persons who desire to form a partnership.
2. The object of the partnership should be to share the profits of a business.

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3. The business must be carried on by all the partners or any of them acting for all.

The Act also clarifies that the sharing of profits or losses, or the mutual agency relationship between partners, is proof of the existence of a partnership.

Key Features and Provisions of the Act

The Indian Partnership Act is divided into sections, each dealing with different aspects of a partnership.

Section 4 - Definition and Nature of Partnership: This section defines a partnership as the relation between persons who have agreed to share the profits of a business carried on by all or any of them acting for all.

Section 6 - Mode of determining the existence of a partnership: This section defines the ways in which a partnership can be determined. It stipulates that sharing of profits or income from an asset by itself doesn't establish a partnership.

Section 7 - Partnership at will: Where no provision is made by contract between the partners for the duration of their partnership, or for the determination of their partnership, the partnership is "partnership at will".

Section 9 - General Duties of Partners: Every partner is bound to carry on the firm's business to the greatest common advantage, to be just and faithful to each other, and to render true accounts and full information of all

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things affecting the firm to any partner or his legal representative.

Section 13 - Mutual Rights and Liabilities: The partners are bound to share equally the profits earned, and shall contribute equally to the losses sustained by the firm.

Section 14 - The property of the firm: All properties, rights, and interests in a property that are acquired with the money of the firm are deemed to be the firm's property.

Section 25 - Liability of a partner for acts of the firm: Every partner is liable, jointly with all the other partners and also severally, for all acts of the firm done while he is a partner.

Duli Chand v Commissioner of Income Tax, Delhi [1956 AIR 174, 1955 SCR (2) 995]: This is a landmark case that interpreted the provision of partnership at will under the Act. The Supreme Court of India held that a reconstitution of a partnership firm results in a new agreement of partnership and therefore a new partnership. It observed that the partnership at will can be dissolved by any partner by giving notice in writing to all other partners.

CIT vs. R.M. Chidambaram Pillai [1977 AIR 676, 1977 SCR (2) 790]: In this case, the Supreme Court held that the sharing of profits or income from an asset does not of itself establish a partnership, whether the persons sharing such profits have or have not a joint or common

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right or interest in the property which produces the profits. It further held that the mere fact that a business is carried on by persons in joint ownership does not of itself create a partnership.

The Indian Partnership Act, 1932, has been the cornerstone of the legal framework governing partnerships in India. It has clearly defined the rights, duties, and obligations of partners in a partnership, providing a clear and coherent legal structure for businesses to operate under the partnership model. However, it is important to note that each partnership is unique and governed by its specific terms as agreed upon by the partners. This detailed statutory framework, backed by rich judicial interpretation, plays a vital role in enabling partnerships to contribute significantly to the Indian economy.

2.1 NATURE OF PARTNERSHIP FIRM

The Indian Partnership Act, 1932 defines a partnership and provides a framework for understanding the nature and functioning of partnership firms in India. As per Section 4 of the Act, a partnership is defined as a "relation between persons who have agreed to share the profits of a business carried on by all or any of them acting for all". Let's delve into the various aspects that construct the nature of a partnership firm.

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1. Contractual Relationship:

The basis of a partnership is a contractual agreement between the partners. The agreement, which can be oral or written (known as a partnership deed), establishes the rights and obligations of each partner. This contract between the partners is fundamental to the establishment of the partnership. If there is no agreement, there is no partnership. It's also important to note that minors cannot be partners, since they are incapable of entering into a legal contract under the Indian Contract Act, 1872.

2. Sharing of Profits:

One of the fundamental characteristics of a partnership is the sharing of profits and losses among the partners. The profit sharing ratio is typically outlined in the partnership deed. If the partnership deed does not specify the profit sharing ratio, profits and losses are shared equally among the partners, regardless of their capital contribution or level of involvement in the firm's operations, as per Section 13(b) of the Act.

3. Business Entity:

The partnership must be for the purpose of conducting a business. 'Business' includes every trade, occupation or profession as defined in Section 2(b) of the Act.

4. Mutual Agency:

In a partnership, every partner is both an agent and a principal. A partner, when acting in the ordinary course

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of business, can bind the other partners by his actions. This principle of mutual agency is the real test of partnership. If a person has no right to act as an agent on behalf of others and cannot bind them by his actions, then he cannot be a partner.

5. Unlimited Liability:

In a partnership firm, the partners have unlimited liability. This means that if the assets of the firm are insufficient to meet the firm's obligations, the personal assets of the partners can be used for this purpose. Each partner is jointly and severally liable for the actions of the firm and the other partners.

6. Number of Partners:

According to the Act, a partnership must be composed of at least two persons. The maximum number of partners is 50 as per the Companies Act, 2013. If the number of partners exceeds this, the partnership becomes illegal, and the partnership firm would need to be registered as a company.

7. Voluntary Registration:

The registration of a partnership firm is not mandatory under the Indian Partnership Act, 1932. However, if the firm is not registered, it is deprived of certain benefits, thus making registration beneficial.

Khushal Khemgar Shah vs Khorshed Banu [1970 AIR 1153, 1970 SCR (3) 689]: The Supreme Court in

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this case held that the essence of a partnership is that each partner is, in law, the agent and principal of the other partners.

CIT vs. R.M. Chidambaram Pillai [1977 AIR 676, 1977 SCR (2) 790]: This case reinforced the principle that the sharing of profits does not of itself create a partnership and that the real test of partnership is the mutual agency relation.

Understanding the nature of partnership firms is essential, as it clarifies their formation, operation, and legal framework. This knowledge enables potential partners to make informed decisions and navigate the responsibilities and benefits of such business structures effectively.

2.2 RIGHTS /DUTIES OF PARTNERS INTER SE

Rights of Partners Under The Indian Partnership Act, 1932

Partners in a firm have several rights as prescribed under the Indian Partnership Act, 1932. These rights are inherent in their role as partners and are essential for the smooth operation of the partnership firm. These rights can be classified into individual rights and rights vis-à-vis the other partners (inter se rights).

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Individual Rights of Partners

1. **Right to take part in conducting the business (Section 12(a)):** Every partner has the right to participate in the conduct of the firm's business.
2. **Right to be consulted (Section 12(c)):** Decisions affecting the nature of the business must be taken with the consent of all partners.
3. **Right to access and inspect books (Section 12(d)):** Every partner has a right to access and inspect the books of the firm.
4. **Right to remuneration (Section 13(b)):** No partner is entitled to receive remuneration for taking part in the conduct of the business unless otherwise decided by the partnership deed.
5. **Right to interest on capital (Section 13(c)):** A partner is not entitled to interest on the capital subscribed by him, unless it is provided for in the partnership agreement.
6. **Right to interest on advances (Section 13(d)):** If a partner makes any advance beyond the amount of his capital, he is entitled to receive interest on it at the rate of six percent per annum.
7. **Right to share in profits (Section 13(b)):** Every partner has a right to share in the profits of

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Inter Se Rights of Partners

1. **Right to Indemnity (Section 13(e)):** Partners have the right to claim indemnity from the firm for any payments made or liabilities incurred while carrying out the business, in emergency situations.
2. **Right to stop admission of a new partner (Section 31):** No person may be introduced as a partner without the consent of all existing partners.
3. **Right to retire (Section 32):** A partner has the right to retire from the firm with the consent of all other partners or in accordance with the terms of the partnership agreement.
4. **Right to expel a partner (Section 33):** A partner may be expelled by a majority of the partners if such power has been conferred by express agreement, under certain conditions.

The rights of partners are crucial to ensure fair conduct and decision making within a partnership firm. They can be altered by mutual consent or by the terms of the partnership agreement. However, any change that fundamentally alters the nature of the partnership must be agreed upon by all partners.

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Duties of Partners Under The Indian Partnership Act, 1932

The Indian Partnership Act, 1932 prescribes several duties and obligations of partners towards the partnership firm and each other. These are necessary to ensure the smooth and equitable functioning of the partnership firm.

Individual Duties of Partners

- 1. Duty to act in good faith (Section 9):** Every partner is bound to carry on the firm's business to the greatest common advantage, be just and faithful to each other, and render true accounts and full information of all things affecting the firm to any partner or his legal representative.
- 2. 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.
- 3. Duty to attend diligently to his duties in the conduct of the firm's business (Section 12b):** Every partner is bound to attend diligently to his duties in the conduct of the firm's business.
- 4. Duty to work without remuneration (Section 13b):** Partners are not entitled to receive remuneration for participating in the

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conduct of the firm's business, except where a contrary agreement exists.

- 5. Duty to contribute to losses (Section 13b):** Partners must contribute equally to the losses sustained by the firm, unless otherwise agreed in the partnership agreement.

Inter Se Duties of Partners

- 1. Duty to account for private profits (Section 16a):** If a partner derives any profit from any transaction of the firm or from the use of the property or business connection of the firm, he must account for it and pay it to the firm.
- 2. Duty to account for personal profits earned from competing business (Section 16b):** If a partner carries on any business of the same nature as and competing with that of the firm, he must account for and pay to the firm all profits made by him in that business.
- 3. Duty not to assign his interest (Section 29):** A partner cannot make an assignment of his interest in the firm so as to introduce a new partner without the consent of all existing partners.

Narayanappa vs Bhaskara Krishnappa [(1966) 3 SCR 400]: The Supreme Court highlighted the duty of

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every partner to render true accounts and full information of all things affecting the firm to any partner or his legal representative.

The duties of partners are central to the effective functioning of a partnership firm. While a partnership agreement may adjust certain obligations, core duties like acting in good faith are non-negotiable. These foundational responsibilities ensure fairness among partners and contribute to the firm's overall success.

2.3 INCOMING AND OUTGOING PARTNERS, POSITION OF MINOR

In the life of a partnership firm, changes in the constitution of partners are common. New partners may join, and existing partners may leave. The Indian Partnership Act, 1932 has provisions to deal with both incoming (new) partners and outgoing (retiring or expelled) partners.

Incoming Partners (Section 31)

1. **Admission of a new partner:** The admission of a new partner does not dissolve the existing partnership. Instead, it creates a reconstituted firm. The new partner can be admitted only with the consent of all the existing partners unless the partnership deed provides otherwise.

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- 2. Liability of the new partner:** The new partner is not liable for any act of the firm done before he became a partner. His liability is only for the acts of the firm done after he joins the firm.
- 3. Rights of the new partner:** Unless otherwise agreed, the new partner does not have a right to participate in the property of the firm existing at the time of his admission. He only acquires a share in the future profits.

Outgoing Partners

- 1. Retirement of a partner (Section 32):** A partner may retire from the partnership with the consent of all other partners or in accordance with the terms of the partnership agreement. If the partnership is at will, a partner can retire by giving notice to all the other partners.
- 2. Expulsion of a partner (Section 33):** A partner may be expelled from the partnership by a majority of the partners, only if the power to expel has been conferred by an express agreement and the power is exercised in good faith.
- 3. Insolvency of a partner (Section 34):** If a partner becomes insolvent, he ceases to be a partner from the date of his adjudication. His estate is also not liable for any act of the firm done after his insolvency.

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- 4. Liability of outgoing partner:** An outgoing partner continues to be liable for the acts of the firm done before his retirement, unless a public notice is given or there is an agreement with the other partners releasing him from such liability.
- 5. Rights of outgoing partner:** An outgoing partner is entitled to his share of the profits made till the date of retirement and has a right to carry on a competing business, unless otherwise agreed.

Provisions governing incoming and outgoing partners are vital for maintaining a partnership firm's continuity. They ensure that rights and liabilities are clearly defined and managed during transitions, safeguarding the interests of both the firm and its partners.

Position of a Minor in a Partnership Under The Indian Partnership Act, 1932

Under the Indian Partnership Act, 1932, the position of a minor (an individual below 18 years) in a partnership firm is a unique one. A minor cannot become a partner in a firm as he/she is not competent to enter into a contract as per the Indian Contract Act, 1872. However, a minor can be admitted to the benefits of a partnership with the consent of all the existing partners. The provisions governing the position of a minor are covered under Section 30 of the Act.

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Rights of a Minor

1. **Share in the property and profits:** A minor has a right to his share of the property and profits of the firm as agreed upon by the partners.
2. **Access to and inspection of the books:** A minor can have access to and inspect the books of the firm.
3. **Suing the partners for an account or payment of his share of the property or profits:** On severing his connection with the firm, a minor has the right to sue the partners for his share of the property and profits.

Liabilities of a Minor

1. **Liability towards third parties:** A minor's liability towards third parties for the acts of the firm is limited to his share in the partnership assets.
2. **No personal liability:** A minor cannot be made personally liable for any debts of the partnership firm. If the partnership firm incurs losses, the minor's share in the partnership assets can be used to offset these losses, but his personal property cannot be used.

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Option to Become a Partner

Upon attaining the age of majority, the minor has a choice. He may choose to become a partner within six months of attaining majority or of his knowledge that he had been admitted to the benefits of partnership, whichever is later. This decision must be communicated to the firm in writing. If he fails to make this decision, he is considered to have elected to become a partner.

S.C. Mandal vs Krishnadhan Banerjee [AIR 1992 SC 1234]: The Supreme Court held that a minor is not competent to become a partner, though with the consent of all the partners, he may be admitted to the benefits of partnership.

Commissioner of Income Tax, Madras vs M/S. Dwarka Prasad [AIR 1956 SC 256]: The Supreme Court held that the share income from a partnership firm, where a minor has been admitted to the benefits of partnership, can be included in the income of the minor.

The inclusion of a minor in a partnership allows them to benefit from the firm's profits without bearing the burden of unlimited liability. This unique position safeguards their interests while maintaining the partnership's operational integrity.

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2.4 DISSOLUTION AND CONSEQUENCES

Dissolution of Partnership: The Indian Partnership Act, 1932

The dissolution of a partnership refers to the termination of the existing relationship between the partners. This does not necessarily mean the end of the business, which may continue under new arrangements. The provisions governing the dissolution of partnership are covered under Sections 39 to 44 of the Indian Partnership Act, 1932.

Modes of Dissolution

1. **Dissolution by Agreement (Section 40):** A firm can be dissolved with the consent of all partners or in accordance with a contract between the partners.
2. **Compulsory Dissolution (Section 41):** A firm is compulsorily dissolved if all partners (or all but one partner) become insolvent, or if the business of the firm becomes illegal.
3. **Dissolution on the Happening of Certain Contingencies (Section 42):** A firm can be dissolved upon the expiry of the term of the partnership, upon the completion of the venture for which it was formed, by the death of a partner, or by the adjudication of a partner as insolvent.

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- 4. Dissolution by Notice (Section 43):** In the case of a partnership at will, a firm can be dissolved if a partner gives notice in writing to all the other partners of his intention to dissolve the firm.
- 5. Dissolution by Court (Section 44):** The court may order a firm to be dissolved on a partner's application, on grounds such as mental incapacity, permanent incapability, misconduct, persistent breach of agreement, transfer of interest or continuous losses.

Consequences of Dissolution

- 1. Settlement of accounts (Section 48):** Upon dissolution, the firm's assets are used to settle accounts in the following order - debts to third parties, loans and advances by partners, capital contributed by partners, and lastly, any surplus is divided among the partners in their profit-sharing ratio.
- 2. Continuing authority of partners for purposes of winding up (Section 47):** Even after dissolution, the partners continue to have the authority to complete transactions necessary for winding up the affairs of the firm.
- 3. Return of premium on premature dissolution (Section 37):** If a partner has paid a premium on entering into a partnership for a

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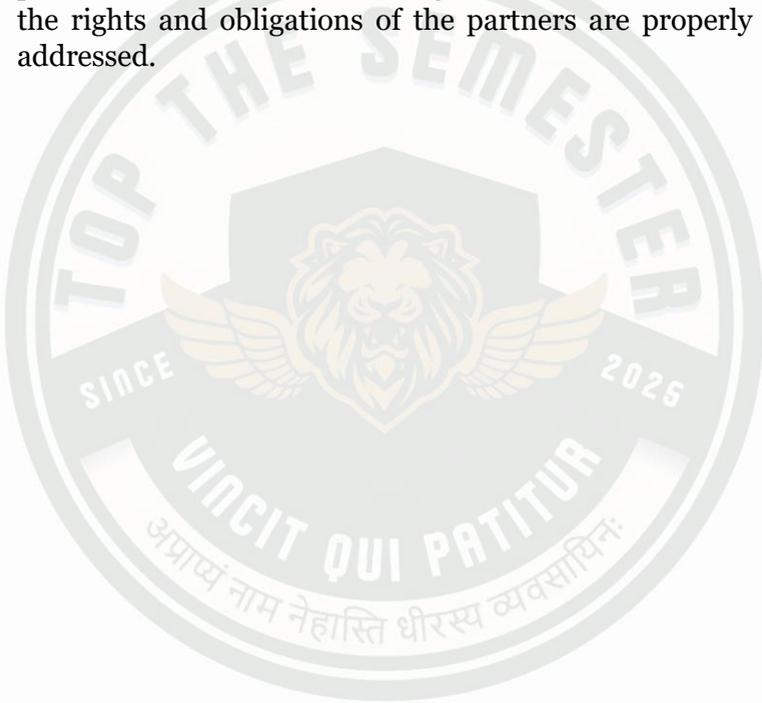
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fixed term, and the firm is dissolved before the expiry of that term, he may be entitled to a return of the premium or part thereof.

The dissolution of a partnership is a significant event that alters the legal relationships between partners. It is a process that needs careful management to ensure that all the rights and obligations of the partners are properly addressed.



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UNIT 3

THE SALE OF GOODS ACT, 1930

Overview of The Sale of Goods Act, 1930

The Sale of Goods Act, 1930 is a significant piece of legislation that governs the sale and purchase of goods in India. This Act replaced Chapter VII of the Indian Contract Act, 1872, which dealt with the sale of goods. The main reason for a separate Act was to define and amend the law relating to the sale of goods, and to provide uniformity in law across the country.

Scope and applicability of the Act

The Act applies to the whole of India except Jammu and Kashmir. It applies to contracts for the sale of goods where the property in goods is transferred from the seller to the buyer for a price. It also applies to an agreement to sell goods where the transfer of property in goods is to take place at a future date or subject to some conditions to be fulfilled later.

The Sale of Goods Act applies to all types of goods, movable and immovable, tangible and intangible. However, it does not apply to immovable property, money, actionable claims, and things in action.

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3.1 DEFINITIONS, DISTINCTION BETWEEN SALE AND AGREEMENT TO SALE

Contract of Sale

A contract of sale of goods is a contract by which the seller transfers or agrees to transfer the property in goods to the buyer for a price. Such a contract may be absolute or conditional. It includes both a sale and an agreement to sell.

Goods

'Goods' mean every kind of movable property other than actionable claims and money; and includes stock and shares, growing crops, grass, and things attached to or forming part of the land, which are agreed to be severed before sale or under the contract of sale.

Price

Price is the money consideration for a sale of goods.

Contract of Sale - Sale and Agreement to Sell

The contract of sale can be a 'sale' or an 'agreement to sell'. In a sale, the property in the goods is transferred

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from the seller to the buyer at the time of making the contract. The seller cannot have the right to sell the goods after the sale. On the other hand, an agreement to sell is a contract where the transfer of property in goods will take place at a future time or subject to some conditions being fulfilled.

Essential Elements of a Contract of Sale

1. Two Parties

A contract of sale involves two distinct parties - a buyer and a seller. The buyer and seller must be different persons; a person cannot buy his own goods.

2. Goods

The subject matter of the contract of sale must be 'goods'. As defined earlier, goods can be anything that is movable except money and actionable claims.

3. Transfer of Ownership

The contract involves the transfer of property, i.e., ownership, from the seller to the buyer. The purpose of the contract is to transfer the general property and not just special property.

4. Price

There must be a price in money paid or promised to be paid. The price cannot be paid in kind. If it is not

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determined, it can be determined by the course of dealing between the parties.

Conditions and Warranties

The Sale of Goods Act, 1930 defines conditions and warranties which are stipulations in a contract of sale. A condition is a stipulation that is essential to the main purpose of the contract, the breach of which gives the injured party the right to terminate the contract. On the other hand, a warranty is a stipulation collateral to the main purpose of the contract, the breach of which gives the injured party the right to claim damages but not to reject the goods and treat the contract as repudiated.

To understand the application and interpretation of the Sale of Goods Act, 1930, one can look at some landmark judgments of the Supreme Court of India.

One such case is **M/s Popatlal Shah vs The State Of Madras** (AIR 1953 SC 274). This case dealt with the definition of goods and the question of whether forward contracts could be considered contracts for the sale of goods under the Act. The Supreme Court held that forward contracts for the sale of goods were valid and enforceable under the Sale of Goods Act, 1930. This judgment provided clarity on the applicability of the Act and widened its scope to include forward contracts.

Another important case is **Motilal Padampat Sugar Mills vs State Of Uttar Pradesh** (AIR 1979 SC 621),

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which dealt with the question of when property in goods passes from the seller to the buyer. The Supreme Court held that the property in goods passes when the parties intended it to pass. This judgment highlighted the importance of intention in determining when the property in goods is transferred.

The Sale of Goods Act, 1930, is an important legislation that governs the sale and purchase of goods in India. It lays down the rules relating to the contract of sale, conditions and warranties, delivery and payment, rights and duties of buyer and seller, remedies for breach of contract and so on.

THE CONCEPT OF SALE

The Sale of Goods Act, 1930, is a cornerstone of commercial law in India, regulating the sale and purchase of goods. A clear understanding of the Act's definition of a 'sale' is essential to grasp its foundational principles and their application in business transactions.

A 'sale', as defined in section 4(1) of the Act, is a contract where the seller transfers or agrees to transfer the property or ownership of goods to the buyer for a price. The essence of a sale contract is the transfer of property or ownership from the seller to the buyer.

In simple terms, the property or ownership in the goods signifies the total ownership rights and responsibilities. This means the buyer is free to use or dispose of the goods

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at their will once the sale is concluded. The seller cannot have the right to sell the goods after the sale.

Sale, under the Act, is different from an 'agreement to sell'. In a sale, the property in the goods is transferred from the seller to the buyer at the time of the contract. The ownership of the goods is transferred immediately. However, in an agreement to sell, the transfer of property in the goods will take place at a future time or subject to some conditions being fulfilled.

To illustrate this concept, let's take an example. Suppose you go to a furniture shop and purchase a chair. You pay the shop owner (the seller) the price for the chair and take it home. This transaction is considered a 'sale' as the ownership of the chair is immediately transferred from the shop owner to you (the buyer) at the time of the contract.

Now, let's imagine a different scenario. You go to a furniture shop and like a chair that is not currently in stock. The shop owner promises to deliver it to you next week, and you agree to pay the price upon delivery. This transaction is an 'agreement to sell' as the transfer of ownership from the seller to you is set to take place in the future when the chair is delivered.

Elements of a Sale

For a transaction to qualify as a 'sale' under the Act, there are certain essential elements:

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1. **Two Parties:** There must be at least two parties - the seller and the buyer. They must be different persons; a person cannot buy his own goods.
2. **Transfer of Property:** There must be a transfer of property or ownership in the goods from the seller to the buyer. The property is transferred when the parties intended it to be transferred.
3. **Goods:** The subject of the contract must be goods. Goods mean every kind of movable property other than actionable claims and money. It includes both existing goods, future goods and contingent goods.
4. **Price:** There must be a price in money paid or promised to be paid. The price can be fixed by the contract, left to be agreed by the parties, or determined by the course of dealing between the parties.

These elements create a legally binding agreement between the seller and the buyer, and they are essential in understanding the legalities and intricacies of the Sale of Goods Act, 1930.

THE CONCEPT OF AGREEMENT TO SELL

An agreement to sell is another important concept under the Sale of Goods Act, 1930. It is slightly different from a 'sale' and understanding this distinction is crucial to the

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interpretation of the Act.

Definition of Agreement to Sell

An agreement to sell, according to section 4(3) of the Sale of Goods Act, 1930, is a contract in which the transfer of property or ownership in the goods is to take place at a future time or subject to some conditions to be fulfilled later.

In essence, an agreement to sell is a contract of sale where the property in the goods is yet to be transferred from the seller to the buyer. The transaction is seen as an agreement to sell and not a sale because the conditions necessary for the completion of the sale or the agreed time for the sale has not yet been met.

In an agreement to sell, the seller agrees to transfer the property in goods to the buyer in future, upon fulfilment of certain conditions. The seller may be either the owner of the goods or a person authorised or competent to sell the goods at the time of the agreement.

Elements of an Agreement to Sell

The essentials of an agreement to sell are quite similar to that of a sale:

1. **Two Parties:** There must be two distinct parties involved - the seller who agrees to transfer the property in goods, and the buyer to whom such property is to be transferred in future.

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- 2. Transfer of Property:** The agreement involves a future transfer of property or ownership in goods from the seller to the buyer. The ownership transfer is conditional and does not take place immediately.
- 3. Goods:** The object of the agreement to sell must be goods, which could be either existing, future, or contingent.
- 4. Price:** There must be a price in money, either paid or promised to be paid.

The Transition from an Agreement to Sell to a Sale

An agreement to sell is essentially a sale 'waiting to happen'. It becomes a sale when the time elapses or the conditions necessary for the transfer of property are fulfilled.

To illustrate, suppose you order a custom-made piece of furniture. The furniture store agrees to make it according to your specifications and deliver it to you in a month, and you agree to pay the price upon delivery. This transaction is an agreement to sell as the ownership of the furniture will be transferred to you in the future upon delivery. When the store delivers the furniture to you after a month and you pay the agreed price, the agreement to sell turns into a sale.

Importance of Agreement to Sell

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The concept of an agreement to sell is critical in various commercial transactions, especially those involving goods that are to be manufactured or acquired by the seller after the agreement is made. It provides a legal framework that allows parties to enter into contracts for the future sale of goods, facilitating business transactions and providing legal recourse in case of disputes.

Distinguishing between a sale and an agreement to sell is critical in commercial law, as it determines the rights, obligations, and legal consequences for the parties involved. This distinction is fundamental for both academic understanding and practical application in business transactions.

DISTINCTION BETWEEN SALE AND AGREEMENT TO SELL

The Sale of Goods Act, 1930, highlights two distinctive stages in a transaction involving the transfer of property - a 'sale' and an 'agreement to sell'. Understanding this distinction is important for interpreting the provisions of the Act and their applicability to various commercial transactions.

Transfer of Property (Ownership)

In a 'sale', the property or ownership in the goods is transferred from the seller to the buyer immediately at the time of making the contract. It represents a completed transaction.

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In contrast, an 'agreement to sell' represents an incomplete or inchoate transaction. It is a contract in which the transfer of property in the goods is to take place at a future time or subject to certain conditions that have to be fulfilled.

Risk and Responsibility

In a sale, since the ownership of the goods is transferred to the buyer immediately, the risk associated with the goods also transfers to the buyer, even if the goods are in the possession of the seller.

However, in an agreement to sell, the risk remains with the seller until the conditions are met and the ownership of goods is transferred to the buyer.

Consequences of Breach

In case of a breach of contract in a sale, the owner i.e., the buyer, can sue the seller for the delivery of the goods. Alternatively, if the buyer fails to pay, the seller can sue for the price.

In an agreement to sell, if the seller breaches the contract, the buyer can only claim damages for breach of contract. Similarly, if the buyer fails to accept and pay for the goods, the seller can only sue for damages and not for the price (unless the goods are ascertainable and the property has passed to the buyer).

Insolvency of Buyer/Seller

If the buyer becomes insolvent before he pays the price in

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a 'sale', the seller has to deliver the goods to the official receiver or assignee as the ownership had already been transferred.

In contrast, if the buyer becomes insolvent in an 'agreement to sell' and has not paid the price, the seller can refuse to deliver the goods to the official receiver or assignee as the property in the goods had not yet been transferred.

Right of Resale

In a sale, the seller cannot resell the goods as the property in goods is with the buyer. If he does so, the subsequent buyer does not acquire a better title and the original buyer can sue the seller for the breach of contract and also recover the goods from the subsequent buyer.

In an agreement to sell, the seller can resell the goods as the property in goods is with him. If he does so, the subsequent buyer acquires a good title to the goods. The original buyer can only sue the seller for breach of contract but cannot recover the goods from the subsequent buyer.

To conclude, these fundamental distinctions are instrumental in understanding how the Sale of Goods Act, 1930 operates within the ambit of commercial transactions. They form the basis for determining the rights and obligations of the parties, the transfer of risk and ownership, and the remedies available in the event of a breach. The line of difference between a sale and an

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agreement to sell, hence, lies in the stage of the transaction and the transfer of ownership of the goods.

3.2 CONDITIONS AND WARRANTIES

The Sale of Goods Act, 1930 - Conditions in a Contract of Sale

In a contract of sale under the Sale of Goods Act, 1930, stipulations or terms can take two forms: conditions and warranties. Here, we'll focus on the concept of conditions and their importance in the execution of a contract of sale.

Definition of Conditions

Conditions, as defined under Section 12(2) of the Act, are stipulations essential to the main purpose of the contract. These are the terms that go to the very root of the contract, the breach of which gives the aggrieved party the right to treat the contract as repudiated (cancelled).

In simple words, conditions are the fundamental terms agreed upon by the parties without which the contract would not have been formed. If these conditions are not met, the buyer has the right to reject the goods and terminate the contract, in addition to claiming damages for any loss suffered.

Types of Conditions

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Conditions can be classified into two categories:

1. **Express Conditions:** These are explicitly stated and agreed upon by the parties at the time of the contract. For example, in a contract for the sale of a car, it might be an express condition that the car must be of a particular make and model.
2. **Implied Conditions:** These are not specifically stated in the contract but are implied by law. They are presumed to be so obvious that the parties need not express them. The Sale of Goods Act, 1930, provides for several implied conditions:
 - a. **Condition as to Title (Section 14):** The seller must have a right to sell the goods, and in a sale, the buyer should enjoy the quiet possession of the goods. If the buyer's possession is disturbed by someone with a better title, the buyer can sue the seller for breach of condition.
 - b. **Sale by Description (Section 15):** If the sale is by description, the goods must correspond with the description. If they don't, the buyer can reject the goods.
 - c. **Sale by Sample (Section 17):** In a contract for sale by sample, the bulk of the goods must correspond with the sample in quality, the buyer must have a reasonable opportunity to compare the bulk with the sample, and the goods must be free from any defect which would not be apparent

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on a reasonable examination of the sample.

- d. **Condition as to Fitness (Section 16(1)):** If the buyer makes known to the seller the particular purpose for which he requires the goods and relies on the seller's skill and judgment, there is an implied condition that the goods shall be reasonably fit for such purpose.
- e. **Condition as to Merchantable Quality (Section 16(2)):** When goods are bought by description from a seller who deals in goods of that description, there is an implied condition that the goods are of merchantable quality.

Importance of Conditions

The concept of conditions is critical in any contract of sale. They lay the foundation for the rights and obligations of the parties involved. The breach of a condition by one party provides the other party the right to reject the goods and rescind the contract, offering them protection against the non-performance of the key terms of the contract. Conditions also form the basis for defining what constitutes a breach of contract and the remedies available to the aggrieved party.

Understanding conditions, both express and implied, is crucial for the proper execution and enforcement of a contract of sale. They offer a legal framework that guides the parties in conducting business transactions and provides legal recourse in case of disputes or non-

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WARRANTIES IN A CONTRACT OF SALE

In a contract of sale, the terms or stipulations can be classified into two categories: conditions and warranties. After understanding 'conditions', let's now delve into the concept of 'warranties' under the Sale of Goods Act, 1930.

Definition of Warranties

A warranty is a stipulation collateral to the main purpose of the contract of sale, the breach of which gives rise to a claim for damages but not a right to reject the goods and treat the contract as repudiated. This is as defined under Section 12(3) of the Act.

In simpler words, a warranty is a secondary term or promise in the contract, which is not central to the agreement. While a breach of warranty doesn't allow the buyer to reject the goods or cancel the contract, it does give the buyer the right to claim damages.

Types of Warranties

Like conditions, warranties can be either express or implied:

1. **Express Warranties:** These are explicitly stated in the contract by the parties involved. For example, a seller might provide an express warranty that a car being sold will be free from

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defects for a certain period of time.

2. **Implied Warranties:** These are not specifically stated in the contract but are assumed to be so fundamental that they don't need to be expressly included. The Sale of Goods Act, 1930, provides for several implied warranties:
 - a. **Warranty of quiet possession (Section 14(b)):** In a contract of sale, unless there is a contrary intention, there is an implied warranty that the buyer shall have and enjoy quiet possession of the goods. If the buyer's possession is lawfully disturbed by any third person, the buyer can sue the seller for breach of warranty.
 - b. **Warranty of freedom from encumbrances (Section 14(c)):** There is an implied warranty that the goods shall be free from any charge or encumbrance in favor of any third party, not declared or known to the buyer before or at the time of the contract.
 - c. **Warranty as to quality or fitness by usage of trade (Section 16(3)):** An implied warranty as to the quality or fitness for a particular purpose may also arise from the course of dealing or usage of trade.

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- d. **Warranty in case of a sale by sample (Section 17):** In case of a sale by sample, there is an implied warranty that the bulk of the goods shall correspond with the sample and that the buyer shall have a reasonable opportunity to compare the sample with the bulk, also the goods shall be free from any defect which would not be apparent on reasonable examination of the sample.

Importance of Warranties

Warranties, while secondary to the main purpose of the contract, provide an additional layer of protection to the buyer. They ensure that the buyer receives goods free from undisclosed encumbrances and that they will enjoy quiet possession of the goods. Warranties also safeguard the buyer's interests in case of any latent defects that may not be apparent at the time of the sale but are discovered later.

Understanding warranties, both express and implied, is vital for the effective execution and enforcement of a contract of sale. They provide legal recourse to the buyer to claim damages in the event of a breach, ensuring that their interests and rights are protected in the transaction.

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3.3 PASSING OF PROPERTY

In a contract of sale, the concept of 'passing of property' or 'passing of ownership' is fundamental. The term 'property' here means the ownership or title to the goods. Passing of property from the seller to the buyer is the essence of a contract of sale. It is the point at which the buyer becomes the owner of the goods, bearing all the risks and rewards associated with ownership.

Determination of Passing of Property

The rules for the passing of property from the seller to the buyer are laid down in Chapter III of the Sale of Goods Act, 1930. Here's a brief outline of these rules:

- 1. Goods Identified and Agreed Upon (Section 19):** In the case of a 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. The intention may be expressly stated in the contract, inferred from the terms of the contract, or deduced from the conduct of the parties and circumstances of the case.
- 2. Goods Must be in a Deliverable State (Section 20):** Where there is a contract for the sale of specific goods in a deliverable state, the

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property in the goods passes to the buyer when the contract is made, irrespective of the time of payment of the price or the time of delivery of the goods, unless a different intention appears from the terms of the contract.

- 3. Goods to be Put in 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 the goods to put them into a deliverable state, the property does not pass until the thing is done and the buyer has notice thereof.
- 4. Sale by Approval or "on Sale or Return" (Section 24):** In a sale on approval or on a "sale or return" basis, the property passes to the buyer when he signifies his approval or acceptance to the seller or does any other act adopting the transaction.
- 5. Unascertained Goods and Appropriation (Section 23):** 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. Also, the goods must be unconditionally appropriated to the contract, either by the seller with the assent of the buyer or by the buyer with the assent of the seller.

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Importance of Passing of Property

The moment of the passing of property is crucial in a contract of sale as it determines the point at which the risk of loss or damage to the goods passes from the seller to the buyer. Even if the buyer does not have possession of the goods, if the property in the goods has passed to the buyer, he bears the risk.

In case the buyer refuses to pay for the goods, the seller can sue him if the property has passed to the buyer. Similarly, if the seller refuses to deliver the goods, the buyer can sue for the goods if the property in them has passed to him.

Furthermore, in case the goods are destroyed and the property in them has passed to the buyer, the loss falls on the buyer even if the goods are in the possession of the seller. However, if the property in the goods has not passed to the buyer, the loss falls on the seller even though the goods may be in the possession of the buyer.

Understanding the rules regarding the passing of property in a contract of sale is crucial to ascertain the rights and liabilities of the parties and is indispensable to the study of the Sale of Goods Act, 1930.

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3.3 RIGHTS OF UNPAID SELLER AND REMEDIES FOR BREACH OF CONTRACT

Rights of an Unpaid Seller

The term 'unpaid seller' refers to a seller to whom the whole of the price has not been paid or a bill of exchange or other negotiable instrument has been conditionally received and the condition on which it was received has not been fulfilled by reason of the dishonor of the instrument or otherwise. Section 45 of The Sale of Goods Act, 1930 defines an 'unpaid seller'.

The Act also provides a set of rights for the unpaid seller, protecting their interests in case the buyer defaults in payment. These rights can be categorized as follows:

1. Rights Against the Goods

The unpaid seller, in respect of the goods, has the right of lien, the right of stoppage in transit, and the right of resale.

- a. **Right of Lien (Sections 47-49):** The unpaid seller of goods, who is in possession of them, has the right to retain possession until payment or tender of the price in the following cases: (a) where the goods have been sold without any stipulation as to credit, (b) where the goods have

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been sold on credit, but the term of credit has expired, and (c) where the buyer becomes insolvent.

b. Right of Stoppage in Transit (Sections 50-52): When the buyer of goods becomes insolvent, the unpaid seller who has parted with the possession of the goods has the right of stopping them in transit, that is to say, he may resume possession of the goods as long as they are in the course of transit, and may retain them until payment or tender of the price.

c. Right of Resale (Section 54): In certain circumstances, the unpaid seller has the right to resell the goods. For example, where the goods are of perishable nature or where the unpaid seller gives notice to the buyer of his intention to resell and the buyer does not within a reasonable time pay or tender the price.

2. Rights Against the Buyer Personally

In addition to the rights against the goods, an unpaid seller has certain rights against the buyer personally. They are:

a. Suit for Price (Section 55): Where under a contract of sale, the property in the goods has passed to the buyer and the buyer wrongfully

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neglects or refuses to pay for the goods according to the terms of the contract, the seller may sue him for the price of the goods.

- b. **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.
- c. **Suit for Interest (Section 61):** In case of a breach of a contract of sale by the buyer, the unpaid seller can also sue the buyer for interest and special damages in certain cases.

It is important to note that these rights of the unpaid seller are designed to secure the position of the seller in the transaction, offering remedies in case of non-payment or non-acceptance of goods by the buyer.

Remedies for Breach of Contract

A breach of contract under the Sale of Goods Act, 1930, occurs when either the buyer or the seller fails to perform his obligations as per the contract. The Act provides a set of remedies for the aggrieved party in the event of a breach. These remedies can be classified as remedies available to the seller and remedies available to the buyer.

Remedies Available to the Seller

If the buyer breaches the contract, the seller has several remedies:

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1. **Suit for Price (Section 55):** Where the property has passed to the buyer and he wrongfully neglects or refuses to pay for the goods, the seller can sue him for the price.
2. **Damages for Non-Acceptance (Section 56):** Where the buyer wrongfully neglects or refuses to accept and pay for the goods, the seller can sue him for damages for non-acceptance.
3. **Repudiation of Contract before Due Date (Section 60):** Where the buyer repudiates the contract before the date of delivery, the seller can treat the contract as rescinded and sue for damages.
4. **Interest and Special Damages (Section 61):** In a suit for breach of contract, the seller can also claim interest and special damages, if any.

Remedies Available to the Buyer

Similarly, if the seller breaches the contract, the buyer also has several remedies:

1. **Damages for Non-Delivery (Section 57):** Where the seller wrongfully neglects or refuses to deliver the goods to the buyer, the buyer can sue the seller for damages for non-delivery.
2. **Specific Performance (Section 58):** In certain cases, the court may direct the seller to specifically perform the contract, that is, deliver

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the goods as per the terms of the contract. This remedy is usually granted when the goods are unique or special, and damages would not be an adequate remedy.

- 3. Remedy for Breach of Warranty (Section 59):** Where there is a breach of warranty by the seller, or where the buyer elects or is compelled to treat any breach of condition on the part of the seller as a breach of warranty, the buyer cannot reject the goods. But he can: (a) set up against the seller the breach of warranty in diminution or extinction of the price, or (b) sue the seller for damages for breach of warranty.
- 4. Repudiation of Contract (Section 60):** Where the seller repudiates the contract before the date of delivery, the buyer can treat the contract as rescinded and sue for damages.
- 5. Interest and Special Damages (Section 61):** Like the seller, in a suit for breach of contract, the buyer can also claim interest and special damages, if any.

These remedies are provided by the Act to ensure that the aggrieved party is adequately compensated for any loss resulting from a breach of contract. It's important to understand these remedies in order to ensure the proper execution and enforcement of a contract of sale under the Sale of Goods Act, 1930.

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UNIT 4

THE NEGOTIABLE INSTRUMENT ACT, 1881

4.1 LEGAL RESEARCH AND KINDS OF LEGAL RESEARCH

Introduction and Overview of The Negotiable Instrument Act, 1881

The Negotiable Instruments Act, 1881 is a landmark legislation in India that is responsible for the governing of negotiable instruments. These negotiable instruments include promissory notes, bills of exchange, and cheques. The Act was first introduced by the British in India during the colonial era, and its principles remain largely intact, being integral to the current financial and business systems.

Definition and Nature of Negotiable Instruments

A negotiable instrument, as defined by the Act, is any document guaranteeing the payment of a specific amount of money, either on demand or at a predetermined time. It should also be transferable either by delivery or by endorsement and delivery.

There are three primary types of negotiable instruments recognized under the Act:

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1. **Promissory Notes:** As per Section 4 of the Act, a promissory note is a written promise by one person (the maker) to another (the payee) to pay a certain sum of money. The sum can be payable either on demand or at a future date.
2. **Bills of Exchange:** As defined in Section 5 of the Act, a bill of exchange is an unconditional written order that directs a person (the drawee) to pay a specific sum of money to the order of a designated person (the drawer) or to the bearer of the instrument.
3. **Cheques:** Section 6 of the Act describes a cheque as a bill of exchange that is drawn on a specified banker and not expressed to be payable otherwise than on demand.

The Objective of the Act

The primary aim of the Negotiable Instruments Act is to legally structure and instill trust in the use of negotiable instruments as a secure and reliable method of transferring money. It provides a legal framework for dealing with any discrepancies that may arise during the transactions involving these instruments.

A relevant Supreme Court judgment pertaining to this Act is **Krishna Janardhan Bhat vs Dattatraya G. Hegde** (2008). This judgment clarified the law on the presumption of consideration for a cheque. The court held that once the execution of the cheque is admitted,

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the presumption of existence of a legally enforceable debt comes into play.

Overview of the Act

The Negotiable Instruments Act consists of 147 sections, subdivided into 17 chapters. Each chapter deals with specific provisions related to negotiable instruments. The Act, apart from detailing the features and implications of promissory notes, bills of exchange, and cheques, also delineates the penalties in the event of dishonour of such instruments.

Further, the Act has been amended several times, most notably in 1988, 2002, and 2015, to enhance the efficacy of the Act and to further its objective of ensuring faith in negotiable instruments. The 2002 amendment, for instance, introduced a provision for interim compensation to the complainant, which was a significant milestone in the history of this legislation.

The Negotiable Instruments Act, 1881, serves as the backbone of commercial and trade transactions in India. It fosters trust and reliability in the economy, making transactions smoother and disputes more manageable. The Act has evolved over the years to cater to the changing economic and commercial landscapes, further underlining its pivotal role in India's legal and financial system.

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4.2 DEFINITION AND KINDS OF NEGOTIABLE INSTRUMENTS

Definition of Negotiable Instruments

A negotiable instrument, as defined by the Negotiable Instruments Act, 1881, is a document guaranteeing the payment of a specific amount of money, either on demand, or at a time fixed or determinable in the future, either to order or to bearer. This means, these instruments are transferable by nature, and can be freely used in commercial transactions, providing a certain degree of flexibility and reliability.

These instruments are unique in the way they blend the concept of 'property' and 'debt', because the ownership of these instruments can be transferred by mere delivery (if it is a bearer instrument) or by endorsement and delivery (if it is an order instrument), and the transferee (the endorsee) becomes entitled to the sum of money due under the instrument to the extent of his interest.

Kinds of Negotiable Instruments

The Negotiable Instruments Act, 1881 primarily recognises three types of negotiable instruments: Promissory Notes, Bills of Exchange, and Cheques.

1. **Promissory Notes:** Under Section 4, a promissory note is an instrument in writing (not being a bank-note or a currency-note) containing

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an unconditional undertaking, signed by the maker, to pay a certain sum of money to, or to the order of, a certain person, or to the bearer of the instrument. A promissory note is essentially a promise in writing to pay a specific amount to a certain individual or order or bearer.

- 2. Bills of Exchange:** Section 5 defines a bill of exchange as 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. In simpler terms, it is a document demanding the payment from a third party.
- 3. Cheques:** A cheque, as per Section 6, is a bill of exchange drawn on a specified banker and is payable only on demand. Essentially, a cheque is an order to a bank to pay a specific amount from the drawer's account to the person in whose name the cheque has been issued or to the bearer of the instrument.

However, there are other negotiable instruments as well recognised by usage or custom, such as dividend warrants, share warrants, bearer debentures, port trust debentures, etc. Moreover, some instruments become negotiable by statute, for example, a hundi or Treasury bills.

Demand draft is also a negotiable instrument under

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Section 85(A) of the Negotiable Instruments Act. This widened the understanding and scope of negotiable instruments.

In essence, negotiable instruments play a crucial role in commerce and trade, as they provide a convenient and reliable method for settling payments. The Negotiable Instruments Act, 1881 provides a legal framework for these instruments, outlining the rules and regulations concerning their use, and ensuring a level of trust in their validity and acceptance in the market.

4.3 HOLDER AND HOLDER-IN-DUE COURSE

Holder

A 'holder' of a negotiable instrument, according to Section 8 of the Negotiable Instruments Act, 1881, is an individual entitled in his own name to the possession of the instrument and to receive or recover the amount due therefrom. Thus, the holder must fulfill two conditions: he must be in possession of the instrument, and he must have a legal right to the instrument in his own name.

In simpler terms, a holder is the person who is legally in possession of the instrument and has the right to receive the amount therein. This includes a promissory note, bill of exchange, or cheque that is either originally made

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payable to him, or has been endorsed to him, or the bearer thereof.

Holder in Due Course

A 'holder in due course', according to Section 9 of the Act, is a person who, for consideration, became the possessor of a negotiable instrument before the amount mentioned in it became payable, and without having sufficient cause to believe that any defect existed in the title of the person from whom he derived his title.

In other words, a holder in due course is someone who obtains the negotiable instrument in good faith and for a value, before its maturity, without knowledge of any defects in it or claims against it. He holds a stronger position than a mere holder, as he is protected against certain defenses that might be available if the instrument were merely transferred.

To be a holder in due course, the following conditions must be satisfied:

1. **He must be a holder of a negotiable instrument:** He should legally possess the negotiable instrument and should have the right to recover the amount due on it.
2. **He must have become a holder of it before its maturity:** He should have received the instrument before the payment was due.

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3. **Consideration:** The holder must have acquired the instrument for consideration. In other words, the instrument must not have been received as a gift.
4. **Good Faith:** He must have acquired the instrument in good faith.
5. **Absence of suspicion:** He must not have any suspicion about any defect in the title of the transferor at the time of acquiring the instrument.

Endorsement of a negotiable instrument in favor of a bank for the purposes of collection makes the bank a holder in due course and the bank becomes entitled to the rights of a holder in due course.

The concepts of 'holder' and 'holder in due course' are crucial in the law of negotiable instruments. While both possess the negotiable instrument lawfully, the holder in due course enjoys a stronger position and is entitled to a better title. This distinction protects innocent persons who obtain defective titles without any fault on their part, which is a fundamental premise of the law of negotiable instruments.

The primary sections of the Negotiable Instruments Act, 1881 that relate to the holder and holder in due course are:

- **Section 8: The Holder**

This section states, "The 'holder' of a promissory note, bill

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of exchange or cheque means any person entitled in his own name to the possession thereof and to receive or recover the amount due therefrom from the parties thereto."

- **Section 9: Holder in Due Course**

This section defines 'holder in due course' as, "A person who for consideration became the possessor of a promissory note, bill of exchange or cheque if payable to bearer, or the payee or endorsee thereof, if payable to order, before the amount mentioned in it became payable, and without having sufficient cause to believe that any defect existed in the title of the person from whom he derived his title."

These sections are pivotal in defining and distinguishing between the terms 'holder' and 'holder in due course' within the context of the Act. It is important to note that while both 'holder' and 'holder in due course' have legal possession of the instrument, the holder in due course enjoys added protection and privileges under the law.

MATERIAL ALTERATIONS AND CROSSING OF CHEQUE, ETC.

Material Alteration

Material alteration refers to any change or modification in a negotiable instrument that alters its character or the rights and liabilities of any party to the instrument. This

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could include changes to the date, the sum payable, the time of payment, the place of payment, or the addition of a new party to the instrument.

The doctrine of material alteration is a fundamental principle of commercial law, designed to maintain faith in paper transactions by ensuring the negotiable instruments remain unaltered during their lifecycle.

Material Alteration as per Negotiable Instruments Act, 1881

The concept of material alteration is discussed under Section 87 and Section 125 of the Negotiable Instruments Act, 1881.

Section 87 states that any material alteration of a negotiable instrument renders it void as against anyone who is a party to the instrument at the time of the alteration and does not consent to the alteration. This rule is based on the legal maxim "ex turpi causa non oritur actio," meaning no action arises from a disgraceful cause.

Exceptions

The law does make some exceptions for certain alterations. These include:

- 1. Alterations made with the consent of parties:** If all parties agree to the alteration, then it does not void the instrument.

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- 2. Alterations that are not material:** Minor alterations that do not change the character of the instrument or the liabilities of the parties involved do not void the instrument. For example, correcting a spelling mistake would be a minor alteration.
- 3. Filling up blanks in accordance with the authority given:** If a holder fills up blanks in an incomplete instrument, this is not considered a material alteration.

Where a cheque was crossed by the holder with the words "account payee only", it would not amount to material alteration, but only a mandate to the collecting banker.

Material alteration is a significant concept in the domain of negotiable instruments, protecting the parties involved from any unauthorised and substantial modifications to the instrument. Although there are exceptions to the rule, the principle fundamentally safeguards the trust and reliability of commercial transactions involving negotiable instruments.

Crossing of Cheque

Crossing of a cheque refers to the act of drawing two parallel lines, typically across the top left corner of the cheque. It is a direction to the paying banker that the cheque should not be paid over the counter, but must be credited to a bank account. Crossing serves as a measure

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of protection against theft or fraud by ensuring that only the correct payee can cash the cheque.

Types of Crossing

There are two primary types of crossing, as recognised under the Negotiable Instruments Act, 1881:

1. **General Crossing:** This occurs when a cheque bears two parallel lines on its face, optionally with the words 'and company' or any other abbreviation (such as '& co'), or any other equivalent wording. It is deemed 'general' because it does not specify any particular banker to whom the cheque should be presented. It can be presented to the bank by any bona fide holder.
2. **Special Crossing:** According to Section 124, a cheque is said to be specially crossed when it bears the name of a bank (either with or without the words 'not negotiable'). It must be presented to the bank mentioned or to the bank to which it is directed. Thus, the payment is made to a specific bank mentioned between the parallel lines.

Not Negotiable and Account Payee Crossing

Another two types of crossing that are commonly used are 'not negotiable' and 'account payee' crossings:

1. **Not Negotiable Crossing:** When the words 'Not Negotiable' are written in between the two parallel lines, it indicates that the cheque cannot

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become an equivalent of cash. The transferee cannot have better title than the transferor, even if he receives it in good faith and for value. This helps to protect the true owner's rights in case the cheque is lost or stolen.

2. **Account Payee Crossing:** When a cheque is crossed 'Account Payee', it instructs the bank that the cheque should be credited only to the account of the person named in the cheque. This provides a further level of security, ensuring that the cheque cannot be endorsed to another person.

where a cheque crossed 'Account Payee' was collected by a bank for a person who was not the payee, the collecting bank was held to be negligent and was liable to the true owner of the cheque for his loss.

Crossing of a cheque serves as a safety measure, protecting against potential misuse of the instrument. It provides an assurance to the drawer that the amount will be paid to the right person (in case of 'Account Payee' crossing), or that it will only be collected by a banker (in case of 'General' and 'Special' crossing). The Negotiable Instruments Act, 1881 provides a comprehensive framework for the crossing of cheques, thus increasing the security and reliability of cheque-based transactions.

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Acceptance

The term 'acceptance' in the context of negotiable instruments is primarily associated with bills of exchange. A bill of exchange is an instrument in writing containing an unconditional order, signed by the maker (drawer), directing a certain person (drawee) to pay a certain sum of money to the order of a certain person or to the bearer of the instrument.

When the person directed to pay (the drawee) acknowledges or agrees to his obligation to comply with this order, it is called 'acceptance'. Once the bill is accepted, it is called an 'accepted bill' and the person who accepts the bill is known as the 'acceptor'.

Acceptance as per Negotiable Instruments Act, 1881

Section 7 of the Negotiable Instruments Act, 1881, defines acceptance as, "the signification by the drawee of his assent to the order of the drawer." This means that the drawee acknowledges the order of the drawer to pay the sum specified in the bill.

Section 17 of the Act further states that when a bill of exchange has been noted or protested for non-acceptance or for better security, and any person decides to accept it supra protest for the honour of any party liable to the bill, he must, by writing on the bill under his hand, declare himself to be such acceptor for honour and must specify for whose honour he accepts.

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There are different types of acceptance, including:

1. **General Acceptance:** When the drawee accepts the bill without any condition or qualification, it is a general acceptance.
2. **Qualified Acceptance:** When the drawee accepts the bill with certain conditions or qualifications, it is a qualified acceptance.
3. **Partial Acceptance:** This is when the drawee accepts to pay only a part of the amount of the bill. However, such acceptance is considered invalid under the Act.
4. **Acceptance Supra Protest or for Honour:** This is when a third party accepts the bill upon its dishonour by the original drawee, for the sake of honour and credit of the drawer or any endorser.

If a bill is not presented for acceptance within a reasonable time after it is drawn and the drawer or person on whose account it is drawn suffers damage through the delay, he is discharged to the extent of such damage.

Acceptance is a crucial step in the lifecycle of a bill of exchange, as it signifies the drawee's consent to pay the amount specified in the bill. The Negotiable Instruments Act, 1881 provides detailed provisions regulating the acceptance of bills, ensuring a clear and agreed-upon process for all parties involved in a bill transaction.

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Classification of Negotiable Instruments

Negotiable instruments are classified into various types based on different factors such as on usage, on liability, on the basis of documents, and so on. The Negotiable Instruments Act, 1881, specifically recognises three types of negotiable instruments: Promissory Notes, Bills of Exchange, and Cheques. However, other instruments such as Treasury Bills, Dividend Warrants, and Share Warrants can also be negotiable.

1. Promissory Notes

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. It contains a promise to pay money to a certain person or to his order or to the bearer of the instrument.

2. Bills of Exchange

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. It contains an order to pay money and not a promise.

3. Cheques

A cheque is a bill of exchange drawn on a specified banker

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and not expressed to be payable otherwise than on demand. It is always payable on demand and it is drawn on a banker. A cheque includes a demand draft whether it is a pay order or a banker's cheque.

Other Negotiable Instruments

Other negotiable instruments include dividend warrants, share warrants, bearer debentures, deposit certificates, banker's drafts (demand drafts), circular notes, bearer bonds, traveller's cheques, etc.

Based on Liability:

1. **Bearer Instrument:** These instruments are payable to the person bearing the instrument or the person who presents the instrument for payment. The transfer of these instruments can be made by mere delivery without any endorsement.
2. **Order Instrument:** These instruments are payable to a particular person named in the instrument or to any other person or his order. The transfer of these instruments requires endorsement and delivery.

Based on Usage:

1. **Inland Instrument:** These are the instruments drawn or made in India and made payable in, or drawn upon, any person resident in India.
2. **Foreign Instrument:** These are the

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instruments which are not drawn in India but are payable in India or drawn upon any person resident in India.

Promissory note, bill of exchange or cheque is payable to order which is expressed to be so payable or which is expressed to be payable to a particular person, and does not contain words prohibiting transfer or indicating an intention that it shall not be transferable.

Negotiable Instruments are an integral part of the financial and commercial transactions as they standardise the format, responsibilities, and liabilities associated with such transactions. The Negotiable Instruments Act, 1881, provides the legal framework for the creation, transfer, and discharge of these instruments in India. The Act has been amended several times to keep it contemporary and useful in the changing business environment.

Discharge

Discharge of a negotiable instrument means the termination of liability of the parties, either primary (i.e., drawer, acceptor, or maker) or secondary (i.e., indorser), under the instrument. Once discharged, a negotiable instrument loses its negotiability.

Discharge of Negotiable Instruments as per Negotiable Instruments Act, 1881

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The Negotiable Instruments Act, 1881 provides various ways in which a negotiable instrument is discharged:

1. **By Payment (Section 78 and 79):** The most common way to discharge a negotiable instrument is by payment in due course by or on behalf of the drawee or acceptor. It must be made during the usual hours of business, and with the instrument, to the holder thereof, or to the holder's agent duly authorised to receive payment.
2. **By Cancellation (Section 82):** If the holder of the negotiable instrument, voluntarily cancels it, the parties liable on the instrument are discharged.
3. **By Release (Section 82):** A party liable on the instrument can be discharged by an intentional act of the holder. If the holder releases a party, he is discharged while others continue to be liable.
4. **By Allowing Drawee More Than 48 Hours to Accept (Section 83):** In the case of a bill of exchange, if the holder allows the drawee more than forty-eight hours, exclusive of public holidays, to consider whether he will accept the bill, all previous parties not consenting to such allowance are thereby discharged from liability.
5. **By Qualified or Conditional Acceptance (Section 86):** When the holder of a bill of

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exchange accepts the bill conditionally or qualifiedly, all preceding parties whose consent is not obtained to such acceptance are discharged from liability on the bill.

6. **By Material Alteration (Section 87):** A negotiable instrument is also discharged if any material alteration (like altering the date, the sum payable, the time of payment, etc.) is made on the instrument without the consent of all parties.

Person who signs a negotiable instrument otherwise than as a drawer or acceptor is presumed to be an endorser unless he clearly indicates by appropriate words his intention to be bound in some other capacity.

Understanding the concept of discharge is critical in the context of negotiable instruments. The discharge of a negotiable instrument signifies the termination of the instrument and releases the parties from their respective obligations. This process is governed by specific sections of the Negotiable Instruments Act, 1881, which details the different ways a negotiable instrument can be discharged, thereby providing a comprehensive framework for the termination of these instruments.

DISHONOUR OF NEGOTIABLE INSTRUMENTS

A negotiable instrument is said to be dishonoured when the person on whom it is drawn refuses to accept it or make the payment upon being duly required to do so.

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Dishonour of a negotiable instrument can cause significant harm to the reputation of the parties involved, and can also attract legal penalties.

Dishonour of a Bill of Exchange

In the context of a bill of exchange, there are two types of dishonour:

1. **Dishonour by Non-Acceptance (Section 91):** A bill of exchange is said to be dishonoured by non-acceptance when the drawee, or one of several drawees not being partners, makes default in acceptance upon being duly required to accept the bill. This could occur under several circumstances, such as when the drawee is incompetent to contract, or when the drawee is fictitious or non-existent.
2. **Dishonour by Non-Payment (Section 92):** A promissory note, bill of exchange or cheque is said to be dishonoured by non-payment when the maker of the note, acceptor of the bill or drawee of the cheque makes default in payment upon being duly required to pay the same.

Consequences of Dishonour

When a negotiable instrument is dishonoured, the holder or the notary public is required to give a notice of dishonour to all prior parties (i.e., the drawer and all endorsers) who are liable on the instrument, to make them aware that the instrument has been dishonoured.

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Failure to provide this notice can discharge those parties from their liabilities on the instrument.

If the parties to the instrument receive a notice of dishonour and fail to make payment, they could be subject to legal action. Under Section 138 of the Negotiable Instruments Act, the dishonour of a cheque due to insufficient funds in the account is a criminal offence that can result in imprisonment and/or a fine.

One of the landmark judgments related to dishonour of cheques is **Damodar S. Prabhu v. Sayed Babalal H.**(2010), where the Supreme Court of India laid down guidelines for courts in relation to the compounding of offences under Section 138 of the Negotiable Instruments Act.

In another case, **Rangappa Vs. Sri Mohan**, the Supreme Court held that once the execution of the cheque is admitted, the presumption under Section 139 must follow and the burden shifts to the drawer to rebut the presumption.

The concept of dishonour of a negotiable instrument is a crucial aspect of the law of negotiable instruments. It provides a legal mechanism to hold parties accountable for their obligations under the instrument and provides recourse to the holder of the instrument in case of non-acceptance or non-payment.

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Notice of Dishonour

The notice of dishonour is a formal notice given to the drawer or endorser of a negotiable instrument when the instrument has been dishonoured, either by non-acceptance or non-payment. It serves to inform them that the instrument has been dishonoured and that they are liable to pay the holder. This notice can be given by the holder of the instrument or by any other party entitled to give notice.

Notice of Dishonour under the Negotiable Instruments Act, 1881

The following sections of the Act govern the notice of dishonour:

Section 93: When a promissory note, bill of exchange or cheque is dishonoured by non-payment, the holder thereof, or some party thereto who remains liable thereon, must give notice that the instrument has been so dishonoured to all other parties whom the holder seeks to make severally liable thereon, and to some one of several parties whom he seeks to make jointly liable thereon.

The notice of dishonour should include:

1. The fact that the instrument has been dishonoured.
2. The date of dishonour.
3. The reason for dishonour.

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Dispensation of Notice (Section 98)

The notice of dishonour may be dispensed with in the following circumstances:

1. If it is waived by the party entitled to it.
2. If the party charged could not suffer damage for want of notice.
3. If the party entitled to notice cannot after due search be found.
4. If the acceptor is also the drawer.

Consequences of Failure to Give Notice

If a party entitled to receive notice of dishonour does not receive it within a reasonable time, the party who was supposed to give the notice is not able to enforce the instrument against the party who should have received the notice. This rule aims to protect parties who may have been able to take remedial action had they known about the dishonour.

The notice of dishonour is an essential part of the law governing negotiable instruments. It ensures that all parties to the instrument are informed when it has been dishonoured, allowing them the opportunity to take appropriate action. Failure to provide notice of dishonour in accordance with the Negotiable Instruments Act, 1881, can have significant legal implications and may limit the legal recourse available to the holder of the instrument.

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Crossing of Cheques

Crossing of cheques is a unique feature associated with cheques that provides a measure of safety against loss or theft. When a cheque is crossed, it cannot be cashed directly at the counter of the bank and must be collected through a bank account, which ensures traceability of the transaction. This practice encourages cheque users to operate bank accounts and discourages the practice of holding money in cash, which carries security risks.

Types of Crossing (Section 123-131A of the Negotiable Instruments Act)

1. **General Crossing (Section 123):** A cheque is said to be crossed generally when it bears across its face an addition of two parallel transverse lines with or without any words. The payment of such a cheque must be done to a banker only.
2. **Special Crossing (Section 124):** A cheque is said to be crossed specially when it bears across its face an addition of the banker's name, with or without the words "not negotiable". Here, the bank will only pay the amount of the cheque to the banker named.
3. **Account Payee Crossing:** When a cheque bears an addition of words "Account Payee" or "A/C Payee" between the parallel lines

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constituting a crossing, the cheque is said to have been crossed "account payee". It directs the collecting banker that the amount of the cheque is to be credited to the account of the payee only. It ensures that the cheque can only be paid to the person named as the payee.

- 4. Not Negotiable Crossing:** When the term "Not Negotiable" is written between the crossing lines, the cheque is said to be crossed 'Not Negotiable'. A person obtaining a "not negotiable" crossed cheque will not have better title than the person from whom he received it.

Effects of Crossing

Crossing a cheque is essentially a direction to the banker to pay the cheque only through a banker. It also imposes certain obligations on bankers. The primary impact of crossing a cheque is that it ensures that the funds are paid only through the banking channels, which leaves a clear trail that can be used as evidence of the transaction.

Crossing of cheques is a mechanism that significantly enhances the security of cheque-based transactions. It helps ensure that the proceeds of a cheque reach the correct recipient and minimizes the risk of unauthorized or fraudulent encashments. Various forms of crossing are used to indicate how a cheque is to be handle. The Negotiable Instruments Act, 1881, provides comprehensive rules for the crossing of cheques, and users of cheques should be aware of these provisions.

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Protection of Paying Banker

In the transactional cycle of negotiable instruments, the paying banker plays a critical role. The paying banker is the bank on which the cheque is drawn and who is directed to pay the amount specified in the cheque. Given the sheer volume of transactions a banker deals with, it's crucial that they operate within the prescribed legal framework to ensure smooth operations and avoid unnecessary liability.

Under the Negotiable Instruments Act, 1881, several provisions have been incorporated to protect the paying banker's interests.

Payment in Due Course (Section 10)

A payment in due course is a payment made by the banker, which is in accordance with the mandate of the drawer, made at the proper place, and to the person in possession of the cheque who is legally entitled to receive payment.

When the banker makes a payment in due course, it is discharged from its liability. The paying banker should observe utmost good faith, ensure the instrument is not materially altered, and the endorsement is regular.

Payment of Order Cheque to a Wrong Person (Section 85(1))

The banker is discharged from liability if it pays an order cheque in good faith and without negligence to a person,

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who possesses the cheque and shows prima facie title to it, even if the person subsequently turns out to be not entitled to receive the payment.

Payment of Bearer Cheque (Section 85(2))

The banker is discharged from liability if it pays a bearer cheque in good faith and without negligence, even if the bearer is later found to have no title to the cheque.

Payment of Crossed Cheque (Section 128)

If a crossed cheque is paid in good faith and without negligence to the banker to whom it is crossed or his agent for collection, the paying banker would be protected, even if the endorsement turns out to be forged or unauthorized.

The protections provided under the Negotiable Instruments Act, 1881, are essential to ensure the smooth functioning of the banking system, especially for the paying banker who deals with numerous transactions daily. Despite this, it is incumbent on the banker to exercise due diligence and good faith in its operations. The protections do not absolve a banker of liability in cases of negligence or fraud, and banks must implement strong controls to prevent such occurrences.

Dishonour of Cheques

A cheque is a negotiable instrument that promises payment from a drawer (the person who writes the

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cheque) to a drawee (the bank) for the benefit of the payee (the person who receives the cheque). Dishonour of a cheque occurs when the bank does not honour the promise of payment, usually due to insufficient funds in the drawer's account, or for reasons such as a mismatch of signature, overwriting, or if the cheque is stale (not presented within the validity period, i.e., within three months from the date of issue), etc.

Dishonour of Cheque under the Negotiable Instruments Act, 1881

Section 138 of the Act pertains to the dishonour of cheques due to insufficiency of funds in the account of the drawer of the cheque. It states that if a cheque drawn by a person on an account maintained by him for the payment of any amount of money to another person fails due to insufficiency of funds, then the drawer shall be deemed to have committed an offence.

Section 138: This section pertains to the dishonour of a cheque on account of insufficiency of funds. If a cheque drawn by a person for the discharge of any debt or other liability is returned by the bank unpaid due to insufficient funds, the drawer of the cheque is deemed to have committed an offence and is punishable by imprisonment for a term which may extend to two years, or with a fine which may extend to twice the amount of the cheque, or both.

Section 139: This section presumes, unless the contrary is proven, that the holder of a cheque received the cheque

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for the discharge, in whole or in part, of any debt or other liability.

Section 140: This section states that it is not a defence in a prosecution for an offence under Section 138 that the drawer had no reason to believe when he issued the cheque that the cheque may be dishonoured on presentment for the reasons stated in that section.

Section 141: This section extends the liability for the offence of dishonour of cheques to companies, firms, or associations of individuals.

Section 142: This section specifies the conditions that must be met before a complaint can be made under Section 138. The complaint must be made by the payee or the holder in due course, and it must be made within one month of the date on which the cause of action arises under the clauses of the proviso to Section 138.

This offence is punishable with imprisonment for a term up to two years, or with a fine that can extend to twice the amount of the cheque, or with both. However, such offences are compoundable, meaning that the parties can enter into a compromise to stop legal proceedings.

Steps for Legal Action

- 1. Notice to Drawer:** After the cheque has been returned by the bank, the payee must issue a notice in writing to the drawer within 30 days from the receipt of the information by the bank regarding the return of the cheque.

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- 2. Drawer's Liability to Make Payment:** The drawer has 15 days from the receipt of the notice to make the payment. If the drawer fails to make the payment within 15 days of receipt of the notice, the payee may file a criminal complaint.
- 3. Filing of Complaint:** The complaint must be filed within one month of the expiry of the 15 days given to the drawer to settle the payment.

Landmark Judgments

One of the most important cases concerning dishonour of cheques is **Dashrath Rupsingh Rathod v. State of Maharashtra & Anr.** (2014) The Supreme Court held that the territorial jurisdiction for dishonour of cheques is restricted to the court within whose local jurisdiction the offence was committed, i.e., where the cheque is dishonoured by the bank on which it is drawn.

Another important judgement is the **N. Harihara Krishnan vs J. Thomas (2017)** case where the Supreme Court ruled that the period of one month for filing a complaint under Section 138 of the Act will be reckoned from the day immediately following the day on which the period of 15 days from the receipt of the notice by the drawer expires.

Dishonour of a cheque is a serious offence under the Negotiable Instruments Act, 1881. It not only reflects financial unreliability on the part of the drawer but can also cause financial loss and inconvenience to the payee.

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The Act provides strict penalties for such offences to maintain trust and confidence in this crucial financial instrument.



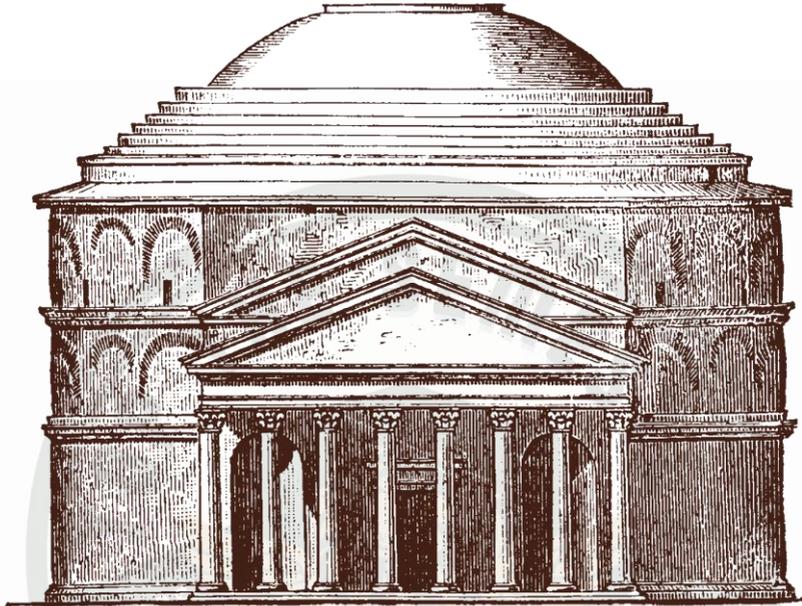
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REQUIRED CASE READINGS

CASE BRIEFS AND ANALYSIS

1. VANCOUVER MALT & SAKE BREWING CO. V. VANCOUVER BREWERIES LTD., AIR 1934 PC 101
2. KORES MFG. CO. LTD. V. KULOK MFG. LTD. (1958) 2 ALL ER 65
3. A.V.M. SALES CORPORATION V. ANURADHA CHEMICALS PVT. LTD. (2012) 2 SCC 315
4. HUNGERFORD INVESTMENT TRUST V. HARIDASMUNDHRA, AIR 1972 SC 1826
5. STATE OF WEST BENGAL V. B K MONDAL & SONS., AIR 1962 SC 779
6. HADLEY V. BAXENDALE, [1854] EWHC J70
7. BANK OF BIHAR LTD. V. DAMODAR PRASAD, AIR 1969 SC 297
8. STATE BANK OF SAURASHTRA V. CHITRANJANRANGNATH RAJA, AIR 1980 SCR (3) 915
9. KALIAPERUMAL PILLAI V. VISALALAKSHMI, AIR 1938 MAD 32
10. BOLTON V. LAMBERT (1889) 41 CH. D. 295

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1.

VANCOUVER MALT & SAKE BREWING CO. V. VANCOUVER BREWERIES LTD.

AIR 1934 PC 101

Facts in Brief

The case arose from an agreement dated **5 December 1927**, under which the appellants, *Vancouver Malt and Sake Brewing Co. Ltd.*, incorporated in **1923** and holding a **brewer's licence under the Dominion Excise Act**, agreed for **\$15,000** not to manufacture or sell **beer** for **fifteen years**, while confining themselves to the production of **sake**. Although licensed to brew beer, the appellants had never done so, their business being limited to sake in **British Columbia**. The respondents, *Vancouver Breweries Ltd.*, incorporated in **1912**, were beer brewers in Vancouver and the only other brewery in the city. When the appellants, on legal advice, refused to be bound by the agreement, the respondents obtained a declaration and injunction from the **Supreme Court of British Columbia**, affirmed by a majority of the **Court of Appeal**, leading to an appeal to the **Privy Council** on the ground that the agreement was an **unreasonable restraint of trade** and contrary to **public policy**.

Issues

The appeal before the Privy Council raised several **interrelated legal issues**, all revolving around the

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doctrine of restraint of trade and public policy. The principal issues may be framed as follows:

1. **Whether the agreement dated 5 December 1927 was legally valid and enforceable**, or whether it was void as being contrary to public policy on the ground of unreasonable restraint of trade.
2. **Whether the restrictive covenants contained in the agreement could be justified as ancillary to a legitimate transaction**, namely the sale of goodwill of a brewer's licence, or whether they constituted a bare covenant not to compete.
3. **Whether goodwill in respect of a brewer's licence, or a part thereof, was capable of being sold or assigned**, particularly when the licence itself was personal and non-transferable.
4. **Whether the scope and duration of the restrictive covenants—fifteen years with no express geographical limitation—were reasonable as between the parties.**
5. **Whether the restrictive covenants were consistent with the interests of the public**, having regard to the doctrine that every person should have freedom to engage in lawful trade.
6. **Whether the payment of monetary consideration (\$15,000) could validate a**

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covenant that effectively amounted to the purchase of freedom from competition.

These issues required the Privy Council to apply established principles governing contracts in restraint of trade, particularly the **twofold test of reasonableness** articulated in prior authorities.

Arguments

Arguments on behalf of the Appellants

- a) The appellants contended that the agreement was **void and unenforceable** as it was contrary to public policy and constituted an **unreasonable restraint of trade**. Their arguments were multifaceted.
- b) First, it was argued that the agreement did not involve any **genuine sale of goodwill**. The appellants had never brewed beer and therefore had **no goodwill associated with beer brewing**. The only business they carried on was the manufacture of sake, and the goodwill relating to sake was expressly excluded from the agreement. Consequently, the purported sale of goodwill of a brewer's licence relating to beer was illusory and incapable of supporting restrictive covenants.
- c) Secondly, the appellants submitted that a **brewer's licence under the Excise Act was personal and non-transferable**. As such, neither the licence nor

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its goodwill could be sold or assigned. The agreement therefore lacked a legitimate subject matter and was merely a façade designed to conceal an otherwise naked restraint of trade.

- d) Thirdly, the appellants argued that the restrictive covenants were **not ancillary to any valid transaction**. They were not designed to protect the purchaser of a business or goodwill, but were instead intended solely to **prevent competition**. Such a bare covenant not to compete, unsupported by a legitimate main transaction, was unknown to English law and had consistently been held unenforceable.
- e) Fourthly, the appellants challenged the **width and severity of the restraint**. The covenant restrained them from brewing beer **anywhere in the world** for a period of fifteen years. This lack of geographical limitation rendered the covenant manifestly unreasonable as between the parties.
- f) Finally, the appellants contended that the agreement failed the **public interest test**, as it restricted trade without any corresponding benefit to the community. The law, they argued, does not permit individuals to barter away their liberty to trade merely for monetary consideration.

Arguments on behalf of the Respondents

- a) The respondents, on the other hand, sought to uphold the agreement as a **legitimate commercial**

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arrangement.

- b) They argued that the agreement amounted to a **valid sale of goodwill** associated with the appellants' brewer's licence insofar as it related to beer. The restrictive covenants, according to the respondents, were necessary to give effect to this transaction and to protect the purchaser from competition.
- c) It was further contended that the appellants had received substantial **monetary consideration**, which enabled them to improve their plant and continue their business of brewing sake. This, the respondents argued, was beneficial not only to the appellants but also to the public, as it prevented the appellants from becoming insolvent.
- d) With respect to the geographical scope of the restraint, the respondents submitted that **practical considerations effectively limited the operation of the covenant to British Columbia**, even though no express limitation was stated in the agreement. They urged the court to impose such a limitation as a matter of construction.
- e) The respondents also relied on **Scottish authorities**, particularly *Stewart v. Stewart* and *Ballachulish Slate Quarries Co. Ltd. v. Grant*, to argue that restrictive covenants could be enforceable even outside the context of a sale of business, provided they were reasonable.

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Held

The **Judicial Committee of the Privy Council** unanimously **allowed the appeal**, thereby **reversing the judgments** of both the **Supreme Court of British Columbia** and the **Court of Appeal of British Columbia**. The Privy Council held that the agreement dated **5 December 1927** was **invalid, void, and unenforceable**, being contrary to public policy as an **unreasonable restraint of trade**.

The Board categorically ruled that the restrictive covenants contained in the agreement could not be sustained under law because they were **not ancillary to any legitimate transaction**, such as a sale of business or goodwill, and were instead designed solely to prevent competition. The agreement, stripped of its ostensible form, amounted to nothing more than a **purchase of protection against competition**, which English law does not recognise as a valid object of contract.

The Privy Council further held that even if the agreement were to be tested independently of its lack of a legitimate main transaction, the **terms of the restraint were in any event unreasonable**, particularly due to their **worldwide geographical scope** and the **lengthy duration of fifteen years**. Such extensive restrictions could not be justified as being reasonable between the parties or consistent with the interests of the public.

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Consequently, the declaration and injunction granted in favour of the respondents were set aside, and the respondents' action was dismissed. The appellants were awarded **costs at all stages of the litigation**, including costs before the Privy Council.

Legal principles with relevant sections:

The judgment is a leading exposition of the **doctrine of restraint of trade**, reaffirming and clarifying several foundational legal principles.

A. Doctrine of Restraint of Trade

At the core of the case lies the common law doctrine that **agreements in restraint of trade are prima facie void**, unless they can be justified. This doctrine reflects a balance between two competing public policy considerations:

1. **Freedom of contract**—the principle that parties of full age and capacity should be bound by the agreements they voluntarily enter into.
2. **Freedom of trade**—the principle that every individual should be free to exercise their skills and engage in lawful trade for their own benefit and that of the community.

The Privy Council emphasised that this doctrine remains **“of full force and vitality”**, notwithstanding changes in economic conditions.

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B. The Twofold Test of Justification

The authoritative test for determining the enforceability of a contract in restraint of trade was restated by the Privy Council by relying on **McEllistrim v. Ballymacelligott Co-operative Agricultural and Dairy Society (1919) AC 548**. According to this test, a restrictive covenant is enforceable only if:

1. **It is reasonable as between the parties**, and
2. **It is consistent with the interests of the public.**

Both limbs of the test must be satisfied. Failure on either ground renders the covenant void.

C. Ancillary Restraints vs. Bare Restraints

A central legal principle emerging from the case is the distinction between:

- **Ancillary restraints**, which are attached to and necessary for the effectiveness of a legitimate transaction (such as the sale of a business or goodwill), and
- **Bare restraints**, which exist independently and merely seek to prevent competition.

The Privy Council reaffirmed that **only ancillary restraints are capable of justification**. A bare covenant not to compete, unsupported by a valid main transaction, is unenforceable.

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Obiter dictum :

Several observations made by the Privy Council, though not strictly necessary for the decision, constitute significant **obiter dicta** with enduring persuasive value.

One such observation relates to the **evolving nature of public policy**. The Board acknowledged that public policy is not static and may change with economic conditions. However, it cautioned that such evolution does not erode the fundamental prohibition against unreasonable restraints of trade.

Another important obiter concerns **worldwide restraints**. The Privy Council observed that while such restraints have occasionally been upheld, this has occurred only where the nature of the business itself was global. This observation has guided later courts in assessing the proportionality of restrictive covenants.

The Board also made a noteworthy comment on **drafting practices**, suggesting that the agreement in question was artificially structured to appear as a sale in order to evade the law's hostility towards bare restraints. This observation serves as a cautionary note against attempts to disguise unlawful restraints through clever drafting.

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Important para from judgement :

Several passages from Lord Macmillan's opinion are of exceptional doctrinal importance.

One of the most significant paragraphs is where the Court dismantles the purported sale:

"What exactly is meant by the goodwill of a licence or part of a licence, it is difficult to conceive... They had no goodwill to sell so far as regards the brewing of beer."

This paragraph is crucial because it establishes that **goodwill cannot exist in the abstract**; it must be attached to an existing business activity.

Subsequent Impact :

The decision in *Vancouver Malt and Sake Brewing Co. Ltd. v. Vancouver Breweries Ltd.* has had a **lasting influence** on the law relating to restraint of trade across common law jurisdictions.

A. Doctrinal Impact

The case reinforced the orthodox position that **bare covenants not to compete are unenforceable**, and it clarified the necessity of a legitimate main transaction to support restrictive covenants. It has been repeatedly cited in subsequent cases dealing with non-compete clauses, particularly in commercial and employment contexts.

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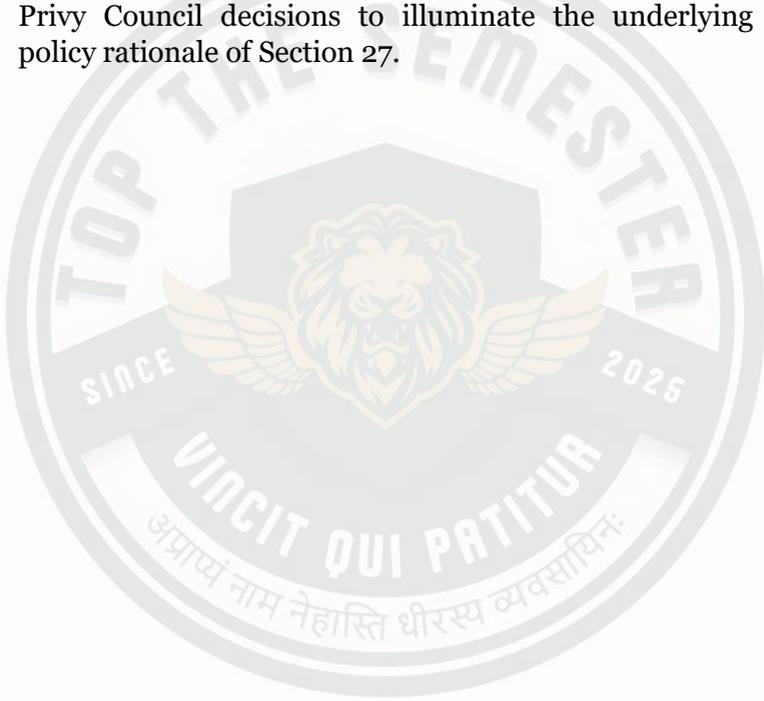
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B. Comparative Relevance

The judgment has been influential not only in Canada and the United Kingdom but also in jurisdictions such as **India**, where **Section 27 of the Indian Contract Act, 1872** embodies a stricter statutory prohibition against restraint of trade. Indian courts have often referred to Privy Council decisions to illuminate the underlying policy rationale of Section 27.



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2.

KORES MFG. CO. LTD. V. KULOK MFG. LTD.

(1958) 2 ALL ER 65

Facts in Brief

Kores Manufacturing Co. Ltd. v. Kolok Manufacturing Ltd. arose from a dispute concerning the enforceability of a **restrictive covenant in a contract of employment**. Kores Manufacturing Co. Ltd. was engaged in the manufacture of **carbon paper and duplicating materials**, involving specialised and confidential manufacturing processes. A senior technical employee of Kores, who had access to **trade secrets and confidential information**, left the company and became associated with Kolok Manufacturing Ltd., a competing concern engaged in a similar business.

The employee's contract contained a **post-employment restrictive covenant** restraining him from engaging in a competing business or using confidential information acquired during employment. Kores sought an **injunction** on the ground that the competing business was founded upon the **misuse of confidential technical knowledge**. The defendants contended that the covenant was an **unreasonable restraint of trade**, arguing that the employee was entitled to use his general skill and experience. The dispute ultimately came before the **Court of Appeal**, which was required to determine the **validity and scope of post-**

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employment restraints aimed at protecting confidential information.

Issues

The case raised several **important and nuanced legal issues**, central to the law governing **restrictive covenants in contracts of employment**:

1. **Whether the restrictive covenant imposed on the former employee constituted an unreasonable restraint of trade**, and was therefore void and unenforceable.
2. **Whether an employer is entitled to restrain a former employee from engaging in a competing business** where the employee had access to confidential information and trade secrets during employment.
3. **What constitutes “confidential information” or “trade secrets”**, as opposed to general skill, experience, or knowledge that an employee is free to use after leaving employment.
4. **Whether the covenant was reasonably necessary for the protection of the employer’s legitimate business interests**, having regard to its scope, duration, and purpose.
5. **Whether the formation of a competing company by a former employee using**

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specialised knowledge acquired during employment amounts to misuse of confidential information.

These issues required the Court of Appeal to balance **freedom of trade and employment** against the **legitimate proprietary interests of employers.**

Arguments

Arguments on behalf of the Plaintiffs (Kores Manufacturing Co. Ltd.)

- f) The plaintiffs argued that the restrictive covenant was **valid and enforceable**, as it was narrowly tailored to protect their **legitimate business interests**, particularly their **trade secrets and confidential manufacturing processes**.
- g) They contended that the employee had been entrusted with **highly specialised technical information**, which went beyond ordinary skill or experience. Allowing him to immediately set up or assist a competing business would, in effect, permit him to **appropriate the fruits of Kores' research, investment, and expertise**.
- h) Kores further argued that the covenant did not impose a blanket prohibition on employment, but merely restrained the employee from **engaging in competing activities that would inevitably**

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involve the misuse of confidential information. The restraint, they submitted, was reasonable both in duration and scope, and consistent with established principles governing employment covenants.

- i) Reliance was placed on earlier authorities recognising that trade secrets and confidential information constitute proprietary interests deserving of protection, even after the termination of employment.

Arguments on behalf of the Defendants (Kolak Manufacturing Ltd. and Others)

- j) The defendants argued that the restrictive covenant was excessive and oppressive, and that it effectively prevented the employee from earning a livelihood in his chosen field.
- k) They submitted that the law draws a clear distinction between confidential information and general technical skill or experience, and that an employee cannot be restrained from using the latter merely because it was acquired during employment.
- l) According to the defendants, the covenant sought to protect Kores not against misuse of secrets, but against mere competition, which the law does not permit. They contended that any confidential information could be protected through narrower obligations of non-disclosure, without imposing a

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broad restraint on post-employment activity.

Held

The **Court of Appeal held** that the restrictive covenant was **valid and enforceable**, to the extent that it was designed to **protect the employer's trade secrets and confidential information**, and that the defendants were **not entitled to exploit confidential technical knowledge acquired during employment for the purpose of establishing a competing business**.

The Court emphasised that while the law recognises an individual's right to **freely engage in trade or employment**, this freedom is subject to the **equitable obligation not to misuse confidential information or trade secrets** obtained in the course of employment. Where an employee occupies a **technical or managerial position involving access to confidential processes**, the employer is entitled to impose reasonable restraints to prevent unfair competition.

The Court distinguished between **general skill and experience**, which an employee is free to use after leaving employment, and **trade secrets or confidential processes**, which remain the proprietary interest of the employer and cannot be appropriated by the employee.

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The injunction sought by Kores was therefore granted, restraining the defendants from using the confidential information and trade secrets in the competing business.

Legal principles with relevant sections:

(A) Doctrine of Restraint of Trade in Employment Contracts

- a) The case reaffirmed the fundamental common law principle that **all restraints of trade are prima facie void**, unless they are **reasonable as between the parties and not injurious to the public**. This principle originates from *Nordenfelt v. Maxim Nordenfelt Guns and Ammunition Co. Ltd.* [1894] AC 535.
- b) In the context of employment contracts, the courts apply **stricter scrutiny** than in commercial sale-of-business agreements, because employees are typically in a **weaker bargaining position** and restraints may affect their livelihood.
- c) However, *Kores* clarified that **restraints designed to protect trade secrets and confidential information are legitimate and enforceable**.

(B) Distinction Between Trade Secrets and General Skill or Knowledge

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- a) A central doctrinal contribution of *Kores* is the **refinement of the distinction between:**
1. **Trade secrets and confidential information**, and
 2. **General skill, experience, and knowledge**
- b) The Court held that:
- **General skill and experience** acquired during employment belong to the employee and may be freely used after termination.
 - **Trade secrets and confidential information** remain the property of the employer and cannot be used for competitive purposes.
- c) This distinction is foundational in modern employment law and intellectual property jurisprudence.

(C) Employer's Legitimate Protectable Interests

- a) The Court recognised that employers have **legitimate proprietary interests** that justify post-employment restraints, including:
- Trade secrets
 - Confidential manufacturing processes

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- Customer lists and business connections
 - Technical know-how that is not publicly available
- b) A restrictive covenant is enforceable if it is **reasonably necessary to protect such interests**, and not merely to prevent competition per se.

Reasonableness Test

- a) The Court reiterated the two-fold test for enforceability:
1. **Reasonableness between the parties** – whether the covenant is necessary to protect the employer's interests.
 2. **Reasonableness in the public interest** – whether it unduly restricts competition or the employee's freedom of trade.
- b) In *Kores*, the covenant was upheld because it was directed at preventing misuse of trade secrets rather than imposing a blanket prohibition on employment.

Obiter dictum:

The Court made several important **obiter observations** that have influenced later jurisprudence.

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It was observed that:

- The law must strike a **balance between protecting innovation and preserving free competition.**
- Excessively broad restraints that prevent an employee from working in an entire industry would be **prima facie void**, even if the employee had access to confidential information.
- Employers should not use restrictive covenants as a tool to **stifle legitimate competition**, but only to protect proprietary interests.

The Court also remarked that **confidential information varies in degree**, and that courts must examine the **nature, importance, and accessibility** of the information in each case to determine whether it constitutes a trade secret.

Important para from judgement:

The Court famously articulated the distinction between trade secrets and general knowledge in a passage that has been widely cited in later cases:

An employee is entitled to use the skill and experience which he has gained in the course of his employment, but he is not entitled to use or disclose trade secrets or confidential information which are the property of his employer.

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Another significant observation was:

A covenant restraining an employee from using confidential information is not in restraint of trade in the strict sense, but rather an equitable means of preventing unfair competition.

Subsequent Impact of the judgement:

Kores Manufacturing Co. Ltd. v. Kolok Manufacturing Ltd. has had a **lasting and profound impact on common law jurisprudence**, particularly in the areas of **employment law, trade secrets, and intellectual property protection.**

(A) Influence on English Law

The case is frequently cited alongside *Faccenda Chicken Ltd. v. Fowler* [1987] Ch 117, which further classified confidential information into three categories. *Kores* laid the conceptual groundwork for that classification by emphasising the **graduated nature of confidentiality.**

(B) Influence on Commonwealth Jurisdictions

Courts in **India, Canada, Australia, and other common law jurisdictions** have relied on *Kores* in determining the enforceability of post-employment restrictive covenants. Indian courts, in cases such as *Niranjan Shankar Golikari v. Century Spinning* (1967) and *Superintendence Company of India v. Krishan*

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Murgai (1980), have echoed the distinction between **negative covenants during employment** and **post-employment restraints**, while recognising the protection of trade secrets.



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3.

A.V.M. SALES CORPORATION V. ANURADHA CHEMICALS PVT. LTD.

(2012) 2 SCC 315

Facts in Brief

The case in question is a civil appellate case between A.V.M. Sales Corporation and M/S Anuradha Chemicals Pvt. Ltd. heard by the Supreme Court of India. The parties entered into an agreement on 23rd December, 1988, at Calcutta for the supply of chemicals manufactured by the respondent to the petitioner. This agreement was followed by a mutual understanding on 15th May, 1989, where the respondent agreed to adjust the advance lying with it and would exclusively supply to the petitioner its two products, Sodium Chromate and Sodium Dichromate, in West Bengal, Bihar, Orissa, and Assam. This understanding was reduced into writing in an agreement executed at Calcutta on 5th August, 1989. The agreement contained an additional clause indicating that "Any dispute arising out of this agreement will be subject to Calcutta jurisdiction only."

However, differences arose between the parties relating to the supply of goods, leading to the petitioner filing a suit in the Calcutta High Court on 27th August, 1991, for recovery of its alleged dues from the respondent. In response, the respondent filed a separate suit against the petitioner at Vijayawada for recovery of a sum of

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3,86,453.05. The petitioner contested this suit, raising several issues, including the jurisdiction of the Vijayawada Court to entertain the suit due to the exclusion clause in the agreement. The Principal Senior Civil Judge, Vijayawada, decreed the respondent's suit with costs for a sum of 3,86,453.05, together with interest at the rate of 12% per annum. The petitioner appealed this decision in the Andhra Pradesh High Court, which was dismissed. The petitioner then filed the present Special Leave Petition against this judgment.

The main issues in this case revolve around the exclusive jurisdiction of the Courts at Calcutta agreed to by the parties in the agreement and whether this was binding upon the parties. A further issue is whether, in breach of the agreement, the respondent was entitled to invoke the jurisdiction of a Court at Vijayawada, whose jurisdiction stood ousted by the agreement entered into between the parties.

Issues

The case presents several key issues:

1. The first issue is whether the Court at Vijayawada had territorial jurisdiction to entertain the suit. This issue arises from the fact that the agreement between the parties contained a clause indicating that "Any dispute arising out of this agreement will be subject to Calcutta jurisdiction only." The petitioner argued that

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its place of business was at Calcutta, the agreement for the supply of the goods was also entered into at Calcutta, the goods were to be delivered at Calcutta, and payment in respect thereof was to be made at Calcutta. Therefore, according to the petitioner, the Court at Vijayawada had no territorial jurisdiction to entertain the suit under Section 20 of the Code of Civil Procedure as no part of the cause of action had arisen within its jurisdiction.

2. The second issue is whether the parties to an agreement can contract in violation of Sections 23 and 28 of the Indian Contract Act, 1872. The petitioner argued that the parties cannot contract against the statutory provisions.
3. The third issue is whether the parties to an agreement can confer jurisdiction on a Court which has no territorial or pecuniary jurisdiction to entertain a matter. This issue arises from the fact that the respondent's registered office was situated at Vijayawada, the invoices for the goods were raised at Vijayawada, the goods were dispatched from Vijayawada, and the money was payable to the respondent or its nominee at Vijayawada, by way of Demand Drafts. Therefore, according to the respondent, the Courts at Vijayawada had jurisdiction to entertain the suit.
4. The fourth issue is whether if two Courts have jurisdiction to try a suit, can the parties to an agreement mutually agree to exclude the jurisdiction

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of one Court in preference to the other and as to whether the same would amount to violation of the provisions of Sections 23 and 28 of the Indian Contract Act.

Arguments

The arguments in this case revolve around the jurisdiction of the courts and the interpretation of the agreement between the parties.

1. The petitioner argued that the Court at Vijayawada had no territorial jurisdiction to entertain the suit under Section 20 of the Code of Civil Procedure as no part of the cause of action had arisen within its jurisdiction. The petitioner's place of business was at Calcutta, the agreement for the supply of the goods was also entered into at Calcutta, the goods were to be delivered at Calcutta, and payment in respect thereof was to be made at Calcutta. Furthermore, the agreement contained a clause indicating that "Any dispute arising out of this agreement will be subject to Calcutta jurisdiction only."
2. On the other hand, the respondent contended that its registered office was situated at Vijayawada, the invoices for the goods were raised at Vijayawada, the goods were dispatched from Vijayawada, and the money was payable to the respondent or its nominee at Vijayawada, by way of Demand Drafts. Therefore,

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according to the respondent, the Courts at Vijayawada had jurisdiction to entertain the suit.

3. The court considered the question of whether the parties to an agreement can contract in violation of Sections 23 and 28 of the Indian Contract Act, 1872. It was noted that parties cannot contract against the statutory provisions. A connected question was whether the parties to an agreement can confer jurisdiction on a Court which has no territorial or pecuniary jurisdiction to entertain a matter. The court also considered whether if two Courts have jurisdiction to try a suit, can the parties to an agreement mutually agree to exclude the jurisdiction of one Court in preference to the other and as to whether the same would amount to violation of the provisions of Sections 23 and 28 of the Indian Contract Act..

Held

The Supreme Court of India held that both the Courts within the jurisdiction of Calcutta and Vijayawada had jurisdiction under Section 20 of the Code of Civil Procedure to try the Suit, as part of the cause of action of the Suit had arisen within the jurisdiction of both the said Courts. However, the jurisdiction of the Courts at Vijayawada would stand ousted by virtue of the exclusion clause in the Agreement.

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The Court stated that it is a settled principle that where there may be two or more competent Courts which can entertain a suit consequent upon a part of the cause of action having arisen therewithin, if the parties to the contract agreed to vest jurisdiction in one such Court to try the dispute which might arise as between themselves, the agreement would be valid. If such a contract is clear, unambiguous and explicit and not vague, it is not hit by Sections 23 and 28 of the Contract Act and cannot also be understood as parties contracting against the statute.

The Court also held that the mutual agreement to exclude the jurisdiction of the Delhi Courts to entertain the suit was not opposed to public policy and was valid.

Therefore, the Special Leave Petition was allowed. The decree passed by the Principal Senior Civil Judge, Vijayawada in O.S. No.519 of 1991, and the impugned judgment of the High Court dated 18th January, 2007, were set aside. The Trial Court at Vijayawada was directed to return the plaint of the Original Suit No.519 of 1991 to the Plaintiff to present the same before the appropriate Court in Calcutta having jurisdiction to try the suit. The Special Leave Petition was, accordingly, allowed, but there was no order as to costs.

Legal principles with relevant sections

The case primarily revolves around the interpretation of the following legal principles and sections:

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1. Section 20 of the Code of Civil Procedure: This section deals with the jurisdiction of courts and states that a suit can be instituted in a court within the local limits of whose jurisdiction the defendant resides or carries on business, or where the cause of action wholly or in part arises. In this case, both the courts within the jurisdiction of Calcutta and Vijayawada had jurisdiction under Section 20 of the Code of Civil Procedure to try the suit, as part of the cause of action of the suit had arisen within the jurisdiction of both the said courts.
2. Sections 23 and 28 of the Indian Contract Act, 1872: Section 23 of the Act indicates what considerations and objects are lawful and what are not, including the considerations or objects of an agreement, if forbidden by law. Section 28 of the Act spells out that any agreement in restraint of legal proceedings is void. The court held that if any mutual agreement is intended to restrict or extinguish the right of a party from enforcing his/her right under or in respect of a contract, by the usual legal proceedings in the ordinary Tribunals, such an agreement would to that extent be void. In other words, parties cannot contract against a statute.

The court also referred to the case of A.B.C. Laminart Pvt. Ltd. & Anr. Vs. A.P. Agencies, Salem [AIR 1989 SC 1239 = (1989) 2 SCC 163] and Hanil Era Textiles Ltd. Vs. Puromatic Filters (P) Ltd. [AIR 2004 SC 2432 = (2004) 4 SCC 671] to establish the principle that where there may

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be two or more competent courts which can entertain a suit consequent upon a part of the cause of action having arisen therewithin, if the parties to the contract agreed to vest jurisdiction in one such court to try the dispute which might arise as between themselves, the agreement would be valid.

Obiter dictum

An obiter dictum is a remark or observation made by a judge that, although included in the body of the court's opinion, does not form a necessary part of the court's decision. In the context of this case, the court made several observations that can be considered as obiter dicta.

1. The court observed that a cause of action comprises a bundle of facts which are relevant for the determination of the lis between the parties. In this case, since the invoices for the goods in question were raised at Vijayawada, the goods were dispatched from Vijayawada, and the money was payable to the Respondent or its nominee at Vijayawada, these comprised part of the bundle of facts giving rise to the cause of action for the Suit.
2. The court also discussed the question of whether, if two Courts have jurisdiction to entertain a Suit, the parties may by mutual agreement exclude the jurisdiction of one of the Courts, having regard to the

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provisions of Sections 23 and 28 of the Indian Contract Act, 1872. The court concluded that if any mutual agreement is intended to restrict or extinguish the right of a party from enforcing his/her right under or in respect of a contract, by the usual legal proceedings in the ordinary Tribunals, such an agreement would to that extent be void. In other words, parties cannot contract against a statute.

3. The court further observed that the question of whether the parties to an agreement can contract in violation of Sections 23 and 28 of the Indian Contract Act, 1872, is not new and has been considered by this Court earlier in several decisions

Important para from judgement

There are several important paragraphs from the judgement that encapsulate the essence of the case:

1. Para 8: This paragraph discusses the cause of action and how it arose in both Vijayawada and Calcutta. It also introduces the question of whether parties can mutually agree to exclude the jurisdiction of one of the courts.
2. Para 9: This paragraph discusses the provisions of Sections 23 and 28 of the Indian Contract Act, 1872, and how they apply to the case. It also quotes Section 28 in full.

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3. Para 11-14: These paragraphs discuss previous cases where similar questions had arisen and how the court had ruled in those cases. They also discuss the principle that parties cannot contract against a statute.
4. Para 15-17: These paragraphs contain the final judgement of the court. The court held that the jurisdiction of the Courts at Vijayawada would stand ousted by virtue of the exclusion clause in the Agreement. The decree passed by the Principal Senior Civil Judge, Vijayawada in O.S. No.519 of 1991, and the impugned judgment of the High Court dated 18th January, 2007, are set aside. The Trial Court at Vijayawada is directed to return the plaint of the Original Suit No.519 of 1991 to the Plaintiff to present the same before the appropriate Court in Calcutta having jurisdiction to try the suit.

Subsequent Impact of the judgement

The subsequent impact of the case is not explicitly mentioned in the document. However, based on the judgement and the principles it established, we can infer the following:

1. This case sets a precedent for future cases where there is a dispute over jurisdiction due to an exclusion clause in a contract. It establishes that if two courts have jurisdiction over a case, parties can mutually

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agree to exclude the jurisdiction of one of the courts, as long as the jurisdiction agreed upon is also a proper jurisdiction in the matter of the contract.

2. The judgement reinforces the principle that parties cannot contract against a statute. Any agreement that restricts or extinguishes the right of a party from enforcing his/her right under or in respect of a contract, by the usual legal proceedings in the ordinary tribunals, would be void.
3. The case also highlights the importance of the cause of action in determining the jurisdiction of a court. It establishes that a cause of action comprises a bundle of facts which are relevant for the determination of the dispute between the parties.
4. Lastly, the judgement could have implications for contractual agreements in general, especially those with exclusion clauses. Parties entering into a contract must be aware of the implications of such clauses and ensure that they do not contract against a statute.

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4.

HUNGERFORD INVESTMENT TRUST V. HARIDASMUNDHRA

AIR 1972 SC 1826

Facts in brief

The case involves an agreement between the appellant (Hungerford Investment Trust) and the respondent (Haridas Mundhra) for the purchase of shares in a company. The respondent exercised their option to purchase the remaining shares, but as the company's financial position deteriorated, the appellant sought to rescind the agreement.

The appellant had already rescinded the contract and the decree by its letter dated February 11, 1967, stating that the respondent had forfeited his right to purchase the 51 per cent shares in pursuance of the decree in suit No. 600 of 1961, as he failed to fulfil his obligation in pursuance to the notice of the appellant on January 11, 1967. The appellant only wanted a declaration by adjudgment by the Court that it was justified in doing so.

The respondent raised the objection that the appellant was not in a position to give a good title to the shares because 'A' company claimed a lien in respect of the shares. The respondent also contended that the appellant was not in a position to give delivery of the shares and that it was not ready and willing to perform its part of the contract only to avoid payment of the purchase money.

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Issues

1. The primary issue was whether the appellant was justified in rescinding the contract and the decree by its letter dated February 11, 1967, stating that Mundhra had forfeited his right to purchase the 51 per cent shares in pursuance of the decree in suit No. 600 of 1961, as he failed to fulfil his obligation in pursuance to the notice of the appellant on January 11, 1967.
2. Another issue was whether the appellant was in a position to give a good title to the shares, as 'A' company claimed a lien in respect of the shares.
3. The question of whether the appellant was in a position to deliver the shares was also raised.
4. The respondent argued that he was always ready and willing to pay the purchase money, but since the decree did not specify any time for payment of the money, there was no default on his part.
5. The issue of whether the appellant was prevented from performing his part of the obligation under the decree or obtain satisfaction thereof due to attachments of the decree by creditors was also raised.

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Arguments

Appellant's Arguments:

1. The appellant argued that they were justified in rescinding the contract and the decree by its letter dated February 11, 1967, as Mundhra had forfeited his right to purchase the 51 per cent shares in pursuance of the decree in suit No. 600 of 1961, as he failed to fulfil his obligation in pursuance to the notice of the appellant on January 11, 1967.
2. The appellant contended that when they came to the Court with its application for rescission, there was already a rescission of the contract and the decree. They only wanted a declaration by adjudgment by the Court that they were justified in doing so.
3. The appellant argued that the Court does not create any right which parties did not possess when it makes a declaration that a contract has been validly rescinded. Merely because it is necessary for the Court to pass an order of rescission, when a controversy arises, it does not follow that it is the Court that rescinds the contract. The Court is only passing upon the validity of the rescission already made by the party.
4. The appellant argued that the respondent could not complain that, because the appellant obtained a stay of the order passed by the trial court giving the respondent a fortnight's time to pay the purchase

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money, the appellant prevented him from paying the purchase money, and resist the prayer for rescission.

Respondent's Arguments:

1. Mundhra contended that he was always ready and willing to pay the purchase money, but since the decree did not specify any time for payment of the money, there was no default on his part.
2. Mundhra argued that the appellant was not in a position to give a good title to the shares because 'A' company claimed a lien in respect of the shares.
3. Mundhra also contended that the appellant was not in a position to deliver the shares.

Held

The court held that when the appellant came to the court with its application for rescission, there was already a rescission of the contract and the decree by its letter dated February 11, 1967. The appellant only wanted a declaration by adjudgment by the court that it was justified in doing so. The court did not create any right which the parties did not possess when it made a declaration that the contract had been validly rescinded. It is only deciding upon the validity of the rescission already made by the party.

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The court found no substance in the contention of the respondent that the appellant was not in a position to give a good title to the shares because 'A' company claimed a lien in respect of the shares.

The court held that a decree for specific performance is a decree in favor of both the plaintiff and defendant in the suit, but it could be executed only in the manner prescribed by 0.31, r. 32, C.P.C. The appellant could not have executed the decree against the respondent as a money decree and realized the purchase money from him. Therefore, if the respondent refused to pay the purchase money there was nothing which prevented the appellant from applying for rescission of the decree.

The court was concerned with whether the respondent had disabled himself from performing his part of the obligation under the decree. The fact that attachments of the decree by creditors prevented him from performing his part of the obligation under the decree or obtain satisfaction thereof would not make him any less a defaulter so far as performance of his part of the obligation under the decree is concerned.

Legal principles with relevant sections

The court reiterated the principle that when a party to a contract expresses by word or act in an unequivocal manner that by reason of fraud or essential error of a material kind inducing him to enter into the contract he

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has resolved to rescind it, and refuses to be bound by it, the expression of his election, if justified by the facts, terminates the contract, puts the parties in status quo ante and restores things, as between them, to the position in which they stood before the contract was entered into. This principle was highlighted in the case of *Abram Steamship Company Ltd. and another v. Westville Shipping Company Ltd.*

The court also emphasized that a decree for specific performance is a decree in favor of both the plaintiff and defendant in the suit, but it could be executed only in the manner prescribed by Order 21, Rule 32, Civil Procedure Code (C.P.C). The appellant could not have executed the decree against the respondent as a money decree and realized the purchase money from him. Therefore, if the respondent refused to pay the purchase money there was nothing which prevented the appellant from applying for rescission of the decree.

The court referred to the Specific Relief Act, 1963, stating that it is not an exhaustive enactment. It does not consolidate the whole law on the subject. As the preamble would indicate, it is an Act "to define and amend the law relating to certain kinds of specific relief". It does not purport to lay down the law relating to specific relief in all its ramifications.

The court also referred to the principle that the court which passes a decree for specific performance retains control over the decree even after the decree has been passed. This principle was highlighted in the cases of

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Mahommadalli Sahib v. Abdul Khadir Saheb and Pearisundari Dasee v. Hari Charan Mozumdar Chowdhry.

Obiter dictum

The court made an important observation that when a party to a contract expresses by word or act in an unequivocal manner that by reason of fraud or essential error of a material kind inducing him to enter into the contract he has resolved to rescind it, and refuses to be bound by it, the expression of his election, if justified by the facts, terminates the contract, puts the parties in status quo ante and restores things, as between them, to the position in which they stood before the contract was entered into.

The court also noted that a decree for specific performance is a decree in favor of both the plaintiff and defendant in the suit. It could be executed only in the manner prescribed by Order 21, Rule 32, C.P.C. The appellant could not have executed the decree against the respondent as a money decree and realized the purchase money from him. Therefore, if the respondent refused to pay the purchase money there was nothing which prevented the appellant from applying for rescission of the decree.

The court further observed that the court retains control over the matter even after passing a decree for specific

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performance and that virtually, the decree is in the nature of a preliminary one.

Important para from judgement

The court adjudicated that when a party to a contract expresses by word or act in an unequivocal manner that by reason of fraud or essential error of a material kind inducing him to enter into the contract he has resolved to rescind it, and refuses to be bound by it, the expression of his election, if justified by the facts, terminates the contract, puts the parties in status quo ante and restores things, as between them, to the position in which they stood before the contract was entered into.

The court held that the appellant was justified in rescinding the contract and the decree by its letter dated February 11, 1967. The court did not create any right which the parties did not possess when it made a declaration that the contract had been validly rescinded. It is only deciding upon the validity of the rescission already made by the party.

The court observed that the Specific Relief Act, 1963, is not an exhaustive enactment

Subsequent Impact of the Judgement

The court's decision in this case clarified the law regarding the rescission of contracts and decrees. It

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established that when a party to a contract expresses by word or act in an unequivocal manner that by reason of fraud or essential error of a material kind inducing him to enter into the contract he has resolved to rescind it, and refuses to be bound by it, the expression of his election, if justified by the facts, terminates the contract, puts the parties in status quo ante and restores things, as between them, to the position in which they stood before the contract was entered into. This has had a significant impact on subsequent cases dealing with similar issues.

The court's decision also clarified the law regarding the execution of decrees for specific performance. It held that a decree for specific performance is a decree in favor of both the plaintiff and defendant in the suit, but it could be executed only in the manner prescribed by Order 21, Rule 32, C.P.C. The appellant could not have executed the decree against the respondent as a money decree and realized the purchase money from him. Therefore, if the respondent refused to pay the purchase money there was nothing which prevented the appellant from applying for rescission of the decree. This has had a significant impact on subsequent cases dealing with the execution of decrees for specific performance.

The court's decision also clarified the law regarding the court's control over the matter even after passing a decree for specific performance. It held that the court retains control over the matter even after passing a decree for specific performance and that virtually, the decree is in the nature of a preliminary one. This has had a significant

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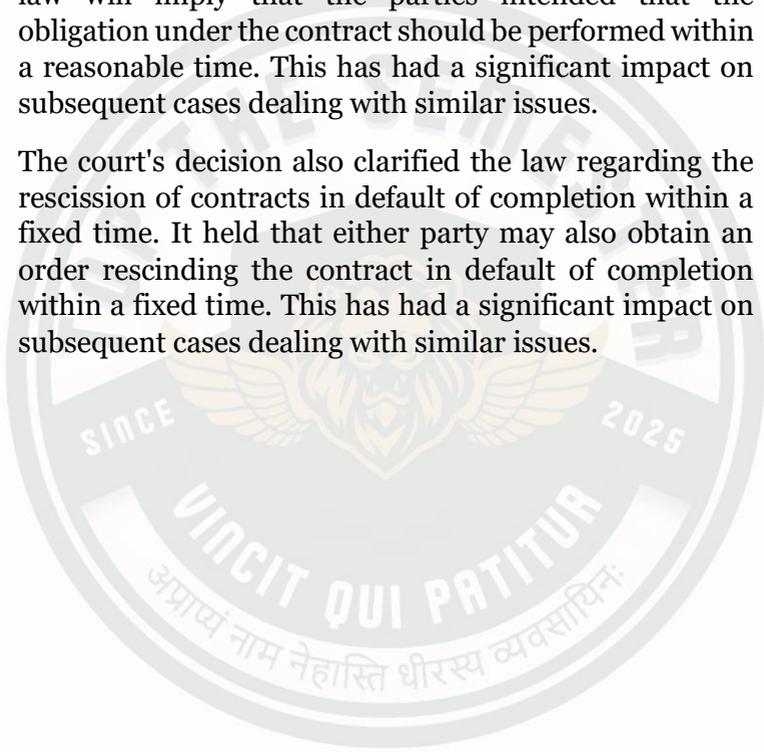
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impact on subsequent cases dealing with similar issues.

The court's decision also clarified the law regarding the time for performance of contracts. It held that if a contract does not specify the time for performance, the law will imply that the parties intended that the obligation under the contract should be performed within a reasonable time. This has had a significant impact on subsequent cases dealing with similar issues.

The court's decision also clarified the law regarding the rescission of contracts in default of completion within a fixed time. It held that either party may also obtain an order rescinding the contract in default of completion within a fixed time. This has had a significant impact on subsequent cases dealing with similar issues.



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5.

STATE OF WEST BENGAL V. B K MONDAL & SONS.

AIR 1962 SC 779

Facts in Brief:

The State of West Bengal was sued by M/S. B. K. Mondal and Sons for non-payment of compensation for non-gratuitous work. The work was done by the respondent (M/S. B. K. Mondal and Sons) in fact in pursuance of the requests invalidly made by the relevant officers of the State of West Bengal. The respondent constructed a warehouse for the State of West Bengal, which was accepted and used by the State. However, there was no valid contract between the parties as the contract was not made in compliance with the provisions of section 175(3) of the Government of India Act, 1935. The respondent, therefore, claimed compensation under section 70 of the Indian Contract Act, 1872, which provides for compensation to be paid in a case where goods are delivered or work is done, and the person for whom the work is done or to whom the goods are delivered voluntarily accepts the goods or enjoys the work done.

Issues:

The main issue in this case was whether the three requisites of Section 70 of the Contract Act had been

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satisfied. The three conditions that must be satisfied for Section 70 to be invoked are:

1. A person should lawfully do something for another person or deliver something to him.
2. In doing the said thing or delivering the said thing, he must not intend to act gratuitously.
3. The other person for whom something is done or to whom something is delivered must enjoy the benefit thereof.

The Government had taken benefit of the work, and it was clear that the respondent did not intend to do the work gratuitously. The work was done lawfully. However, the question was whether the work done under a contract invalid under Section 175(3) of the Government of India Act would be unlawful because of evasion of it. That section does not say that work done without any contract at all, as in this case, would be work unlawfully done nor does it make it unlawful for the Government to take benefit of work done for it without any contract at all.

Section 175(3) of the Government of India Act applies to a consensual contract which the Government makes and not to something which is also called a contract but which the law brings into existence by a fiction irrespective of the consent of the parties. Section 70 of the Contract Act applies where its requisites exist, if it is necessary to imply a contract or contemplate a quasi-contract for applying the section that must be done and neither Section 175(3)

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of the Government of India Act nor any other impediment can stand in the way.

Arguments:

The arguments in this case revolved around the interpretation and application of Section 70 of the Indian Contract Act, 1872, and Section 175(3) of the Government of India Act, 1935.

The respondent argued that they had done the work for the State of West Bengal, not intending to do so gratuitously, and the State had enjoyed the benefit of the work. Therefore, under Section 70 of the Contract Act, the State was bound to make compensation to the respondent.

On the other hand, the State of West Bengal argued that there was no valid contract between the parties as the contract was not made in compliance with the provisions of Section 175(3) of the Government of India Act, 1935. Therefore, the State was not liable to pay compensation to the respondent.

The respondent countered this argument by stating that Section 175(3) of the Government of India Act applies to a consensual contract which the Government makes and not to something which is also called a contract but which the law brings into existence by a fiction irrespective of

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the consent of the parties. Section 70 of the Contract Act applies where its requisites exist, if it is necessary to imply a contract or contemplate a quasi-contract for applying the section that must be done and neither Section 175(3) of the Government of India Act nor any other impediment can stand in the way.

Held:

The Supreme Court held that Section 70 of the Contract Act applies to this case and the decree of the High Court should be confirmed. The Court rejected the argument that there could be no implied contract or quasi-contract with the Government because a contract could be made with it only in accordance with Section 175(3) of the Government of India Act.

The Court clarified that a contract implied in law or a quasi-contract is not a real contract or, as it is called, a consensual contract and Section 175(3) is concerned only with such contracts. The section applies to consensual contracts which the Government makes and not to something which is also called a contract but which the law brings into existence by a fiction irrespective of the parties having agreed to it.

Now, by its terms, Section 70 of the Contract Act must be applied where its requisites exist, if it is necessary to imply a contract or to contemplate the existence of a quasi-contract for applying the section that must be done

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and the Court did not think that Section 175(3) of the Government of India Act prevents that, nor are they aware of any other impediment in this regard.

Legal principles with relevant sections

The legal principles and relevant sections discussed in this case are:

1. Section 70 of the Indian Contract Act, 1872: This section deals with obligations of a person who enjoys the benefit of a non-gratuitous act. According to this section, if a person lawfully does something for another person or delivers something to him, not intending to do so gratuitously, and such other person enjoys the benefit thereof, the latter is bound to make compensation to the former in respect of, or to restore, the thing so done or delivered.
2. Section 175(3) of the Government of India Act, 1935: This section provides for the manner in which contracts are to be made by the Government. It states that all contracts made in the exercise of the executive authority of the Province shall be expressed to be made by the Governor of the Province, and all such contracts and all assurances of property made in the exercise of that authority shall be executed on behalf of the Governor by such persons and in such manner as he may direct or authorize.

The Court held that Section 70 of the Contract Act applies

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to this case and the decree of the High Court should be confirmed. The Court clarified that a contract implied in law or a quasi-contract is not a real contract or, as it is called, a consensual contract and Section 175(3) is concerned only with such contracts.

Obiter dictum

The obiter dictum in this case can be found in the following excerpts:

1. "The position then is that the respondent had done the work for the Government without any contract with anybody. The question is, are the three requisites of s. 70, as very correctly formulated by G. K. Mitter, J., satisfied ? We think they are. There is no dispute that Government had taken the benefit of the work. We also feel no doubt that the respondent did not intend to do the work gratuitously. It submitted its estimate for the work and was very prompt in submitting its bill after the work was done. It had earlier in similar circumstances without proper contract with the Government done work for it at the request of its officers and received payment from the Government. It was a firm of contractors whose trade it was to carry out works of construction for payment and the Government was aware of this. There is no reason to think that in the present case it did the work gratuitously. On its part the Government never thought that the work had been done gratuitously for

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it raised objections to the bill submitted by the respondent on grounds of bad quality of the work and that it had been done without proper sanction. The Government urgently needed the work and no sooner was it completed, it promptly put it to its use. It was plainly fully aware that the work was done for it by a party whose trade was to work for remuneration and who had previously done similar work and had been paid for it by the Government."

2. "It was contended that the obligation under s. 70 of the Contract Act arises only in circumstances in which English law would have created an obligation on the basis of an implied contract or a quasi-contract. We do not think that is so. The section itself lays down when the obligation arises and that is when its three requisites are satisfied. It is not concerned with the question as to when an obligation would have arisen under the English law. It is true that the section has been enacted to provide for one of the classes of cases in which under the English law a quasi-contract is said to arise. But it does not follow from that that the section must be read in the light of the English decisions dealing with cases of quasi-contracts. The section is express on the point and it must be interpreted as it stands."

Important para from judgement

1. "The position then is that the respondent had done

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the work for the Government without any contract with anybody. The question is, are the three requisites of s. 70, as very correctly formulated by G. K. Mitter, J., satisfied ? We think they are. There is no dispute that Government had taken the benefit of the work. We also feel no doubt that the respondent did not intend to do the work gratuitously. It submitted its estimate for the work and was very prompt in submitting its bill after the work was done. It had earlier in similar circumstances without proper contract with the Government done work for it at the request of its officers and received payment from the Government. It was a firm of contractors whose trade it was to carry out works of construction for payment and the Government was aware of this. There is no reason to think that in the present case it did the work gratuitously. On its part the Government never thought that the work had been done gratuitously for it raised objections to the bill submitted by the respondent on grounds of bad quality of the work and that it had been done without proper sanction. The Government urgently needed the work and no sooner was it completed, it promptly put it to its use. It was plainly fully aware that the work was done for it by a party whose trade was to work for remuneration and who had previously done similar work and had been paid for it by the Government."

2. "It was contended that the obligation under s. 70 of the Contract Act arises only in circumstances in which English law would have created an obligation on the

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basis of an implied contract or a quasi-contract. We do not think that is so. The section itself lays down when the obligation arises and that is when its three requisites are satisfied. It is not concerned with the question as to when an obligation would have arisen under the English law. It is true that the section has been enacted to provide for one of the classes of cases in which under the English law a quasi-contract is said to arise. But it does not follow from that that the section must be read in the light of the English decisions dealing with cases of quasi-contracts. The section is express on the point and it must be interpreted as it stands."

3. "Section 70 reads thus: "Where a person lawfully does anything for another person, or delivers anything to him, not intending to do so gratuitously, and such other person enjoys the benefit thereof, the latter is bound to make compensation to the former in respect of, or to restore, the thing so done or delivered."

Subsequent Impact of the judgement

The subsequent impact of this case is significant in the interpretation and application of Section 70 of the Indian Contract Act, 1872. The judgement clarified the conditions under which this section can be invoked and how it operates. It emphasized that the person said to be made liable under Section 70 always has the option not to accept the thing or to return it. It is only where he voluntarily accepts the thing or enjoys the work done that the liability under Section 70 arises. This case has thus set

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a precedent for future cases involving similar circumstances.

The judgement also discussed the distinction between cases where the requirement of a seal was the result of the common law rule as to contracts by corporations and those where the said requirement was based on a statutory provision. It clarified that the non-observance of the statutory provision requiring that a contract of the specified type should be in writing and sealed with the common seal of the authority in question renders the contract void and as such exempts the corporation from any liability to pay compensation for the performance of the contract even where the corporation may have had the full benefit and enjoyment of the said contract.

Furthermore, the judgement highlighted that Section 70 is not intended to entertain claims for compensation made by persons who officiously interfere with the affairs of another or who impose on others services not desired by them. It deals with cases where a person does a thing for another not intending to act gratuitously and the other enjoys it.

In terms of its impact on the Government of a State, the judgement clarified that even if the work done or the goods delivered are the result of a request made by some officer or other on behalf of the said Government, the request may be ineffective or invalid for the reason that the officer making the request was not authorised under Section 175(3) of the Government of India Act, 1935, or, if the said officer was authorised to make the said request

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the request becomes inoperative because it was not followed up by a contract executed in the manner prescribed by Section 175(3). In either case, the thing has been delivered or the work has been done without a contract and that brings in Section 70.



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6.

HADLEY V. BAXENDALE

[1854] EWHC J70

Facts in Brief:

Hadley v. Baxendale arose out of a commercial contract for the **carriage of goods**, and the dispute concerned the **extent of liability for consequential damages arising from breach of contract**.

The plaintiffs, **Hadley and another**, were proprietors of a **flour mill**. The mill's operations depended upon a **crankshaft**, which formed an essential component of the milling machinery. When the crankshaft broke, the mill was rendered **inoperative**, resulting in a complete halt of production.

The plaintiffs engaged the services of the defendants, **Baxendale and others**, who were **common carriers**, to transport the broken crankshaft from the plaintiffs' mill to the manufacturers in Greenwich, where it was to be used as a **model for the manufacture of a new crankshaft**. The defendants were informed that the crankshaft was broken and needed to be delivered to the manufacturers; however, they were **not expressly informed** that the mill would remain shut until the new shaft was delivered, nor that any delay would result in loss of profits.

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Due to the **negligence of the defendants**, the delivery of the crankshaft was delayed beyond the agreed time. As a result, the new crankshaft could not be manufactured in time, and the plaintiffs' mill remained **idle for a longer period**, causing them to suffer **loss of profits**.

The plaintiffs brought an action against the defendants claiming **damages for loss of profits** resulting from the delay. The defendants contended that such losses were **too remote** and could not reasonably have been contemplated by them at the time of contracting.

The matter came before the **Court of Exchequer**, which was required to determine the **scope of recoverable damages for breach of contract**, particularly in relation to **consequential losses**.

Issues:

The principal legal issues before the Court were:

1. **Whether the plaintiffs were entitled to recover damages for loss of profits** caused by the delay in delivery of the crankshaft.
2. **What is the proper test for determining the remoteness of damages in contract**, and which losses can be said to arise naturally from the breach.
3. **Whether special circumstances must be communicated to the defendant at the time of contract** in order to make consequential losses

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recoverable.

4. **Whether the defendants could reasonably be taken to have contemplated the plaintiffs' loss of profits** as a probable result of delay.

Arguments:

Arguments on behalf of the Plaintiffs (Hadley)

- a) The plaintiffs argued that the defendants were aware that the crankshaft was a **critical component of the mill machinery**, and that any delay in its delivery would naturally result in the mill remaining closed. Consequently, the **loss of profits** was a direct and natural consequence of the breach.
- b) They contended that the defendants, as experienced carriers, ought reasonably to have **foreseen** that delay in delivering such an essential machine part would cause operational losses, and therefore the damages claimed were not remote.

Arguments on behalf of the Defendants (Baxendale)

- a) The defendants argued that they had **no knowledge of the special circumstances** that the plaintiffs' mill would remain shut until the crankshaft was returned. They contended that it was not within their

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contemplation that delay would result in loss of profits.

- b) They maintained that damages for loss of profits were **too remote**, as such losses did not arise naturally in the usual course of things, and no special circumstances had been communicated to them at the time of contracting.

Held:

The **Court of Exchequer** held that the plaintiffs were **not entitled to recover damages for loss of profits**, as such loss was **too remote** and did not arise naturally in the usual course of things from the breach of contract.

The Court ruled that the defendants could not reasonably be taken to have **contemplated the loss of profits** as a probable consequence of delay at the time the contract was made. Although the defendants were aware that the crankshaft was broken and required repair, they were **not informed of the special circumstance** that the mill would remain shut until the new shaft was delivered.

Accordingly, the defendants were held liable only for such damages as **may fairly and reasonably be considered either arising naturally from the breach**, or such as **may reasonably be supposed to have been in the contemplation of both parties** at the time of contracting. Since the loss of profits did not satisfy either category in the present case, it was held to

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be **irrecoverable**.

Legal Principles with Relevant Sections

The judgment in *Hadley v. Baxendale* laid down the **foundational rule governing remoteness of damages in contract law**, which continues to influence common law and statutory formulations worldwide.

Rule of Remoteness of Damages

The Court formulated the now-classic **two-limb test** for determining recoverable damages for breach of contract:

1. **First Limb (Ordinary Damages):**
Damages which **arise naturally**, i.e., according to the usual course of things, from the breach of contract itself.
2. **Second Limb (Special Damages):**
Damages which may reasonably be supposed to have been **in the contemplation of both parties** at the time they made the contract, as the probable result of the breach, owing to **special circumstances communicated** to the defendant.

Only losses falling within either of these limbs are recoverable.

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Incorporation into Indian Contract Law – Section 73

- c) The principles of *Hadley v. Baxendale* are statutorily incorporated into **Section 73 of the Indian Contract Act, 1872**, which provides:
- d) “When a contract has been broken, the party who suffers by such breach is entitled to receive 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.”
- e) Indian courts have consistently applied the **Hadley rule** in cases such as:
- *Kouser Husain Khan v. Kothari*
 - *ONGC v. Saw Pipes Ltd.* (with certain expansions)

Obiter Dictum

The Court made important **obiter observations** underscoring the rationale behind limiting contractual damages.

The Court observed that allowing recovery for every

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conceivable loss would make parties **liable for consequences they never intended to assume**, thereby discouraging commercial certainty. This observation reinforces the idea that **contractual liability is based on assumed risk**, not moral blameworthiness.

The Court further remarked that parties are free to **expand or restrict liability by express terms**, highlighting the importance of communication and express stipulation in commercial contracts.

Important Para from Judgement

The most frequently cited passage from the judgment, delivered by **Alderson B.**, is:

“Where two parties have made a contract which one of them has broken, the damages which the other party ought to receive... should be such as may fairly and reasonably be considered either arising naturally, i.e., according to the usual course of things, from such breach of contract itself, or such as may reasonably be supposed to have been in the contemplation of both parties, at the time they made the contract, as the probable result of the breach of it.”

This passage constitutes the **core doctrinal statement** of the law on remoteness of damages.

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Subsequent Impact of the Judgement

Influence on Indian Jurisprudence

Indian courts routinely apply the *Hadley* test under **Section 73**, including in landmark cases such as:

- *ONGC v. Saw Pipes Ltd.*
- *Fateh Chand v. Balkishan Das*

Foundational Authority on Damages

The case is universally recognised as the **cornerstone of the law of contractual damages**, governing the doctrine of remoteness in common law jurisdictions.

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7.

BANK OF BIHAR LTD. V. DAMODAR PRASAD

AIR 1969 SC 297

Facts in brief:

The plaintiff, Bank of Bihar Ltd., lent money to the first respondent, Damodar Prasad, on the guarantee of the second respondent, Paras Nath Sinha. Despite demands, neither the principal debtor nor the guarantor paid the dues. The plaintiff filed a suit against them in the Court of the Subordinate Judge, 1st Court, Patna, claiming a decree for the amount due. The Trial Court decreed the suit against both the defendants. However, the Trial Court directed that the plaintiff bank shall be at liberty to enforce its dues in question against defendant No. 2 only after having exhausted its remedies against defendant No. 1. The plaintiff filed an appeal challenging the legality and propriety of this direction. The High Court dismissed the appeal. The plaintiff has filed the present appeal after obtaining a certificate.

Issues:

The main issue in the case was the direction given by the Trial Court that the plaintiff bank shall be at liberty to enforce its dues in question against defendant No. 2 only after having exhausted its remedies against defendant

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No. 1. The plaintiff challenged this direction.

Arguments:

The plaintiff argued that the direction given by the Trial Court was unjustified. The plaintiff contended that the surety has no right to restrain execution against him until the creditor has exhausted his remedies against the principal. The plaintiff also argued that the solvency of the principal is not a sufficient ground for restraining execution of the decree against the surety.

Held:

The Supreme Court held that the direction given by the Trial Court must be set aside. The Court stated that in the absence of some special equity, the surety has no right to restrain execution against him until the creditor has exhausted his remedies against the principal. The Court also held that the solvency of the principal is not a sufficient ground for restraining execution of the decree against the surety. The Court stated that it is the duty of the surety to pay the decretal amount. On such payment, he will be subrogated to the rights of the creditor under sec. 140 of the Indian Contract Act and he may then recover the amount from the principal. The Court concluded that the appeal is allowed, the direction of the court below that the "plaintiff-bank shall be at liberty to enforce its dues in question against defendant No. 2 only

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after having exhausted its remedies against defendant No. 1" is set aside. The respondent Dr. Paras Nath Sinha shall pay to the appellant costs in this Court and in the High Court.

Legal principles with relevant sections

The case revolves around the principles of surety and guarantee as per the Indian Contract Act. The relevant sections include:

- Section 128: The liability of the surety is co-extensive with that of the principal debtor unless it is otherwise provided by the contract.
- Section 140: On payment of the debt or performance of all that he is liable for, the surety has the right to benefit from the securities which the creditor has against the principal debtor.

Obiter dictum

The obiter dictum in this case is the court's observation that a surety has no right to restrain execution against him until the creditor has exhausted his remedies against the principal. The court also noted that the very object of the guarantee is defeated if the creditor is asked to postpone his remedies against the surety.

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Important para from judgement

An important paragraph from the judgement is: "It is the duty of the surety to pay the decretal amount. On such payment he will be subrogated to the rights of the creditor under s. 140 of the Indian Contract Act. and he may then recover the amount from the principal. The very object of the guarantee is defeated if the creditor is asked to postpone his remedies against the surety. In the present case the creditor is a banking company. A guarantee is a collateral security usually taken by a banker. The security will become useless if his rights against the surety can be so easily cut down."

Subsequent Impact of the judgement

The case set a precedent in the interpretation of the rights and obligations of a surety under the Indian Contract Act. It clarified that a surety cannot dictate terms to the creditor and ask him to pursue his remedies against the principal in the first instance. This has implications for banking and financial institutions, as guarantees are a common form of security in these sectors. The judgement reinforced the principle that a guarantee will become useless if the rights of the creditor against the surety can be easily cut down.

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8.

STATE BANK OF SAURASHTRA V. CHITRANJANRANGNATH RAJA

AIR 1980 SCR (3) 915

Facts in brief:

The State Bank of Saurashtra filed a suit for recovery of Rs. 76,368.04 P. from the legal representative of the deceased principal debtor Harilal Parmananddas Adatia and his surety, Chitranjan Rangnath Raja. The principal debtor had approached the bank seeking a cash credit facility of up to Rs. 75,000/-, offering to give security for the cash credit by pledge of groundnut oil tins and a personal guarantee of Chitranjan Rangnath Raja. After the principal debtor's death, the bank called upon the surety to pay the outstanding balance in the cash credit account of the principal debtor

Issues:

The main issue was whether the surety would be discharged from his obligation under the letter of guarantee if it was proven that the security of pledged goods was lost due to the negligence of the creditor Bank. The surety claimed relief of discharge under section 141 of the Indian Contract Act, which states that if the creditor loses or parts with the security without the consent of the surety, the surety is discharged to the

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extent of the value of the security.

Arguments:

The surety argued that clauses 5, 7, and 13 of the letter of guarantee, Ext. 31, would still hold him liable even if the creditor Bank was found to be negligent in losing the security of pledged goods. The Bank argued that the contract of guarantee entered into by the surety was independent of the pledge of goods given by the principal debtor, so the surety is not discharged from his liability under the guarantee.

Held

The court held that the surety is entitled to restitution. The court found that the Bank was negligent in its handling of the pledged goods, which resulted in the loss of the security. As such, the surety was discharged from his obligation under the letter of guarantee. The court also held that the surety and the pledge of goods were not two independent transactions but part of one composite transaction. Therefore, the surety was wholly discharged due to the loss of the entire security. The appeal was dismissed.

Legal principles with relevant sections

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The case primarily revolves around the interpretation of Section 141 of the Indian Contract Act, which states:

"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."

The court interpreted this section in the context of the case, where the creditor (the bank) had taken two securities from the principal debtor - the pledge of goods and the personal guarantee of the surety. The court held that the surety was discharged from his obligations because the bank, due to its negligence, lost the pledged goods which were one of the securities.

Obiter dictum

The court, in its obiter dictum, made observations about the responsibilities of a creditor and the rights of a surety. It emphasized that a surety is usually described as a preferred debtor and that a court should not enable a creditor to act negligently and yet not be accountable. The court also questioned whether the guarantee was a guarantee against proper performance of the contract or a guarantee covering the bank's utter disregard of its responsibility.

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Important paras from the judgement

An important paragraph from the judgement is:

"First security, namely, the pledged goods are lost to the Bank and the concurrent finding again incontrovertible is that the pledged goods were lost on account of the negligence of the creditor Bank. Whole of the security was lost and, therefore the surety would be discharged in entirety because it is crystal clear that the principal debtor had agreed and had in fact pledged 5,000 tins of oil which even if sold at the then current market price would have satisfied the Bank's entire claim. Accordingly, the surety would be discharged in entirety."

Subsequent Impact of the Judgement

The judgement in this case has had a significant impact on the interpretation of the rights and obligations of sureties and creditors under the Indian Contract Act. It has clarified that a surety can be discharged from his obligations if the creditor, due to its negligence, loses a security that was provided by the principal debtor at the time of entering into the contract of suretyship. This has implications for the banking sector and other sectors where guarantees and sureties are commonly used. It emphasizes the importance of creditors acting responsibly and diligently in managing the securities they hold.

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9.

KALIAPERUMAL PILLAI V. VISALALAKSHMI

AIR 1938 MAD 32

Facts in Brief:

The plaintiff entrusted certain **old gold jewels** to the defendant for the purpose of melting and converting them into **new ornaments** through goldsmiths who worked in the defendant's house, allegedly due to better accommodation available there. After the gold was melted, the **melted gold was returned to the plaintiff**, who thereafter **personally supervised the work on a daily basis**.

At the end of each working day, the **half-finished ornaments were handed back to the plaintiff**, who placed them in a **box provided by the defendant**, kept inside a room in the defendant's house. The **key of the room remained with the plaintiff** at all times. One morning, when the plaintiff opened the room to resume work, the ornaments were found **missing**.

The plaintiff sued the defendant, alleging that he was a **bailee** of the gold and was therefore **liable for the loss**. The lower court accepted this contention and decreed in favour of the plaintiff. The defendant challenged the decision before the Madras High Court, contending that **no bailment existed** at the time of loss as there had been **no delivery or possession** of the goods with him.

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Issues:

The principal legal issues before the Madras High Court were:

1. **Whether the defendant could be legally regarded as a “bailee” under Sections 148 and 149 of the Indian Contract Act, 1872**, in respect of the gold or the half-finished ornaments that were lost.
2. **Whether mere storage of goods in the defendant’s house, without transfer of possession, constitutes “delivery” sufficient to create bailment.**
3. **Whether an initial bailment, once completed, can be presumed to continue in respect of subsequent dealings involving the same goods**, in the absence of fresh delivery.
4. **Whether the burden of proof regarding loss could be shifted to the defendant**, assuming bailment was established.

Arguments:

Arguments on behalf of the Plaintiff (Respondent)

- It was contended that the defendant initially

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received the plaintiff's jewels for melting, thereby creating a **bailment relationship**.

- The plaintiff argued that this bailment **continued throughout the process** of making the new ornaments.
- Since the ornaments were kept in a room within the defendant's house, it was argued that the defendant had **constructive possession**.
- On this basis, the plaintiff asserted that the defendant, as bailee, was **liable to account for the loss** under the law of bailment.
- The plaintiff further relied on the presumption under bailment law that **loss of goods in the bailee's custody casts the burden of explanation on the bailee**.

Arguments on behalf of the Defendant (Petitioner)

- The defendant argued that any bailment that existed **came to an end** once the melted gold was returned to the plaintiff.
- It was emphasised that thereafter the plaintiff retained **exclusive possession and control**, including daily supervision and custody of the ornaments.
- The defendant denied any **subsequent delivery** of the ornaments to him, actual or constructive.

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- Mere permission to keep the box in a room of the defendant's house, **with the key retained by the plaintiff**, could not amount to delivery under Section 149.
- In the absence of bailment, the defendant argued that **no statutory liability could be fastened upon him**.

Held:

The Madras High Court **allowed the revision petition**, set aside the decree of the lower court, and held that:

- **No bailment existed at the time of loss**, as there was **no delivery or possession of the goods with the defendant**.
- The defendant **could not be treated as a bailee** and therefore could not be held liable for the loss of the ornaments.
- In the absence of bailment, the burden of proof **could not be shifted onto the defendant**.

Legal principles with relevant sections:

The Court's reasoning was primarily grounded in **Sections 148 and 149 of the Indian Contract Act, 1872**.

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Section 148 – Bailment

- Bailment requires **delivery of goods** by one person to another for some purpose, upon a contract that the goods shall be returned or disposed of when the purpose is accomplished.

Section 149 – Delivery

- Delivery may be:
 - **Actual**
 - **Constructive**
 - **Symbolic**
- However, delivery must result in **transfer of possession**, not mere physical proximity.

The Court held that:

- Possession implies **control and dominion**, not mere location.
- Since the plaintiff:
 - Took back the gold daily,
 - Retained the key of the room,
 - Exercised exclusive control,

no delivery within the meaning of Section 149 was established.

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Obiter dictum:

Though unnecessary for the decision, the Court observed that:

- There was **no evidence whatsoever** to support the lower court's speculation that the defendant might have appropriated the jewels.
- Courts must avoid **conjecture or moral suspicion** in civil liability, particularly where statutory relationships like bailment are invoked.
- Sympathy for a party **cannot substitute legal proof**.

Important para from judgement:

“The mere leaving of the box in a room in the defendant's house, when the plaintiff herself took away the key of that room, cannot certainly amount to delivery within the meaning of Section 149.”

“If the plaintiff wanted to fasten a liability upon the defendant for the loss of the goods, she must make out an affirmative ground of liability and cannot ask the Court to treat the defendant as a bailee.”

“Every day when the unfinished jewels were handed back by the goldsmith to the plaintiff, the jewels came back to her possession.”

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Subsequent Impact of the judgement:

- a) The case is a leading authority on the concept of delivery and possession in bailment under Indian law.
- b) It clearly distinguishes between:
 - **Custody vs. possession**
 - **Physical location vs. legal control**
- c) The judgment prevents **automatic extension of bailment** beyond its actual duration.
- d) It is frequently cited to:
 - Deny bailment where **keys and control remain with the owner**
 - Emphasise **strict proof of delivery** under Sections 148–149.

The case reinforces that **burden of proof in bailment arises only after bailment is conclusively established.**

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10.

BOLTON V. LAMBERT

(1889) 41 CH. D. 295

Facts in Brief

Bolton v. Lambert arose out of a dispute concerning the **doctrine of ratification in agency law** and its retrospective effect on contractual relations. The plaintiff, Bolton, was the owner of a sugar refinery. A company known as the **Britannia Distillery Company Ltd.** entered into negotiations with him for the purchase of the refinery.

The negotiations were conducted by **Bolton's agent**, who **purported to accept an offer** made by the defendant, Lambert, for the purchase of the refinery. However, at the time of acceptance, the agent **lacked actual authority** from Bolton to conclude the contract.

Before Bolton formally ratified the agent's unauthorised acceptance, **Lambert withdrew his offer**, contending that no binding contract had come into existence. Subsequently, Bolton **ratified the agent's act**, asserting that the ratification related back to the date of acceptance and thus created a binding contract.

Lambert refused to complete the transaction, arguing that his withdrawal of the offer prior to ratification rendered the acceptance ineffective. Bolton sued for

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specific performance, giving rise to the central legal question regarding the **effect and timing of ratification**.

Issues:

The Court of Appeal was required to determine the following issues:

1. **Whether an unauthorised act of an agent can be ratified by the principal after the third party has withdrawn from the transaction.**
2. **Whether ratification operates retrospectively**, so as to relate back to the date of the agent's unauthorised act.
3. **Whether the withdrawal of the offer by the third party prior to ratification prevents the formation of a binding contract.**
4. **Whether the doctrine of ratification can prejudice the rights of a third party who acted in the interim period.**

Arguments:

Arguments on behalf of the Plaintiff (Bolton)

- The plaintiff contended that the agent had

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accepted the defendant's offer, albeit without authority.

- Under the law of agency, the principal is entitled to **ratify an unauthorised act** performed on his behalf.
- Such ratification, once made, **relates back to the date of the act**, thereby validating it from inception.
- Consequently, the defendant's withdrawal of the offer after acceptance but before ratification was **legally irrelevant**.
- The plaintiff argued that a **binding contract came into existence** upon ratification, entitling him to specific performance.

Arguments on behalf of the Defendant (Lambert)

- The defendant argued that **no valid acceptance existed** at the time of withdrawal because the agent lacked authority.
- Since the offer was withdrawn **before ratification**, there was no subsisting offer capable of being accepted.
- The defendant contended that ratification **cannot impose contractual obligations retrospectively** so as to prejudice the third party.

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- Allowing ratification in such circumstances would subject third parties to **unfair uncertainty**.

Held:

The Court of Appeal **decided in favour of the plaintiff** and held that:

- The principal was entitled to **ratify the unauthorised acceptance** by his agent.
- **Ratification operates retrospectively**, relating back to the date on which the agent purported to act.
- The defendant's withdrawal of the offer **after acceptance but before ratification did not prevent the formation of a binding contract**.
- Accordingly, a valid contract existed, and the defendant was bound by it.

Legal principles with relevant sections:

Doctrine of Ratification

- a) Ratification is the **subsequent adoption by the principal of an act done on his behalf without authority**. Once ratified, the act is treated as if it had been authorised from the beginning.
- b) The Court reaffirmed the classic principle:

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- c) “*Omnis rati habitio retrotrahitur et mandato aequiparatur*”
(Every ratification relates back and is equivalent to a prior authority)

Retrospective Effect

- Ratification **dates back to the time of the agent's act**, not the time of ratification.
- The legal consequence is that the contract is deemed to have been **validly concluded at the time of acceptance**.

Relevance under Indian Law

- d) Though an English case, the principle directly aligns with **Sections 196–197 of the Indian Contract Act, 1872**:
- **Section 196**: A principal may ratify unauthorised acts done on his behalf.
 - **Section 197**: Ratification may be express or implied.
- e) This case is often cited in India to explain the **retroactive operation of ratification**.

Obiter dictum:

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The Court observed that:

- While ratification generally binds third parties, it **cannot be permitted where it would cause injustice** in exceptional cases.
- However, mere withdrawal of an offer **after unauthorised acceptance does not constitute such injustice.**
- Commercial inconvenience alone **cannot defeat settled principles of agency law.**

These observations underline the **limits of equitable intervention** in the doctrine of ratification.

Important para from judgement:

“The ratification has a retrospective effect and is equivalent to an authority given beforehand.”

“The defendant cannot withdraw his offer after it has been accepted, even though the acceptance was originally unauthorised, if it is subsequently ratified.”

“The acceptance was in fact complete when made, subject only to ratification.”

Subsequent Impact of the judgement:

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- a) The case is a leading authority on ratification in agency law.
- b) It firmly establishes that **ratification relates back**, even if it disadvantages the third party.
- c) The decision brings **certainty to commercial transactions**, preventing third parties from escaping liability due to internal authority defects.
- d) It is widely cited in:
- Contract law (offer and acceptance)
 - Agency law (authority and ratification)
- e) In Indian legal education, the case is routinely read alongside **Sections 196–200 of the Indian Contract Act**.
- f) The judgment clarifies that **third-party withdrawal is ineffective once acceptance has occurred**, provided valid ratification follows.

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PREVIOUS YEAR QUESTION PAPERS (PYQs) SOLUTIONS

PAPER 1

PART A

QUESTION 1: WRITE SHORT NOTES ON THE FOLLOWING:

QUESTION (A): WRITE SHORT NOTE ON ROLE OF THREE PARTIES IN A CONTRACT OF GUARANTEE

A Contract of Guarantee is a trilateral agreement involving three parties: the Creditor, the Principal Debtor, and the Surety (or Guarantor). It is enshrined under Sections 126 to 147 of the Indian Contract Act, 1872. In this type of agreement, the Surety provides a guarantee to the Creditor on behalf of the Principal Debtor. This agreement requires the mutual consent of all the parties involved.

- **Creditor:** The Creditor is the party to whom the debt or obligation is owed. In the context of a Contract of Guarantee, the Creditor's primary relationship is with

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the Principal Debtor. However, in case the Principal Debtor defaults, the Creditor has the legal right to seek fulfillment of the obligation from the Surety. Landmark case, State of M.P. v. Kaluram clarified the relationship between the Creditor and the Guarantor/Surety in case of the default by the Principal Debtor.

- **Principal Debtor:** The Principal Debtor is the party that owes the debt or obligation to the Creditor. In the event the Principal Debtor defaults, the Surety will be called upon to fulfill the obligation. It is also crucial to note that the Surety has the right of recourse against the Principal Debtor, which means that if the Surety is called upon to pay the debt, he can subsequently claim the same from the Principal Debtor.
- **Surety (or Guarantor):** The Surety, or Guarantor, is the party who guarantees the Creditor that the Principal Debtor will perform his obligation. If the Principal Debtor defaults, the Surety is liable to fulfill the obligation. The role of the Surety was elucidated in the case of Bank of Bihar v. Damodar Prasad, where it was held that the liability of the Surety is co-extensive with that of the Principal Debtor unless it is otherwise provided by the contract.

In sum, the Contract of Guarantee is a risk management mechanism for the Creditor. The Principal Debtor gets an opportunity to perform, and the Surety guarantees that performance. All parties have specific obligations and

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rights within the framework of the law, contributing to the robustness of the contractual agreement.

QUESTION (B): RIGHTS OF OUTGOING PARTNER TO CARRY ON COMPETING BUSINESS

The Indian Partnership Act, 1932, governs the rights and obligations of partners in a partnership firm. An outgoing partner, according to Section 32 of the Act, is one who retires or is expelled from the partnership.

The rights of an outgoing partner to carry on a competing business are defined under Section 36 of the Indian Partnership Act, 1932. Unless the partners have an agreement to the contrary, an outgoing partner may carry on a business competing with that of the firm and can even advertise such business. However, without the consent of the other partners, he cannot:

- Use the firm's name,
- Represent himself as carrying on the business of the firm, or
- Solicit the custom of persons who were dealing with the firm before he ceased to be a partner.

These provisions aim to strike a balance between the outgoing partner's right to carry on a livelihood and the remaining partners' right to protection against unfair

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competition.

The case of *Churton v. Douglas* serves as a classic example of this balance. It was held that an outgoing partner had the right to solicit the customers of the old firm, but this right was subject to the condition that he did not represent himself as carrying on the business of the old firm.

In *Trego v. Hunt*, it was further clarified that an outgoing partner could not make use of the firm's trade secrets, trade connections, or other privileged information obtained during the tenure of the partnership.

In a more recent case, *Khushal Khemgar Shah & Ors. v. Khorshed Banu Dadiba Boatwalla & Anr.*, the Supreme Court of India held that an outgoing partner had a right to start a competing business unless specifically restricted by a non-compete clause in the partnership deed.

Thus, while the law recognizes the rights of an outgoing partner to carry on a competing business, it is not an unfettered right. The restrictions aim to protect the legitimate interests of the remaining partners and maintain fair competition in the business environment.

QUESTION (C): WRITE SHORT NOTE ON SALE BY SAMPLE AND DESCRIPTION

The concept of a "sale by sample and description" as

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provided under the Sale of Goods Act, 1930 in India, provides an interesting intersection of the two unique methods of conducting sales. This concept is mentioned in Section 15 of the Act. Herein, a sale can be said to be by sample and description when the goods are agreed upon based on a representative sample and an associated verbal or written description provided by the seller.

In a sale by sample and description, the buyer's acceptance of the goods is premised on two conditions. The first is that the goods must align with the sample provided, and the second is that the goods should correspond to the description.

The dual requirement of a "sale by sample and description" introduces a layer of reassurance for the buyer. This reassurance is necessary because a sample provides a tangible representation of the goods, while a description can elaborate on attributes that may not be visually identifiable.

However, it's also critical to understand the distinctions and legal implications of both "sale by sample" and "sale by description" individually:

Sale by Sample: In a sale by sample, the seller provides a physical representation of the goods to the buyer. This is governed by Section 17 of the Act. Three key aspects must be observed in a sale by sample:

1. The quality of the bulk of the goods must correspond with the sample.

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2. The buyer should have been given an adequate opportunity to compare the bulk of the goods with the sample.
3. The goods should not have any latent defect, making them unmerchantable, which would not be apparent upon reasonable examination of the sample.

This means the buyer has the right to reject the goods if they do not correspond to the sample provided.

Sale by Description: In a sale by description, goods are sold based on the verbal or written depiction provided by the seller. This kind of sale applies irrespective of whether the goods are specific or unascertained. According to the case of *Ashington Piggeries Ltd v. Christopher Hill Ltd*, for a sale to qualify as a sale by description, the goods must correspond precisely with the description.

In the landmark case of *Varley v. Whipp*, the court examined a situation where a sale was conducted by sample as well as by description. The court held that the bulk of the goods must correspond with both the sample and the description. The presence of a sample does not nullify the need for the goods to meet the description.

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QUESTION (D): WRITE SHORT NOTE ON PARTNER'S AUTHORITY IN EMERGENCY SITUATIONS

The doctrine of a partner's authority in emergency situations is a significant provision in partnership law, allowing for a flexible response to unpredictable circumstances that could jeopardize the firm's interests. This principle is enshrined in Section 21 of the Indian Partnership Act, 1932, which vests in a partner the authority to act in an emergency to prevent a loss to the firm.

This authority is not unrestricted. The Act requires that the actions taken must be such that a person of ordinary prudence would undertake under similar circumstances, in their own case. Therefore, the law expects the partner to exercise this authority responsibly, justifiably, and in the best interests of the firm.

This concept acknowledges the exigencies of business and respects the need for swift action to prevent damage to the firm's interests. It also takes into account that in a partnership, not all partners might be available or capable of immediate decision-making in times of crisis. By vesting emergency powers in any partner, the Act allows for a flexible and practical functioning of partnerships.

In the case of *Hurst v. Bryk*, the court held that the actions of a partner in an emergency that were done to protect the firm from an imminent loss would bind the

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firm. This case reinforced the principle that partners, due to their agency relationship with the firm, have the authority to bind the firm by their actions, provided that their decisions are justifiable under the circumstances and are in the best interest of the firm.

The provision emphasizes both the fiduciary nature of a partner's role and the principle of agency that underlies a partnership. It strengthens the capacity of a partnership to survive and adapt to challenges, enhancing its viability as a business structure. It also sets a standard of reasonable care and prudence that is expected of partners in such circumstances, reinforcing the inherent trust and reliance in a partnership.

QUESTION (E): WRITE SHORT NOTE ON LIABILITY OF MAKER OF NOTE AND ACCEPTOR OF BILL

The Negotiable Instruments Act, 1881, in India provides a legal framework for transactions involving negotiable instruments, which include promissory notes, bills of exchange, and cheques. A core tenet of this Act is the establishment of the liability of various parties to these instruments.

Liability of Maker of a Promissory Note:

In the context of a promissory note, the maker is the person who promises to pay a certain sum of money to another person (the payee) or to his order. As per Section

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32 of the Act, the maker of a promissory note is bound, in the absence of a contract to the contrary, to pay the amount upon due date to the payee or the holder of the note. This is an absolute liability that arises from the moment the maker signs the note.

This is illustrated by the case of Bibhuti Bhusan Das Gupta vs The Official Assignee Of Calcutta And Anr, where it was held that the maker of a note would be liable for payment upon the note's maturity.

Liability of Acceptor of a Bill of Exchange:

A bill of exchange involves three parties - the drawer (who makes the bill), the drawee (to whom it is addressed), and the payee (to whom the payment is to be made). Upon the drawee's signing and thus accepting the bill, he becomes the acceptor. As per Section 30 of the Negotiable Instruments Act, the acceptor of a bill of exchange, by accepting it, engages that he will pay the bill according to its tenor.

He is thus bound to compensate any party to the bill for any loss or damage resulting from his failure to pay the bill upon its maturity. This liability of the acceptor is absolute and unconditional, and it is valid until the bill is fully discharged. The acceptor's liability is emphasized in Surajmal Rameshwar vs Bishamber Nath Banshidhar And Anr, where the court reaffirmed that an acceptor is bound to pay the bill upon its due date unless it is duly discharged.

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It is worth noting that the liability of these parties can be discharged or altered based on certain conditions, such as the cancellation of the instrument, payment, material alteration, or by the process of release and discharge under Sections 82 to 92 of the Negotiable Instruments Act, 1881. However, unless there is a legal reason for the discharge of these liabilities, both the maker of a note and the acceptor of a bill bear significant legal obligations to honor the instruments they have respectively made and accepted.

PART B

Q.2. EXPLAIN THE NATURE & SCOPE OF LIABILITY OF SURETY. WHAT ARE THE MODES OF DISCHARGE OF LIABILITY OF SURETY UNDER CONTRACT OF GUARANTEE?

The Contract of Guarantee is a trilateral agreement involving the principal debtor, the creditor, and the surety (or guarantor). Governed by Sections 126 to 147 of the Indian Contract Act, 1872, this contract involves the surety providing a guarantee to the creditor to fulfill the obligations of the principal debtor in case of his default.

Nature and Scope of Liability of Surety:

The role and liability of a surety are defined in Section 128 of the Indian Contract Act, which states, "The liability of

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the surety is co-extensive with that of the principal debtor unless it is otherwise provided by the contract." This essentially means that the surety is liable to the same extent as the principal debtor and this liability is immediate and can be enforced without exhausting remedies against the principal debtor first, a principle clarified in the landmark case of *Bank of Bihar v. Damodar Prasad*.

The surety's liability is secondary and contingent upon the default of the principal debtor. The surety steps into the shoes of the creditor upon paying off the debt, thereby acquiring the rights, remedies, and securities that the creditor held against the principal debtor. This concept, known as the 'doctrine of subrogation', is enshrined in Section 140 of the Act. The case of *State of M.P. v. Kaluram* affirms the right of subrogation of a surety.

Furthermore, the liability of the surety is not affected by the death of the principal debtor, as per Section 128. It can only be discharged upon fulfillment of the debt or through other specific modes discussed below.

Modes of Discharge of Liability of Surety:

Several modes for the discharge of the surety's liability are specified under the Indian Contract Act, 1872. They are as follows:

1. **By Notice of Revocation:** As per Section 130, a continuing guarantee can be revoked by the surety, at any point, for future transactions by giving a notice to

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the creditor. This doesn't affect the liability for any transactions already occurred.

2. **By Death of Surety:** In the case of a continuing guarantee, the death of the surety, unless there is a contract to the contrary, discharges him from liability as regards future transactions, as per Section 131.
3. **By Variance in Terms of Contract:** Any alteration in the terms of the contract between the principal debtor and the creditor, without the consent of the surety, discharges the surety as to transactions after the alteration, as per Section 133. The landmark case of *Lakshmi Vilas Bank v. M/s S.Ve. Alagappachettiar & Sons* reiterated this principle.
4. **By Release or Discharge of Principal Debtor:** As per Section 134, the surety is discharged if the creditor releases the principal debtor or compounds with him or promises to give him time, or not to sue him, without surety's consent.
5. **By Creditor's Act or Omission impairing surety's eventual remedy:** Any act or omission of the creditor which results in the surety's loss of a remedy or right, discharges the surety, as per Section 139.
6. **By Impairment of Security:** As per Section 141, if the creditor, without the consent of the surety, parts with or loses a security, the surety is discharged to the extent of the value of the security.

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These principles make clear that while a surety's liability is co-extensive with that of the principal debtor, there are several provisions within the Indian Contract Act, 1872, which provide for the discharge of the surety's liability. These provisions exist to protect the surety from undue or unanticipated liability and to ensure that the creditor does not act in a way that could prejudice the surety's interests.

Q.3. EXPLAIN THE CONCEPT OF GENERAL & PARTICULAR LIEN UNDER THE CONTRACT OF BAILMENT, WITH THE HELP OF DECIDED CASES ON THE SUBJECT.

A contract of bailment is a type of contractual relationship governed under Sections 148 to 181 of the Indian Contract Act, 1872. In this contract, one party (the bailor) delivers goods to another party (the bailee) for a specific purpose, with the understanding that the goods will be returned or otherwise disposed of according to the bailor's directions once the purpose has been fulfilled.

One of the important rights provided to the bailee under this contract is the 'right of lien'. Lien, derived from the Latin term 'ligamen', meaning a bond, refers to the right of one person to retain possession of another's goods until a claim is satisfied. There are two types of lien recognized under the Indian Contract Act: general lien and particular lien, outlined in Sections 171 and 170 respectively.

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1. Particular Lien (Section 170):

A particular lien is the right of the bailee to retain possession of the goods bailed until he receives due compensation for the services he has rendered in respect of those specific goods. This is a limited right because it only applies to the particular goods for which the services were rendered. The bailee can't retain any other goods of the bailor against any other dues.

The case of *Pandurang v. Maruti* (AIR 1966 SC 153) demonstrates the concept of particular lien. In this case, a goldsmith who was given gold to make an ornament but was not paid for his services, was allowed to retain the ornament until he was paid.

2. General Lien (Section 171):

General lien, on the other hand, is a broader right. It allows a bailee, subject to any contract to the contrary, to retain any goods of the bailor as security not only for the charges and expenses incurred for those specific goods, but also for any balance of general account that may be due from the bailor. However, this right is only granted to certain specific professions mentioned in Section 171, namely bankers, factors, wharfingers, attorneys of a High Court, and policy brokers.

The principle of general lien was discussed in the case of *Jagannath Ganeshram Agarwala v. Shivnarayan Bhagirath* (AIR 1949 Nag 362). In this case, an attorney exercised his right of general lien for the recovery of his

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professional charges by retaining all documents of his client until his dues were cleared.

These lien rights serve as self-help remedies for the bailee to ensure that he is compensated for his services or care provided in respect to the goods. However, it's crucial to note that the right of lien is only a right to retain possession of the goods as a security and does not include the right to sell. Also, it can only be exercised while the bailee is in possession of the goods, and the moment he voluntarily parts with the possession, the right is lost, as decided in *Bank of India v. Grains & Gunny Agencies* (AIR 1971 SC 2310).

In summary, a lien is an important right given to a bailee under a contract of bailment to protect his interests and ensure due compensation for his services. While a particular lien provides security for services rendered in respect to specific goods, a general lien provides broader protection and can be used to settle any general balance due from the bailor.

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Q.4. EXPLAIN THE CONCEPT OF HOLDING OUT IN PARTNERSHIP FIRM? SUBSTANTIATE YOUR ANSWER BY CITING DECIDED CASES ON THE POINT.

The concept of 'holding out', also known as the doctrine of estoppel in the context of a partnership firm, is enshrined in Section 28 of the Indian Partnership Act, 1932. According to this section, anyone who by words spoken or written, or by conduct, represents or knowingly allows himself to be represented as a partner in a firm, is liable to any person who has on the faith of any such representation given credit to the firm.

In essence, the doctrine of holding out aims to protect the interests of a person who, based on a representation, has extended credit or entered into a contract with a firm, assuming that the person making the representation is a partner.

Holding Out Through Representation:

This representation could be made explicitly, as in the case of a person openly stating that they are a partner or silently, such as when a person fails to correct a situation where he knows he is being falsely perceived as a partner. It's important to note that the representation must have been communicated to the party who ultimately extends credit to the firm, as was held in *Young vs. Tredgold*.

Liability under Holding Out:

The liability that arises from holding out is not that of a

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partner per se, but it is similar in that the person held out as a partner can be held liable to third parties for the firm's debts. This was affirmed in the case of *Rai Bahadur Shree Ram vs Kallu Mian* where a person who represented himself as a partner was held liable as if he were an actual partner.

However, the person held out can only be held liable by a person who has extended credit to the firm based on the representation, as decided in *S.N. Namasivaya Mudaliar vs. A.M. Somasundaram Mudaliar*.

Protection from Holding Out:

A person who has allowed himself to be represented as a partner can absolve themselves from liability by giving notice of the cessation of such representation. This was established in the case of *Hardanahalli M. Siddalingaiah vs Canara Bank* where it was held that a person who has given a public notice about the cessation of his partnership is not liable to third parties for the acts of the firm done after the date of the notice.

In conclusion, the doctrine of holding out or estoppel is a provision in the Indian Partnership Act that ensures that a person who represents himself as a partner, or knowingly allows himself to be represented as such, can be held liable for the firm's obligations. This doctrine emphasizes the importance of honesty and clarity in business dealings and protects parties who have relied in good faith on such representations. However, a person held out as a partner can limit their liability by giving

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appropriate public notice about the cessation of their representation.

Q.5. WHAT ARE THE MODES OF DISSOLUTION OF PARTNERSHIP FIRM? WHAT ARE THE RIGHTS & LIABILITIES OF PARTNERS AFTER DISSOLUTION?

The concept of dissolution of a partnership firm is comprehensively covered under Chapter VI (Sections 39 to 55) of the Indian Partnership Act, 1932. The dissolution of a partnership firm refers to the cessation of the existing relationship among the partners. After dissolution, the firm ceases to exist, but the relationship among the partners continues until the affairs of the firm are wound up and its liabilities are met.

Modes of Dissolution of Partnership Firm:

There are several modes through which a partnership firm can be dissolved:

- 1. Dissolution by Agreement (Section 40):** A partnership firm may be dissolved if all partners mutually consent to end the partnership.
- 2. Compulsory Dissolution (Section 41):** This happens under certain circumstances, such as insolvency or when all partners (or all but one) become mentally incapable or are declared insolvent.
- 3. Dissolution on the Happening of Certain**

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Contingencies (Section 42): These contingencies may include death of a partner, expiry of the term of partnership, or completion of the project for which the partnership was formed.

- 4. Dissolution by Notice (Section 43):** In the case of partnerships entered into for an undefined period, any partner may dissolve the partnership by giving notice of his intent to other partners.
- 5. Dissolution by the Court (Section 44):** A court may dissolve a partnership on certain grounds, such as a partner becoming of unsound mind, permanent incapacity of a partner, misconduct, persistent breach of agreement by a partner, or the business consistently making losses.

Rights and Liabilities of Partners After Dissolution:

The dissolution of a partnership firm does not free partners from their obligations to each other and to third parties. The rights and liabilities of partners after dissolution are outlined in the following sections:

- 1. Rights of Partners (Section 46):** Upon dissolution of the firm, every partner has the right to have the firm's property applied in payment of the debts and liabilities of the firm, and to have the surplus distributed among the partners according to their sharing ratio.
- 2. Continuing Authority of Partners for**

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Purposes of Winding Up (Section 47): Even after dissolution, unless otherwise agreed, the partners retain authority to act for the firm for the purpose of winding up its business.

- 3. Continuing Liability of Partners to Third Parties (Section 45):** After dissolution, partners remain liable to third parties for any act done by any of them which would have been an act of the firm if done before the dissolution, until public notice is given of the dissolution.
- 4. Liabilities for Acts of Partners Done After Dissolution (Section 38):** Partners are held jointly and severally liable for any act done after the firm's dissolution if it was done without the knowledge of the partner sought to be made liable.
- 5. Rights of Partners to Return of Premium on Premature Dissolution (Section 51):** In case of dissolution before the end of a specified term, the partner who paid a premium on entering into the partnership may have a right to get the premium or a part thereof back.
- 6. Right of Outgoing Partner in Certain Cases to Share Profits Made After Dissolution (Section 37):** An outgoing partner or the representative of a deceased partner is entitled to a share of the profits made since dissolution as may be attributable to the use of his share of the property of the firm.

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The principles mentioned above clearly underline that while the dissolution marks the end of the partnership firm, it does not absolve the partners of their rights and obligations. These rights and obligations are necessary to ensure that the affairs of the firm are wound up properly and that all liabilities are met in a fair and just manner. The law seeks to balance the rights and obligations of all parties involved to bring about an equitable resolution to the dissolution of the partnership firm.

Q.6. EXPLAIN THE PRINCIPLE OF “NEMO QUOD DOT HABET” UNDER SALES OF GOODS ACT, 1930 WITH EXAMPLES. WHAT IS THE MEANING OF THE PHRASE “RISK PRIMA FACIE PASSES WITH PROPERTY” AS PER SALE OF GOODS ACT, 1930?

The Sale of Goods Act, 1930, is a comprehensive legislation that provides a legal framework for the sale and purchase of goods in India. It includes a number of principles that are fundamental to understanding and interpreting transactions of sale and purchase. Among these are the principle of "Nemo Dat Quod Non Habet" and the concept that "Risk Prima Facie Passes with Property."

Principle of "Nemo Dat Quod Non Habet":

"Nemo dat quod non habet" is a Latin term which translates to "no one gives what they do not have". This

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fundamental legal principle underpins much of property law and essentially means that a person cannot convey a better title than they themselves possess.

This principle is explicitly recognized in Section 27 of the Sale of Goods Act, 1930, which states that "where goods are sold by a person who is not the owner thereof and who does not sell them under the authority or with the consent of the owner, the buyer acquires no better title to the goods than the seller had".

For example, if A steals a mobile phone from B and sells it to C, C does not get a good title to the phone. Even though C might be a bona fide purchaser (i.e., C purchased the phone without knowing it was stolen), C cannot get a better title than A, the thief. Hence, B, the original owner, can claim the phone back from C.

However, this principle is not absolute and is subject to certain exceptions as provided under the Act. These exceptions are: sale by a mercantile agent, sale by one of joint owners, sale by a person in possession under a voidable contract, sale by a seller in possession after the sale, and sale under provisions of other laws.

Meaning of the Phrase "Risk Prima Facie Passes with Property" in the Sale of Goods Act, 1930:

Section 26 of the Sale of Goods Act, 1930 embodies the rule that risk follows ownership, stating, "Unless otherwise agreed, the goods remain at the seller's risk until the property therein is transferred to the buyer, but

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when the property therein is transferred to the buyer, the goods are at the buyer's risk whether delivery has been made or not."

This concept, "risk prima facie passes with property", means that once the ownership of goods is transferred from the seller to the buyer, the buyer assumes the risk of loss or damage to the goods, regardless of whether the goods have been delivered or not. It is based on the rationale that the person who has the enjoyment of goods should bear the risk.

For instance, if A agrees to sell a refrigerator to B, and the ownership of the refrigerator has passed from A to B, but the refrigerator is still in A's warehouse, the refrigerator is at the risk of B. If the warehouse catches fire and the refrigerator is destroyed, B bears the loss, not A, because the property in the goods had been transferred to B.

However, as stated in the Act, the parties to the contract may agree to terms that alter this default rule. It is quite common in commercial transactions for parties to agree that risk passes at a different time than ownership, such as upon delivery of the goods.

In conclusion, the principles of "Nemo Dat Quod Non Habet" and "Risk Prima Facie Passes with Property" are two significant concepts in the Sale of Goods Act, 1930, that form the basis of many transactions of sale and purchase.

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Q.7 (A) WHAT IS THE MEANING OF CONDITION AS TO MERCHANTABILITY? SUBSTANTIATE YOUR ANSWER WITH EXAMPLES.

(B) EXPLAIN THE, PURPOSE & PROCESS OF STOPPAGE IN TRANSIT UNDER SALES OF GOODS ACT, 1930? SUBSTANTIATE YOUR ANSWER WITH EXAMPLES.

(a) Condition as to Merchantable Quality:

The term "merchantable quality" refers to a basic level of quality that any goods, sold by a seller in the course of a business, must meet. This implies that the goods should be such as are commercially saleable under the description by which they are known in the market. This is a legal requirement and forms part of the implied conditions in a contract of sale.

As per Section 16(2) of the Sale of Goods Act, 1930, "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."

However, if the buyer has examined the goods, there is no implied condition as regards defects which such examination ought to have revealed.

To illustrate, let's consider a hypothetical case. Suppose A purchases a microwave from an electronics store. Under the condition of merchantable quality, the

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microwave must be fit for the purpose for which microwaves are usually purchased - i.e., heating and cooking food. If it turns out that the microwave does not heat food properly, it would not be of merchantable quality, and A could potentially return the microwave or ask for a refund or replacement from the store.

(b) Stoppage in Transit: Purpose & Process:

Stoppage in transit is a right of the unpaid seller against the buyer, outlined in Sections 50-52 of the Sale of Goods Act, 1930. This right is exercisable when the buyer of goods becomes insolvent and the goods have been dispatched to him but he has not yet received them. The purpose of stoppage in transit is to protect the seller's interest when the buyer is insolvent, and it allows the seller to regain possession of the goods and potentially find another buyer.

The process of stoppage in transit involves the following steps:

- 1. Existence of Unpaid Seller:** The right can only be exercised by an unpaid seller, i.e., a person who has sold goods for a price but has not been paid or a person who has an immediate right of action for the price.
- 2. Buyer's Insolvency:** This right is only exercisable when the buyer has become insolvent.
- 3. Goods in Transit:** The goods must be in transit. Goods are deemed to be in transit from the time they

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are delivered to a carrier or other bailee for transmission to the buyer, up to the time when the buyer or his agent takes delivery.

- 4. Notice to Carrier or Bailee:** To exercise the right of stoppage in transit, the unpaid seller must give notice to the carrier or other bailee in possession of the goods. Upon receipt of such notice, the carrier is bound to deliver the goods to the seller, not the buyer.

For example, A sells and ships 100 TVs to B. Before the TVs reach B, A learns that B has filed for bankruptcy and is unlikely to pay for the TVs. A can then exercise his right of stoppage in transit by notifying the shipping company to stop the TVs from being delivered to B and to return them to A.

Q.8. ELUCIDATE THE MAIN CHARACTERISTICS WHICH ENABLE AN INSTRUMENT TO BE NEGOTIABLE. HOW DOES ENDORSEMENT FACILITATE NEGOTIATION? EXPLAIN IN THE LIGHT OF LEGAL PROVISIONS.

Negotiable instruments play a pivotal role in modern business transactions. They provide a reliable medium for making payments and can be transferred from one person to another. The Negotiable Instruments Act, 1881, governs the use of negotiable instruments in India, including promissory notes, bills of exchange, and

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cheques.

Characteristics of Negotiable Instruments:

A negotiable instrument has several defining characteristics which are as follows:

- a. Transferability and Assignability:** The primary characteristic of a negotiable instrument is that it is freely transferable. It can be transferred from one person to another in accordance with the rules laid down by law.
- b. Title:** A bona fide transferee for value, who possesses the instrument in good faith and without negligence, gets the instrument free from all defects, and his/her title to the instrument is not affected by any defect in the title of the transferor.
- c. Rights of the Holder:** The holder of a negotiable instrument is entitled to the amount promised therein. If the payment is withheld, the holder has a right to sue upon the instrument.
- d. Presumptions:** Certain presumptions apply to all negotiable instruments unless the contrary is proved. For instance, every negotiable instrument is considered to have been drawn for a consideration, to have been issued on the date it bears, to be accepted or endorsed in good faith and for consideration, etc.

Role of Endorsement in Facilitating Negotiation:

Endorsement is a mechanism by which the transfer of the

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negotiable instrument to another party is authenticated and validated. The endorser, by signing on the instrument, not only transfers the instrument but also undertakes the liability, in case of dishonor.

An endorsement may be blank or full. In a blank endorsement (Section 16, Negotiable Instruments Act, 1881), the endorser merely signs his name, without specifying the endorsee. The instrument so endorsed becomes payable to bearer. A full endorsement specifies the name of the endorsee, and the instrument becomes payable to the endorsee.

Moreover, the endorser also has the ability to restrict the further negotiation of the instrument by expressing such intent at the time of endorsement.

To illustrate, let's assume A holds a promissory note that B has issued. If A wants to transfer this note to C, he can do so by endorsing it - i.e., by signing his name on the back of the note. By doing so, A not only transfers his rights on the note to C but also promises to compensate C if B fails to pay. This way, endorsement facilitates the safe and effective negotiation of the instrument.

In conclusion, the negotiable instrument is a unique instrument with distinct characteristics, making it an essential tool in the conduct of commerce. The process of endorsement further enhances its usability by facilitating smooth, verified transfers of the instrument, thereby enabling a fluid and reliable system of credit in the market.

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Q.9. WRITE SHORT NOTES ON FOLLOWING:

(A) GROUNDS FOR DISHONOR OF CHEQUES UNDER NEGOTIABLE INSTRUMENT ACT, 1881.

(B) 'PRESUMPTION IN FAVOR OF HOLDER' UNDER NEGOTIABLE INSTRUMENT ACT, 1881.

Grounds for Dishonour of Cheques:

A cheque is a type of negotiable instrument, which is essentially an order in writing, addressed by the drawer (issuer) to a bank, signed by the person who has deposited money with the bank, requiring the bank to pay on demand a certain sum of money to, or to the order of, a certain person, or to the bearer of the instrument.

Under Section 138 of the Negotiable Instruments Act, 1881, the dishonour of a cheque is a punishable offence. However, a cheque may be dishonoured for various reasons, some of which are as follows:

- a. **Insufficient Funds:** The most common ground for dishonouring a cheque is insufficient funds in the account of the drawer. A bank will not honour a cheque if the drawer's account does not have enough funds to cover the amount specified in the cheque.
- b. **Irregular Signature:** If the signature on the cheque does not match the specimen signature available with the bank, the cheque will be dishonoured.
- c. **Post-Dated or Stale Cheque:** A cheque is dishonoured if it is presented after a period of three

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months from the date mentioned on the cheque. This is referred to as a 'stale cheque'. On the other hand, if a cheque is dated for a future date and is presented before that date, it is considered a 'post-dated cheque' and will not be honoured until that date.

- d. **Alteration on Cheque:** If there are alterations in the date, amount, or name of the payee and such alterations are not authenticated by the drawer's signature, the cheque will be dishonoured.
- e. **Frozen Account:** If the drawer's account has been frozen due to legal issues, the bank will dishonour the cheque.
- f. **Death or Insolvency of the Drawer:** Upon receiving the news of the death or insolvency of the drawer, the bank may dishonour the cheque.
- g. **Stop-Payment Instructions:** If the drawer issues stop-payment instructions to the bank, the bank will dishonour the cheque.

Presumption in Favour of Holder:

The concept of 'presumption in favour of holder' is enshrined in Sections 118 and 119 of the Negotiable Instruments Act, 1881. This concept means that there are certain assumptions made by the law in favour of the holder of a negotiable instrument until the contrary is proved. These presumptions are:

- a. **Consideration:** It is presumed, unless proven

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otherwise, that every negotiable instrument was made or drawn for consideration. The holder does not need to prove that he gave consideration to receive the instrument.

- b. **Date:** Unless the contrary is proved, it is presumed that the instrument was made or drawn on the date it bears.
- c. **Time of Acceptance:** Unless the contrary is proved, it is presumed that every accepted bill of exchange was accepted within a reasonable time after its date and before its maturity.
- d. **Time of Transfer:** It is presumed that every transfer of a negotiable instrument was made before its maturity.
- e. **Order of Endorsements:** Unless the contrary is proved, the endorsements appearing on the negotiable instrument are presumed to have been made in the order in which they appear on the instrument.
- f. **Stamp:** It is presumed that a lost promissory note, bill of exchange or cheque was duly stamped.
- g. **Holder in Due Course:** Every holder of a negotiable instrument is presumed to be a holder in due course. However, if it was obtained from its lawful owner, or from any person authorized to negotiate it, by means of an offence or fraud, or for an unlawful consideration, the burden of proving these

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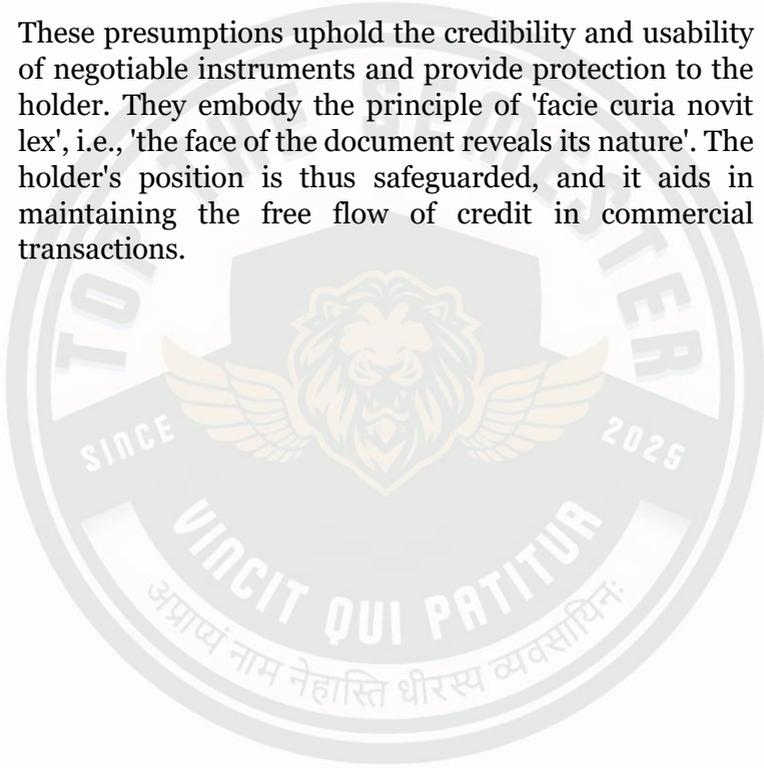
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lies upon the person alleging it.

- h. **Acceptance:** In the case of a bill of exchange, it is presumed that the drawee had the capacity to accept the bill.

These presumptions uphold the credibility and usability of negotiable instruments and provide protection to the holder. They embody the principle of 'facie curia novit lex', i.e., 'the face of the document reveals its nature'. The holder's position is thus safeguarded, and it aids in maintaining the free flow of credit in commercial transactions.



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PAPER 2

PART A

QUESTION 1: WRITE SHORT NOTES ON THE FOLLOWING

QUESTION (A): WRITE A SHORT NOTE ON MUTUAL AGENCY IN PARTNERSHIP

A **partnership**, as defined under Section 4 of the Indian Partnership Act, 1932, is "the relation between persons who have agreed to share the profits of a business carried on by all or any of them acting for all." The concept of mutual agency is a defining characteristic of this relation, and it can be found in this definition itself, in the words "carried on by all or any of them acting for all".

Mutual agency refers to the principle that every partner is both an agent and a principal. As an agent, a partner acts on behalf of the other partners, and as a principal, the partner is liable to be bound by the actions of the other partners.

Section 18 of the Indian Partnership Act further elucidates this concept. It states, "Subject to the provisions of this Act, a partner is an agent of the firm for the purposes of the business of the firm". This clearly establishes the principle of mutual agency, where a partner, acting within his/her authority, has the power to bind the firm and its partners.

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Moreover, **Section 19** provides that a partner has the authority to bind the firm in doing any act necessary for carrying on in the usual way, the business of the kind carried on by the firm. This principle was applied in the landmark case of **Hamlyn v Houston & Co** (1903), where it was held that a partner's act will bind the firm if it falls within his authority, either actual or ostensible.

However, mutual agency also implies mutual liability. **Section 25** of the Act stipulates that "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 joint and several liabilities of the partners have been confirmed in the case of **Bank of Maharashtra v Pandurang Keshav Gorwardkar & Ors** (2013).

To conclude, mutual agency in partnership implies that each partner is an agent of the firm and the other partners, and can thus bind them by his actions within the scope of the partnership business. This is a unique and vital aspect of the law of partnership which differentiates it from other forms of business associations.

QUESTION (B): WRITE A SHORT NOTE ON NEMO DAT QUID NON HABET

The legal maxim "**Nemo dat quid non habet**", roughly translating to "No one can give what they do not have," is

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a fundamental principle in property law, particularly in the context of the sale of goods.

The principle finds its manifestation in **Section 27** of the Indian Sale of Goods Act, 1930, which reads: "Unless the owner of the goods or a person authorised to sell goods on their behalf is the seller, the buyer acquires no better title to the goods than the seller had". This implies that if the seller does not have a valid title to the goods, the buyer will not acquire a valid title either.

However, the law also provides certain exceptions to the "nemo dat quid non habet" principle, recognising that there may be situations where an individual who is not the owner of the goods may transfer a good title to the transferee. These exceptions are laid out in **Sections 14, 25(1), 27, 28, 29 and 54** of the Sale of Goods Act. These include situations of sale by a mercantile agent, sale by one of the joint owners, sale by a person in possession under a voidable contract, and sale by a seller in possession after sale, among others.

A landmark case that can be cited here is **Morison v London County & Westminster Bank (1914)**. In this case, it was held that a motor vehicle dealer who was a fraudulent purchaser and had obtained possession of a vehicle, could not pass good title to a bona fide purchaser because the principle of 'Nemo dat quid non habet' applied.

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QUESTION (C): WRITE A SHORT NOTE ON INDEMNITY

Indemnity is a contract by which one party promises to save the other from loss caused to him by the conduct of the promisor himself, or by the conduct of any other person. This definition is enshrined in **Section 124** of the Indian Contract Act, 1872.

In an indemnity contract, there are two parties involved - the indemnifier and the indemnity-holder. The indemnifier is the person who promises to compensate for the loss, and the indemnity-holder is the person whose loss is to be compensated.

Section 125 of the Act outlines the rights of the indemnity-holder when indemnified. The indemnity-holder has the right to recover all damages, costs, and sums which he might have been compelled to pay in any suit in respect of any matter to which the promise to indemnify applies.

The principle of indemnity is commonly used in insurance contracts. For example, in a fire insurance policy, the insurance company (indemnifier) promises to compensate the policyholder (indemnity holder) for the loss suffered due to a fire.

The principle of indemnity was underscored in the case of **Gajanan Moreshwar Parelkar v Moreshwar Madan Mantri (1942)**, where it was observed that the liability of the indemnifier arises only when the

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indemnity holder is actually damaged.

In summary, the principle of indemnity, as embodied in the Indian Contract Act, 1872, serves to protect parties from financial loss. It's a critical element in many forms of contracts, most notably in insurance policies, guaranteeing that any losses sustained by a party will be compensated by the other party to the contract.

QUESTION (D): WRITE A SHORT NOTE ON PARTICULAR LIEN

In the law of bailment, a **lien** is a right to retain possession of goods until certain charges are paid. The Indian Contract Act, 1872, under **Section 170**, defines the principle of 'Particular Lien' stating that, "Where the bailee has, in accordance with the purpose of the bailment, rendered any service involving the exercise of labour or skill in respect of the goods bailed, he has, in the absence of a contract to the contrary, a right to retain such goods until he receives due remuneration for the services he has rendered in respect of them."

In other words, a particular lien is the right of a bailee to retain possession of specific goods until the payment is made for the labour or skill applied to those goods by the bailee.

There are certain important elements for a valid

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particular lien:

1. The goods upon which the lien is claimed must be bailed.
2. The bailee must have rendered some service involving labour or skill.
3. The bailee's labour or skill must add value to, or preserve or mend the goods.
4. The charges for such labour or skill must be unpaid.

The case of **Chapman v Allen (1631)** illustrates the concept of a particular lien. In this case, a tailor was given clothes to make a suit. The tailor had a right to retain the suit until he was paid for his labour.

However, it's crucial to note that a particular lien is a 'passive' right, i.e., it only allows the bailee to retain the goods and does not entitle him to sell them. The right of selling the goods to recover dues is granted only under certain conditions specified in Section 171 of the Indian Contract Act, 1872, which pertain to the 'General Lien'.

In conclusion, a particular lien is an important right granted to a bailee. It is designed to protect the interests of individuals who add value to goods through their labour or skill, by ensuring that they receive due compensation for their services.

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QUESTION (E): HIERARCHY OF COURTS

An agency relationship is established when one person, the principal, authorizes another, known as the agent, to act on their behalf. The agent has the legal authority to create a contractual relationship between the principal and a third party. The principal is then bound by the acts of the agent done within the scope of the authority. This relationship is governed by the provisions of the Indian Contract Act, 1872 (the Act), in Sections 182 to 238.

The creation of an agency relationship can occur through several modes. They are primarily: by express agreement, by implied agreement, by estoppel, by necessity, and by ratification.

- 1. Express Agreement (Section 187):** An agency can be created by express agreement, either orally or in writing. Section 187 of the Act states that "an authority is said to be express when it is given by words spoken or written". For example, a principal may directly appoint an agent to act on their behalf in a specific transaction. This is the simplest and most direct form of agency creation.
- 2. Implied Agreement (Section 187):** An agency can also be created by implication through the conduct, situation, or relationship of the parties involved. The Act states, "an authority is said to be implied when it is to be inferred from the circumstances of the case". This can happen when a person, by their words or conduct, leads a third party

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to believe that they have appointed an agent to act on their behalf. For example, if a person allows another to manage their shop, an agency relationship is implied between the two.

- 3. Agency by Estoppel or Holding Out (Section 237):** Agency by estoppel occurs when a person, by their words or conduct, intentionally or negligently induces another to believe that a certain person is their agent, and a third party acts on that belief. The principal is then estopped from denying the agency relationship. This principle is encapsulated in Section 237 of the Act, which states that "when an agent has, without authority, done acts or incurred obligations to third persons on behalf of his principal, the principal is bound by such acts or obligations, if he has by his words or conduct induced such third persons to believe that such acts and obligations were within the scope of the agent's authority".
- 4. Agency by Necessity (Section 189):** This type of agency arises in situations of emergency where the agent is forced to act without the principal's authority in order to prevent loss to the principal with respect to the goods, property, or interest in his charge. Section 189 of the Act mentions that "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".
- 5. Agency by Ratification (Section 196 to 200):**

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Ratification refers to the retrospective approval of an act done on behalf of another person. If a person, without any authority, does an act or makes a contract with a third person on behalf of another, the latter might ratify the act or contract, thus validating it from the date it was done or made. This is outlined in Sections 196 to 200 of the Act.

Each mode of agency creation serves a unique purpose and caters to different situations in contractual dealings. They ensure flexibility in commercial transactions, and the ability to respond to a variety of circumstances that might arise. The Act provides a comprehensive framework for the creation of agency, ensuring that both the agent and the principal are protected, and their rights and obligations are clearly defined.

In conclusion, the creation of an agency can occur in various ways under the Indian Contract Act, 1872. Regardless of the mode of creation, an agency relationship has profound legal implications, as it confers authority on an individual to act on behalf of another, thereby creating rights and obligations not just between the principal and agent, but also between the principal and third parties. The Act, through its provisions, offers a well-balanced system that regulates the creation of agency, ensuring the protection of all parties involved.

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PART B

QUESTION 2: THE RELATION OF AGENCY ARISES WHENEVER ONE PERSON HAS AUTHORITY TO ACT ON BEHALF OF ANOTHER. DISCUSS VARIOUS MODES OF CREATION OF AGENCY AS PER THE PROVISIONS IN THE INDIAN CONTRACT ACT, 1872.

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2. Implied Agreement (Section 187): An agency can also be created by implication through the conduct, situation, or relationship of the parties involved. The Act states, "an authority is said to be implied when it is to be inferred from the circumstances of the case". This can happen when a person, by their words or conduct, leads a third party to believe that they have appointed an agent to act on their behalf. For example, if a person allows another to manage their shop, an agency relationship is implied between the two.

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mentions that "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".

5. Agency by Ratification (Section 196 to 200):

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agency, ensuring the protection of all parties involved.

QUESTION 3: DECIDE AND ALSO PROVIDE RELEVANT CASE LAWS:

A. MR. BEAN WENT TO HOTEL RADISON BLU, DWARKA FOR DINNER. WHILE DINING THERE, HIS COAT WAS TAKEN AND HUNG ON A HOOK BEHIND MR. BEAN BY A WAITER. THE COAT GOT STOLEN FROM THERE. CAN MR. BEAN SUE THE HOTEL FOR DAMAGES?

B. A BANK GRANTED A LOAN ON THE SECURITY IN THE GODOWN. THE LOAN WAS ALSO GUARANTEED BY A SURETY. THE GOODS WERE LOST FROM THE GODOWN DUE TO THE NEGLIGENCE OF THE BANK OFFICIALS. WHAT IS THE LIABILITY OF THE SURETY?

Mr. Bean went to Hotel Radison Blu, Dwarka for dinner. While dining there, his coat was taken and hung on a hook behind Mr. Bean by a waiter. The coat got stolen from there. Can Mr. Bean sue the hotel for damages?

The situation of Mr. Bean falls under the ambit of the law of bailment. Bailment is defined under Section 148 of the Indian Contract Act, 1872, as "the delivery of goods by one person to another for some purpose, upon a contract that they shall, when the purpose is accomplished, be

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returned or otherwise disposed of according to the directions of the person delivering them."

In this case, the hotel acted as a bailee when the waiter took Mr. Bean's coat and hung it on a hook. This action amounts to the delivery of goods for a purpose - the safekeeping of the coat while Mr. Bean dined at the hotel.

Section 151 of the Act lays down that "in all cases of bailment, the bailee is bound to take as much care of the goods bailed to him as a man of ordinary prudence would, under similar circumstances, take of his own goods of the same bulk, quantity, and value as the goods bailed."

In this case, if it is found that the hotel did not take as much care of the coat as a man of ordinary prudence would, under similar circumstances, the hotel could be held liable for negligence, and Mr. Bean can sue the hotel for damages. This principle was upheld in the case of **Lakshmi Insurance Company vs. Atma Ram Chadha (AIR 1967 Del 141)**, where it was held that when goods are given to another for a specific purpose, the bailee is responsible for taking due care of the goods, and if any damage is caused to the goods due to his negligence, he will be held responsible.

A bank granted a loan on the security in the godown. The loan was also guaranteed by a surety. The goods were lost from the godown due to the negligence of the bank officials. What is the liability of the surety?

A surety's liability, in general, is co-extensive with that of

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the principal debtor unless it is otherwise provided by the contract. This is as per Section 128 of the Indian Contract Act, 1872. However, Section 139 of the Act states that "if the creditor does any act which is inconsistent with the rights of the surety, or omits to do any act which his duty to the surety requires him to do, and the eventual remedy of the surety himself against the principal debtor is thereby impaired, the surety is discharged."

In this situation, it can be argued that the bank's negligence led to the loss of goods from the godown, which was the security for the loan. This could be seen as an act inconsistent with the rights of the surety. Since the loss of the goods impaired the surety's eventual remedy against the principal debtor, the surety may be discharged from his liability under the guarantee.

In the landmark case of **State of Madhya Pradesh vs. Kaluram (AIR 1967 SC 1100)**, it was held that any act or omission of the creditor which results in the surety's rights being adversely affected will discharge the surety from his obligations.

In conclusion, it would seem that Mr. Bean, based on the law of bailment, might be able to sue the hotel for damages if it is found that the hotel did not take due care of his coat. On the other hand, due to the bank's negligence in the loss of the goods from the godown, the surety may be discharged from his liability. However, these conclusions will be subject to the specific facts and circumstances of the case, and a court's interpretation of the same.

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QUESTION 4: Q. COMMENT ON THE FOLLOWING:

A. IMPLIED AUTHORITY OF A PARTNER CAN BE EXTENDED OR RESTRICTED.

B. POSITION OF MINOR IN PARTNERSHIP

Implied Authority of a Partner can be Extended or Restricted

Partnership in business signifies a mutual agency relationship, where each partner acts on behalf of the other. According to Section 4 of the Indian Partnership Act, 1932, a partnership is defined as "the relation between persons who have agreed to share the profits of a business carried on by all or any of them acting for all".

The concept of implied authority of a partner emanates from this definition and is codified under Section 19(1) of the Act, which states that "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." This implies that a partner's actions, when acting within the usual way of business of the firm, are binding on all other partners.

However, this implied authority is not absolute and can be extended or restricted by agreement between the partners, as long as this agreement is not known to third parties dealing with the firm. As per Section 19(2) of the

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Act, "The partners in a firm may, by contract between the partners, extend or restrict the implied authority of any partner."

The landmark case of **Mercantile Credit Co. Ltd. vs Garrod [(1962) 3 All ER 1103]** demonstrated that an agreement to restrict a partner's authority has to be made known to the third party, to make it binding on them. In the absence of such notice, a partner's act binds the firm.

Position of Minor in Partnership

The position of a minor in a partnership is a unique one. The Indian Partnership Act, 1932, in Section 30(1) allows a minor to be admitted to the benefits of a partnership with the consent of all the partners.

A minor, according to this provision, has a right to his share of the property and profits of the firm, as agreed upon by the partners. However, the minor's liability is limited only to the extent of his share in the partnership assets and profits. He cannot be made personally liable for any of the debts of the firm.

Furthermore, a minor cannot become a full-fledged partner while still a minor. Upon attaining majority, the minor has the option to decide whether he would like to become a partner in the firm. This decision must be made within six months of attaining majority, and he must notify his decision to all the partners.

This position was well-explained in the case of **S.C. Mandal vs Krishnadhan Banerjee (AIR 1950 Cal**

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488), where it was held that a minor can be admitted to the benefits of a partnership with the consent of all the partners, but cannot be made personally liable for any of the firm's debts.

In conclusion, while the implied authority of a partner in a firm can be extended or restricted by mutual agreement, the position of a minor in a partnership is nuanced. While a minor may be admitted to the benefits of a partnership, his liability is restricted. Upon attaining majority, he can decide whether or not to continue as a partner.

QUESTION 5 DECIDE WITH THE HELP OF RELEVANT CASE LAW AND PROVISIONS OF INDIAN PARTNERSHIP ACT, 1932:

A. X AND Y STARTED BUSINESS IN A PARTNERSHIP. AFTER A COUPLE OF YEARS, THEY FOUND THAT THE FIRM IS INCURRING CONTINUOUS LOSSES. CAN IT BE A GROUND FOR DISSOLUTION OF A FIRM.

B. THERE WAS PARTNERSHIP BETWEEN TWO SOLICITORS FOR THEIR JOINT LIVES. ONE OF THEM FRAUDULENTLY SOLD OUT THE FUNDS OF THE TRUST AND APPLIED THEM TO HIS PERSONAL USE. CAN THIS CONDUCT OF A PARTNER BE A GROUND FOR DISSOLUTION?

X and Y started a business in a partnership. After a couple of years, they found that the firm is incurring continuous losses. Can it be a ground

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for dissolution of a firm?

Under the Indian Partnership Act, 1932, the dissolution of a partnership firm may occur under several circumstances, one of which includes mutual agreement between the partners. As per Section 40 of the Act, a firm may be dissolved when all the partners, or all but one partner, consent to its dissolution.

However, continuous losses in a business do not automatically constitute a ground for dissolution unless it can be demonstrated that the business can only be carried on at a loss. As per Section 44(d) of the Act, a firm may be dissolved by the court when "a business of the firm can only be carried on at a loss." Therefore, it must be established that the business cannot possibly be carried on without a loss.

In this case, if X and Y can convincingly demonstrate that the business is only capable of operating at a loss, they might petition the court for dissolution. However, it should be noted that a temporary period of losses or financial hardship does not necessarily meet this threshold. This principle was discussed in the case of **Srinivas vs Narayan [(AIR 1956 Mad 273)]**.

There was a partnership between two solicitors for their joint lives. One of them fraudulently sold out the funds of the trust and applied them to his personal use. Can this conduct of a partner be a ground for dissolution?

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Yes, a partner's fraudulent conduct can indeed be a ground for dissolution of the firm. This is stipulated in Section 44(c) of the Indian Partnership Act, 1932, which provides that a firm may be dissolved by the court "when a partner, other than the partner suing, becomes in any way permanently incapable of performing his duties as partner."

Fraudulent conduct on the part of a partner, particularly in a manner that adversely affects the firm's interests, can be seen as rendering that partner 'permanently incapable' of performing his duties as a partner. In the case of **Sampson vs. Hartland [(1885) 2 TLR 532]**, it was held that fraudulent conduct on the part of a partner could be a ground for dissolution.

Thus, in this case, the fraudulent conduct of the solicitor who misused the trust's funds for his personal use can be considered as ground for dissolution of the partnership. The other partner can approach the court seeking dissolution of the partnership on this basis. It's important to note that the ultimate decision will depend on the court's evaluation of the facts and circumstances of the case.

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QUESTION 6: COMMENT ON THE FOLLOWING:

A. BREACH OF A CONDITION IN A SALE OF GOODS CAN BE TREATED AS A BREACH OF WARRANTY BUT NOT OTHERWISE.

B. A CONTRACT OF SALE IS NOT AVOIDED EVEN ON ACCOUNT OF BREACH OF A CONDITION

Breach of a Condition in a Sale of Goods can be Treated as a Breach of Warranty but not Otherwise

The Sale of Goods Act, 1930, distinguishes between 'conditions' and 'warranties' in a contract of sale. Section 12 of the Act provides that a condition is a stipulation that is essential to the main purpose of the contract. The breach of a condition gives rise to a right to treat the contract as repudiated. On the other hand, a warranty is a stipulation collateral to the main purpose of the contract, the breach of which gives rise to a claim for damages but not a right to reject the goods and treat the contract as repudiated.

Section 13(1) of the Act establishes that a breach of a condition can be treated as a breach of a warranty. However, it is crucial to note that this is not automatic but is subject to the choice of the aggrieved party. In the event of a breach of a condition, the aggrieved party has two options. They can either (1) treat the contract as

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repudiated and reject the goods, or (2) elect to treat the breach as a breach of warranty, accept the goods, and claim damages for the breach.

The reverse, however, is not true. A breach of warranty cannot be treated as a breach of a condition. The reason for this is that a warranty is not considered essential to the main purpose of the contract. Therefore, the breach of a warranty only gives rise to a claim for damages and does not afford the right to reject the goods or treat the contract as repudiated. This principle was emphasized in the case of **Bentsen vs. Taylor, Sons & Co. [(1893) 2 QB 274]**.

A Contract of Sale is Not Avoided Even on Account of Breach of a Condition

A breach of condition in a contract of sale does not automatically render the contract void. Section 13 of the Sale of Goods Act, 1930, allows the aggrieved party, in case of a breach of a condition, to either treat the contract as repudiated or elect to treat the breach as a breach of warranty.

While a breach of a condition gives the aggrieved party a right to repudiate the contract, this is not an obligation. The party can choose to waive the condition and continue with the contract, treating the breach as a breach of warranty instead, and claim damages. This was established in the landmark case of **Schuler AG vs. Wickman Machine Tool Sales Ltd. [(1973) 2 WLR 683]**, where it was held that whether a term is a

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condition depends not just on the wording of the contract, but also on the intent of the parties and the circumstances surrounding the breach.

Therefore, even if there is a breach of a condition in a contract of sale, the contract is not automatically avoided. The aggrieved party has the discretion to either treat the contract as repudiated or treat the breach as a breach of warranty and claim damages. The ultimate decision depends on the choice of the aggrieved party.

QUESTION 7: DISCUSS:

A. SELLER'S RIGHT OF LIEN AND SELLER'S RIGHT OF STOPPAGE IN TRANSIT

B. REMEDIES AVAILABLE TO A BUYER

Seller's Right of Lien and Seller's Right of Stoppage in Transit

The Sale of Goods Act, 1930 provides specific rights to an unpaid seller against the goods, including the right of lien and the right of stoppage in transit.

Seller's Right of Lien (Section 47 to 49)

The right of lien is the right to retain possession of goods until the full price is paid or tendered. Section 47(1) specifies that the unpaid seller can exercise the right of lien, (1) where the goods have been sold without any stipulation as to credit; (2) where the goods have been

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sold on credit, but the term of credit has expired; and (3) where the buyer becomes insolvent.

The lien is lost in certain situations as outlined in Section 49: (1) when the seller delivers the goods to a carrier or other bailee for the purpose of transmission to the buyer without reserving the right of disposal of the goods; (2) when the buyer or his agent lawfully obtains possession of the goods; (3) by waiver.

Seller's Right of Stoppage in Transit (Section 50 to 52)

Stoppage in transit is the right of the seller to resume possession of the goods while they are in transit, render them to his disposition, and retain them until payment. This right is exercisable when the buyer of goods becomes insolvent and the seller has parted with the possession of the goods.

The duration of transit is determined by the situations under Section 51. Transit comes to an end when the buyer or his agent takes delivery of the goods before their arrival at the agreed destination, or when the carrier acknowledges to the buyer that he holds the goods on his behalf.

The exercise of the right of stoppage in transit is outlined in Section 52. The unpaid seller may exercise this right 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.

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Remedies Available to a Buyer

The Sale of Goods Act, 1930 provides several remedies to the buyer in case of breach of contract by the seller:

1. **Damages for Non-Delivery (Section 57):** If the seller wrongfully neglects or refuses to deliver the goods to the buyer, the buyer may sue the seller for damages for non-delivery.
2. **Suit for Specific Performance (Section 58):** Subject to the provisions of the Specific Relief Act, 1963, in case of breach of contract by the seller, the buyer may sue him for specific performance of the contract.
3. **Suit for Breach of Warranty (Section 59):** The buyer can sue the seller for breach of warranty or for breach of a condition treated as a breach of warranty.
4. **Recession of Contract (Section 62):** In case of breach of a condition by the seller, the buyer may repudiate the contract.
5. **Remedy for Breach of Condition as to Quality or Fitness (Section 16):** If the goods do not comply with the conditions as to quality or fitness, the buyer can reject the goods and claim damages.

The specific remedy to be availed depends on the nature of the breach and the circumstances of the case. The

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principles discussed here were affirmed in cases such as **Karsandas H. Thacker vs Sarabhai M. Kamdar [(AIR 1976 SC 541)]** and **Ram Singh vs S. Dalip Singh [(AIR 1965 Punj 269)]**.

QUESTION 8: A. COMMENT ON THE STATEMENT 'A NEGOTIABLE INSTRUMENT IS A PIECE OF PAPER WHICH ENTITLES THE HOLDER TO A SUM OF MONEY MENTIONED IN IT'

B. A BILL OF EXCHANGE IS DRAWN STATING- 'PAY TO X OR HIS ORDER A SUM OF TEN THOUSAND RUPEES'. HOWEVER, IN THE MARGIN, THE AMOUNT STATED IS RS.1000. IS IT A VALID BILL? IF YES, HOW MUCH AMOUNT IT WILL REPRESENT? IF NO WHY?

a. Comment on the Statement 'A Negotiable Instrument is a Piece of Paper which Entitles the Holder to a Sum of Money Mentioned in It'

This statement is a simple way to describe the basic concept of a negotiable instrument but falls short in fully capturing its intricacies as defined under the law. A negotiable instrument, according to Section 13 of the Negotiable Instruments Act, 1881, is a document guaranteeing the payment of a specific amount of money, either on demand, or at a set time, with the payer named

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on the document. This includes promissory notes, bills of exchange, and cheques.

It's essential to note the key characteristics of a negotiable instrument that differentiate it from a mere 'piece of paper which entitles the holder to a sum of money.'

1. **Transferability:** A negotiable instrument can be freely transferred by delivery or by endorsement and delivery. The transferee, when he takes it bona fide and for value, gets it free from all defects, and his title to the instrument is not affected by any defect in the title of the transferor.
2. **Holder in Due Course:** The holder in due course obtains an absolute and unconditional title to the instrument. He holds the instrument free from all defects and can recover the amount thereof against all parties thereto.
3. **Presumptions:** Certain presumptions apply to negotiable instruments under Section 118 and 119 of the Negotiable Instruments Act, 1881, such as the presumption of consideration, and presumption as to the date of the instrument.

b. A Bill of Exchange is Drawn Stating- 'Pay to X or His Order a Sum of Ten Thousand Rupees'. However, in the Margin, the Amount Stated is Rs.1000. Is it a Valid Bill? If Yes, How Much Amount it Will Represent? If No Why?

According to Section 18 of the Negotiable Instruments

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Act, 1881, if there is a discrepancy in the amount stated in figures and in words, the amount stated in words shall be the amount deemed to be of the instrument. The reason behind this provision is that a person when making out an instrument, is less likely to make a mistake in the amount when written in words than when written in figures.

Therefore, in this case, the bill of exchange is valid, and the amount of the bill will be deemed to be 'ten thousand rupees', as stated in words, despite the discrepancy with the figure written in the margin. This position was upheld in the case of **Suryalatha Legal Representative of C.N. Anantha Rangachar vs. Corporation Bank [(2003 (3) ALD 62 (DB)]**. Thus, it emphasizes the significance of accuracy and attention to detail while drafting negotiable instruments, as such discrepancies could lead to disputes and litigation.

QUESTION 9: A. COMMENT ON THE STATEMENT 'A NEGOTIABLE INSTRUMENT IS A PIECE OF PAPER WHICH ENTITLES THE HOLDER TO A SUM OF MONEY MENTIONED IN IT'

B. A BILL OF EXCHANGE IS DRAWN STATING- 'PAY TO X OR HIS ORDER A SUM OF TEN THOUSAND RUPEES'. HOWEVER, IN THE MARGIN, THE AMOUNT STATED IS RS.1000. IS IT A VALID BILL? IF YES, HOW MUCH AMOUNT

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IT WILL REPRESENT? IF NO WHY?

a. **Comment on the Statement 'A Negotiable Instrument is a Piece of Paper which Entitles the Holder to a Sum of Money Mentioned in It'**

While this statement accurately captures the essence of a negotiable instrument, it fails to account for the nuances of the legal concept. The Negotiable Instruments Act, 1881, specifically defines a negotiable instrument, in Section 13, as a document guaranteeing the payment of a specific amount of money, either on demand or at a set time, to the bearer or person named on the document. This includes promissory notes, bills of exchange, and cheques.

Key features of a negotiable instrument include:

1. **Transferability:** A negotiable instrument can be transferred freely, either by delivery or by endorsement and delivery, to another person. The transferee, if they acquire it bona fide and for value, receives it free from all defects, and their title to the instrument is unaffected by any defect in the title of the transferor.
2. **Holder in Due Course:** A holder in due course obtains a good title to the instrument. They hold the instrument free from all defects, meaning they are unaffected by any illegality in the transaction from which they acquired it, provided they had no notice of the defect at the time of their acquisition.

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3. **Presumptions:** Certain presumptions apply to negotiable instruments, which can be found in Sections 118 and 119 of the Negotiable Instruments Act, 1881. These include presumptions as to consideration, as to date of the instrument, as to time of acceptance, etc.

b. A Bill of Exchange is Drawn Stating- 'Pay to X or His Order a Sum of Ten Thousand Rupees'. However, in the Margin, the Amount Stated is Rs.1000. Is it a Valid Bill? If Yes, How Much Amount it Will Represent? If No Why?

Section 18 of the Negotiable Instruments Act, 1881, stipulates that if a negotiable instrument, such as a bill of exchange, includes conflicting amounts stated in figures and in words, the amount stated in words is the amount to be paid.

In the provided scenario, therefore, the bill of exchange is indeed valid. Despite the discrepancy between the margin (figures) and the written instruction (words), the bill represents the sum of 'ten thousand rupees' as stipulated in the written instruction. This interpretation aligns with the intention of the law, which prioritises the written amount in words over the figure in the margin to guard against fraud and mistakes in the drafting of negotiable instruments.

This was upheld in the case of **Suryalatha Legal Representative of C.N. Anantha Rangachar vs. Corporation Bank [(2003 (3) ALD 62 (DB)]**. This

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case emphasised the need for attention to detail and accuracy when drafting negotiable instruments, given that discrepancies between figures and words can lead to disputes and litigation.

QUESTION 9: DISCUSS THE LAW APPLICABLE TO DISHONOR OF NEGOTIABLE INSTRUMENTS WITH THE HELP OF RELEVANT CASE LAW AND NEGOTIABLE INSTRUMENTS ACT, 1881.

Dishonour of a negotiable instrument generally occurs when the party, upon whom it is drawn, refuses or is unable to pay the specified amount to the holder or to the person whom it is endorsed. The Negotiable Instruments Act, 1881 comprehensively provides for cases of dishonour of negotiable instruments, particularly in Chapter XVII covering Sections 138 to 142.

Section 138: Dishonour of Cheque for Insufficiency of Funds

This section states that if a cheque drawn by a person for the discharge of any debt or other liability is returned by the bank unpaid, either due to insufficiency of funds or the amount to be paid exceeds the amount arranged to be paid, such individual shall be deemed to have committed an offence. The punishment for this offence may extend to twice the amount of the cheque or imprisonment for a term which may extend to two years or both.

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Section 139: Presumption in Favour of Holder

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, of any debt or other liability.

Section 140: Defence Which May Not be Allowed

This section makes it clear that it is not a valid defence that the drawer had no reason to believe when he issued the cheque that the cheque may be dishonoured on presentment for the reasons stated in Section 138.

Section 141: Offences by Companies

This section provides for cases where the person committing an offence under Section 138 is a company. It determines that not only the company but also every person who was in charge of, and was responsible to, the company for the conduct of the business of the company, shall be deemed to be guilty of the offence.

Section 142: Cognizance of Offences

No court shall take cognizance of any offence punishable under Section 138 except upon a complaint, in writing, made by the payee or, as the case may be, the holder in due course of the cheque.

In the case of **Moran Mar Basselios Catholicos and Another vs. Most Rev. Mar Poulouse Athanasius and Others [AIR 1954 SC 526]**, the Supreme Court held that the primary objective of Chapter XVII of the Act

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was to inculcate faith in the efficacy of banking operations and credibility in transacting business on negotiable instruments.

Also, in the case of **M.M.T.C. Ltd. and Another vs. Medchl Chemicals and Pharma (P) Ltd. and Another [(1999) 8 SCC 686]**, the Supreme Court held that dishonour of a cheque is a statutory offence and just because the drawer issued notice to the drawee or the drawee demanded security for providing the amount does not discharge the drawer of liability under Section 138.

In **Rangappa vs. Sri Mohan [(2010) 11 SCC 441]**, the Supreme Court held that the presumptions under Sections 138 and 139 impose an evidentiary burden and not a persuasive burden. Thus, once the complainant discharges his burden to prove that the cheque was issued for discharging a legally enforceable debt and that it was dishonoured, the burden shifts onto the accused to disprove the presumptions.

In conclusion, the law related to dishonour of negotiable instruments under the Act aims to promote the efficacy of bank operations and ensure credibility in business transactions involving negotiable instruments. Moreover, it provides for stringent penalties and procedures for the dishonour of cheques.

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PAPER 2

PART A

QUESTION 1: WRITE SHORT NOTES ON THE FOLLOWING

QUESTION (A): WRITE SHORT NOTE ON DIFFERENCE BETWEEN PROMISSORY NOTE AND BILL OF EXCHANGE.

Promissory Note: A promissory note, as per Section 4 of the Negotiable Instruments Act, 1881, is a written instrument containing an unconditional promise by a person, known as the maker, to another person, known as the payee, to pay a certain sum of money, either to the payee or to any other person or to the bearer of the instrument.

Some of the defining characteristics of a promissory note are:

1. **Written and Unconditional Promise:** It must contain a clear, unambiguous, and unconditional promise to pay. The promise should be in writing and not merely verbal.
2. **Specific Amount:** The amount to be paid must be specified and certain.
3. **Parties:** The two parties involved are the maker

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(who makes the promise and is liable to pay) and the payee (to whom the payment is to be made).

4. **Signature of the Maker:** The promissory note must be signed by the maker of the promise.

Bill of Exchange: A bill of exchange, as per Section 5 of the Negotiable Instruments Act, 1881, is a written instrument containing an unconditional order directed by one person, known as the drawer, to another person, known as the drawee, to pay a certain sum of money, either to a named person or to the bearer of the instrument.

Some of the defining characteristics of a bill of exchange are:

1. **Written and Unconditional Order:** It consists of an unconditional order to pay money, unlike a promissory note which is a promise to pay.
2. **Specific Amount:** Like a promissory note, the amount to be paid must be specified and certain.
3. **Parties:** A bill of exchange involves three parties - the drawer (who orders the payment), the drawee (to whom the drawer's order is directed), and the payee (to whom the payment is to be made).
4. **Acceptance by the Drawee:** A bill of exchange needs to be accepted by the drawee, indicating the

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drawee's assent to the order given by the drawer. This acceptance transforms the bill into an "accepted" bill of exchange, a critical step that doesn't exist in case of a promissory note.

Thus, the principal difference between a promissory note and a bill of exchange lies in the number of parties involved and the nature of the instrument - a promissory note contains a promise to pay, while a bill of exchange is an order to pay.

QUESTION (B): WRITE SHORT NOTE ON EXPLAIN THE DIFFERENCE BETWEEN HOLDER AND HOLDER IN DUE COURSE.

Holder: According to Section 8 of the Negotiable Instruments Act, 1881, a holder of a negotiable instrument is the person entitled in his own name to the possession of the instrument and to receive or recover the amount due thereon from the parties thereto. A holder may obtain the instrument either by endorsement or by delivery.

Key elements of a holder are:

1. **Possession:** The person must have the instrument in his possession.
2. **Entitlement:** The person must be entitled to the possession of the instrument in his own name.

Holder in Due Course: A holder in due course is a

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special category of holder. Section 9 of the Act defines a holder in due course as any person who, for consideration, becomes the possessor of a negotiable instrument before its maturity, and without having sufficient cause to believe that any defect existed in the title of the person from whom he derived his title.

Key elements of a holder in due course are:

1. **Possession by Valid Transfer:** The person must have obtained the instrument by a valid transfer, i.e., by negotiation.
2. **Good Faith and Without Notice:** The person must obtain the instrument in good faith, without notice of any defect in the title of the previous holder, and before the instrument is due.
3. **Consideration:** The person must have given valuable consideration for the instrument.

A holder in due course enjoys several privileges over a simple holder, such as immunity from certain defenses and equities that might be available against the previous holder (Sections 36-60 of the Act). The concept of a holder in due course has been incorporated into the Act to encourage the free circulation of negotiable instruments by ensuring good faith transferees are protected in their transactions.

In conclusion, the key difference between a holder and a holder in due course is that while the former simply possesses the instrument in his own name, the latter

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acquires the instrument for value, in good faith, and without notice of any defects in the instrument or in the title of the transferor.

QUESTION (C): WRITE SHORT NOTE ON EXPLAIN THE DIFFERENCE BETWEEN SALE AND AGREEMENT TO SALE

The Indian Sale of Goods Act, 1930 differentiates between a 'sale' and an 'agreement to sell'. Both represent different stages in the process of finalizing a sales transaction.

Sale: According to Section 4(1) of the Sale of Goods Act, a contract of sale is a contract where the seller transfers or agrees to transfer the property in goods to the buyer for a price. In the case of a 'sale', the transfer of property for a price takes place immediately.

Key features of a 'sale' are:

1. **Immediate Transfer of Ownership:** Ownership or title to the goods is transferred immediately at the time of the contract.
2. **Risk and Reward:** As ownership is transferred, the buyer becomes responsible for any loss or damage to the goods, irrespective of whether the possession of goods is transferred.
3. **Remedies to the Seller:** In case of a buyer's default, the seller can sue for the price, as the

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property has already passed to the buyer.

Agreement to Sell: An 'agreement to sell', as per Section 4(3) of the Sale of Goods Act, is a contract wherein the transfer of the property in goods is to take place at a future date or subject to some conditions to be fulfilled later.

Key features of an 'agreement to sell' are:

1. **Future Transfer of Ownership:** Ownership of the goods is to be transferred at a future date or upon fulfilment of certain conditions.
2. **Risk and Reward:** The seller remains the owner and bears the risk of loss or damage until the specific conditions are met and ownership is transferred.
3. **Remedies to the Seller:** If the buyer defaults, the seller can only sue for damages and not for the price because ownership hasn't been transferred yet.

In summary, a 'sale' denotes an immediate transfer of ownership, while an 'agreement to sell' implies a transfer of ownership to take place in the future or upon fulfilment of certain conditions.

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QUESTION (D): WRITE SHORT NOTE ON DIFFERENCE BETWEEN INDEMNITY AND GUARANTEE

The Indian Contract Act, 1872 differentiates between contracts of 'indemnity' and 'guarantee'.

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

Key features of 'indemnity' are:

1. **Two Parties:** There are only two parties - the indemnifier and the indemnity holder.
2. **Single Contract:** There is only one contract between the indemnifier and the indemnity holder.
3. **Nature of Liability:** The liability of the indemnifier is primary and independent.
4. **Purpose:** The purpose of an indemnity contract is to protect the indemnity holder against potential losses.

Guarantee: A 'guarantee', as per Section 126 of the Act, is a contract to perform the promise or discharge the liability of a third person in case of his default.

Key features of 'guarantee' are:

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1. **Three Parties:** There are three parties - the creditor, the principal debtor, and the surety or guarantor.
2. **Three Contracts:** There are three contracts – between the creditor and the principal debtor, between the principal debtor and the surety, and between the surety and the creditor.
3. **Nature of Liability:** The liability of the surety is secondary; the primary responsibility lies with the principal debtor.
4. **Purpose:** The purpose is to provide an assurance to the creditor that his dues will be paid, not necessarily to protect against losses.

In conclusion, a contract of indemnity involves a promise to compensate for a loss, while a guarantee is a promise to pay if a third party fails to do so. The indemnifier's liability in an indemnity contract is primary and independent, while in a guarantee, the surety's liability is secondary and contingent on the default of the principal debtor. The primary intent of an indemnity contract is to protect against loss, whereas a guarantee seeks to ensure that payment or performance obligations are duly met.

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QUESTION (E): WRITE SHORT NOTE ON POSITION OF MINOR IN THE PARTNERSHIP FIRM.

The Indian Partnership Act, 1932, governs the law relating to partnership firms in India, including the position of a minor in a partnership firm. The relationship between partners and their standing within the firm is guided by this statute.

According to Section 30 of the Indian Partnership Act, a minor cannot become a partner in a partnership firm, but, with the consent of all the partners, a minor may be admitted to the benefits of an existing partnership.

Following are the key points highlighting the position of a minor in a partnership firm:

1. **Admission to Benefits:** A minor cannot become a full-fledged partner but can be admitted to the benefits of a partnership, i.e., he can share the profits of the business. However, this can only occur with the consent of all existing partners.
2. **Liability:** A minor's liability in the firm is limited. He cannot be made personally liable for any of the firm's liabilities. His liability is limited to his share in the partnership's profits and the capital contributed by him, if any.
3. **No Participation in Management:** A minor does not have the right to participate in the conduct of the partnership business. He cannot

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make decisions that can affect the firm.

4. **Right to Inspect and Copy:** A minor has the right to access, inspect, and copy any of the partnership's books.
5. **Option to Become a Partner:** Once the minor attains majority (turns 18), he has a choice to decide whether he wants to become a full-fledged partner or not. He has six months from the date of attaining majority to make this decision. During this period, he is treated as a full partner for all intents and purposes.

If the minor chooses to become a partner, his share in the firm and his liability become equal to that of any other partner. If the minor decides not to become a partner, his rights and liabilities continue as they were before, and he is entitled to sue the partners for his share of the property and profits.

The landmark case of **S.C Mandal v. Krishnadhan Banerjee** (AIR 1962 SC 779) clarified the position of a minor in a partnership firm. The Supreme Court held that a minor cannot become a partner, but with the consent of all the partners, he can be admitted to the benefits of partnership.

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PART B

Q2: EXPLAIN THE RIGHTS OF SURETY AGAINST THE CREDITOR, THE PRINCIPAL DEBTOR AND CO-SURETIES.

Rights of Surety

In contracts of guarantee, a surety is a person who guarantees the performance of another person, known as the principal debtor. The Indian Contract Act, 1872, specifically Sections 140-145, elucidates the rights a surety enjoys against the creditor, the principal debtor, and co-sureties. Let's analyze these rights in detail.

1. Rights of Surety Against the Creditor

A surety has the following rights against the creditor:

a. Right of Subrogation: As per Section 140, once a surety has discharged the liabilities under the contract, he steps into the shoes of the creditor. This means that any remedy which the creditor had against the principal debtor now becomes the right of the surety. This right begins immediately after the surety has paid off the debt.

b. Right to Securities: As per Section 141, if the creditor has any securities or collateral from the principal debtor, the surety has the right to benefit from them once the surety has paid the debt or performed the duty. It's noteworthy that this right exists even if the surety was unaware of the security when he entered into the contract of guarantee.

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c. Right of Set-off: If the creditor owes any money to the principal debtor, the surety has the right to claim a set-off when sued by the creditor for the debt guaranteed.

2. Rights of Surety Against the Principal Debtor

The surety also enjoys certain rights against the principal debtor:

a. Right to Indemnity: As per Section 145, the surety has a right to claim from the principal debtor all sums which he has rightfully paid under the guarantee. This right arises as soon as the surety's liability under the guarantee comes into existence.

b. Right of Subrogation: As per Section 140, on payment of the debt or performance of all that he is liable for, the surety steps into the shoes of the creditor and acquires all the rights, remedies, and securities against the principal debtor that the creditor had.

c. Right to Proceed Against the Principal Debtor First: A surety is entitled to compel the creditor to first exhaust the principal debtor's assets before enforcing the liability against him. However, this is not an absolute right and can be contractually excluded.

3. Rights of Surety Against Co-Sureties

In situations where there are multiple sureties for the same debt, each co-surety has certain rights:

a. Right to Contribution: As per Section 146, when a surety pays an amount that is greater than his share in the

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debt, he can demand that his co-sureties contribute equally, i.e., pay their respective shares in the deficiency. This right doesn't arise until one of the sureties has paid more than his share.

b. Right to Benefit of Co-Surety's Securities: Under Section 141, a surety who has paid off the whole debt is entitled to the benefit of all securities which the creditor had against the principal debtor, even if they were provided by a co-surety.

To fully understand the rights of a surety, let's consider a few case laws.

In the landmark case of **State Bank of India v. Mula Sahakari Sakhar Karkhana Ltd** (AIR 2006 SC 3029), the Supreme Court reaffirmed the principle of subrogation, ruling that a guarantor, after discharging the debt, steps into the creditor's shoes and is entitled to all rights that the creditor has against the debtor.

In another case, **Bank of Bihar v. Damodar Prasad** (AIR 1969 SC 297), the Supreme Court held that a surety has a right to benefit from the securities held by the creditor, even if he was unaware of them at the time of entering into the contract of guarantee.

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Q3: (A) MR. RAMESH HIRED LOCKER NO. 15 ON 10-1-1996 IN ABCD BANK AND HAD DEPOSITED JEWELLERY IN THE VALUE OF RS. 14,26,160/-. THE LOCKER OF MR. RAMESH ALONG WITH OTHERS WAS BROKEN BY MISCREANTS AND THE CONTENTS THEREOF WERE STOLEN. IN THE LIGHT OF ABOVE MENTIONED FACTS DECIDE THE LIABILITY OF THE BANK BY PROVIDING COGENT REASONING, STATUTORY PROVISIONS AND JUDICIAL PRONOUNCEMENTS. WHETHER MERE HIRING OF A LOCKER IN A BANK IS SUFFICIENT TO CONSTITUTE A CONTRACT OF BAILMENT?

(B) EXPLAIN THE DIFFERENCE BETWEEN BAILMENT AND AGENCY.

Liability of the Bank in Locker Hiring and the Question of Bailment

In the given situation, the relationship between Mr. Ramesh and ABCD bank raises the question of whether there is a contract of bailment and, if so, the bank's liability under such a contract.

In the Indian Contract Act, 1872, a bailment is defined under Section 148 as "the delivery of goods by one person to another for some purpose, upon a contract that they shall, when the purpose is accomplished, be returned or otherwise disposed of according to the directions of the person delivering them."

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Applying this to the present case, if we consider the locker's contents as 'goods', and the bank's providing of a locker service as 'delivery for some purpose', it could be argued that the hiring of a locker might constitute a contract of bailment. However, a critical point of contention in such scenarios is whether the bank has 'knowledge' of the goods kept in the locker because the obligation and liability of the bank would change based on this.

In a series of cases, Indian courts have held that the relationship between a bank and a customer in respect of a locker is that of a 'bailor and bailee', meaning that the bank owes a duty of care to its customers. This implies that the bank is obligated to ensure the safety of the lockers.

In the landmark case of **Amitabha Dasgupta vs United Bank of India**, the National Consumer Disputes Redressal Commission held that the bank couldn't be seen as a landlord merely providing space. Instead, the bank's relationship with the customer for locker services is that of a bailor and bailee.

However, the liability of the bank has certain limitations. The bank cannot be held responsible if the loss of the contents of the locker is due to reasons beyond its control, such as a natural disaster or an act of war. But in case the loss is due to the bank's negligence, as in the given case, where the lockers were broken into by miscreants, the bank can be held liable for the loss.

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The Reserve Bank of India, recognizing the nature of the relationship, has issued guidelines to the banks for the operation of safe deposit lockers and the liability for loss of contents of lockers. The bank's liability for any loss or damage to the contents of the locker due to its negligence would depend on whether the bank has complied with these guidelines.

In conclusion, while the hiring of a locker in a bank can constitute a contract of bailment, the bank's liability is contingent upon whether the loss occurred due to its negligence.

Difference Between Bailment and Agency

While both bailment and agency are types of special contracts under the Indian Contract Act, 1872, they differ in their nature, purpose, and the relationship between the involved parties.

Bailment: As defined under Section 148 of the Act, a bailment is a contract where a person delivers goods to another person for a specific purpose, with the understanding that the goods will be returned or disposed of once the purpose is accomplished.

The key aspects of a bailment are:

1. It involves the transfer of possession of goods from the bailor (person delivering the goods) to the bailee (person to whom goods are delivered).
2. The goods are delivered for a specific purpose and

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are returned once that purpose is accomplished.

3. The bailor and bailee's relationship involves duties and obligations towards the goods, such as the duty of care.

Agency: An agency, as defined under Section 182 of the Act, is a contract where a person, known as the agent, is employed by another person, called the principal, to do an act on his behalf or to represent him in dealings with third parties.

The key aspects of an agency are:

1. It involves the creation of a fiduciary relationship, where the agent acts on behalf of the principal.
2. The agent can create legal relations between the principal and third parties.
3. An agency can be created expressly or impliedly and can even be created by ratification, necessity, or by the operation of law.

In conclusion, while both bailment and agency involve some form of relationship and duty, they differ significantly. A bailment involves the delivery of goods for a specific purpose, whereas an agency involves a person representing another in dealings with third parties.

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Q4: (A) A AND B ARE CARPENTERS. THEY DECIDE TO WORK TOGETHER. BUT THEY HAVE AN AGREEMENT UNDER WHICH A WILL KEEP ALL THE PROFITS AND PAY B A PREDETERMINED SALARY. HERE, A AND B ARE NOT PARTNERS. EXPLAIN THE NATURE OF AGREEMENT BETWEEN A AND B AFTER EXPLAINING THE ESSENTIALS OF PARTNERSHIP.

(B) A HINDU UNDIVIDED FAMILY "XYZ" WANTS TO BE THE PARTNER OF A FIRM "BCD". ADVISE XYZ, A HINDU UNDIVIDED FAMILY BY REFERRING THE PROVISIONS OF INDIAN PARTNERSHIP ACT.

(a) Essentials of Partnership and the Agreement Between A and B

According to the Indian Partnership Act, 1932, a partnership is the relation between persons who have agreed to share the profits of a business carried on by all or any of them acting for all. Therefore, the essentials of a partnership are:

1. **Agreement between two or more persons:** There must be a valid contract between two or more persons competent to contract.
2. **Business:** There must be a business to be conducted. 'Business' includes every trade, occupation, or profession.

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3. **Sharing of profits:** The agreement should be to share the profits of the business.
4. **Mutual agency:** The business must be carried on by all partners or by any of them acting for all. This is known as the principle of 'mutual agency'.

Now, when we apply these essentials to the agreement between A and B, we see that they meet some but not all of the requirements. While A and B have agreed to conduct a business together, which meets the first two requirements, their agreement deviates from the third and fourth essentials.

In their case, B is paid a predetermined salary and does not share the profits of the business. This arrangement does not meet the criteria of 'profit sharing' as required in a partnership. Furthermore, if B is simply a salaried employee without any decision-making power, he cannot represent A or make decisions that bind the business, thus missing the 'mutual agency' aspect.

Therefore, their agreement seems to constitute an employer-employee relationship rather than a partnership. In this relationship, A is the employer (business owner) who bears the business risk and B is the employee, who gets a fixed salary irrespective of profit or loss.

The Supreme Court of India in **Duli Chand v. Commissioner Of Income-Tax, Delhi** has held that the sharing of profits or gross returns arising from a

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property does not of itself make the recipients partners. They do not become partners until they join in conducting the business.

Q4 (b) **Hindu Undivided Family (HUF) and Partnership**

A Hindu Undivided Family (HUF) is a unique legal and social institution. Under Hindu law, an HUF is a family with all members lineally descended from a common ancestor and includes their wives and unmarried daughters. HUF itself is not recognized as a 'person' under the Indian Partnership Act and cannot become a partner in a partnership firm.

However, a Karta, or the head of an HUF, can represent the HUF in a partnership. The Karta can enter into a partnership with others on behalf of the HUF. But it is essential to remember that it is the individual (Karta) who is recognized as the partner and not the HUF.

In the case of **Commissioner of Income Tax v. Bagyalakshmi & Co**, the Madras High Court held that an HUF itself cannot enter into a partnership, but the Karta of an HUF can enter into a partnership on behalf and for the benefit of the HUF.

Furthermore, it's also important to note that other members of the HUF cannot be partners in the same firm where the Karta is a partner representing the HUF, as their liability would be unlimited, and it could lead to a situation of conflict of interest.

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Thus, advising the HUF "XYZ", it can be said that while the HUF itself cannot become a partner of the firm "BCD", the Karta of the HUF can enter into a partnership with "BCD" on behalf of and for the benefit of the HUF.

Q5: (A) A, B, C AND D MADE A CONTRACT OF PARTNERSHIP TO CARRY ON THE BUSINESS OF BANKING IN DWARKA SECTOR 16, NEW DELHI. IT WAS DISCOVERED THAT A DEVELOPED ILLICIT RELATIONSHIP WITH FEW LADY CUSTOMERS OF THE BANK. B ONE OF THE PARTNERS FILED A SUIT TO SEEK THE DISSOLUTION OF THE PARTNERSHIP ON ACCOUNT OF THIS MISCONDUCT OF PARTNER A. DECIDE WITH REASON AND WITH THE HELP OF DECIDED CASES WHETHER THE PARTNERSHIP MUST BE DISSOLVED OR NOT?

(B) WHETHER THE DEATH OF ONE OF THE PARTNERS IN A PARTNERSHIP CONSISTING OF ONLY TWO PARTNERS WILL DISSOLVE THE FIRM?

(a) Dissolution of Partnership due to Misconduct of a Partner

The Indian Partnership Act, 1932, provides for the dissolution of a partnership firm in several circumstances. Under Section 44(d), a court may dissolve a partnership firm on a suit by a partner when a partner,

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other than the partner suing, has been guilty of conduct that is likely to affect prejudicially the carrying on of the business.

In the present case, A's illicit relationships with the lady customers may indeed affect the business's reputation, affecting its operations prejudicially. As banking is an industry that relies heavily on trust and reputation, A's conduct could potentially harm the firm's standing and customer relations.

The Supreme Court, in the case of **Kushal Pal Singh Mann vs Ramesh Chander Anand**, held that the court could order dissolution if the conduct of a partner is likely to affect the business prejudicially.

However, it's important to note that the court exercises discretion when deciding on such matters. The partner seeking dissolution (in this case, B) would have to show that A's misconduct has indeed had a detrimental effect on the business.

Given the nature of A's conduct, it's reasonable to argue that such behavior, particularly in a banking environment where ethical conduct and professionalism are essential, could cause reputational harm to the business, leading to a loss of customers and revenue. Consequently, the court might rule in favor of B and order the dissolution of the partnership.

Q5 (b) Dissolution of a Partnership Firm Due to the Death of a Partner

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The death of a partner in a partnership firm does have implications on the existence of the firm. As per Section 42(c) of the Indian Partnership Act, 1932, a firm is dissolved if constituted for a fixed term, by the death of a partner.

When it comes to a partnership firm with only two partners, the death of one partner would automatically result in the dissolution of the firm. This is because, by definition, a partnership involves two or more persons. If one of the two partners dies, the partnership can't continue with only one person. Therefore, in the case of a partnership firm consisting of only two partners, the death of one partner would indeed lead to the dissolution of the firm.

However, it's crucial to note that the surviving partner has the right to carry on the business. In this case, the relationship between the surviving partner and the legal heirs of the deceased partner would be governed by the terms of the partnership deed, if any exists. This would include provisions related to the payment of the deceased partner's capital contribution and his/her share of profits until the time of death.

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Q6: EXPLAIN THE RIGHTS OF AN UNPAID SELLER AGAINST THE GOODS AS WELL AS AGAINST THE BUYER PERSONALLY. SUBSTANTIATE YOUR ANSWERS WITH THE HELP OF STATUTORY PROVISIONS AND DECIDED CASES.

Rights of an Unpaid Seller

The Sale of Goods Act, 1930, defines an unpaid seller as a person who has sold the goods for a price but price has not been paid or a bill of exchange or other negotiable instrument has been received but the same has been dishonored. The rights of an unpaid seller against the goods are classified under two heads:

1. Where the property in the goods has passed to the buyer.
2. Where the property in the goods has not yet passed to the buyer.

Rights When Property in the Goods has Passed to the Buyer

When the property in the goods has passed to the buyer, the unpaid seller has two rights as per Section 46(1) of the Act:

i. **Right of Lien (Sections 47 to 49):** The seller can retain possession of the goods until payment is made. The right of lien can be exercised when goods are in the actual possession of the seller, in the possession of the seller as

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a bailee, or when buyer becomes insolvent.

ii. **Right of Stoppage in Transit (Sections 50 to 52):** When the seller has parted with the goods and they are in transit, he has a right to stop them in transit and regain possession, provided the buyer has become insolvent.

iii. **Right of Resale (Section 54):** The unpaid seller can resell the goods in the following situations: where the goods are of perishable nature, where the seller expressly reserves the right of resale in case the buyer defaults, and where the buyer has not paid the price within a reasonable time.

Rights When Property in the Goods has not Passed to the Buyer

If the property in goods has not passed, the unpaid seller may withhold delivery of the goods, as per Section 46(2) of the Act.

Rights Against the Buyer Personally

The rights of an unpaid seller against the buyer personally are under Sections 55 to 61:

i. **Suit for Price (Section 55):** Where under a contract of sale, the property in the goods has passed to the buyer and the buyer wrongfully neglects or refuses to pay for the goods according to the terms of the contract, the seller may sue him for the price of the goods.

ii. **Damages for Non-Acceptance (Section 56):**

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Where the buyer wrongfully neglects or refuses to accept and pay for the goods, the seller may sue him for damages for non-acceptance.

iii. **Repayment of Price (Section 59):** Where the seller has rightfully refused to deliver the goods due to the buyer's breach of contract, the seller may recover the price from the buyer where payment has been made.

iv. **Interest and Special Damages (Section 61):** In a suit for breach of the contract, the court may allow interest at such rate as it thinks fit on the amount of the price from the date of the payment of the price.

Relevant Case Law

In the case of **Keshavlal Lallubhai Patel Vs Lalbhai Trikumlal Mills**, the court held that the right of lien and stoppage in transit are not lost by part delivery of the goods. This means that even if part of the goods has been delivered, the unpaid seller still retains his right to the remainder of the goods until payment is made.

In another case, **Kaliaperumal Vs Visalakshi Achi**, the court held that the seller can exercise the right of lien even when he is in possession of the goods as an agent or bailee.

Therefore, it is clear that an unpaid seller is equipped with robust rights both against the goods and the buyer personally to secure the payment for the goods sold, thereby minimizing the risks associated with credit sales.

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Q7: (A) WHILE EXPLAINING THE TYPE OF CROSSING, EXPLAIN THE STATUS OF CHEQUE BEARING “NOT NEGOTIABLE” (SECTION 130).

(B) EXPLAIN THE STATUS OF FOLLOWING BY GIVING COGENT REASONING:

(I) WHAT IS THE STATUS OF POST-DATED CHEQUE?

(II) WHETHER A SIGNED BLANK CHEQUE IS A CHEQUE?

(III) WHAT IS THE STATUS OF A DRAFT?

(a) Cheque Bearing “Not Negotiable” (Section 130)

The term "crossing" in relation to cheques is elucidated in Section 123 to Section 131 of the Negotiable Instruments Act, 1881. A cheque is said to be crossed when two parallel transverse lines, with or without additional words, are drawn on the face of the cheque. A crossed cheque is a directive to the paying banker to pay the amount mentioned in the cheque through a banker only and not directly to the person presenting it at the counter.

There are two types of crossings, general and special. In a general crossing, the cheque bears across its face two parallel lines. The cheque can also include the words "and company" or any abbreviation thereof, between the lines. In a special crossing, in addition to the two parallel lines, the name of the banker is added.

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A cheque marked "not negotiable" can still be transferred, but the transferee does not get and cannot give a better title than the transferor. In simple terms, the phrase "not negotiable" serves as a warning to the person taking the cheque that he does so subject to any defect in the title of the transferor. This is elucidated in Section 130 of the Act.

Q8 (b) Status of Various Types of Cheques

(i) Status of Post-Dated Cheque

A post-dated cheque is one that carries a future date. It cannot be honoured by the banker until the date mentioned on the cheque. As per Section 5 of the Negotiable Instruments Act, 1881, 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. A cheque, being a variety of a bill of exchange, follows the same rule. A post-dated cheque is not payable till the date which is shown on the face of the said document. It will only become cheque on the date shown on it and prior to that it remains a bill of exchange under Section 5 of the Act.

(ii) Status of Signed Blank Cheque

A signed blank cheque, essentially, is an open cheque. It's a cheque signed by the drawer but with the other fields left blank. As per the provisions of Section 20 of the Negotiable Instruments Act, 1881, where the drawer or

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maker of a negotiable instrument leaves it incomplete and delivers it without filling the full context, he authorises the person in possession to make or complete it as he pleases for any amount. In this case, it becomes a valid cheque, provided it's completed by the person to whom it's given, within the authority conferred by the drawer.

(iii) Status of a Draft

A bank draft, often referred to as a banker's cheque, is a negotiable instrument wherein payment is guaranteed by the issuing bank. Since a bank issues it, a draft is safer for the payee because the responsibility for payment shifts from the account holder to the issuing bank. As per the Negotiable Instruments Act, 1881, a draft is considered a bill of exchange drawn by a bank, payable on demand. Thus, its status is similar to a cheque, with the additional guarantee by the issuing bank providing more security. This makes drafts a preferred method for significant transactions where the payer and the payee require additional safeguards.

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Q8: WHILE DISCUSSING THE PURPOSE OF ATTACHING CRIMINAL LIABILITY TO THE OFFENCE UNDER SECTION 138 OF THE ACT, WHICH IS MORE IN THE NATURE OF A CIVIL DISPUTE, EXPLAIN THE ESSENTIALS TO FILE A CRIMINAL COMPLAINT UNDER SECTION 138. SUBSTANTIATE YOUR ANSWERS WITH THE HELP OF STATUTORY PROVISIONS AND DECIDED CASES.

Purpose of Attaching Criminal Liability to Section 138 of the Act

Section 138 of the Negotiable Instruments Act, 1881, which deals with the dishonour of cheques for insufficiency of funds, attaches a criminal liability to what is generally a civil dispute. This was enacted with the aim of enhancing the credibility of cheques in commercial transactions, which forms the backbone of trade and commerce in today's world.

The underlying intention of the legislation is to penalize dishonesty and to promote faith in the efficacy of banking operations and credibility in transacting business on negotiable instruments. This section has been inserted to curb the growing menace of dishonour of cheques which were being used as a tool of dishonesty.

While the principal remedy available to the aggrieved party in case of dishonour of cheque is civil in nature, that is to say, the realisation of the amount of the cheque, criminal liability has been imposed to deter people from

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issuing cheques without having sufficient funds with them and causing unnecessary inconvenience and harassment to the payee.

The honour of a cheque is a trust that the drawer creates irrespective of the relations between the parties. It has been judicially held in the landmark case of *K. Bhaskaran vs. Sankaran Vaidhyan Balan (1999)* that the offence under Section 138 of the Act can be completed only with the concatenation of a number of acts. These acts are: 1) Drawing of the cheque, 2) Presentation of the cheque to the bank, 3) Returning the cheque unpaid by the drawee bank, 4) Giving notice in writing to the drawer of the cheque demanding payment of the cheque amount, 5) Failure of the drawer to make payment within 15 days of the receipt of the notice.

Essentials to File a Criminal Complaint under Section 138

To file a criminal complaint under Section 138 of the Act, the following conditions must be satisfied:

1. **The cheque must be drawn by the person on an account maintained by him** - The cheque must be issued by the person (drawer) in favour of another person (payee) to discharge a legally enforceable debt or liability.
2. **The cheque should have been presented to the bank within a period of three months** - From the date on which it is drawn or within the

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period of its validity, whichever is earlier.

3. **The cheque is returned by the bank unpaid** - This could be either because of the insufficiency of funds or it exceeds the amount arranged to be paid from that account by an agreement with that bank.
4. **A demand notice must be served within 30 days** - The payee must make a demand for the payment of the said amount of money by giving a notice in writing to the drawer of the cheque within 30 days of the receipt of information by him from the bank regarding the return of the cheque as unpaid.
5. **The drawer fails to pay the cheque amount within 15 days of receipt of the demand notice** - The drawer of the cheque fails to make the payment of the said amount of money to the payee within 15 days of the receipt of the said notice.

Only when the above conditions are met, does a statutory offence under section 138 gets constituted. The burden of proving that the cheque had been issued for discharge of a debt or liability is on the complainant.

One of the crucial issues that had arisen for consideration before the courts is the computation of '15 days' for making the payment. In the case of *Sil Import, USA vs. Exim Aides Silk Exporters, Bangalore*, the Supreme

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Court has held that the '15 days' have to be reckoned from the date of receipt of the notice by the drawer.

To conclude, Section 138 of the Act is a penal provision aimed at deterring individuals from issuing cheques without ensuring sufficient funds, thereby causing unnecessary inconvenience to the payee. It strikes a balance between prosecution and opportunities for amicable settlement and is an effective tool in maintaining the credibility of negotiable instruments in commercial transactions.



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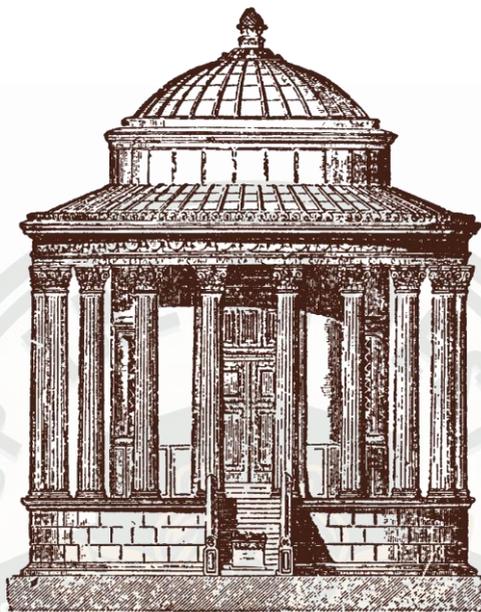
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UNIT 1

DUTIES OF INDEMNIFIER (SECTION 125)

PRIMARY DUTY

- Fundamental principles of marketing
- Foundation for creating, delivering value

CONDITIONS FOR LIABILITY

- Liability arises upon actual loss incurred by the indemnity-holder.
- Not contingent on whether the indemnity-holder has sued a third party.

SCOPE OF LIABILITY

- Determined by the terms of the indemnity contract.

LEGAL PRECEDENTS

- Duffield v. Scott: No need to prove direct or indirect nature of loss.
- Nallappa Reddi vs. Vridhachala Reddi: Duty arises as soon as a decree is passed against the promisee.



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Difference between Indemnity and Guarantee

Basis	Contract of Indemnity	Contract of Guarantee
Nature	Bipartite agreement	Tripartite agreement
Liability	Contingent upon loss	Conditional upon principal debtor's default
Parties	Two parties (indemnifier & indemnified)	Three parties (creditor, debtor, surety)
Purpose	Protects against specific losses	Ensures performance or payment obligations



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RIGHTS OF INDEMNIFIER (SECTION 125 & 126)

RIGHT OF SUBROGATION (SECTION 140)

- After compensating the indemnity-holder, the indemnifier can claim rights against third parties responsible for the loss.

RIGHT OF RECOUPMENT

- If loss occurs due to the fault of the indemnity-holder, the indemnifier can recover losses from them.

RIGHT TO CONTROL LEGAL DEFENSE

- The indemnifier can manage legal proceedings related to claims.

RIGHT TO BE COMPENSATED FOR DAMAGES

- The indemnifier is entitled to recover all damages or losses incurred in fulfilling their duties under the indemnity agreement.



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By Revocation (Section 130)

- A continuing guarantee can be revoked by the surety for future transactions by giving notice to the creditor.

By Death of Surety (Section 131)

- The death of the surety acts as a revocation for future transactions in a continuing guarantee.

Discharge of Principal Debtor (Section 134)

- A surety is discharged if any contract between the creditor and principal debtor releases the principal debtor from their obligation.

Variation in Terms of Contract (Section 133)

- If the terms of the contract between the creditor and principal debtor are altered without the consent of the surety, the surety is discharged from liability for future transactions.

Composition (Section 135)

- If the creditor makes a composition or promises not to sue the principal debtor, the surety is discharged unless they consented to such an arrangement.

Creditor's act/omission (Section 139)

- If the creditor performs an act inconsistent with the rights of the surety or fails to act when required, impairing the surety's eventual remedy against the principal debtor, they are discharged.

GROUNDS
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Duty to Take Care of Goods (Section 151)

The bailee must take as much care of the bailed goods as a person of ordinary prudence would take of their own goods.

DUTIES OF BAILEE

Duty to Return Any Accretion to Goods (Section 163)

The bailee must return any increase or profit that has accrued from the goods (excluding expenses incurred by the bailee).

Duty Not to Make Unauthorized Use (Section 154)

The bailee must use the goods only for the purpose stipulated in the contract.

Duty to Return the Goods (Section 160)

The bailee must return or deliver the bailed goods according to the bailor's directions once the purpose has been accomplished or time period has expired.

Duty Not to Mix Bailor's Goods (Sections 155, 156, 157)

The bailee must not mix the bailor's goods with their own or with those of others without consent, otherwise the bailee is liable to pay for the loss.

Right to Recover Expenses (Section 158)

The bailee has the right to recover necessary expenses incurred for the preservation of the bailed goods.

RIGHTS OF BAILEE

Right to Return Goods in Cases of Joint Bailers (Section 165)

If multiple owners bail goods, the bailee may return them to one owner without needing consent from all joint owners unless specified otherwise.

Right to Lien (Sections 170, 171)

The bailee has the right to retain possession of the goods until they receive due remuneration for services rendered.

Right to Compensation (Section 159)

If the bailor wrongfully deprives the bailee of using the goods, the bailee is entitled to compensation from the bailor.

Right to Indemnification (Sections 164, 167)

The bailee has the right to receive compensation from the bailor for any harm incurred due to faults in the goods.

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ESSENTIAL ELEMENTS OF AGENCY

AGREEMENT BETWEEN PRINCIPAL AND AGENT

- There must be an agreement between the principal and agent.
- It may either be express or implied agreement

LEGAL PURPOSE

- The agency must be for a legal purpose; any agency formed for illegal acts is void.

INTENTION TO ACT AS AGENT AND PRINCIPAL

- Both the agent and principal must intend to enter into an agency relationship.

CONTROL OF THE PRINCIPAL

- The principal has the right to control the actions of the agent.
- The agent must act according to the principal's directions.

COMPETENCY OF PRINCIPAL

- The principal must be competent to contract (Section 183).
- He/she must be of age and sound mind; minors or mentally unstable individuals cannot be principals.

NO FORMAL CONSIDERATION REQUIRED

- An agency can be established without any payment to the agent; no formal consideration is necessary.

FIDUCIARY RELATIONSHIP

- The relationship is fiduciary, meaning it is based on trust and confidence.



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UNIT 2

DUTIES OF PARTNERS

Duty to Act in Good Faith (Section 9)

Partners must conduct the business for the greatest common advantage, be just and faithful to each other, and provide true accounts and full information affecting the firm.

Duty to Work Without Remuneration (Section 13(b))

Partners are not entitled to remuneration for participating in business unless otherwise agreed in the partnership deed.

Duty to Indemnify for Loss Caused by Fraud (Section 10)

Partners must indemnify the firm for any loss caused by their fraud in conducting business.

Duty to Contribute to Losses (Section 13(b))

Partners must contribute equally to losses sustained by the firm unless agreed otherwise.

Duty to Attend Diligently to Duties (Section 12(b))

Each partner is bound to diligently attend to their responsibilities in managing the firm's business.

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ESSENTIAL ASPECTS OF PARTNERSHIP

CONTRACTUAL RELATIONSHIP

- Established through a partnership agreement (partnership deed), which can be oral or written.

SHARING OF PROFITS

- Profit Sharing Ratio:** Defined in the partnership deed; if unspecified, profits and losses are shared equally (Section 13(b)).
- Sharing profits is a fundamental characteristic of partnerships.

BUSINESS ENTITY

- The partnership must be formed for conducting a business, which includes any trade, occupation, or profession (Section 2(b)).

MUTUAL AGENCY

- Each partner acts as both an agent and principal; actions taken by one partner in the ordinary course of business bind all partners.

UNLIMITED LIABILITY

- Partners have unlimited liability; personal assets may be used to settle the firm's debts if necessary.
- Each partner is jointly and severally liable for the obligations of the partnership.

VOLUNTARY REGISTRATION

- Registration is not mandatory but beneficial for legal recognition and certain advantages.

NUMBER OF PARTNERS

- At least two persons are required to form a partnership.
- Maximum Limit:** Maximum of 50 partners as per the Companies Act, 2013; exceeding this requires registration as a company.



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RIGHT TO TAKE PART IN CONDUCTING THE BUSINESS (SECTION 12(A))

- Every partner has the right to participate in managing the firm's business.

RIGHT TO BE CONSULTED (SECTION 12(C))

- Decisions affecting the business must be made with the consent of all partners.

RIGHT TO REMUNERATION (SECTION 13(B))

- No partner is entitled to remuneration for participating in business unless agreed upon in the partnership deed.

RIGHT TO INTEREST ON CAPITAL (SECTION 13(C))

- A partner is not entitled to interest on their capital unless provided for in the agreement.

RIGHT TO INTEREST ON ADVANCES (SECTION 13(D))

- Partners can receive interest at a rate of six percent per annum on any advances made beyond their capital contribution.

RIGHT TO SHARE IN PROFITS (SECTION 13(B))

- Every partner has a right to share in the profits of the firm.

RIGHT TO ACCESS AND INSPECT BOOKS (SECTION 12(D))

- Every partner has the right to access and inspect the firm's books.

INDIVIDUAL RIGHTS OF PARTNERS



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INCOMING PARTNERS

SECTION 31

1

Admission of a New Partner

-The admission of a new partner does not dissolve the existing partnership; it creates a reconstituted firm.

-Admission can only be made with the consent of all existing partners.

2

Liability of New Partner

-The new partner is not liable for any acts of the firm done before their admission.

-Liability is only for acts done after joining the firm.

3

Rights of New Partner

-Unless agreed otherwise, the new partner does not have rights to existing firm property but acquires a share in future profits.

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OUTGOING PARTNERS

Retirement of a Partner (Section 32)

- A partner may retire with consent from all other partners or as per the partnership agreement. In a partnership at will, notice must be given to all partners.

Expulsion of a Partner (Section 33)

- A partner can be expelled by a majority if such power is conferred by an express agreement and exercised in good faith.

Insolvency of a Partner (Section 34)

- If a partner becomes insolvent, they cease to be a partner from the date of adjudication.

Rights of Outgoing Partner

- Entitled to share in profits made until the date of retirement.
- Has the right to carry on a competing business unless restricted by agreement (Section 36).

Liability of Outgoing Partner

- An outgoing partner remains liable for acts done before retirement unless public notice is given or an agreement releases them from liability.

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CONSEQUENCES OF DISSOLUTION

Settlement of Accounts (Section 48)

- Upon dissolution, assets are used to settle accounts in this order:
 - a. Debts to third parties.
 - b. Loans and advances by partners.
 - c. Capital contributed by partners.
 - d. Any surplus divided among partners in their profit-sharing ratio.

Continuing Authority for Winding Up (Section 47)

- Partners retain authority to complete transactions necessary for winding up affairs.

Return of Premium on Premature Dissolution (Section 37)

- If a partner has paid a premium for a fixed term and the partnership is dissolved prematurely, they may be entitled to a return of some or all of that premium.



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UNIT 3

IMPLIED CONDITIONS

Condition as to Title (Section 14)

- The seller must have the right to sell the goods. If a buyer's possession is challenged by someone with a better title, they can sue for breach.

Sale by Description (Section 15)

- Goods sold by description must correspond with that description. If they do not, the buyer can reject them.

Sale by Sample (Section 17)

- In sales conducted via samples, the bulk must match the sample in quality and be free from defects that are not apparent upon reasonable inspection.

Condition as to Merchantable Quality (Section 16(2))

- When goods are purchased by description from a seller who regularly sells such goods, there is an implied condition that they will be of merchantable quality.

Condition as to Fitness for Purpose (Section 16(1))

- If a buyer informs the seller of a specific purpose for which they require goods and relies on the seller's expertise, there is an implied condition that those goods will be fit for that purpose.

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ADV. SHIVANG VERMA

Difference between Sale and Agreement to Sell

Basis	Sale	Agreement to Sell
Transfer of Property (Ownership)	Ownership is transferred immediately at the time of the contract. Represents a completed transaction.	Ownership transfer occurs at a future time or upon fulfillment of certain conditions. Represents an incomplete transaction.
Risk and Responsibility	Risk transfers to the buyer immediately upon sale, even if the goods remain with the seller.	Risk remains with the seller until conditions are met and ownership is transferred.
Consequences of Breach	If breached, the buyer can sue for delivery; if the buyer fails to pay, the seller can sue for the price (Section 55).	If breached by the seller, the buyer can only claim damages; if the buyer fails to accept, the seller can sue for damages (Section 56).
Insolvency of Buyer/Seller	If the buyer becomes insolvent before payment, ownership has already transferred, and goods must be delivered to the official receiver.	If the buyer becomes insolvent before payment, the seller can refuse delivery as ownership has not yet been transferred.
Right of Resale	Seller cannot resell goods as ownership is with the buyer. Any resale would not confer a better title (Section 29).	Seller retains ownership and can resell goods; subsequent buyers acquire good title (unless otherwise agreed).



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IMPLIED WARRANTIES

WARRANTY OF QUIET POSSESSION (SECTION 14(B))

Unless otherwise stated, there is an implied warranty that the buyer shall have and enjoy quiet possession of the goods. If a third party lawfully disturbs this possession, the buyer can sue the seller for breach of warranty.

WARRANTY OF FREEDOM FROM ENCUMBRANCES (SECTION 14(C))

There is an implied warranty that goods shall be free from any charge or encumbrance in favor of any third party that was not disclosed to the buyer before or at the time of the contract.

WARRANTY AS TO QUALITY OR FITNESS BY USAGE OF TRADE (SECTION 16(3))

An implied warranty regarding quality or fitness for a specific purpose may arise from customary trade practices or previous dealings between the parties.

WARRANTY IN CASE OF SALE BY SAMPLE (SECTION 17)

In sales conducted via samples, there is an implied warranty that the bulk will correspond with the sample in quality and that buyers will have a reasonable opportunity to compare them. Additionally, goods must be free from defects that would not be apparent upon reasonable examination.

Goods Identified and Agreed Upon (Section 19)

- Property is transferred to the buyer at the time intended by both parties. This intention can be express or implied

DETERMINATION OF PASSING OF PROPERTY

Sale by Approval or "on Sale or Return" (Section 24)

- In a sale on approval or "sale or return," ownership passes when the buyer signifies approval or acceptance to the seller or takes any action adopting the transaction.

Goods Must be in a Deliverable State (Section 20)

- Ownership passes to the buyer when the contract is made, regardless of payment or delivery timing, unless otherwise stated in the contract.

Unascertained Goods and Appropriation (Section 23)

- For unascertained goods, property does not transfer until they are ascertained and unconditionally appropriated to the contract, either by seller consent with buyer assent or vice versa.

Goods to be Put in a Deliverable State (Section 21)

- If specific goods require actions by the seller to make them deliverable, ownership does not pass until those actions are completed and the buyer is notified.

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RIGHTS OF UNPAID SELLER AGAINST GOODS

Right of Lien (Sections 47-49)

- The unpaid seller has the right to retain possession of the goods until payment is made in certain situations:
 - When goods are sold without any credit stipulation.
 - When goods are sold on credit but the credit term has expired.
 - When the buyer becomes insolvent.

Right of Stoppage in Transit (Sections 50-52)

- If the buyer becomes insolvent after the seller has parted with possession, the unpaid seller may stop the goods in transit and reclaim possession as long as they are still in transit.

Right of Resale (Section 54)

- The unpaid seller may resell the goods under specific circumstances, such as when:
 - The goods are perishable.
 - The seller notifies the buyer of their intention to resell and does not receive payment within a reasonable time.



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RIGHTS OF UNPAID SELLER AGAINST BUYER SECTION 55, 56, 61

1

Suit for Price (Section 55)

-If property in the goods has passed to the buyer and they refuse to pay, the seller can sue for the price.

2

Damages for Non-Acceptance (Section 56)

-If a buyer wrongfully neglects or refuses to accept and pay for goods, the seller can claim damages.

3

Suit for Interest (Section 61)

-In cases of breach by the buyer, an unpaid seller can sue for interest and special damages.

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UNIT 4

CONDITIONS TO BE HOLDER IN DUE COURSE

Must be a holder

Absence of suspicion
about defects

Instrument acquired
before maturity

In good faith

Acquiring instrument for
consideration



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KINDS OF NEGOTIABLE INSTRUMENTS

SECTIONS 4, 5, 6

1

Promissory Notes

-Written instrument (not being a bank-note or currency-note) containing an unconditional promise, signed by the maker, to pay a certain sum of money to a specified person or to the bearer

2

Bills of Exchange

-Instrument in writing that contains an unconditional order, signed by the maker, directing a certain person to pay a specified sum of money only to a designated person or bearer. It serves as a demand for payment from a third party.

3

Cheques

-A bill of exchange drawn on a specified banker and payable on demand. It instructs the bank to pay a specific amount from the drawer's account to the person named on the cheque or to the bearer.

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MATERIAL ALTERATIONS AND CROSSING OF CHEQUE

Important section regarding Material alterations - Section 87

- Section 87 states that any material alteration of a negotiable instrument renders it void against anyone who is a party to the instrument at the time of the alteration and does not consent to it.

Exceptions to Material Alteration

- Alterations made with consent is allowed.
- Non-material alterations do not create any liability.
- Filling up blanks is also permissible.

Types of Crossing

- **General crossing** - When two parallel lines are drawn. This type of crossing does not specify any particular bank to which the cheque should be presented, allowing it to be presented by any bona fide holder.
- **Special crossing (S. 124)** - A cheque is considered specially crossed when it bears the name of a specific bank

DISHONOUR OF CHEQUE (SECTIONS)

Section 138

If a cheque drawn by a person on an account maintained by him is returned unpaid due to insufficient funds, the drawer shall be deemed to have committed an offence.

Section 142

This section specifies conditions for filing a complaint under Section 138. The complaint must be made by the payee or holder in due course within one month from when the cause of action arises.

Section 139

This section presumes that the holder of a cheque received it for the discharge, in whole or in part, of any debt or other liability unless proven otherwise.

Section 141

This section extends liability for dishonour offences to companies, firms, or associations of individuals.

Section 140

It states that it is not a valid defence in prosecution under Section 138 that the drawer had no reason to believe that the cheque might be dishonoured.

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ADV. SHIVANG VERMA



MR. MOHIT TANWAR, FOUNDING MENTOR, TTS

Mohit Tanwar, a distinguished scholar, holds the prestigious Indraprastha Research Fellowship (IPRF) from Guru Gobind Singh Indraprastha University, New Delhi and is currently pursuing a Ph.D. in law at the University School of Law Legal Studies, GGS IP University, specialising in Digital Payments and Corporate Governance. As an esteemed IPRF scholar at USLLS, he possesses knowledge in diverse legal subjects, including Alternative Dispute Resolutions (ADR), Law of Tort, Code of Civil Procedure, Constitutional Law & Criminal Law. Mohit is the visionary Founding

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ADV. SHIVANG VERMA

Mentor of Top The Semester (Formerly, Verdict Vault), a legal Ed-Tech platform dedicated to enlightening minds and fostering success. He is active in the field of Web3, Crypto and Blockchain Technology since the year 2014, in both academic and practical fields.



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ADV. MOHIT TANWR

ADV. SHIVANG VERMA



MR. SHIVANG VERMA, FOUNDER, TTS

Mr. Shivang Verma is an accomplished legal professional with a wealth of expertise and brings a dynamic perspective to Top The Semester (Formerly, Verdict Vault). He is passionate about enhancing legal education and empowering the next generation of legal minds. As a lawyer dedicated to innovation and excellence, he embodies Top The Semester's commitment to reshaping the future of legal learning.



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