



SYLLABUS

Class: - B.B.A. IV Semester

Subject: - Indian Legal System for Business

UNIT - I	The Indian Contract Act, 1872: Essentials of a Valid Contract, Void and Voidable Agreements, Performance of Contracts, Breach of a Contract and Its Remedies, Quasi- Contracts. Indemnity and Guarantee, Bailment and Pledge, Contract of Agency.
UNIT - II	The Sale of Goods Act. 1930: Formation of a Sales Contract.
UNIT - III	Negotiable Instrument Act, 1881: Definition and Essential Features of Negotiable Instruments, Types of Instruments and Endorsement, Parties to Negotiable Instrument.
UNIT - IV	Consumer Protection Act- Provisions related to consumer protection and Redressal of consumer Grievances
UNIT - V	Evolution of Indian Companies Act, 1956, The Companies Act, 1956: Types of Companies, Memorandum and Article of Association, Shareholders and Debenture Holders, Minority Protection, Winding-up
UNIT - VI	Law of Partnership: Definition and Nature of Partnership, Formation of Partnership, Rights, Duties and Liabilities of Partners, Dissolution of Partnership Firm.



UNIT-I THE INDIAN CONTRACT ACT 1872

The law of contract in India contained in Indian Contract Act 1872, which is based on English common Law. It extends to whole of India except the state of Jammu and Kashmir. It came into force on the first sep., 1872. The Act lays down general principles governing all contracts, but not the rights and duties of the parties. The rights and duties are decided by the parties themselves.

Scheme of the Act – The scheme can be divided into two main groups –

1. General principles of the law of contract. (Section 1-75)
2. Specific kinds of contracts viz. (section 124-238)
 - a. Indemnity and Guarantee
 - b. Contracts of Bailment and Pledge
 - c. Contract of Agency.

Meaning and Definition of an Agreements

An Agreement consist of an offer by one party and its acceptance by other words, an agreements comes into existence only when one party make a proposal to the other party and that other party gives acceptance.

Agreement = Proposal + Acceptance of proposal

According to section 2(e) of Indian Contract Act 1872 “Every promise and every set of promise forming the consideration for each other is an obligation.”

Meaning and Definition of a Contract –

A contract is a promise or set of promise for the breach of which the law given a remedy or the performance of which the law in some way recognize as duty. In other words, a contract is an agreement the object of which is to create a legal obligation. The contract consists of two elements.

1. An Agreement and
2. Legal obligation i.e. enforceability by law

Contract = An Agreement + enforceability by Law

According to section 2(h) of the Indian Contract Act 1872 “An agreement enforceable by law is a contract.”

Essential Elements of a Valid Contract –

1. Offer and Acceptance – there must be a “lawful offer” and a “lawful acceptance” of the offer, thus resulting in an agreement.
2. Intention to create legal relation – there must be an intention among the parties that the agreement should be attached by legal consequences and create legal obligations. Social agreements do not contemplate legal relations, and so they do not give rise in a contract.
3. Lawful Considerations – An Agreement is legally enforceable only when each of the parties to it gives something and gets something. This something is the price to the promise and is called consideration.
4. Capacity of parties – The parties to an agreement must be competent to contract; otherwise it cannot be enforced by a court. To be competent the parties must be on majority age and sound mind and must not be disqualified from contracting by any law to which they are subject. ‘
5. Free Consent – “Consent “means that the parties must have agreed upon the same thing in the same sense. Consent is not enough for making a contract. That must be free. It is said to be free when it is not caused by –
 - (i) Coercion, or (ii) undue influence, or (iii) fraud, or (iv) misrepresentation, or (v) mistake.



6. Lawful object – For the formation of a valid contract, it is also necessary that the parties to an agreement must agree for a lawful object. The object must not be fraud or illegal or immoral or must not imply injury to the person or property of other.
7. Writing and Registration – Generally the contracts may be oral or written. But in special cases, it lays down that the agreement must be in writing or registered to be valid.
8. Certainty – an agreement can be enforced, if its meaning is certain or capable of being made certain, agreements the meaning of which is not certain are void.
9. Possibility of performance – the terms of the agreement must also be capable of performance physically as well as legally.
10. Not expressly declared void – the agreement must not have been expressly declared void under the act. There are some types of agreements which have been expressly declared to be void.

Kinds of classification of Contracts

A. On the basis of Enforceability

1. **Valid contract** – A valid contract is an agreement enforceable by law. An agreement becomes enforceable by law when all the essential elements of a valid contract are present.
2. **Voidable Contract** – “An agreement which is enforceable by law at the option of one or more of the parties, but not at the option of one or more of the other, is a voidable contract.”
3. **Void Contract** – Void means not binding in law. It is at the time of making it but becomes void subsequently due to change in circumstances.
Void Agreement – “An agreement not enforceable by law is said to be void”. Thus a void agreement does not give rise to any legal consequences and is void an initio.
“Void Agreement” should be distinguished from “Void Contract”. A voids agreement never becomes a contract as it is void from beginning but a void contract is valid when it is entered into, but later on something happens which makes it unenforceable by law.
4. **Unenforceable contract** – It is one which is valid in itself, but is not capable of being enforced in a court of law because of some technical defect such as absence of writing, registration requisite stamp.
5. **Illegal or unlawful contract** – An agreement is illegal and void if its object or consideration, (a) is forbidden any law, or (b) is of such nature that it would defeat the provisions of any law; of (c) is fraud; (d) involves injury to the other person or property of other person.

B. On the basis of Creation

1. **Express Contract** – Where both the offer and acceptance making an agreement enforceable at law made in word spoken or written, it is an express contract. Ex. A says to B on phone that he want to sell his car for Rs. 50,000 and B accepts that offer. It is an Express Contract.
2. **Implied Contract** – where both the offer and the acceptance constituting an agreement enforceable at law are made otherwise than in words i.e. by act or conduct it is an implied contract.
3. **Constructive or Quasi Contract** – It is not a contract made intentionally by the parties by exchange or promise. It is a contract imposed by the law. The basis of this contract is that no one can allowed to enrich him at the cost of the other.

C. On the basis of Execution

1. **Executed Contract** – When both the parties to a contract have completely performed their share of obligations and nothing remains to be done by either party under the contract.
2. **Executor Contract** – When either party have still to perform their share of obligation in to or there remains something to be done under the contract on both sides.

Distinction between an Agreement and a contract

Basis of distinction	Agreement	Contract
1. Definition	Every promise and every set of promises forming consideration for each other is agreement	An agreement enforceable by law is a contract



2. Creation	An agreement is created by acceptance of an offer.	Agreement and its enforceability together create a contract
3. Legal rights and obligation	An agreement may not create legal rights and obligations of the parties	A contract creates legal rights and obligation between the parties.
4. Necessity	No contract is required to make an agreement	Valid agreement is necessary for making a contract
5. Legally binding	An agreement is not a concluding or legally	A contract is a concluding or legally binding on the parties.
6. Concept	Agreement is a wider concept and includes contracts.	Contract is a narrow concept and it is only a specific of agreement.

Distinction between an Agreement and Void contract

Basis of distinction	Agreement	Void contract
1. Definition	An agreement not enforceable by law is said to be void (Sec. 2(g))	A contract which ceases to be enforceable by law becomes void when it ceases to be enforceable [Sec. 2(j)]
2. Time when becomes void	It is void from every beginning	It becomes void subsequently due to change in law or change in circumstances.
3. Restitution	Generally no restitution is granted, however, the Court may on equitable grounds grant restitution in case of fraud or misrepresentation by minors.	Restitution may be granted when the contract is discovered to be void or becomes void.
4. Description in the Act	Such agreement has been mentioned as void in the Act. Agreement without consideration, agreements with lawful object or consideration and some other agreements have expressly been declared to be void.	There is no mention of cases of void contracts in the Act. They are created by circumstances and law Courts decide whether they have become void or not.

Distinction between Void Agreement and Voidable contract

Basis of distinction	Void Agreement	Voidable contract
1. Definition	An agreement not enforceable by law is said to be void.	A contract enforceable by law at the option of the aggrieved party is a voidable contract.
2. Period of validity	It is void from the beginning i.e. void ab initio	It is valid till it is avoided by the aggrieved party to the contract.
3. Legal existence	It is nullity, hence, does not exist in the eye of law.	It has its existence in the eye of law till it is repudiated.
4. Change in status	Status of void agreement does not change with the change in circumstances.	Status of such contract change when the aggrieved party elects to avoid it within a reasonable time. It becomes void when the aggrieved party elects to rescind it.
5. Causes	Any agreement is void when it is made with incompetent parties or for unlawful objects and consideration, or without consideration, or without consideration or it is expressly declared to be void under the law.	A contract is voidable when the consent of the party is caused by coercion or undue influence or fraud or misrepresentation.



6. Transfer of title	The party obtaining goods under void agreement cannot transfer a good title to the third party	The party obtaining goods under voidable agreement can transfer a good title to the third party if the third party obtains it in good faith and for consideration and the aggrieved party has not avoided the contract before such transfer.
7. Restitution	Parties do not have right to restore the benefits passed on to the other unless the parties were unaware of the impossibility of performance at the time of arrangement or the party to the agreement was minor.	Generally, right restitution is available if the party elects to avoid the contract.
8. Damages	No party as a right to get compensation for damages because such agreement has no legal effect.	If a party rightfully rescinds (i.e. puts and end) the contract, he can claim compensation, he can claim compensation of damages sustained by him due to non-fulfillment of the promise.

Distinction between Void and Voidable contract

Basis of distinction	Void Contract	Voidable contract
1. Definition	A contract which ceases to be enforceable by law becomes void, when it ceases to be enforceable.	A contract which is enforceable by law at the option of the aggrieved party is a voidable contract.
2. Period of validity	It remains valid till it does not cease to be enforceable.	It remains valid if the aggrieved party does not elect to avoid it within a reasonable time.
3. Will of the party	Its validity is not affected by the will of any party. It is decided by the Law court	Its validity is affected by the will of the aggrieved party. Aggrieved party has option to treat it either Binding or repudiate it.
4. Causes	Contracts become void due to change in circumstances or in the law of land.	Contract is voidable when the consent of the party is caused by coercion, undue influence, fraud or misrepresentation. Sometimes, it may be voidable under provisions of the sections 36, 53 and 55.

Distinction between Void an Illegal Agreement

Basis of distinction	Void Agreement	Illegal Agreement
1. Definition	An agreement not enforceable by law is void	An agreement which is expressly or impliedly prohibited by law is illegal.
2. Effect on collateral agreement	The agreement collateral to the void agreement is not necessarily void.	The agreement collateral to an illegal agreement is always void.
3. Scope	All void agreements need not necessarily be illegal agreements. Hence, the scope is wider than that of the illegal agreements.	All illegal agreements are void.
4. Restitution	The court may grant restitution of money advanced it is minor or if the parties were unaware of the impossibility of performance of the agreement.	Restitution of money is not granted in case of an illegal agreement.



Performance contract

Two parties enter into a legal contract with a view to fulfilling objectives in the form of reciprocal promise. After the formation of a contract, the next normal step in the contractual course is the doing of the piece of work which has been promise to do by each party.

In other words, the parties have to perform their respective legal obligation arising out of the contract.

According to section 37 of the contract act prescribes that "The parties to a contract must either perform or offer to perform their respective promises, unless such performance is dispensed with or excused under the provision of this act or of any other law".

Non performance will amount to a breach of contract if the performance is dispensed with or excused its legal consequence is a discharge from the obligations.

Types of performance

1. Actual performance – When a party to a contract has done, what he had under taken to do their remains nothing to be done by him, the promise is said to have been actually performed by him and the liability to such party comes to an end.
2. Attempted performance or tender – When the performance becomes due and the promisor offers to perform his obligation under the contract at the proper time, place and in the proper manner, but the promisee does not accept or refuses to accept the performance such attempt made by the promisor is known as 'Attempted Performance' or 'Tender'.

Kinds of Tender –

- a. Tender of goods or services
- b. Tender of money

Essentials or Rules of valid Tender (Attempted Performance)

1. It must be unconditional
2. It must be made at a proper opportunity of inspection of goods
3. It must provide proper opportunity of inspection of goods
4. A 'Tender' must be for the whole obligation
5. It must be made to a proper person
6. It must to be made in proper form
7. The person making a 'Tender' must be able and willing to perform his obligation.

Effect of Refusal to Accept offer of Performance (To Accept Tender) – (Section-38) – Lays down that where a promisor has made an offer of performance to the promisee but the promisee has not accepted the offer; the promisor is not responsible for non-performance, and more over dose not there by lose his rights under the contract".

Effect to Refusal of party to perform promise wholly

According to section-39 of the contract act when a party to a contract has either refuses to perform or disabled himself from performing the promise in its entirety (completely or wholly) the promise may put an end to the contract. If he has not signified by word or by conduct his acceptance.

"He may put an end to the contract" in the below courses of action –

1. He may refuses to perform his part of the promise
2. He may reject the incomplete work done by the promisor and refuses to pay for the same or may refuse further deliveries.
3. He may return the defective goods.
4. He may treat the refusal to perform as breach and sue for damages.

Who can demand performance	By whom contract must be performed
1. Promisee	1. Promisor himself
2. Legal Representative	2. Legal Representative
3. Third Party	3. Agent



4. Joint Promisee	4. Third Person
5. Authorized Person	5. Authorized Person

Performance of Joint Promises – When two or more persons enter into a contract with one or more persons. The promises under such a contract are known joint promises; the conditions regarding the performance of joint promises may be discussed as follows –

1. Devolution (passing or transfer) of joint liabilities (section-42)
2. Any one from the joint promisor may be compelled to perform (section-43)
3. Right and liabilities of joint promisors, among themselves (Section-43)
4. Release of a joint promisor and its effect (Section-44)
5. Devolution of joint rights

Performance of reciprocal promises – “Promises which form the consideration or part of the consideration for each other are called reciprocal promises.”

Kinds of reciprocal promises and the relevant rules regarding their performance may be discussed as follows–

1. Mutual and concurrent promises (section 51)
2. Mutual and independent promises (section 51)
3. Mutual dependent promises (Section 51)
4. Order of performance of reciprocal promises (Section 52) – These promises are to be performed is expressly fixed by the contract and it must be performed in that order.
5. Effects of preventing a party from performance of his promise (section 53) – the contract becomes voidable at the option of the party so prevented is entitled to compensation from the preventing party for any loss which he may sustain as a result of the non-performance of his promise.
6. Effect of default in relation to that promise which of should be performed first (Section-54) – Where the nature of reciprocal promises is such that one of them cannot be performed till the other party has performed his promise then if the other party fails to perform it, he cannot claim the performance of the reciprocal promise from the first party.
7. Reciprocal promise to do thing legal and also other thing illegal (Section-57) – The first set of promises is a contract but the second is a void agreement.
8. Promises in which one branch is legal and the other illegal (Section 57) – The legal branch alone can be enforced by law.

Time and Place for Performance

Rules regarding time & place in contract

1. Performance of the promise where ‘no time’ is specified and no request is made by the promisee than the contract in such cases must be performed within a reasonable time which is decided on the basis of the circumstances (Section-46)
2. Performance of promise where time is specified but no request is to be made by the promisee than in such cases the promisor may perform the promise at any time during the usual hours of business on the fixed day and at the place at which the promise should be performed (Section-47)
3. Performance of promise where ‘time is specified’ but a ‘request is to be made’ by the promisee in such cases it is the duty of the promisee to apply for performance at a proper place and within the usual hours of business (section-48)
4. Performance of promise where no place is specified also and no request is to be made by the promisee. In such cases it is the duty of the promisor to apply the promisee to fix or decide a reasonable place for the performance of the promise and then to perform it at such place (section 49)



5. Performance of the Promise where the manner and time is prescribed in such cases the performance of promise must be made in the prescribed manner and at the prescribed time (Section 50)

Performance where time is an Essential factor (time as the essence of contract) – when time as the essence of contract means that the time is an essential factor and therefore the concerned parties must perform their promises within the specified time.

Time is generally considered to be the essence of the contract in the following cases –

1. Where the parties have expressly agreed to treat the time as the essence of the contract
2. Where the delay in performing the promise operates as an injury to the party.
3. Where the nature and the necessity of the contract requires the time to the essence of the contract.

When time is not the essence of contract in the following cases –

1. Where the parties have not agreed to treat the time as the essence of the contract
2. Where the delay in performing the contract does not have an effect as an injury to the party.
3. Where the nature of the contract does not establish that time is the essence of contract neither there is any other necessity to make it so.

(According to section-55)

- A. Effect of failure to performance within fixed time where time is the essence of the contract than the contract becomes voidable at the option of the Promisee.
- B. Effect of failure to perform within fixed time where time is not the essence of the contract than the contract does not become voidable however, the promisee is entitled to compensation from the promisor for any loss suffered by him due to such failure.
- C. Effect of acceptance of performance at a time other than that agreed and resulting the contract become voidable however if he opts to accept the performance after the agreed time he cannot claim compensation for any loss suffered by him due to the non performance of the promise at the agreed time.

Contracts which need not be performed

1. When its performance become impossible (section 56)
2. When the concerned parties agree to substitute a new contract in its place or agree to cancel or alter it (section 62).
3. When the promises releases from performance either wholly or in part or extends the time for its performance or accepts any other satisfaction in place (section 63)
4. When it become voidable and the person at whose option it is voidable & rescinds (cancel) (Section 64)
5. When the promises neglects or refuses to afford the promisor reasonable facilities for its performance (section 67)
6. When it is illegal

Appropriation of payments:

Appropriation of a payment means setting a part of payment for a specific use.

1. Application of payment where the debt to be discharged is indicated or instruction is given then the payment is to be applied to the discharge of some particulars debt (section-59).
2. Application of payment where the debt to be discharged is not dictated then the payment is applied according to creditor's discretion to any lawful debt actually due and payable to him from the debtor the amount may be applied to a dept which has become time barred (section-60)
3. Application of payment where neither the debtor nor the creditor makes any appropriation then the Payment shall be applied in discharge of the debts in 'order of time, whether they barred or



not barred by the existing law of limitation, if debts are of equal standing (of the same date) the payment shall be applied in discharge of each proportionately.

When the rights and obligations arising out of a contract are extinguished, the contract is said to be discharged or terminated. A contract may be discharged by any of the following ways –

1. By performance – Actual or Attempted
2. By mutual consent or arrangement
3. By subsequent or supervening impossibility or illegality
4. By lapse of time
5. By operation of law
6. By breach of contract

A. **Discharge by Performance** – Performance of a contract is the most popular manner of discharge of a contract. The performance may be either Actual performance of attempted performance.

1. **Actual Performance** – When each party fulfils his obligations arising out of the contract within the time and in a manner prescribed, it is called the actual performance and the contract comes to an end.
2. **Attempted performance or Tender** – When the promisor offers to perform his obligation, but is unable to do so because the promisee does not accept the performance, it is called “Attempted performance” or “tender”. Thus tender is not actual performance but is only an offer to perform the obligation under the contract. A valid tender of performance is equivalent to performance.

Essentials of a valid tender – It fulfills the following conditions –

1. It must be unconditional – If A who is a debtor of company B, offers to pay if share are allotted to him at par. It is not a tender.
2. It must be made at proper time and place – A is tenant of B. A offers him rent at a marriage party. B is not bound to accept as tender is not made at a proper place.
3. It must be of the whole obligation contracted for and not only of the part – e.g. deciding of his own to pay in the installments and offering the first installment was held invalid tender as it was not of the whole amount due.
4. If the tender related to the delivery of good it must give a reasonable opportunity to the promisee for inspection of goods so that he may be sure that the goods tendered are of contract description.
5. It must be made by a person who is in a position and is willing to perform the promise.
6. It must be made to the proper person i.e. the promisee or his authorized person.
7. If there are several joint promises, an offer to any one of them is a valid tender (but the actual payment must be made to all joint promises and not to any one of them).
8. In case of tender of money, exact amount should be tendered in the legal tender money.

Effect of refusal to accept a valid tender – The effect of refusal to accept a properly made “offer of performance” is that the contract is deemed to have been performed by the promisor. And the promisee can be sued for breach of contract. Thus we can say that “a valid tender discharges the contract.”

B. **Discharge By Mutual Consent or Agreement** – A contract is created by means of an agreement, it may also be discharged by another agreement between the same parties.

1. **Novation** – “Novation occurs when a new contract is substituted for an existing contract, either between the same parties or different parties, the consideration mutually being the discharge of the old contract.” If the parties are same, then small changes in the terms of contract are called “alteration” and not “Novation”. For being “Novation”, the changes must be of significant nature. Novation cannot be compulsory; it can only with the mutual consent of all the parties.
2. **Alteration** – It means that change of one or more of the material terms of a contract. A material alteration is one which alters the legal effect of the contract e.g. change in the amount of money, change in the rate of interest etc.

Note that a material contract made in a contract by one party without the consent of the other



will make the whole contract void and no person can maintain alteration upon it.

3. **Rescission** – A Contract may be discharged before the date of performance, by agreement between the parties to the effect that it shall no longer bind them. Such an agreement amounts to "Rescission" or cancellation of the contract, the consideration being the abandonment by the respective parties of their rights under the contract. Example A promises to deliver Some goods to B on say 14th Nov. 2006. But before the date of performance i.e. 14th Nov. 2006, A and B mutually agree that the contract will not be performed. The contract stand discharged by rescission.
Note – in rescission, the existing contract is cancelled by mutual consent without substituting a new contract in its place.
 4. **Remission** – It is defined as "Acceptance of Lesser amount than what was contracted for or it lesser fulfillment of the premise made"
 5. **Waiver** – It means deliberate giving up of a right which a party is entitled to under a contract where upon the other party to the contract is released from his obligation. Example a Promise to stitch a shirt for B if B sings a song in A's party and accepting if B sings a song in A's party. Then later on B says there is no need to stitch shirt for me to which A gives his consent. Thus the contract is terminated.
- C. **Discharge By Subsequent or Supervening Impossibility or Illegality** – Impossibility at the time of contract. If you contract for something impossible the agreement is void ab initio the promisee knows about the impossibility after using reasonable efforts the promisor is bound to compensate the promise for any loss he may suffer because of non performance of the promise, even if the agreement being void ab initio.
Subsequent impossibility is found out after the contract is made, "A contract to do an act which after making the contract, become impossible or unlawful, becomes void when the act becomes impossible or unlawful."
Conditions for It...
1. The act should have become impossible.
 2. The impossibility should be by reason of some event which the promisor could not prevent.
 3. The impossibility should not be self induced by the promisor or due to negligence.
- To be impossible, it is sufficient that it becomes impracticable or extremely hazardous or unless from the point of view of the object and purpose which the parties had in view,
If the performance of a contract becomes impossible by reason of supervening imposition or illegality of the act it's logical to absolve the parties from further performance of it as they never did promise to perform impossibility.
- D. **Discharge by Lapse of time** – In some circumstances, the lapse of time may also discharge a contract, e.g. the period of limitation for simple contracts is three years under the limitation Act and therefore on default by a debtor, if the creditor does not file a suit for a recovery against him within three years of default the debt becomes time barred and the creditor will not get the help of the law. This in effect discharges the contract.
Where the time is of essence, if the contract is not performed on time, the contract comes to an end, and the party not at fault need not perform his obligation and may sue the other party for damages.
- E. **Discharge by operation of law** – A contract is discharged by operation of law in the following cases –
1. Death – Sometimes a contract involves personal skills of promise. In such cases the contract is discharged on the death of the promisor.
 2. Insolvency – When a person is adjudged Insolvent then he is released from his all his previous liabilities. His rights (Assets) and liabilities are transferred to the official assignee or official receiver as the case may be.
 3. Merger – Sometimes, inferior right of a person is merged into superior right contract, in such a case the inferior, right is vanished and is not required to be enforced. For example an ordinary debt can be merged. In order of ownership in such case the inferior rights need not to be enforced because these rights have merged to a superior right of mortgage or ownership.



4. Loss of evidence of contract – If the evidence of the existence of the contract is lost or vanished. The contract is discharged; for example document of contract is lost or destroyed and no other evidence is available the contract is discharged.
- F. **Discharge by Breach of contract** – A contract is something discharged, by its breach generally breach of contract means refusal of any one party to perform his contractual obligations under the contract specially a breach of contract occurs when a party to a contract does any of the following things
 1. Fails or refuses to perform his obligation under the contract
 2. Disable him from performing his contract.
 3. Make the performance of contract impossible by his own acts

BREACH OF CONTRACT

Meaning – A breach of contract occurs if any party refuses or fails to perform his part of contract or by his act makes it impossible to perform his obligation under the contract.

In case of breach, the aggrieved party is relieved from performing his obligation and gets a right to proceed against the party at fault.

TYPES OF BREACH OF CONTRACT

Anticipatory breach of contract – Anticipatory breach of contract occurs when the party declares his intention of not performing the contract before the due date of performance.

A party can declare the intention of anticipatory breach of contract by following ways

1. A party can refuse to perform promise.
2. Party can disable himself from performing promise in its entirety

OPTIONAL AVAILABLE TO AGGRIEVED PARTY

- (a) Rescind the contract and claim damages for breach of contract without waiting until the due date of performance.
- (b) Treat the contract as operative and wait till the due date of performance.
- (c) Treat the contract as operative and wait till the due date of performance and claim damages if the promise still remains unperformed.

Actual breach of contract – Actual breach of contract takes place in following ways –

- (a) On due date of performance – If any party to contract refuses or fails to perform his part of contract at the time fixed for performance. It is called an actual breach of contract on due date of performance.
- (b) During the course of performance – If any part has performed a part of the contract and then refuses or fails to perform the remaining part of the contract. It is called an actual breach of contract during the course of performance.

Remedies for breach of contract

A remedy is a method or process prescribed or provided by law for the enforcement of a right of the aggrieved or injured party. Thus, the process of enforcing of a right of the injured party is known as remedies for breach of contract. Remedies are the courses of action which may be pursued by the aggrieved party. The aggrieved or injured party is that person in the contract who is not involved in the breach and has been adversely affected by it.

When there is actual breach, one or more of the following remedies are available to the aggrieved party.

- a. Rescission of the contract
- b. Suit for damages or monetary compensation
- c. Suit upon quantum meruit.
- d. Suit for specific performance of the contract
- e. Suit for injunction.
- f. Restitution of benefit.



1. **Rescission of the Contract** – Section 39 of the Contract Act lays down that when a party to a contract has refused to perform or has disabled him from performing his promise in its entirety; the promisee may put an end to the contract. This is called the right of rescission which means a right to set aside (i.e. reject) the contract. When the aggrieved party rescinds the contract, he is discharged from the obligation under the contract
2. **Suit for damages** – Damages is the monetary compensation which is been paid by the party breaching the contract to the aggrieved party for any kind of loss occurring due to breach of contract. The object of awarding damages is not to punish the party at fault but to the recovery of financial loss occurring to aggrieved party. Following kinds of damages can be claimed in case of breach of contract.

Amount of Damages

Amount of damages are calculated in following ways:

S.No	Options	Amount of Damages
1	When the aggrieved party rescinds the contract at the date of breach	The amount of damages will be equal to the difference between the price prevailing on the date of breach and the control price.
2	When the aggrieved party does not rescind the contract at the date of breach	The amount of damages will be difference between price on date of performance and the contract price.

- a. **Ordinary Damages** – Ordinary damages also called general damages. These are those damages which arise as a result of breach of contract. General damages are such damages which the law presumes from the breach of contract. They are awarded to compensate the injured party and not to punish party at fault. These damages are assessed on the basis of actual loss suffered by the party i.e. difference between contract price and market price of such goods to breach of contract. Ex: X contracted to sell 50 tons of wheat @ 8000 Rs. Per ton to y on 1st Jan. Afterward y contracted to sell those goods to Z @ Rs 10000 per ton. X fails to deliver goods on 1st Jan when price of wheat was 9500Rs per ton. Y is entitled to receive 75000 Rs. i.e. $(9500-8000 \times 50)$ as ordinary damages i.e. difference between contract price and market price.
- b. **Special damages** – Special damages are those damages which are result of unusual circumstances affecting party and their interest. These are the damages which the parties know when they made the contract as likely to arise from the breach of contract. These damages can be recovered if special circumstances which would result in special loss of breach of contract. In case of loss aggrieved party to contract can claim for such damages only when an advance notice of such damages is given before.
- c. **Exemplary or punitive or vindictive damages** – These are those damages which are given in nature of punishment. The court may award these damages in case of
 1. Breach of promise to marry
 2. Wrong full dishonor of a Cheque by banker.
- d. **Nominal Damages** – Nominal damages are those damages which are awarded where there is only a technical relation but aggrieved party has not suffered any loss because of breach of contract.
- e. **Damages for Inconvenience and discomfort** – If a party has suffered any physical inconvenience and discomfort due to breach of contract, that party can recover the damages for the same discomfort.
- f. **Liquidated damages & penalty** – Liquidated damages is the specified sum which represents a fair and genuine pre-estimate of the damages likely to arise due to breach. Penalty is disproportionate sum to damages likely to result due to breach. These specified sum is payable by the party responsible for breach and is been decided at the time of formation of contract. In India there is no distinction between penalty and liquidated damages. In English law, liquidated damages are enforceable and penalty is unenforceable.



- g. Forfeiture of security deposit or (earnest money) – A clause in a contract which provides for forfeiture of security deposit in the event of failure to perform. In such cases, the court may award reasonable Compensation only.
- 3. Suit for quantum meruit – The phrase 'Quantum meruit' means payment in proportion to the 'amount of work done' A right to sue on quantum meruit arises where a contract, partly performed by one party has discharged by breach of the contract by other party.
- 4. Suit for specific performance – Suit for specific performance means demanding the court's direction to the defaulting party to carry out the promise according to the terms of the contract.

Cases where suit for specific performance is not maintained are

- a. Where damages are considered as an adequate remedy.
- b. Contract of personal nature.
- c. Contract beyond the scope of memorandum of association.
- d. Impossibility of court to supervise-the performance of the contract.
- e. Contract with minor.
- f. Inequitable contracts.
- 5. Suit for injunction: Injunction is the preventive relief. It is an order of the court restraining the Wrong door from doing continuing the wrongful complained of and not mentioned in contract. Injunction means an order of the court which prohibits a person to do a particular act.
- 6. Restitution, of Benefit – Restitution return or restoration of benefit received by one party from the other under a Void contract.

Measure of Damages

The general principle on which damages are assessed is that the injured party must be placed so far as Possible in the same position as he would occupied if no breach had taken place, but in applying this principle, the court will not necessarily award the relief to the plaintiff for all the damages he has suffered.

Meaning & Features of Quasi contracts

A Quasi contract is not a contract at all because one or the other essentials far the formation of contracts is absent. It is an obligation imposed by law upon a person for the benefit of one another even in the absence of a contract. It is based on the principle of equity, which means no person shall be allowed to unjustly enrich himself at the expense of another. Such obligations are called quasi contract.

Features of a Quasi Contract –

- a. It is imposed by law & does not arise from any agreement.
- b. The duty of a party and not the promise of any party is the Basis of Such contract.
- c. The right under it is always a right to money & generally, though not always, to a liquidated sum of money.
- d. The right under it is available against specific person & not against the world.
- e. A suit for its breach may be filed in the same way as in case of a completed contract.

Quasi contracts & other contracts

S.No	Basis of destination	Quasi contract	Contract
1	Essential for the formation of a valid contract	The essential for the formation of a valid contract are absent	The essential for the formation of a valid contract are present
2	Obligation	Obligation is imposed by law.	Obligation is created by the consent of parties.

Kinds of Quasi Contract –



- a. Right to recover or the Price of Necessaries supplied – The person who has supplied the necessaries to a person who is incapable of contracting or anyone whom such incapable person is legally bound to support, is entitled to claim their price from the property of such incapable person.
- b. Right to Recover Money period for another person – A person who is interested in the payment of money which another is bound by law to pay & who therefore pays it entitled to be reimbursed by the other.
- c. **Right to Recover for Non-Gratuitous Act** – Such right to recover arises if the following conditions are satisfied –
 1. The things must have been delivered lawfully.
 2. The person who has done or delivered the thing must not have intended to do so gratuitously.
 3. The person for whom the act is done must have enjoyed the benefit of the act.
- d. **Responsibility of finder of Goods** – A person, who finds goods belonging to another & takes them into his custody, is subject to the same Responsibility as a Bailee.
- e. **Right to recover from a person to whom money is paid or thing is delivered, by mistake or under coercion** – A person to whom money has been paid or anything delivered by mistake or under coercion, must repay or return it.

Quantum Meruit –

The term 'Quantum Meruit' means as much as merited or 'as much as earned'. In other words it means payment in proportion to the amount of work done. Generally one cannot claim performance from another unless one has performed his obligation in full but in certain cases, a person who has performed some work under a contract can claim remuneration for the work which he has already done.

Cases in which the claim of Quantum Meruit arises –

- a. In case of void agreements or contract that becomes void — When an agreement is discovered to be void or when a contract becomes void, any person who has received any advantage under such agreement or contract is bound to restore it, or to make compensation for it to the person from whom he received it
- b. In case of Non-Gratuitous Act — The obligation to pay arises in the following three conditions:-
 1. The thing must have been done or delivered lawfully
 2. The person who had done or delivered the thing must have intended to do so gratuitously.
 3. The person for whom the act is done must have enjoyed the benefit of the Act.
- c. In case of preventing the completion of contract – If a party does not complete the contract or prevents the other party to complete the contract the aggrieved party can sue on Quantum meruit.
- d. In case of Divisible Contract – The party at default may sue on a Quantum meruit the following conditions are satisfied.
 1. If the contract is divisible
 2. If the party not at default has enjoyed benefits of the part performance.
- e. In case of indivisible contract performed completely but badly.

INDEMNITY AND GUARANTEE CONTRACT

The contract of indemnity and guarantee are special kinds of contract. These contracts are therefore also required to fulfill all the essentials of a valid contract.

Indemnity Contract – Indemnity contract is a type of contingent contract. The term 'Indemnity' simply means 'Making Somebody Safe' or 'Paying Somebody back'.

Section 124 of contract Act defines that "A contract by which one party. Promises to save the other from loss caused to him by the conduct of the promise himself by the conduct of any other person, is called a contract of indemnity".

The party who gives indemnity or who promises to compensate for or to make good the loss, is called Indemnifier and the party for whose protection or safety the indemnity is given or the party whose loss is



made good is called 'Indemnified' or 'Indemnity holder'.

Important features of an indemnity contract -

1. Two party.
2. Promise for pay compensation of loss/damage.
3. Loss/damage may by the own or other person.
4. Creation of liability
5. All essential features of valid contract.
6. Compensation for actual loss/damages
7. It may be express or implied.

Loss/damages may be caused by some event or accident, or some natural phenomenon or disaster.

Rights to Indemnified (Indemnity Holder) -

1. Right to claim for all damages/losses
2. Right to claim for all costs which is related to contract
3. Right to claim for all sums which he may have paid for contract.

Liability/Duties of indemnified -

1. Liability to pay all damage/losses
2. Liability to pay all costs related to contract
3. Liability to pay all sums which is received by self for contract from indemnified.

Contract of Guarantee

The object of the contract of guarantee is to enable a person to obtain an employment, or a loan, or some goods or service on credit.

According to section 126 of the contract Act "A contract of guarantee is a contract to perform the promise, or discharge the liability, of a third person in case of his default."

The person who gives the guarantee is called the 'Surety' or 'Guarantor' & the person in respect of whose default the grantee is given is called the principal debtor, he is the party on whose behalf guarantee is given and the person to whom the guarantee is given is called the 'Creditor'.

Essential features of a Contract of Guarantee

1. Three parties
2. Three agreement
3. Concurrence of the three parties
4. It may be oral or written
5. Liability of surety is secondary is dependent on principal debtor's default.
6. Guarantee must be in the knowledge of principal debtor.
7. All essentials of a valid contract.
8. Guarantee must not be obtained by means of misrepresentation.
9. Existence of a primary liability.

Distinction between a Contract of Indemnity and Guarantee

S.No	Difference Basis	Indemnity Contract	Contract of Guarantee
1	Nature of Contract	Promises to save the other from loss	One party promises to discharge the liability of a third party in case of his default
2	No. of Parties	Only two parties are there	There are three parties
3	No. of Contract	There is only one contract	There are three contracts between debtors, creditors and surely
4	Nature of	The liability of the indemnifier is	The liability of the surety is secondary and



	Liability	primary and independent	dependent
5	Arising of Liability	Indemnifier's liability arises only on the happening of a contingency	Arises only after the default of debtor in payment
6	Existence of debt or duty	There is no existing debt or duty in this contract	There is always some existing debt or duty in this contract
7	Request by the debtor	It is not necessary for the indemnifier to act at the request indemnified.	The surely generally gives guarantee at the request of the debtor
8	Right to sue	The indemnifier cannot sue the third party for loss in his own name	It surety has discharged the debt after the default of the principal debtor; he becomes entitled to sue the debtor in his own name.

Kinds of Guarantee

1. **Specific or Simple Guarantee** – When a guarantee is given in respect of a single debt or specific transaction and it's to come an end when the guarantee debt is paid or the promise is duly performed. It is called a specific or simple guarantee.
2. **Continuing guarantee** – Section 129, of the contract Act defines a guarantee which extends to a series of transactions, is called a continuing guarantee. Thus, a continuing guarantee is not confined to a single transaction but keeps on moving to prevail transaction continuously.

Revocation of Guarantee – Revocation of guarantee means cancellation of guarantee already given. It may be noted that the specific guarantee cannot be revoked if the liability has already accrued. However a continuing guarantee can be revoked and on the revocation of such a guarantee. The liability of the surety or guarantor comes to an end for the future transactions. The surety continues to be liable for the transaction which have taken place up to the time of revocation.

A guarantee may be revoked in any of the following ways –

1. By notice of revocation
2. By death of surety
3. By discharge of surety in various circumstances
 - A. By novation (Sec. 62)
 - B. By variance in terms (Sec. 133)
 - C. By release/discharge of principal Debtor (Sec. 134)
 - D. When the creditor enters into an agreement with the principal debtor (Sec 135)
 - E. By creditor act or omission impairing surety's eventual remedy (Sec. 139)
 - F. By loss of security (Sec. 141)
 - G. By invalidation of contract (Sec 142, 143, 144)

Nature and Extent of Surety's Liability —

1. The liability of surety is co-extensive
2. The liability of surety arises the same moment when default is made by the principal debtor.
3. The, surely is free to restrict limit his liability.
4. Sometimes the surely is liable though the principal debtor is not liable.
5. If there is a condition precedent for the surety's liability; the surety will be liable, only when that condition is fulfilled first.
6. In a continuing guarantee liability of surety extends to a series of transaction over a period of time.
7. The surety will not be liable if the creditor has obtained guarantee either by misrepresenting a material fact regarding the transaction or by keeping silence to material circumstances.
8. A discharge of principal debtor by operation of law does not discharge the surety from liability.

Discharge of surety from liability -

The following are the modes or circumstances under which a surety is discharge from his liability -



1. By revocation
 - a. Notice by surety
 - b. Death of surety
 - c. Notation
2. By the conduct of the creditor
 - a. Variance (change) in terms of the contract
 - b. Release or discharge of the principal debtor
 - c. Certain arrangement made by the creditors with the principal debtors without the consent of surety
 - d. Creditors act or omission impairing surety's eventual (ultimate) remedy.
 - e. Loss of security
3. By invalidation of contract of guarantee
 - a. Guarantee obtained by misrepresentation
 - b. Guarantee by concealment
 - c. Failure of co-surety to join a surety

Bailment and Pledge

Bailment

The word 'bailment' is derived from the French word 'baillier' which means 'to deliver'. Etymologically, it means any kind of handling over'. In legal sense, it involves change of possession of goods from one person to another for some specific purpose.

Definitions of Bailment

Sec. 184 defines Bailment 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. The person delivering the goods is called the 'bailor' and the person to whom they are delivered is called the 'bailee'.

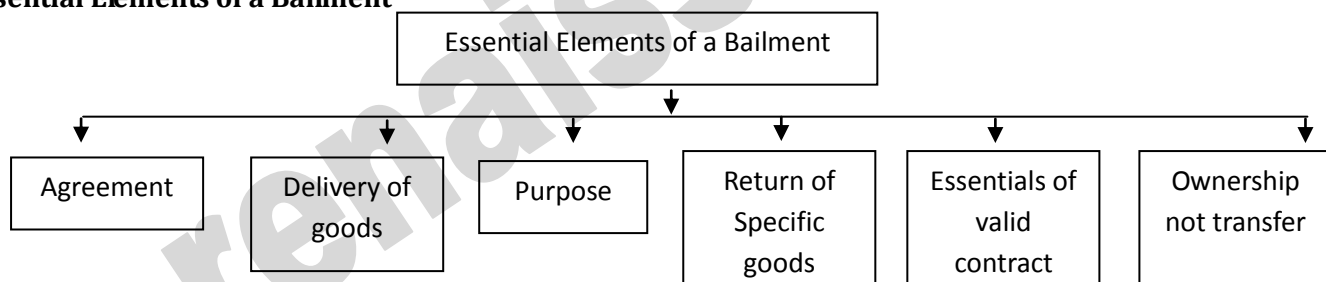
Examples

- (a) A delivers a piece of cloth to B, a tailor, to be stitched into a suit. There is a contract of bailment between A and B.
- (b) A sells certain goods to B who leaves them in the possession of A. The relationship between B and A is that of bailor and bailee.

Consideration in a contract of bailment

In a contract of bailment, the consideration is generally in the form of money payment either by the bailor or the bailee, as for example, when A gives his bicycle to B for repair, or when A gives his car to B on hire. Such consideration in money form, however, is not necessary to support the promise on the part of the bailee to return the goods. The detrainment suffered by the bailor, in parting with possession of the goods, is a sufficient consideration to support the contract of bailment.

Essential Elements of a Bailment



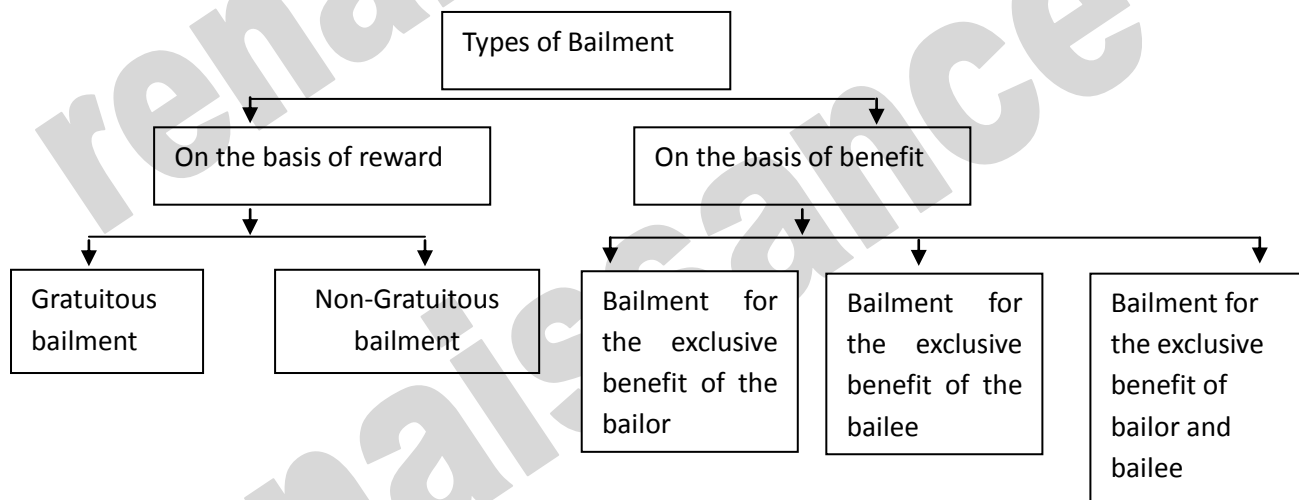


Distinction between Bailment and Contract of Sale

A contract of bailment differs from a contract of sale in the following respects:

S. No.	Basis of distinction	Bailment	Contract of Sale
1	Transfers of ownership/possession	There is only a transfer of possession of goods from the bailor to the bailee.	There is a transfer of ownership of goods from the seller to the buyer.
2	Consideration need not be passed	The consideration need not be passed between bailor and bailee.	The consideration in terms of price must be passed between seller and buyer.
3	Return of goods	The bailee must return the goods to the bailor on the fulfillment of the purpose for which the bailment is made.	There is no question of such return of goods in contract of sale.

Kinds/types of Bailment



DUTIES OF A BAILOR

- Duty to disclose defects [Section 151]
- Duty to bear expenses [Section 158]
- Duty to indemnify the bailee in case of premature termination of gratuitous bailment [Section 159]
- Duty to indemnify the bailee against the defective title of bailor [Section 164]
- Duty to receive back the goods [Section 164]
- Duty to bear the risk of loss [Section 152]

DUTIES OF A BAILEE

- Duty to take care of the goods bailed [Section 151 & 152]
- Duty not to make any unauthorized use of goods [Sections 154]
- Duty not to mix bailor’s goods with his own goods [Section 155 to 157]
- Duty to return the goods [Section 160 & 161]
- Duty to return accretions to the goods [Section 163]

Rights of a Bailor

1. Right to claim damages in case of negligence [Section 152]
2. Right to terminate the contract in case of unauthorized use [Section 153]
3. Right to claim compensation in case of unauthorized use [Section 154]
4. Right to claim the separation of goods in case of unauthorized mixture [Section 156]



5. Right to claim compensation in case of unauthorized mixture of goods which cannot be separated [Section 157]
6. Right to demand return of goods [Section 160]
7. Right to claim compensation in case of unauthorized retention of goods [Section 161]
8. Right to demand accretions to goods [Section 163]

RIGHTS OF A BAILEE

- Right to claim damages [Section 150]
- Right to claim reimbursement of expenses [Section 158]
- Right to be indemnified in case of premature termination of gratuitous bailment [Section 159]
- Right to recover loss in case of bailor's defective title [Section 164]
- Right to recover loss in case of bailor's refusal to take the goods back [Section 164]
- Right to deliver goods to any one of the joint bailors [Section 165]
- Right to deliver goods to bailor in case of bailor's defective title [Section 166]
- Right to particular lien [Section 170]

RIGHTS OF BAILOR AND BAILEE AGAINST WRONGDOERS

Rights of Bailor and Bailee against Wrongdoer [Section 180] If a third party wrongfully deprives a bailee of the use or possession of the goods bailed, or does them any injury, the bailee is entitled to such remedies as the owner might have used in the like case if no bailment had been made; and either the bailor or the bailee may bring a suit against a third person for such deprivation or injury.

Apportionment of Relief or Compensation Obtained by Such Suits [Section 181] whatever is obtained by way of relief or compensation in any such suit shall, as between the bailor and the bailee, be dealt with according to their respective interests.

Example X delivered a TV to Y for repairs. Z forcefully takes possession of TV from Y's shop. In this case, either X or Y may sue Z. If Y files the suit, he shall hand over the amount received after deducting his repair charges to X.

TERMINATION OF BAILMENT

I. Termination of every Contract of Bailment (whether Gratuitous or not)

Every contract of bailment comes to end under the following circumstances:

- (a) On the Expiry of Fixed Period
- (b) On fulfillment of the Purpose
- (c) Inconsistent Use of Goods
- (d) Destruction of the Subject Matter of Bailment

II. Termination of Gratuitous Bailment

A contract of gratuitous bailment is terminated in the following circumstances also.

- (a) Before the Expiry of a Fixed Period
- (b) On Death of Bailor/Bailee

Meaning of Lien

Lien means the right of a person having possession of goods belonging to another to retain those goods until the satisfaction of sum claimed by the person in possession of the goods. It may be noted that the possession of goods must be lawful and continuous. For example, X took Y's godown on a rent of Rs. 5,000 p.m on an agreement that X can at any time deposit or take out his goods from the godown. After six months, X stopped paying the rent. Y auctioned X's goods and claimed lien. Y cannot claim lien because it was agreed that X can take out his goods whenever he wanted.

Type of Lien

(a) Particular Lien [Section 170] a particular lien is a right to retain only those goods in respect of which some charges are due.

Example: - X gives a piece of cloth to Y, a tailor, to make a coat. Y promises X to deliver the coat as soon



as it is finished. Y is entitled to retain the coat till he is paid for (if he has not allowed any credit period) but is not entitled to retain the coat (if he has allowed one month's credit for the payment.)

(b) General Lien [Section 171] a general lien is a right to retain all the goods as a security for the general balance of account until the full satisfaction of the claims due whether in respect of those goods or other goods. The general lien is available to other persons only when there is an express contract to that effect.

Example: - X deposited US 64 units and shares of Reliance Industries Ltd. as security with Citi Bank and took a loan against the shares of Reliance Industries Ltd. Citi Bank may retain both the securities until its claim are fully satisfied.

Distinction between Particular Lien and General Lien

S. No.	Basis of distinction	Particular lien	General lien
1	Goods in respect of which lien available	It is available against those goods in respect of which some charges are due.	It is available against all goods whether in respect of which claims are due or not.
2	Purpose	It is available only for non-payment of remuneration for the services.	It is available for a general balance of account.
3	To whom available in the absence of contract to contrary	It is available to every bailee to whom the goods have been bailed.	It is available only to specific bailees like bankers, factors, Wharfingers, attorneys of High Court and policy brokers.
4	Rendering of service	It is available only when some service involving the exercise of labour or skill has been rendered.	It is available even when no such service has been rendered.
5	Purpose of delivery of goods	The purpose of delivery of goods is to confer an additional value as the goods bailed.	The purpose of delivery of goods is to deposit the goods as security.

FINDER OF GOODS

Finder of goods is the person who finds some goods which do not belong to him.

Example If X finds a purse or a diamond ring or a watch, which does not belong to him, he will be called as finder of goods.

Rights of a Finder of Goods

- Right to lien [Section 168]
- Right to sue for reward [Section 168]
- Right to sell [Section 169]

Duties of a Finder of Goods [Section 171]

Finder of goods is subject to the same responsibility as a bailee. The duties of a finder of goods are as follows:-

- Duty to take reasonable care
- Duty not to use for personal purpose
- Duty not to mix with his own goods
- Duty to find the owner

PLEDGE

Meaning of Pledge (or Pawn) [Section 172]

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

Example X borrows of Rs. 1,00,000 from Citi Bank and keeps his shares as security for payment of a debt. It is a contract of pledge.

Meaning of a pawnor (or Pledgor) [Section 172]



The person who delivers the goods as security for payment of a debt or performance of promise is called the pawnor or Pledgor. In aforesaid example X is pawnor

Meaning of Pawnee (or pledgee) [Section 172]

The person to whom the goods are delivered as security for payment of a debt or performance of a promise is called the Pawnee or Pledgee. In the aforesaid example. Citi Bank is the pawnee.

Rights of a Pawnee

- Right of retainer [Section 173]
- Right to claim reimbursement of extraordinary expenses [Section 173]
- Right to sue pawnor [Section 176]
- Right to sell [Section 176]
- Right against true owner [Section 178 A]

Duties of a Pawnee

- Duty to take reasonable care of the goods pledged
- Duty not to make unauthorized use of goods
- Duty not to mix pawnor’s goods with his own goods
- Duty to return goods
- Duty to return accretions to the goods

Rights of a Pawnor

- Right to get pawnee’s duties duly enforced
- Right to redeem [Section 177]

Duties of a Pawnor

- Duty to comply with the terms of pledge
- Duty to compensate the pawnee for extraordinary expenses [Section 175]

Distinction between Pledge and Bailment

Basis of distinction	Pledge	Bailment
1. Purpose	Pledge is bailment of goods for a specific purpose, i.e. repayment of a debt or performance of a duty.	Bailment is for a purpose of any kind.
2. Right to use	Pawnee cannot use the goods pledged.	Bailee can use the goods as per terms of bailment.
3. Right to sell	Pawnee can sell the goods pledge after giving notice to the pawnor in case of default by the pawnor.	Bailee can either retain the goods or sue the bailor for his dues.

Distinction between Pledges and Hypothecation

Hypothecation is also one of the modes of providing security. However, it is different from pledge in the following respects:

Basis of distinction	Pledge	Hypothecation
1. Possession of goods	Borrower transfers the possession of goods.	Borrower does not transfer the possession of goods.
2. Right to deal with the goods.	Borrower has no right to deal with the goods pledged.	Borrower has a right to deal with the goods hypothecated.



AGENCY

Meaning of Agency: Agency is relation between an agent and his principal created by an agreement.

Section 182 of the Contract Act 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".

Essential Features of Agency

1. The principal
2. The agent
3. An agreement
4. Consideration not necessary
5. Representative capacity
6. Good faith
7. The competence of the principal

Modes or Methods of Creation of Agency

1. **Agency by express agreement:** A contract of agency may be made by express words, whether written or oral.
2. **Agency by implied agreement:** "An authority is said to be implied when it is to be inferred from the circumstances of the case.
 - (a) **Agency by estoppels:** When a principal by his conduct or act causes a third person to believe that a certain person is his authorized agent, the agency is said to be an agency by estoppels.
 - (b) **Agency by necessity:** It means the agency which comes into existence when certain circumstances compel a person to act as an agent for another without his express authority.
 - (c) **Agency by holding out:** When a principal by his active conduct or act and without any objection permits another to act as his agent, the agency is the result of principal's conduct as to the agent.
3. **Agency by ratification:** Ratification means confirmation of an act which has already been done. Sometimes, an act is done by a person on behalf of another person but without another person's knowledge and authority. If he accepts and confirms the act, he is said to have ratified it.
4. **Agency by operation of law:** In certain circumstances the law treats a person as an agent of another person. For examples, (a) when a partnership is formed, every partner automatically becomes agent of another partner. (b) When a company is formed its promoters are treated as its agents by operation of law.

RIGHTS AND DUTIES OF AGENT

Rights of an Agent

1. Right to retain money received on principal's account.
2. Right to receive remuneration.
3. Right of lien on principal's property.
4. Right to be indemnified.
5. Right to compensation for injury caused by principal's neglect.

Duties of an Agent

1. To follow the directions of the principal.
2. To conduct the business of agency with reasonable skill and diligence.
3. To render accounts on demand
4. To communicate with the principal.
5. Not to deal on his own account



6. To pay the amounts received for the principal
7. Not to delegate his authority
8. Not to act in excess of authority
9. Duty on termination of agency by principal's death or insanity.

TERMINATION OF AGENCY

Termination of agency means revocation (cancellation) of authority of the agent. All the modes of termination of agency may be classified as:

(A) Termination of Agency by the Act of the Parties.

1. by revocation of authority by the principal
2. by renunciation (giving up) of business of agency by the agent.
3. by mutual agreement

(B) Termination of Agency by Operation of Law

1. Completion of business of agency
2. Death or insanity of principal or agent
3. Insolvency of the principal
4. Destruction of subject matter
5. Expiry of time
6. Agency subsequently becoming unlawful
7. Termination of sub agent's authority

Irrevocable Agency

When the authority of agent cannot be revoked by the principal, it is said to be an irrevocable agency. An agency is irrevocable in the following cases:

1. If the agency is coupled with interest : When an agent himself has a special interest in the property which forms the subject matter of the agency, such agency is said to be coupled with interest.
2. Where the agent has partly exercised his authority
3. When the agent has incurred a personal liability.



UNIT-II
SALE OF GOODS ACT, 1930

Contract of Sale of Goods

According to Section 4, a contract of sale of goods is a contract whereby the seller:

- (i) Transfers or agrees to transfer the property in goods
- (ii) To the buyer,
- (iii) For a money consideration called the price.

It shows that the expression "contract of sale" includes both a sale where the seller transfers the ownership of the goods to the buyer, and an agreement to sell where the ownership of goods is to be transferred at a future time or subject to some conditions onto be fulfilled later.

It is a bilateral contract because the property in goods has to pass from one party to another. A person cannot buy the goods himself. The object of a contract of sale must be the transfer of property (meaning ownership) in goods from one person to another.

The subject matter must be some goods. The goods must be sold for some price, where the goods are exchanged for goods it is barter system and it will not be considered as sale.

All essential elements of a valid contract must be present in a contract of sale.

Distinction between Sale and Agreement to Sell

The following points will bring out the distinction between sale and an agreement to sell:

- (a) In a sale, the property in the goods sold passes to the buyer at the time of contract so that he becomes the owner of the goods. In an agreement to sell, the ownership does not pass to the buyer at the time of the contract, but it passes only when it becomes sale on the expiry of certain time or the fulfillment of some conditions subject to which the property in the goods is to be transferred.
- (b) An agreement to sell is an executory contract; a sale is an executed Contract.
- (c) An agreement to sell is a pure and simple contract, but a sale is contract plus conveyance
- (d) In the case of an agreement to sell if the goods are destroyed by an accident, Seller will bear the loss, while in the case of a sale; the loss will fall on the buyer, even though the goods are with the seller.
- (e) If there is an agreement to sell and the seller commits a breach, the buyer has only a personal remedy against the seller, namely, a claim for damages. But if there has been a sale, and the seller commits a breach by refusing to deliver the goods; the buyer has not only a personal remedy against him but also the other remedies which an owner has in respect of goods themselves such as a suit for conversion or detinue, etc.

Sale and Bailment

A "bailment" is a transaction under which goods are delivered by one person (the bailor) to another (the bailee) for some purpose, upon a contract that they be returned or disposed of as directed after the purpose is accomplished (Section 148 of the Indian Contract Act, 1872).

The property in the goods is not intended to and does not pass on delivery though it may sometimes be the intention of the parties that it should pass in due course. But where goods are delivered to another on terms which indicate that the property is to pass at once the contract must be one of sale and not bailment.

Sale and Contract for Work and Labour

The test generally applied is that if as a result of the contract, property in an article is transferred to one who had no property therein previously, for a money consideration, it is a sale. Where it is otherwise it is a contract for work and labour.



Sale and Hire Purchase Agreement

"Sale", is a contract by which property in goods passes from the seller to the buyer for a price.

A "hire purchase agreement" is basically a contract of hire, but in addition, it gives the hirer an option to purchase the goods at the end of the hiring period.

The distinction between the two is very important because, in a hire-purchase agreement the risk of loss or deterioration of the goods hired lies with the owner and the hirer will be absolved of any responsibility therefore, if he has taken reasonable care to protect the same as a bailee. But it is otherwise in the case of a sale where the price is to be paid in installments.

Subject matter of Contract of Sale of Goods

Goods

According to Section 2(7) "goods" means every kind of movable property' other than actionable claims and money and includes stock and shares, growing crops, grass and things attached to or forming part of the land which are agreed to be served before sale or

Under the contract of sale.

Actionable claims and money are not goods and cannot be bought and sold under this Act. Money means current money, i.e., the recognized currency in circulation in the country, but not old and rare coins which may be treated as goods. An actionable claim is what a person cannot make a present use of or enjoy, but what can be recovered by him by means of a suit or an action. Thus, a debt due to a man from another is an actionable claim and cannot be sold as goods, although it can be assigned.

Goods may be (a) existing, (b) future, or (c) contingent. The existing goods may be (i) specific or generic, (ii) ascertained or unascertained.

Existing Goods

Existing goods are goods which are either owned or possessed by the seller at the time of the contract.

Existing goods are specific goods which are identified and agreed upon at the time of the contract of sale. Ascertained goods are either specific goods at the time of the contract or ascertained or identified to the contract later on i.e. made specific.

Generic or unascertained goods are goods which are not specifically identified but are indicated by description.

Future Goods

Future goods are goods to be manufactured or produced or acquired by the seller after the making of the contract of sale.

Contingent Goods

Where there is a contract for the sale of goods, the acquisition of which by the seller depends upon a contingency which may or may not happen - such goods are known as contingent goods. Contingent goods fall in the class of future goods.

Actual sale can take place only of specific goods and property in goods passes from the seller to buyer at the time of the contract, provided the goods are in a deliverable state and the contract is unconditional.

Effect of Perishing of Goods

In a contract of sale of goods, the goods may perish before sale is complete. Such a stage may arise in the following cases:

(i) Goods perishing before making a contract

Where in a contract of sale of specific goods, the goods without the knowledge of the seller have



perished, at the time of making of the contract or become as damaged as no longer to their description in the contract, the contract is void. (Section 7)

If the seller was aware of the destruction and still entered into the contract, he is stopped from disputing the contract. Moreover, perishing of goods not only includes loss by theft but also where the goods have lost their commercial value.

(ii) Goods perishing after agreement to sell

Where there is an agreement to sell specific goods and subsequently, the goods without any fault of any party perish or are so damaged as no longer to answer to their description in the agreement before the risk passes to the buyer, the agreement is thereby avoided. If the sale is of unascertained goods. The perishing of the whole quantity of such goods in the possession of the seller will not relieve him of his obligation to deliver. (Section 8)

Conditions and Warranties (Sections 10-17)

As a rule, before a contract of sale is concluded, certain statements are made by the parties to each other. The statement may amount to a stipulation, forming part of the contract or a mere expression of opinion which is not part of the contract. If it is a statement by the seller on the reliance of which the buyer makes the contract, it will amount to a stipulation. If it is a mere commendation by the seller of his goods it does not amount to a stipulation and does not give the right of action.

The stipulation may either be a condition or a warranty. Section 12 draws a clear distinction between a condition and a warranty.

Conditions

If the stipulation forms the very basis of the contract or is essential to the main purpose of the contract. it is a condition. The breach of the condition gives the aggrieved party a right to treat the contract as repudiated. Thus, if the seller fails to fulfill a condition, the buyer may treat the contract as repudiated, refuse the goods and, if he has already paid for them, and recover the price. He can also claim damages for the breach of contract.

Warranties

If the stipulation is collateral to the main purpose of the contract, i.e. it is a subsidiary promise, it is a warranty. The effect of a breach of a warranty is that the aggrieved party cannot repudiate the contract but can only claim damages. Thus, if the seller does not fulfill a warranty. the buyer must accept the goods and claim damages for breach of warranty.

Section 11 states that the stipulation as to time of payment are not to be deemed conditions (and hence not to be of the essence of a contract of sale) unless such an intention appears from the contract. Whether any other stipulation as to time (e.g., time of delivery) is the essence of the contract or not depends on the terms of the contract.

Implied Warranties/Conditions

Even where no definite representations have been made, the law implies certain representations as having been made which may be warranties or conditions. An express warranty or condition does not negative an implied warranty or condition unless inconsistent therewith.

There are two implied warranties:

Implied Warranties

(a) ***Implied warranty of quiet possession:*** If the circumstances of the contract are such as there is an implied warranty that the buyer shall have and enjoy quiet possession of the goods.

(b) ***Implied warranty against encumbrances:*** There is a further warranty that the goods are not subject to any right in favour of a third-party, or the buyer's possession shall not be disturbed by reason of the existence of encumbrances.

This means that if the buyer is required to, and does discharge the amount of the encumbrance,



there is breach of warranty, and he is entitled to claim damages from the seller.

Different implied conditions apply under different types of contracts of sale of goods, such as sale by description, or sale by sample, or sale by description as well as sample. The condition, as to title to goods applies to all types of contracts, subject to that there is apparently no other intention.

Implied Conditions as to title

There is an implied condition that the seller, in an actual sale, has the right to sell the goods, and, in an agreement to sell, he will have this right only when property is passed to him. As a result, if the title of the seller turns out to be defective, the buyer is entitled to reject the goods and can recover the full price paid by him.

Implied conditions under a sale by description

(a) Goods must correspond with description: Under Section 15, when there is a sale of goods by description, there is an implied condition that the goods shall correspond with description.

(b) Goods must also be of merchantable quality:

Merchantable quality means that the goods must be such as would be acceptable to a reasonable person, having regard to prevailing conditions. They are not merchantable if they have defects which make them unfit for ordinary use, or are such that a reasonable person knowing of their condition would not buy them.

But, if the buyer has examined the goods, there is no implied condition as regards defects which such examination ought to have revealed. If, however, examination by the buyer does not reveal the defect, and he approves and accepts the goods, but when put to work, the goods are found to be defective, there is a breach of condition of merchantable quality.

(c) Condition as to wholesomeness: The provisions, (i.e., eatables) supplied must not only answer the description, but they must also be merchantable and wholesome or sound.

(d) Condition as to fitness for a particular purpose: Ordinarily, in a contract of sale, there is no implied warranty or condition as to the quality of fitness for any particular purpose of goods supplied.

But there is an implied condition that the goods are reasonably fit for the purpose for which they are required if:

- (i) The buyer expressly or impliedly makes known the intended purpose, so as to show that he relies on the seller's skill and judgment, and
- (j) The goods are of a description which it is in the course of the seller's business to supply (whether he be the manufacturer or not). There is no such condition if the goods are bought under a patent or trade name.

Implied conditions under a sale by sample (Section 15)

In a sale by sample:

- (a) there is an implied condition that the bulk shall correspond with the sample in quality;
- (b) there is another implied condition that the buyer shall have a reasonable opportunity of comparing the bulk with the sample;
- (c) it is further an implied condition of merchantability, as regards latent or hidden defects in the goods which would not be apparent on reasonable examination of the sample. "

Implied conditions in sale by sample as well as by description

In a sale by sample as well as by description, the goods supplied must correspond both with the samples as well as with the description.



Implied Warranties

Implied warranties are those which the law presumes to have been incorporated in the contract of sale in spite of the fact that the parties have not expressly included them in a contract of sale. Subject to the contract to the contrary, the following are the implied warranties in the contract of sale:

- (i) **Warranty as to quiet possession:** Section 14(b) provides that there is an implied 'warranty that the buyer shall have and enjoy quiet possession of goods'. If the buyer's possession is disturbed by anyone having superior title than that of the seller, the buyer is entitled to hold the seller liable for breach of warranty.
- (ii) **Warranty as to freedom from encumbrances:** Section 14(c) states that in a contract for sale, there is an implied warranty that the goods shall be so free from any charge or encumbrances in favour of any third party not declared or known to the buyer before or at the time when the contract is made'. But if the buyer is aware of any encumbrance on the goods at the time of entering into the contract, he will not be entitled to any compensation from the seller for discharging the encumbrance.
- (iii) **Warranty to disclose dangerous nature of goods:** If the goods are inherently dangerous or likely to be dangerous and the buyer is ignorant of the danger, the seller must warn the buyer of the probable danger:
- (iv) **Warranties implied by the custom or usage of trade:** Section 16(3) provides that an implied warranty or conditions as to quality or fitness for a particular purpose may be annexed by the usage of trade.

Doctrine of Caveat Emptor

The term *caveat emptor* is a Latin word which means "let the buyer beware". This principle states that it is for the buyer to satisfy himself that the goods which he is purchasing are of the quality which he requires. If he buys goods for a particular purpose, he must satisfy himself that they are fit for that purpose. In simple words, it is not the seller's duty to give to the buyer the goods which are fit for a suitable purpose of the buyer. If he makes a wrong selection, he cannot blame the seller if the goods turn out to be defective or do not serve his purpose health.

Exceptions to the doctrine of Caveat Emptor:

- (1) Where the seller makes a false representation and the buyer relies on it.
- (2) When the seller actively conceals a defect in the goods which is not Visible on a reasonable examination of the same.
- (3) When the buyer, relying upon the skill and judgment of the seller, has expressly or impliedly communicated to him the purpose for which the goods are required.
- (4) Where goods are bought by description from a seller who deals in goods of that description.

Passing of Property or Transfer of Ownership (Sections 18-20)

The sole purpose of a sale is the transfer of ownership of goods from the seller to the buyer. It is important to know the precise moment of time at which the property in the goods passes from the seller to the buyer for the following reasons:

- (a) The general rule is that risk follows the ownership, whether the delivery has been made or not. If the goods are lost or damaged by accident or otherwise, then, subject to certain exceptions, the loss falls on the owner of the goods at the time they are lost or damaged.
- (b) When there is a danger of the goods being damaged by the action of third parties it is generally the owner who can take action.
- (c) The rights of third parties may depend upon the passing of the property if the buyer resells the goods to a third-party, the third-party will only obtain a good title if the property in the goods has passed to the buyer before or at the time of the resale. Similarly, if the seller, in breach of his contract with the buyer, attempts to sell the goods to a third party in the goods, has not passed to the buyer, e.g., where there is only an agreement to sell.
- (d) In case of insolvency of either the seller or the buyer, it is necessary to know whether the goods



can be taken over by the official assignee or the official receiver. It will depend upon whether the property in the goods was with the party adjudged insolvent.

Thus in this context, ownership and possession are two distinct concepts and these two can at times remain separately with two different persons.

Passing of property in specific goods

In a sale of specific or ascertained goods, the property passes to the buyer as and when the parties intended to pass. The intention must be gathered from the terms of the contract, the conduct of the parties, and the circumstances of the case.

Unless a contrary intention appears, the following rules are applicable for ascertaining the intention of the parties:

- (a) Where there is an unconditional contract for the sale of specific goods in a deliverable state, the property passes to the buyer when the contract is made.
- (b) Where there is a contract for the sale of specific goods not in a deliverable state, i.e., the seller has to do something to the goods to put them in a deliverable state, the property does not pass until that thing is done and the buyer has notice of it. (Section 21)
- (c) Where there is a sale of specific goods in a deliverable state, but the seller is bound to weigh, measure, test or do something with reference to the goods for the purpose of ascertaining the price, the property to the goods for the purpose of ascertaining the price, does not pass until that thing is done and the buyer has notice of it. (Section 22)
- (d) When goods are delivered to the buyer on approval or "on sale or return", the property therein passes to the buyer:
 - (i) when he signified his approval or acceptance to the seller, or does any other act adopting the transaction;
 - (ii) if he retains the goods, without giving notice of rejection, beyond the time fixed for the return of goods, or if no time is fixed, beyond a reasonable time.

Ownership in unascertained goods

The property in unascertained or future goods does not pass until the goods are ascertained.

Unless a different intention appears, the following things are applicable for ascertaining the intention of the parties in regard to passing of property in respect of such goods:

- (a) The property in unascertained or future goods sold by description passes to the buyer when goods of that description and in deliverable state are 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. (Section 23)
- (b) If there is a sale of a quantity of goods out of a large quantity.
- (c) Delivery by the seller of the goods to a carrier or other buyer for the purpose of transmission to the buyer in pursuance of the contract is an appropriation sufficient to pass the property in the goods.
- (d) The property in goods, whether specific or unascertained, *does not pass* if the seller reserves a right of disposal of the goods. Apart from an express reservation of the right of disposal, the seller is deemed to reserve the right of disposal in the following two cases:
 - i) where goods are shipped and by the bill of lading of the goods deliverable to the order or the seller or his agent.
 - ii) when the seller sends the bill of exchange for the price of the goods to the buyer for this acceptance, together with the bill of lading, the property in the goods does not pass to the buyer unless he accepts the bill of exchange.

Passing of Risk (Section 26)

The general rule is that goods remain at the seller's risk until the ownership is transferred to the



buyer. After the ownership has passed to the buyer, the goods are at the buyer's risk whether the delivery has been made or not. For example, 'A' buys goods of 'B' and property has passed from 'B' to 'A': but the goods remain in 'B's warehouse and the price is unpaid. Before delivery, 'B's warehouse is burnt down for no fault of 'B' and the goods are destroyed. 'A' must pay 'B' the price of the goods, as he was the owner.

Transfer of Title by Person not the Owner (Section 27-30)

The general rule is that only the owner of goods can sell the goods. Conversely, the sale of an article by a person who is not or who has not the authority of the owner, gives no title to the buyer. The rule is expressed by the maxim; "*Nemo dot quod non habet*" i.e. no one can pass a better title than what he himself has. As applied to the sale of goods, the rule means that a seller of goods cannot give a better title to the buyer than he himself possess.

Exception to the General Rule

The Act while recognizing the general rule that no one can give a better title than what he himself has, laid down important exceptions to it. Under the exceptions the buyer gets a better title of the goods than the seller himself. These exceptions are given below:

- (a) **Sale by a mercantile agent:** A buyer will get a good title if he buys in good faith from a mercantile agent who is in possession either of the goods or' documents of title of goods with the consent of the owner, and who sells the goods in the ordinary course of his business.
- (b) **Sale by a co-owner:** A buyer who buys in good faith from one of the several joint owners who is in sale possession of the goods with the permission of *his co-owners will get good title to the goods.*
- (c) **Sale by a person in possession under a voidable contract:** A buyer buys in good faith from a person in possession of goods under a contract which is voidable, but has not been. rescinded at the time of the sale.
- (d) **Sale by seller in possession after sale:** Where a seller, after having sold the goods, continues in possession of goods, or documents of title to the goods and again sells them by himself or through his mercantile agent to a person who buys in good faith and without notice of the previous sale, such a buyer gets a good title to the goods.
- (e) **Sale by buyer in possession:** If a person has brought or agreed to buy goods obtains, with the seller's consent, possession of the goods or of the documents of title to them, any sale by him or by his mercantile agent to a buyer who takes in good faith without notice of any lien or other claim of the original seller against the goods, will give a good title to the buyer. In any of the above cases, if the transfer is by way of pledge or pawn only, it will be valid as a pledge or pawn.
- (f) **Estoppel:** If the true owner stands by and allows an innocent buyer to pay over money to a third-party, who professes to have the right to sell an article, the true owner will be estopped from denying the third-party's right to sell.
- (g) **Sale by an unpaid seller:** Where an unpaid seller has exercised his right of lien or stoppage in transit and is in possession of the goods, he may resell them and the second buyer will get absolute right to the goods.
- (h) **Sale by person under other laws:** A pawnor on default of the pawnee to repay, has a right to sell the goods, pawned and the buyer gets a good title to the goods. The finder of lost goods can also sell under certain circumstances. The Official Assignee or Official Receiver, Liquidator, Officers of Court selling under a decree, Executors, and Administrators, all these persons are not owners, but they can convey better title than they have.

12. Performance of the Contract of Sale

It is the duty of the seller and buyer that the contract is performed. The duty of the sellers is to deliver the goods and that of the buyer to accept the goods and pay for them in accordance with the contract of sale.

Unless otherwise agreed, payment of the price and the delivery of the goods and concurrent



conditions, *i.e.*, they both take place at the same time as in a cash sale over a shop counter.

Delivery

Delivery is the voluntary transfer of possession from one person to another. Delivery may be actual, constructive or symbolic. Actual or physical delivery takes place where the goods are handed over by the seller to the buyer or his agent authorised to take possession of the goods. Constructive delivery takes place when the person in possession of the goods acknowledges that he holds the goods on behalf of and at the disposal of the buyer

Rules as to delivery

The following rules apply regarding delivery of goods:

- (a) Delivery should have the effect of putting the buyer in possession.
- (b) The seller must deliver the goods according to the contract.
- (c) The seller is to deliver the goods when the buyer applies for delivery; it is the duty of the buyer to claim delivery.
- (d) Where the goods at the time of the sale are in the possession of a third person, there will be delivery only when that person acknowledges to the buyer that he holds the goods on his behalf.
- (e) The seller should tender delivery so that the buyer can take the goods. It is not the duty of the seller to send or carry the goods to the buyer unless the contract so provides. But the goods must be in a deliverable state at the time of delivery or tender of delivery. If by the contract the seller is bound to send the goods to the buyer, but no time is fixed, the seller is bound to send them within a reasonable time.
- (f) The place of delivery is usually stated in the contract. Where it is so stated, the goods must be delivered at the specified place during working hours on a working day. Where no place is mentioned, the goods are to be delivered at a place at which they happen to be at the time of the contract of sale and if not then in existence they are to be delivered at the place they are produced.
- (g) The seller has to bear the cost of delivery unless the contract otherwise provides. While the cost of obtaining delivery is said to be of the buyer, the cost of putting the goods into deliverable state must be borne by the seller. In other words in the absence of an agreement to the contrary, the expenses of and incidental to making delivery of the goods must be borne by the seller, the expenses of and incidental to receiving delivery must be borne by the buyer.
- (h) If the goods are to be delivered at a place other than where they are, the risk of deterioration in transit will, unless otherwise agreed, be borne by the buyer.
- (i) Unless otherwise agreed, the buyer is not bound to accept delivery in Installments.

Acceptance of Goods by the Buyer

Acceptance of the goods by the buyer takes place when the buyer:

- (a) intimates to the seller that he has accepted the goods; or
- (b) retains the goods, after the lapse of a reasonable time without intimating to the seller that he has rejected them; or
- (c) does any act on the goods which is inconsistent with the ownership of the seller, e.g., pledges or resells. If the seller sends the buyer a larger or smaller quantity of goods than ordered, the buyer may:
 - (a) reject the whole; or
 - (b) accept the whole; or
 - (c) accept the quantity ordered and reject the rest.

If the seller delivers, with the goods ordered goods of a wrong description, the buyer may accept the goods ordered and reject the rest, or reject the whole.

Where the buyer rightly rejects the goods, he is not bound to return the rejected goods to the seller. It is sufficient if he intimates to seller that he refuses to accept them. In that case, the seller has to remove them.



Installment Deliveries

When there is a contract for the sale of goods to be delivered in stated installments which are to be separately paid for, and either the buyer or the seller commits a breach of contract, it depends on the terms of the contract whether the breach is a repudiation of the whole contract or a severable breach merely giving right to claim for damages.

Suits for Breach of Contract

Where the property in the goods has passed to the buyer, the seller may sue him for the price.

Where the price is payable on a certain day regardless of delivery, the seller may sue for the price, if it is not paid on that day, although the property in the goods has not passed.

Where the buyer wrongfully neglects or refuses to accept the goods and pay for them, the seller may sue the buyer for damages for non-acceptance.

Where the seller wrongfully neglects or refuses to deliver the goods to the buyer, the buyer may sue him for damages for non-delivery.

Where there is a breach of warranty or where the buyer elects or is compelled to treat the breach of condition as a breach of warranty, the buyer cannot reject the goods. He can set breach of warranty in extinction or diminution of the price payable by him and if loss suffered by him is more than the price he may sue for the damages.

If the buyer has paid the price and the goods are not delivered, the buyer can sue the seller for the recovery of the amount paid. In appropriate cases the buyer can also get an order from the Court that the specific goods ought to be delivered.

Anticipatory Breach

Where either party to a contract of sale repudiates the contract before the date of delivery, the other party may, either treat the contract as still subsisting and wait till the date of delivery, or he may treat the contract as rescinded and sue for damages for the breach.

In case the contract is treated as still subsisting it would be for the benefit of both the parties and the party who had originally repudiated will not be deprived of:

- (a) his right of performance on the due date in spite of his prior repudiation or
- (b) his rights to set up any defense for non-performance which might have actually arisen after the date of the prior repudiation.

Measure of Damages

The Act does not specifically provide for rules as regards the measure of damages except stating that nothing in the Act shall affect the right of the seller or the buyer to recover interest or special damages in any case where by law they are entitled to the same. The inference is that the rules laid down in Section 73 of the Indian Contract Act will apply.

Unpaid Seller

The seller of goods is deemed to be unpaid seller:

- (a) When the whole of the price has not been paid or tendered; or
- (b) When a conditional payment was made by a bill of exchange or other negotiable instrument, and the instrument has been dishonoured.



Rights of an Unpaid Seller against the Goods

An unpaid seller's rights against the goods are:

- (a) A lien or right of retention
- (b) The right of stoppage in transit.
- (c) The right of resale.
- (d) The right to withhold delivery.

(a) Lien: - An unpaid seller in possession of goods sold, may exercise his lien on the goods, i.e., keep the goods in his possession and refuse to deliver them to the buyer until the fulfillment or tender of the price in cases where:

the goods have been sold without stipulation as to credit; or

- (i) the goods have been sold on credit, but the term of credit has expired; or
- (ii) the buyer becomes insolvent.

The lien depends on physical possession. The seller's lien is *possessory lien*, so that it can be exercised only so long as the seller is in possession of the goods. It can only be exercised for the non-payment of the price and not for any other charges.

A lien is lost

- (i) 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;
- (ii) When the buyer or his agent lawfully obtains possession of the goods;
- (iii) By waiver of his lien by the unpaid seller.

(b) Stoppage in transit: - The right of stoppage in transit is a right of stopping the goods while they are in transit, resuming possession of them and retaining possession until payment of the price.

The right to stop goods is available to an unpaid seller

- (i) when the buyer becomes insolvent; and the goods are in transit.

The buyer is insolvent if he has ceased to pay his debts in the ordinary course of business, or cannot pay his debts as they become due. It is not necessary that he has actually been declared insolvent by the Court.

The goods are in transit from the time they are delivered to a carrier or other bailee like a wharfinger or warehouse keeper for the purpose of transmission to the buyer and until the buyer takes delivery of them.

The transit comes to an end in the following cases:

- (i) If the buyer obtains delivery before the arrival of the goods at their destination;
- (ii) If, after the arrival of the goods at their destination, the carrier acknowledges to the buyer that he holds the goods on his behalf, even if further destination of the goods is indicated by the buyer.
- (iii) If the carrier wrongfully refuses to deliver the goods to the buyer.

If the goods are rejected by the buyer and the carrier or other bailee holds them, the transit will be deemed to continue even if the seller has refused to receive them back.

The right to stop in transit may be exercised by the unpaid seller either by taking actual possession of the goods or by giving notice of the seller's claim to the carrier or other person having control of the goods. On notice being given to the carrier he must redeliver the goods to the seller, who must pay the expenses of the redelivery.

The seller's right of lien or stoppage, in transit is not affected by any sale on the part of the buyer unless the seller has assented to it. A transfer, however, of the bill of lading or other document of seller to a *bona fide* purchaser for value is valid against the seller's right.

(c) Right of re-sale: - The unpaid seller may re-sell:

- (i) where the goods are perishable;



- (ii) where the right is expressly reserved in the contract;
- (iii) where in exercise of right of lien or stoppage in transit, the seller gives notice to the buyer of his intention to re-sell, and the buyer, does not pay or tender the price within a reasonable time.

If on a re-sale, there is a deficiency between the price due and amount realized, the re-seller is entitled to recover it from the buyer. If there is a surplus, he can keep it. He will not have these rights if he has not given any notice and he will have to pay the buyer any profits.

(d) Rights to withhold delivery:- If the property in the goods has passed, the unpaid seller has right as described above. If, however, the property has not passed, the unpaid seller has a right of withholding delivery similar to and co-extensive with his rights of lien and stoppage in transit.

Rights of an unpaid seller against the buyer

An unpaid seller may sue the buyer for the price of the goods in case of breach of contract where the property in the goods has passed to the buyer or he has wrongfully refused to pay the price according to the terms of the contract.

The seller may sue the buyer even if the property in the goods has not passed where the price is payable on a certain day.

Under Section 56, the seller may sue the buyer for damages for breach of contract where the buyer wrongfully neglects or refuses to accept and pay for the goods.

Thus an unpaid seller's right against the buyer personally is:

- (a) a suit for the price.
- (b) a :suit for damages.

Auction Sales (Section 64)

A sale by auction is a public sale where goods are offered to be taken by bidders. It is a proceeding at which people are invited to compete for the purchase of property by successive offer of advancing sums.

Section 64 lays down the rules regulating auction sales. Where goods are put up for sale in lots, each, lot is *prima facie* deemed to be the subject of a separate contract of sale. The sale is complete when the auctioneer announces its completion by the fall of the hammer or in other customary manner. Until such announcement is made, any bidder may retract his bid.



UNIT-III

Negotiable Instruments Act, 1881

The Negotiable Instruments Act was enacted, in India, in 1881 and it came into force on 1st March, 1881. Prior to its enactment, the provision of the English Negotiable Instrument Act were applicable in India, and the present Act is also based on the English Act with certain modifications. It extends to the whole of India except the State of Jammu and Kashmir. The Act operates subject to the provisions of Sections 31 and 32 of the Reserve Bank of India Act, 1934

Definition

A “negotiable instrument” means a promissory note, bill of exchange or cheque payable either to order or to bearer.

Explanation (i) - A 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.

Explanation (ii) - A promissory note, bill of exchange or cheque is payable to bearer which is expressed to be so payable or on which the only or last endorsement is an indorsement in blank.

Explanation (iii) - Where a promissory note, bill of exchange or cheque, either originally or by endorsement, is expressed to be payable to the order of a specified person, and not to him or his order, it is nevertheless payable to him or his order at his option.

(2) A negotiable instrument may be made payable to two or more payees jointly, or it may be made payable in the alternative to one of two, or one or some of several payees. The word negotiable means ‘transferable by delivery,’ and the word instrument means ‘a written document by which a right is created in favour of some person.’ Thus, the term “negotiable instrument” literally means ‘a written document which creates a right in favour of somebody and is freely transferable by delivery.’

A negotiable instrument is a piece of paper which entitles a person to a certain sum of money and which is transferable from one to another person by a delivery or by endorsement and delivery.

“According to **Blackburn J**, a negotiable instrument has two characteristics namely

1. It is transferable, like cash, by delivery (which assumes it is in a deliverable state) so that the transferee can enforce the rights embodied in it in his own name.
2. The transferee being a bonafide holder for value can acquire a better title to it than that of his transferor.”

Negotiable Instrument is moreover a document of title which clearly explains the rights towards the payment of money or a security for money which is transferable by delivery either by custom or by legislation. The use of negotiable Instrument is mainly to facilitate payment for exports and imports of trade. The rapid growth of technology has revolutionized the world with computer, which is used in every field of profession. This has reduced the use of negotiable instrument and in future it may decline more. Even though the electronic revolution has got more advantages it may be considered as the next step because the world needs time to get used to it. But, the negotiable instrument are still in use.

Characteristics of Negotiable Instruments

1. Free transferability or easy negotiability

Negotiable instrument is freely transferable from one person to another without any formality. The property (right of ownership) in these instruments passes by either endorsement and delivery (in case it is payable to order) or by delivery merely (in case it is payable to bearer) and no further evidence of transfer is needed.

2. Title of holder is free from all defects

A person who takes negotiable instrument bona-fide and for value gets the instrument free from all defects in the title. The holder in due course is not affected by defective title of the transferor or of any other party.



3. Transferee can sue in his own name without giving notice to the debtor:

A bill, promissory note or a cheque represents a debt, i.e., an “actionable claim” and implies the right of the creditor to recover something from the debtor.

The creditor can either recover this amount himself or can transfer his right to another person.

In case he transfers his right, the transferee of a negotiable instrument is entitled to sue on the instrument in his own name in case of dishonour, without giving notice to the debtor of the fact that he has become holder.

In case of transfer or assignment of an ordinary “actionable claim” i.e., a book debt evidenced by an entry by the creditor in his account book, under the transfer of property act, notice to the debtor is necessary in order to make the transferee entitled to sue in his own name.

4. Presumptions:

Certain presumptions apply to negotiable instruments. Section 118, 119 and 139 lay down the following presumptions:

(a) For consideration : that every negotiable instrument, was made, drawn, accepted, endorsed or transferred for consideration.

(b) As to date : that every negotiable instrument bearing a date was made or drawn on such date.

(c) As to time of acceptance : that every bill of exchange was accepted within a reasonable time after its date and before its maturity.

(d) As to transfer: that every transfer of a negotiable instrument was made before its maturity

(e) As to time of endorsements : that the endorsements appearing upon a negotiable instrument were made in the order in which they appear thereon.

(f) As to stamps : that a lost promissory-note, bill of exchange or cheque was duly stamped.

(g) As to a holder in due course: that every holder of a negotiable instrument is holder in due course (this presumption would not arise where it is proved that the holder has obtained the instrument from its lawful owner, or from any person in lawful custody thereof, by means of an offence, fraud or for unlawful consideration and in such a case the holder has to prove that he is a holder in due course)

(h) As to dishonour: that the instrument was dishonoured, in case a suit upon a dishonoured instrument is filed with the court and the fact of protest is proved.

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.

“The effect of these presumptions is to place the evidential burden on the accused of proving that the cheque was not received by the complainant towards the discharge of any liability. Because both sections 138 and 139 require that the court shall presume the liability of the drawer of the cheques for the amounts for which the cheques are drawn...it is obligatory on the courts to raise this presumption in every case where the factual basis for the raising of this presumption had been established. It introduced an exception to the general rule as to the burden of proof in criminal cases and shifts the onus on to the accused.”

Types of Negotiable Instruments

There are two types of Negotiable instruments:-

Negotiable Instruments recognized by statutes: The Negotiable Instruments Act mentions only three kinds of negotiable instruments (**Section 13**).

These are: **1. Promissory Notes**

2. Bills of Exchange, and

3. Cheques

Negotiable instruments recognized by usage or customs of trade: There are certain other instruments which have acquired the characteristic of negotiability by the usage or custom of trade.

For example: Exchequer bills, Bank notes, Share warrants, Circular notes, Bearer debentures, Dividend



warrants, Share certificates with blank transfer deeds, etc.

Promissory Note

Definition: According to **Section 4 of Negotiable Instruments Act**, "A promissory note is an instrument in writing (not being a bank-note or a currency-note) containing an unconditional undertaking, signed by the maker, to pay a certain sum of money only to, or to the order of, a certain person, or to the bearer of the instrument."

Parties to a Promissory Note

There are primarily two parties involved in a promissory note. They are:

(i) The Maker or Drawer: The person who makes the note and promises to pay the amount stated therein.

(ii) The Payee – The person to whom the amount is payable i.e. to whom the payment is to be made is called a payee.

In course of transfer of a promissory note by payee and others, the parties involved may be –

(a) The Endorser – the person who endorses the note in favour of another person.

(b) The Endorsee – the person in whose favour the note is negotiated by endorsement.

Characteristics of Promissory Note

1. It must be in writing:

A promissory note has to be in writing

An oral promise to pay does not become a promissory note

The writing may be on any paper or book

Illustrations: A signs the instruments in the following terms:

"I promise to pay B or order Rs.500/-"

"I acknowledge myself to be indebted to B in Rs.1,000/- to be paid on demand, for value received"

Both the above instruments are valid promissory notes.

2. It must contain a promise or undertaking to pay:

There must be a promise or an undertaking to pay

The undertaking to pay may be gathered either from express words or by necessary implication.

A mere acknowledgement of indebtedness is not a promissory note, although it is valid as an agreement and may be sued upon as such

Illustrations: A signs the instruments in the following terms:

"Mr. B I owe you Rs.1,000"

"I am liable to pay to B Rs.500"

The above instruments are not promissory notes as there is no undertaking or promise to pay.

There is only an acknowledgement of indebtedness.

Where A signs the instrument in the following terms:

"I acknowledge myself to be indebted to B in Rs.1,000, to be paid on demand, for value received," there is a valid promissory note

3. The promise to pay must be unconditional:

A promissory note must contain an unconditional promise to pay

The promise to pay must not depend upon the happening of some uncertain event, i.e., a contingency or the fulfillment of a condition

Illustrations: A signs the instruments in the following terms:

"I promise to pay B Rs. 500 seven days after my marriage with C"

"I promise to pay B Rs. 500 as soon as I can"

The above instruments are not valid promissory notes as the payment is made depending upon the happening of an uncertain event which may never happen and as a result the sum may never become



payable

4. It must be signed by the maker: It is imperative that the promissory note should be duly authenticated by the 'signature' of the maker

'Signature' means the writing or otherwise affixing a person's name or a mark to represent his name, by himself or by his authority with the intention of authenticating a document.

5. The maker must be a certain person:

The instrument must itself indicate with certainty who is the person or are the persons engaging himself or themselves to pay

Alternative promisors are not permitted in law because of the general rule that "where liability lies no ambiguity must lie"

6. The payee must be certain:

Like the maker the payee of a pronote must also be certain on the face of the instrument

A note in favour of fictitious person is illegal and void

A pronote made payable to the maker himself is a nullity, the reason being the same person is both the promisor and the promisee

7. The undertaking must be to pay a certain and definite sum of money only.

For a valid pronote it is also essential that the sum of money promised to be payable must be certain and definite

The amount payable must not be capable of contingent additions or subtractions

Illustrations: A signs the instruments in the following terms:

"I promise to pay B Rs.500 and all other sums which shall be due to him"

"I promise to pay B Rs.500, first deducting thereout any money which he may owe me"

The above instruments are invalid as promissory notes because the exact amount to be paid by A is not certain

8. The amount payable must be in legal tender money of India:

A document containing a promise to pay a certain amount of foreign money or to deliver a certain quantity of goods is not a pronote. The payment must be in a legal money of the country.

9. Revenue stamps or requisite value under the stamp Act of the country should be affixed.

10. Other matters of form like number, date, place etc, are usually found given in notes, but they are not essentials in law.

11. A bank note or a currency note is not a promissory note within the meaning of this section.

12. A promissory note cannot be made payable to bearer on demand.

Bill of Exchange

Definition: Section 5 of the Negotiable Instruments Act defines a Bill of Exchange as follows:

"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 is also called a Draft.

Illustration:

Mr. X purchases goods from Mr. Y for Rs.1000/-

Mr. Y buys goods from Mr. S for Rs.1000/-

Then Mr. Y may order Mr. X to pay Rs.1000/- Mr. S which will be nothing but a bill of exchange.

Parties to a Bill of Exchange

There are three parties involved in a bill of exchange

(i) The Drawer – The person who makes the order for making payment.

(ii) The Drawee – The person to whom the order to pay is made. He is generally a debtor of the drawer. The person directed to pay the money by the drawer is called the drawee.



(iii) The Payee – The person to whom the payment is to be made. The person named in the instrument, to whom or to whose order the money are directed to be paid by the instruments are called the payee.

The drawer can also draw a bill in his own name thereby he himself becomes the payee. Here the words in the bill would be Pay to us or order.

In a bill where a time period is mentioned, is called a Time Bill.

But a bill may be made payable on demand also. This is called a Demand Bill.

Essentials of a Bill of Exchange

1. **It must be in writing**
2. **It must contain an order to pay. A mere request to pay on account, will not amount to an order**
3. **The order to pay must be unconditional**
4. **It must be signed by the drawer**
The drawer, drawee and payee must be certain. A bill cannot be drawn on two or more drawees but may be made payable in the alternative to one of two or more payees
5. **The sum payable must be certain**
6. **The bill must contain an order to pay money only**
7. **It must comply with the formalities as regards date, consideration, stamps, etc**

Cheque

Definition: A cheque is bill of exchange drawn on a specified banker and not expressed to be payable otherwise than on demand and it includes the electronic image of a truncated cheque and a cheque in the electronic form. (Sec. 6, NIA)

Explanation I - For the purposes of this section, the expressions-

- (a) a cheque in the electronic form means a cheque which contains the exact mirror image of a paper cheque, and is generated, written and signed in a secure system ensuring the minimum safety standards with the use of digital signature (with or without biometrics signature) and asymmetric crypto system;
- (b) a truncated cheque means a cheque which is truncated during the course of a clearing cycle, either by the clearing house or by the bank whether paying or receiving payment, immediately on generation of an electronic image for transmission, substituting the further physical movement of the cheque in writing.

Explanation II - For the purposes of this section, the expression clearing house means the clearing house managed by the Reserve Bank of India or a clearing house recognised as such by the Reserve Bank of India.

A cheque is a kind of bill of exchange but it has additional qualification namely-

1. **It is always drawn on a specified banker and**
2. **It is always payable on demand without any days of grace.**

Parties to a cheque

Drawer: Drawer is the person who draws or makes the cheque.

Drawee: Drawee is the drawer's banker on whom the cheque has been drawn.

Payee: Payee is the person who is entitled to receive the payment of a cheque.

Crossing of Cheques

A Crossed Cheque is one which bears across its face two parallel transverse lines with or without certain words. Such lines are usually drawn on the left side top corner of the face of the Cheque. However, such lines can be drawn anywhere on the face of the Cheque.

Crossing of Cheque is a direction to the drawee bank to pay the amount of the Cheque to a bank or to a particular bank. Therefore, a crossed Cheque is not payable to the payee or holder at the counter of the bank. In order to get the payment of the Cheque, it is required to be deposited in an account with a bank.



The bank, in turn, presents the Cheque to the drawee bank and gets payment on behalf of the payee or indorsee of the Cheque.

The objects of crossing of a Cheque are as follows:

To direct the drawee bank to pay the amount of the Cheque only to a bank or a particular bank;

To prevent the payment of the Cheque to an unauthorized or wrong person.

KINDS OF CROSSING

Crossing of Cheque is basically of two kinds:-

1. **General crossing, and**
2. **Special crossing.**

These basic kinds of crossing may take several forms. Some of them are:

3. **Restrictive crossing.**
4. **Not negotiable crossing.**

1. General crossing: A Cheque is deemed to be generally crossed in any of the following cases:

- a. When it bears across its face two parallel transverse lines without any words.
- b. When it bears across its face an addition of the words "and company" or any abbreviation thereof between two parallel transverse lines. It may also be with or without the words 'Not negotiable'.

Effects of general crossing

The Cheque is not payable at the counter of the bank.

The drawee bank shall pay the amount of the Cheque only to a banker. Therefore, the holder will have to deposit the Cheque in an account with any banker. [Sec. 126 Para 1]

2. Special crossing: A Cheque is said to be specially crossed when the name of a banker is added across the face of the Cheque, either with or without words, not negotiable. Usually, two parallel transverse lines are used in special crossing but they are required not by law.

Effects of special crossing:

In the case of a Cheque especially crossed, the payment can be obtained only through the particular banker whose name appears across the face of the Cheque or his agent for collection. [Sec. 126, para2]

3. Restrictive crossing: Restrictive crossing has not been described anywhere in the Negotiable Instrument Act. It is a type of crossing which has evolved out of business and banking usage and now recognized by the law. Every Cheque crossed wither generally or specially may be crossed restrictively credit the proceeds of the Cheque only to the account of the payee.

4. Not negotiable crossing: Sometimes, a Cheque crossed generally or specially contains the words 'not negotiable' A crossing with such words is said to be 'not negotiable' crossing.

The words 'not negotiable' on a crossed Cheque destroy the negotiable character of the Cheque but not the transferability of the Cheque. Therefore, any person taking a crossed Cheque bearing the words 'not negotiable' shall not have and shall not be capable of giving a better title to the Cheque than the title of the person from whom he took it. [Sec. 130]

Parties to a Negotiable Instrument

Holder and Holder in due course

Holder (Sec. 8, NIA)

Holder means any person entitled in his own name to the possession a promissory note bill of exchange or cheque and to recover or receive the amount due thereon from the parties thereon. A holder must therefore have the possession of the instrument and also the right to recover the money in his own name.

Therefore, **holder of a negotiable instrument is the person:**



1. Who is entitled in his own name to the possession of the instrument, and
2. Who has the right to receive or recover the amount due thereon from the parties thereto.

Characteristics:

- a) Entitled to possession of an instrument
- b) Entitled to receive or recover the amount
- c) Holder of lost or destroyed instrument

Who can be a Holder?

- i. Payee
- ii. Indorsee
- iii. Bearer
- iv. Legal representative or heir

Who is Not a Holder?

- i. Agent
- ii. Servant
- iii. Beneficial
- iv. Thief or finder
- v. Forged indorsee

Powers of Holder

- I. He is entitled in his own name to the possession of the instrument.
- II. He can receive or recover the amount due on the instrument.
- III. If necessary, he can sue the parties in order to recover the money due on the instrument.
- IV. He can validly discharge the instrument on payment of the instrument.
- V. He may indorse the instrument to any other person

"Holder in due course" (Sec. 9, NIA)

Holder in due course means any person who for consideration became the possessor of a promissory note, bill of exchange or cheque, if payable to the bearer or the payee or indorsee thereof, if payable to the 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'

Thus, a person is a holder in due course if he satisfies the following conditions:

- a) He must be a holder (possessor) of a negotiable instrument.
- b) He must have become holder (possessor) of the instrument for consideration.
- c) He must have become holder before maturity of the instrument.
- d) He must have obtained the instrument in good faith.
- e) He must have received the instrument complete and regular on the face of it.

RIGHTS AND PRIVILEGES OF HOLDER IN DUE COURSE

A holder in due course enjoys certain rights and privileges. They are available in the following particular cases:

In case of an inchoate instrument: Sometimes a person signs a stamped but otherwise incomplete (inchoate) instrument and delivers it to another person. In such a case, it implies that the holder may fill in any amount for which authority has been given by the maker.

In case of a fictitious bill: Sometimes the name of the drawer or the payee or both is fictitious in a bill. Such a bill is called a fictitious bill. The acceptor of such a fictitious bill is not liable to the holder of the bill. But if the same bill is passed on to a holder in due course, he will have a privilege to claim money on it from the acceptor. [Sec.42]

In case of the liability of prior parties: A holder in due course has a privilege to hold every prior party to a negotiable instrument liable on it until the instrument is duly satisfied. [Sec.36]



In case of instrument without consideration: Sometimes an instrument is made, drawn, accepted, indorsed or transferred without consideration. But, if the same instrument comes into the hands of a holder in due course, he has a privilege to recover the amount from any party thereto [Sec.43]

In case of transfer of title to a subsequent holder: A holder in due course has a privilege to transfer the title to an instrument free from all defects to subsequent holder. Therefore, any holder of a negotiable instrument who derives title to a negotiable instrument from a holder in due course enjoys all the rights and privileges of that holder in due course.

In case of an instrument obtained by unlawful means or for unlawful consideration: Sometimes, a person gets a lost instrument or obtains an instrument by means of an offence (i.e. by stealing or defrauding). In such a case, the holder cannot claim any right against the party liable on it. But if the same instrument is negotiated to a holder in due course, he will get good title to it.

DISTINCTION BETWEEN HOLDER AND HOLDER IN DUE COURSE

Basis of Distinction	Holder	Holder in Due Course
1. Definition	Holder is a person who is entitled in his own name to the possession of the instrument and to receive the amount due on it.	Holder in due course is a person who becomes the possessor of the instrument for consideration before its maturity and in good faith. [Sec. 9]
2. Consideration	A holder need not necessarily acquire the instrument for consideration. For instance, a holder may get the instrument by way of gift.	A holder in due course can acquire the instrument for consideration only.
3. Before maturity	A holder may obtain possession before or after the maturity of the instrument.	A holder in due course must obtain the possession before maturity of the instrument.
4. Good faith	A holder need not necessarily acquire possession of the instrument in good faith.	A holder in due course must always acquire possession of the instrument in good faith.
5. Inchoate instrument	A holder can claim only the amount which signer of the inchoate instrument intended to pay.	A holder in due course can claim any amount filled in the inchoate instrument provided it is covered by the stamp affixed on it. [Sec. 20]
6. Right against prior parties	A holder does not have rights against all the prior parties. He has rights against the original parties and his immediate indorser.	A holder in due course has rights against every prior party to the instrument. He can hold them liable jointly and severally.[Sec. 36]
7. Title better than the transferor	A holder can never get a better title than that of the transferor.	A holder in due course can acquire a better title than that of the transferor. In other words he gets the instrument cleansed of all prior defects.



Negotiation

One of the essential features of a negotiable instrument is its transferability. A negotiable instrument may be transferred from one person to another in either of the followings way-

1. **By negotiation**
2. **By assignment**

1) By negotiation - The transfer of an instrument by one party to another so as to constitute the transferee a holder is called Negotiation. Negotiation means as the process by which a third party is constituted the holder of the instrument so as to entitle him to the possession of the same and to receive the amount due thereon in his own name.

According to section 14 of the Act, "when a promissory note, bill of exchange or cheque is transferred to any person so as to constitute that person the holder thereof, the instrument is said to be negotiated." The main purpose and essence of negotiation is to make the transferee of a promissory note, a bill of exchange or a cheque the holder thereof.

Modes of negotiation (Sec. 47 and 48, NIA)

1. Negotiation by delivery (Sec. 47): Where a promissory note or a bill of exchange or a cheque is payable to a bearer, it may be negotiated by delivery thereof.

Example: A the holder of a negotiable instrument payable to bearer, delivers it to B's agent to keep it for B. The instrument has been negotiated.

2. Negotiation by delivery (Sec. 48):

A promissory note, a cheque or a bill of exchange payable to order can be negotiated only by endorsement and delivery. Unless the holder signs his endorsement on the instrument and delivers it, the transferee does not become a holder. If there are more payees than one, all must endorse it.

2) By Assignment -

When a holder of a bill, promissory note or cheque transfers the same to another, he in fact gives his right to receive the payment of the instrument to the transferee.

Difference between Assignment & Negotiation:-

- 1) Mode of transfer- The transfer by negotiation requires only delivery with or without endorsement of a bearer or order instrument. Whereas the transfer by assignment requires a separate written document such as transfer deed signed by the transferor.
- 2) Notice of transfer-Not require in negotiation
- 3) Consideration-consideration must be proved in assignee.
- 4) Title
- 5) Right to sue

Endorsement

The word "endorsement" in its literal sense means, writing on the back of an instrument. But under the Negotiable Instruments Act, it means, the writing of one's name on the back of the instrument or any paper attached to it with the intention of transferring the rights therein. Thus, endorsement is signing a negotiable instrument for the purpose of negotiation. The person who effects an endorsement is called an "endorser", and the person to whom negotiable instrument is transferred by endorsement is called the "endorsee". Who may Endorse / Negotiate [Section 51]: Every Sole maker, drawer, payee or endorsee, or all of several joint makers, drawers, payees or endorsees of a negotiable instrument may endorse and negotiate the same if the negotiability of such instrument has not been restricted or excluded as mentioned in Section 50.

When the maker or holder of a negotiable instrument signs the instrument (otherwise than as maker) for the purpose of its negotiation, it is said to be the Endorsement of the instrument. [Section 15]



Essentials of a Valid Endorsement: Following are the essentials of a valid endorsement:

1. Indorsers must be holder: For a valid Endorsement, the indorser must be holder of the instrument. In other words, indorser must be entitled in his own name to the possession of the instrument and recover or receive the amount due thereon. Therefore, a person who steals or finds a lost instrument cannot indorse the instrument because he is not a holder.

2. On the instrument: Endorsement must be on the face or back of the instrument or on a piece of paper annexed to the instrument.

3. Signature: Endorsement must be signed by the indorser for the purpose of negotiation of the instrument. It may be signed by the maker or holder of the instrument but the maker must not sign the Endorsement in the capacity of the maker.

4. Additional words and form of words: Indorser may sign the Endorsement with a without additional words or statement.

5. Endorsement by joint holders: An Endorsement is valid only when all joint holders (i.e. all makers, drawers, indorsees or payees) join in Endorsement unless any one of them has the authority to indorse for the others.

6. Endorsement of entire instrument: Endorsement must be of the entire instrument. An Endorsement which purports to transfer only a part of the amount of the instrument is not a valid Endorsement.

7. Delivery: In order to make a complete and effective Endorsement, the instrument must be delivered by the indorser to the indorsee.

8. It must be made by the holder of the instrument.

9. It must be completed by the delivery of the instrument.

10. It must be signed by the endorser. It must be on the back or face of instrument or on a slip of paper annexed thereto.

Persons Entitled to Indorse:

1. Payee
2. Maker, drawer or holder
3. Indorsee
4. Joint makers, drawers etc.

Kinds of Endorsements

1. Blank or general Endorsement: When the indorser signs his name only on the instrument for the purpose of its negotiation, it is called the blank or general Endorsement. Illustration: Anta has a Cheque payable to 'Anta or order' Anta merely signs on the instrument. It constitutes a blank Endorsement.

2. Full or special Endorsement: When an indorser signs his name and adds a direction to pay the amount mentioned in the instrument to or to the order of a specified person, it is called the Endorsement in full. Illustration: Anita is a holder of a Cheque. He writes 'Pay Banta or Order or Pay Banta only' and signs the Cheque. It is a full or special Endorsement.

3. Restrictive Endorsement: Illustration: (a) 'Pay the contents to Banta only'. (b) 'Pay Banta for my use'.

4. Partial Endorsement: Sometimes, an Endorsement purports to transfer only a part of the amount of the instrument. Such an Endorsement is called as partial Endorsement. It is not a valid Endorsement for the purpose of negotiation.

5. Conditional or qualified Endorsement: When an indorser inserts a condition in his Endorsement, it is called a conditional Endorsement. Sometimes, an indorser by express words in the Endorsement may exclude his liability on the instrument makes the right of the indorsee to receive the amount due thereon on the happening of a specified event or on the implement of some condition. In such a case, the Endorsement is said to be conditional.



Effects of Endorsement:

1. An unconditional Endorsement of a negotiable instrument followed by an unconditional delivery of the instrument has the following effects:
2. The property in the instrument stands transferred to the indorsee.
3. The indorsee gets the right of further negotiation of the instrument [Sec. 50]
4. The indorsee is entitled to sue all parties, whose names appear on it.

Discharge of a negotiable instrument

“Discharge means release from obligation.” Discharge can take place-

- 1) **By payment in due course:** The instrument is discharged by payment made in due course by the party who is primarily liable to pay, or by a person who is accommodated in case the instrument was made or accepted for his accommodation, The payment must be made at or after the maturity to the holder of the instrument if the maker or acceptor is to be discharged. A payment by a party who is secondarily liable does not discharge the instrument.
- 2) **By party primarily liable by becoming holder (Section 90):** If the maker of a note or the acceptor of a bill becomes its holder at or after its maturity in his own right, The Negotiable Instruments Act, 1881 4.5 instrument is discharged.
- 3) **By express waiver:** When the holder of a negotiable instrument at or after its maturity absolutely and unconditionally renounces in writing or gives up his rights against all the parties to the instrument, the instrument is discharged. The renunciation must be in writing unless the instrument is delivered up to the party primarily liable.
- 4) **By Cancellation:** Where an instrument is intentionally cancelled by the holder or his agent and the cancellation is apparent thereon, the instrument is discharged. Cancellation may take place; by crossing out signatures on the instrument, or by physical destruction of the instrument with the intention of putting an end to the liability of the parties to the instrument.
- 5) **By discharge as a simple contract:** A negotiable instrument may be discharged in the same way as any other contract for the payment of money. This includes for example, discharge of an instrument by innovation or rescission or by expiry of period of limitation.

Dishonour of a negotiable instrument

An instrument is said to be dishonored when the acceptance and/or payment is refused on a duly presented instrument. Thus, a negotiable instrument may be dishonored in two ways:

1. **by non acceptance, and**
2. **by non payment**

Dishonor by Non-acceptance:

Only a bill may be dishonored by non acceptance. A bill is deemed to be dishonored by non acceptance in any of the following cases:

- a. **Refused to accept**
- b. **Not signed by all the drawees**
- c. **Not accepted by any partner**
- d. **Bill not accepted within forty eight hours.**
- e. **Drawee could not be found**

Dishonour by Non-payment:

- a. **Default in payment**
- b. **When excused from presentment**

On the dishonour of a cheque, one can file a suit for recovery of the cheque amount along with the cost &



interest under order XXXVII of Code of Civil Procedure 1908 (which is a summary procedure and) can also file a Criminal Complaint u/s 138 of Negotiable Instrument Act for punishment to the signatory of the cheque for having committed an offence. However, before filing the said complaint a statutory notice is liable to be given to the other party.

NOTICE OF DISHONOUR

When a negotiable instrument is dishonored by non acceptance (bill) or by non-payment, the holder may sue against the parties liable for the same. But he can do so only when he has served a formal notice to the effect.

The notice of dishonor is necessary for two reasons:

- a. To warn the party about his liability.
- b. To secure rights of the holder

Notice by Whom?

The notice of dishonor may be given by any of the following:

- i. By the holder.
- ii. By any party receiving the notice of dishonor. He may do so if he wants to hold any prior party liable to himself.
- iii. By an agent of the holder

Notice to Whom?

- i. To all prior parties.
- ii. To some one of the several parties.
- iii. To an agent of the person.
- iv. To the legal representative, in case the party liable is dead.
- v. To the official assignee, in case the party liable has been declared insolvent.

Time and Place of Notice:

- i. The notice must be given within a reasonable time after dishonour.
- ii. The notice must be given at the place of business. In case the party has no place of business, it must be given at the residence of the party.

Dishonour of certain cheques for insufficiency of funds

Provided that nothing contained in this section shall apply unless-

(a) the cheque has been presented to the bank within a period of three months from the date on which it is drawn or within the period of its validity, whichever is earlier;

(b) the payee or the holder in due course of the cheque, as the case may be, makes a demand for the payment of the said amount of money by giving a notice in writing, to the drawer of the cheque within thirty days of the receipt of information by him from the bank regarding the return of the cheque as unpaid; and

(c) the drawer of such cheque fails to make the payment of the said amount of money to the payee or as the case may be, to the holder in due course of the cheque within 15 days of the receipt of the said notice.

Explanation - For the purposes of this section, debt or other liability means a legally enforceable debt or other liability.

Ingredients of the offence under Section 138, NIA: It is manifest that to constitute an offence under Section 138 of NIA, the following ingredients are required to be fulfilled:

1. a person must have drawn a cheque on an account maintained by him in a bank for payment of a certain amount of money to another person from out of that account for the discharge, in whole or in part, of any debt or other liability; that cheque has been presented to bank within a period



- of three months from the date on which it is drawn or within the period of its validity whichever is earlier;
2. that cheque is returned by the bank unpaid, either because of the amount of money standing to the credit of the account is insufficient to honour the cheque or that it exceeds the amount arranged to be paid from that account by an agreement made with the bank;
 3. the payee or the holder in due course of the cheque makes 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;
 4. The drawer of such cheque fails to make payment of the said amount of money to the payee or the holder in due course of the cheque within 15 days of the receipt of the said notice.

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.

The effect of these presumptions is to place the evidential burden on the accused of proving that the cheque was not received by the complainant towards the discharge of any liability. Because both sections 138 and 139 require that the court shall presume the liability of the drawer of the cheques for the amounts for which the cheques are drawn...it is obligatory on the courts to raise this presumption in every case where the factual basis for the raising of this presumption had been established. It introduced an exception to the general rule as to the burden of proof in criminal cases and shifts the onus on to the accused.

NOTING

Meaning – Noting is the process of recording the fact and reasons of dishonor of negotiable instrument by the notary public upon the dishonored instrument. In other words, noting consists of recording and authenticating the fact and reasons of dishonor of a negotiable instrument by the notary public.

Need – Noting is not compulsory in the case of an inland bill or note. But noting serves as an authentic and official proof of dishonor of an instrument by non acceptance or non-payment. It serves as an evidence of dishonor of a negotiable instrument in the legal proceedings before the Court.

Procedure of Noting – When a promissory note or a bill of exchange is dishonoured, the holder may request within a reasonable time after its dishonor to a notary public for its noting. On receipt of the request, the notary public takes following steps:

The notary public makes a formal demand upon the acceptor or maker for acceptance or payment. It may be noted that such demand may be made either by the notary public personally or by his clerk. If authorized by agreement or usage, the demand may be made by a registered letter.

When it is not then accepted or paid, the notary public records the fact of dishonor upon the instrument, or upon a paper attached thereto or party upon each.

Such a note must specify the following things:

- a) The fact of dishonour.
- b) The date of dishonor of the instrument.
- c) The reasons, if any, assigned for such dishonor.
- d) If the instrument has not been expressly dishonored, the reasons why the holder treats it as dishonored.
- e) The notary's charges. [Sec. 99]

In addition, the notary public also makes a reference of his register and puts signature with seal on the instrument.



PROTEST

Protest is a certificate issued by a notary public attesting the fact of dishonor of a negotiable instrument recorded upon the dishonored instrument.

Contents of protest

1. The instrument itself or a literal transcript of it which must contain everything written or printed thereon.
2. The name of the person for whom and against whom the instrument has been protested.
3. A statement that payment or acceptance, or better security (as the case may be) has been demanded of such person by the notary public; and the terms of his answer, if any
4. If the person gave no answer, or that he could not be found a statement to that effect.
5. The date, place and time of dishonor of the instrument. If better security has been refused; the place and time of refusal

Distinction between Noting and Protest

The notice is different from protest on the following grounds:

Nature - Noting consists of recording the fact and reasons of dishonor of a negotiable instrument upon the instrument. Protest is a certificate as to fact and reasons that an instrument has been dishonored or the acceptor has refused to give a better security for the bill.

Contents - The contents of noting are limited to the date and reasons (express or implied) of dishonor. But contents of protest are more detailed as specified under Section 101.

Scope - Noting can be done even without protest but protest is issued only after the noting has been done.

Requirement - Noting is optional in case of inland bill or note. But a foreign bill must be protested if it is required by the law of the place where they are drawn.

Conclusion

Negotiable Instruments plays a major role in the trade world. We can also see the use of negotiable instruments in the international trade. We can assume that the international trade is also developing with the negotiable instrument. The nature of negotiable instrument is an area of law which has major influence on any person in his professional field. Negotiable instrument plays a major role in different part of the world in raising the economy. The negotiable instrument is of contractual in nature and it characterizes the fact that it is negotiable.



UNIT-IV CONSUMER PROTECTION ACT 1986

Introduction

The Consumer Protection Act, 1986 has been enacted to provide for the establishment of consumer councils and other authorities for the settlement of consumers' disputes and for matters connected therewith. In fact, the basic motive of enacting this important Act is to provide cheaper and speedy remedies to the consumers who are in disadvantageous position in comparison with the traders who were well organized and ruling the market.

Objects of the Act

The objects of the Act are as follows:

1. **Better protection of interests of consumers.** The Act seeks to provide for better protection of the interests of consumers. For that purpose, the Act makes provision for the establishment of Consumer Councils and other authorities for the settlement of consumer disputes and for matters connected therewith.
2. **Protection of rights of consumers.** The Act seeks, inter alia, to promote and protect the rights of consumers such as—
 - a) The right to be protected against marketing of goods or services which are hazardous to life and property ;
 - b) The right to be informed about the quality, quantity, potency, purity, standard and price of goods or services so as to protect the consumers against unfair trade practices ;
 - c) The right to be assured, wherever possible, access to goods and services at competitive prices;
 - d) The right to be heard and to be assured that consumers' interest will receive due consideration at appropriate forums ;
 - e) The right to seek redressal against unfair trade practices or restrictive trade practices or unscrupulous exploitation of consumers ; and
 - f) Right to consumer education.
3. **Consumer Protection Councils.** The above objects are sought to be promoted and protected by the Consumer Protection Councils established at the Central and State levels.
4. **Quasi-Judicial machinery for speedy redressal of consumer disputes.** The Act seeks to provide speedy and simple redressal to consumer disputes. For this purpose, there has been set up quasi-judicial machinery at the district, State and Central levels.

IMPORTANT DEFINITION

COMPLAINANT Sec. 2(1) (13)

"Complainant" means-

- (i) a consumer; or
- (ii) any voluntary consumer association registered under the Companies Act, 1956 (1 of 1956). Or under any other law for the time being in force; or
- (iii) the Central Government or any State Government, who or which makes a complaint;
- (iv) one or more consumers, where there are numerous consumers having the same interest
- (v) in case of death of a consumer, his legal heir or representative*

COMPLAINT Sec. 2(1) (C)

"Complaint" means any allegation in writing made by a complaint that-

- (i) an unfair trade practice or a restrictive trade practice has been adopted by any trader; or **service provider***
- (ii) the goods bought by him or agreed to be bought by him; suffer from one or more defect;
- (iii) the services hired or availed of or agreed to be hired or availed by him suffer from deficiency in any respect;



- (iv) a trader or the **service provider** has charged for the goods or for the service mentioned in the complaint a price in excess of the price (a) fixed by or under any law for the time being in force, (b) displayed on the goods or any package containing such goods, (c) displayed on the price list exhibited by him, (d) agreed between the parties.
- (v) Goods which will be hazardous to life and safety when used are being offered for sale to the public in contravention of any law for the time being in force.
- (vi) service which are hazardous or likely to be hazardous to life and safety of the public when used**

CONSUMER Sec. 2(1) (D)

'Consumer' means any person who:

- (i) Consumer of goods buys any goods for a consideration which has been paid or promised or partly paid and partly promised, or under any system of deferred payment and includes any user of such goods other than the person who buys such goods for consideration paid or promised or partly paid or partly promised, or under any system of deferred payment when such use is made with the approval of such person, but does not include a person who obtains such goods for resale or for any commercial purpose; or
- (ii) Consumer of services hires or avails of any services for a consideration which has been paid or promised or partly paid and partly promised, or under any system of deferred payment and includes any beneficiary of such services other than the person who hires or avails of the services for consideration paid or promised, or partly paid and partly promised, or under any system of deferred payment, when such services are availed of with the approval of the first mentioned person;"

CONSUMER DISPUTE

"Consumer dispute" means a dispute where the person against whom a complaint has been made, denies or disputes the allegations contained in the complaint;

DEFECT

"defect" means any fault, imperfection or shortcoming in the quality, quantity, potency, purity, or standard which is required to be maintained by or under any law for the time being for or under any contract, express or implied or as it claimed by the trader in any manner whatsoever in relation to any goods;"

"Manufacture" means a person who-

- (i) makes or manufactures any goods or parts thereof : or
- (ii) does not make or manufacture any goods but assembles parts thereof made or manufactured by other; or
- (iii) puts or causes to be put his own mark on any goods made or manufactured by any other manufacture.

PERSON

: "person" includes-

- (i) a firm whether registered or not;
- (ii) a Hindu undivided family;
- (iii) a co-operative society
- (iv) every other association of persons whether registered under the Societies Registration Act.

Consumer Disputes Redressal Agencies Three-Tier Redressal System

Introduction

The object of the Consumer Protection, 1986, is to provide better protection to consumers. To secure this object, the Act intends to provide simple, speedy and inexpensive redressal to the consumers' grievances. For this purpose, the Act provides for the establishment of three-tier quasi-judicial



machinery at the District, State and National levels. **The three consumer disputes redressal agencies at the different levels are as under:**

1. Consumer Disputes Redressal Forum to be known as District Forum at the District level.
2. Consumer Disputes Redressal Commission to be known as State Commission at the State level.
3. National Consumer Disputes Redressal Commission to be known as National Commission at the National level.

ESTABLISHMENT OF AGENCIES

1 DISTRICT FORUM

The 'District Forum' is the short name of the Consumer Disputes Redressal Forum established in the District under Section 9(a) of the Consumer Protection Act, It is the redressal agency to deal with the complaints of the consumers at the District level.

Legal provision relating to District forum:

1. Composition of the district forum

The District Forum is a body of three persons appointed by the State Government. The qualifications of the President and other members are as follow:

(a) President: A person who is, or has been or is qualified to be, a District Judge shall be the President of the District Forum.

(b) Other Member: A part from the President, the District Forum shall consist of two other members one of whom shall be a woman. The qualification for appointment of other members are:

- (i) He/She must not be less than 36 years of age.
- (ii) He/She must possess a bachelor's degree from a recognized university.
- (iii) He/She must be a person of ability, integrity and standing and have adequate knowledge and experience of at least 10 years in dealing with problems relating to economics, law, commerce, accountancy, industry, public affairs or administrations.

2. Appointment of members of District Forum: The appointment of the President and of the members shall be made by the State Government on the recommendation of the selection committee consisting of (a) the President of the State Commission, (b) Secretary, Law Department of the State, and (c) Secretary, in charge of the Department dealing with consumer affairs in the State.

3. Disqualifications of members :

- a) If he has been convicted and sentenced to imprisonment for an offence, which, in the opinion of the State Government, involves moral turpitude, or
- b) If he is an undischarged insolvent, or
- c) If he is of unsound mind and stands so declared by a competent court, or
- d) If he has been removed or dismissed from the services of the Government or a body corporate owned or controlled by the Government,

4. Tenure of office of the members of the District Forum

A person may act as a President or a member of the District Forum for 5 years or up to the age of 65 years, whichever is earlier. Thus, in any case, a person cannot hold the office of the President or that of the member beyond the age of 65 years.

5 Vacancy in the office of the District Forum

The officer of the President or of any member of the forum may become vacation on his attaining the age of sixty-five years.

5. Jurisdiction of the District Forum

The District Forum has the jurisdiction to entertain complaints where the value of the goods or services and the compensation, if any, claimed does not exceed rupees 20 lakhs.

PROCEDURE ON RECEIPT OF COMPLAIN SECTION-13

The district forum has to observe the procedure mentioned in section. It may be summarized as follows-



- I. **Reference of complaint to opposite party** – Whenever the district forum receives a complaint, relating to a goods, it should refer a copy of the complaint to the opposite party. It must be given within 30 days of receiving the complaint. However, it may be extended by a further period not exceeding 15 days.
- II. **On refusal of dispute by opposite party** – When the opposite party, on receipt of a complaint, denies or disputes the allegations in the complaint or does not reply within the time, the District Forum shall proceed to settle dispute. The Act does not make mandatory the personal hearing of complaint or opposite party, probably to expedite the disposal of cases.

Who can complaint in the district forum?

A complaint in relation to any goods sold or delivered or any services provided may be filed with a district forum by –

1. Consumer of goods/service
2. Any recognized consumer association.
3. Central or state government

For the purpose of this section “recognized consumer association” means any voluntary consumer association registered under the companies Act 1956 or any other law for the time being in force (Sec. 12)

Power of the District forum –

The district forum shall have the same power as are vested in a civil court under the code of civil procedure, 1908 while trying a suit in respect of the following matter, namely-

1. The summoning and enforcing attendance of any defendant or witness and examining the fitness on oath.
2. The discovery and production of any document or other material object producible as evidence.
3. The reception of evidence on affidavits
4. The requisitioning of the report of the concerned analysis or test from the appropriate laboratory or from any other relevant source.
5. Issuing of any commission for the examination of any witness and
6. Any other matter which may be prescribed.

Findings of the District forum (Sec. 14)

If the district forum is satisfied that the goods suffer from any of the defects specified in the complaint or that any of the allegations contained in the complaint about the services are proved, it shall issue an order to the opposite party directing him to take one or more of the following things namely-

- a) To remove the defect pointed out by the appropriate laboratory from the goods in question.
- b) To replace the goods with new goods of similar description this shall be free from any defect.
- c) To return the price or charge as the case may be paid by the complainant.

STATE COMMISSION

‘State Commission’ is the short name given to the Consumer Disputes Redressal Commission established in the State under Section 9(b) of the Consumer Protection Act, 1986 [Section] 2(1) (p). It is the redressal agency to deal with the complaints of the consumers at the State level.

Composition of the State Commission

Section 16(1) makes the following provisions regarding the qualifications of the President and other members:

- (a) **President:** A person who is or has been a judge of a High Court shall be the President of the State Commission.
- (b) **Other members:** Apart from the President, the State Commission shall consist of two other member one of whom shall be a woman. The qualifications for appointment of the other member are:



- (i) He/She must not be less than 35 year of age.
- (ii) He/She must possess a bachelor's degree from a recognized university.
- (iii) He/She must be a person of ability, integrity and standing and have adequate knowledge or experience of at least 10 years in dealing with problems relating to economics, law, commerce, accountancy, industry, public affairs or administration.

1. Appointment of members of State Commission

The appointment of the President shall be made by the State Government after consultation with the Chief Justice of the High Court of the State. And the appointment of the other members shall be made by the State Government on the recommendation of the selection committee consisting of (a) President of the State Commission, (b) Secretary of the Law Department of the State and (c) Secretary, in charge of Department dealing with consumer affairs in the State.

2. Disqualification of members

These disqualifications are the same as already discussed the District Forum.

3. Tenure of office of the members of the State Commission

The President or the member of the State Commission shall hold office for a term of 5 years or up to the age of 67 year, whichever is earlier. Thus, in any case, a person cannot hold the office of President or that of a member beyond the age of 67 years.

4. Jurisdiction of the State Commission

(a) **Pecuniary jurisdiction:** The State Commission has the jurisdiction to entertain complaints where the value of the goods or services and compensation, if any, claimed exceeds rupees 20 lakhs but does not exceed rupees one crore.

(b) **Appellate jurisdiction:** Any person aggrieved by an order made by the District Forum may prefer an appeal to the State Commission with a period of 30 days from the date of the order.

NATIONAL COMMISSION

The 'National Commission' is the short name given to the National Consumer Disputes Redressal Commission established in the country under Section 9(c) of the Consumer Protection Act, 1986.

Legal provision relating to District forum

1. Composition of the National Commission

The 'National Commission' is a body of minimum five persons appointed by the Central Government. Legally, the National Commission shall consist of a President and at least four other members.

(a) **President:** A person who is or has been a judge of the Supreme Court shall be the President of the National Commission. Thus, only the sitting or retired judges of the Supreme Court are eligible for appointment as President.

(b) **Other members:** A part from the President, the National Commission shall consist of at least four other members one of whom shall be a woman. The qualifications for appointment of other members are:

- (i) He/She must not be less than 35 year of age.
- (ii) He/She must possess a bachelor's degree from a recognized university.

He/She must be a person of ability, integrity and standing and have adequate knowledge or experience of at least 10 years in dealing with problems relating to economics, law, commerce, accountancy, industry, public affairs or administration.

2. Appointment of the members of the National Commission [Section 20(1) (a) (b):

The appointment of the President shall be made by the Central Government after consultation with the Chief Justice of India. The appointment of the other four members shall be made by the Central Government on the recommendation of the selection committee consisting of (a) sitting judge of the Supreme Court, (b) Secretary in the Department of Legal Affairs, Government of India, (c) Secretary of the Department dealing with consumer affairs in the Government of India

3. Disqualification of members



These disqualifications are the same as already discussed in case of members of District Forum and of State Commission. Any other disqualification may also be prescribed the Central Government.

4. **Tenure of office of the members of the National Commission**

The President or the members of the National Commission shall hold the office for a term of 5 year or up to the age of 70 years, whichever is earlier. Thus, in any case, a person cannot hold the office of President or that of a member beyond the age of 70 years.

5. **Jurisdiction of the National Commission**

(a) Pecuniary jurisdiction: The National Commission has the jurisdiction to entertain complaints where the value of the goods or services and compensation, if any claimed exceeds rupees 1 crore. Prior to the Consumer Protection (Amendment) Act, 2002, the National Commission had the jurisdiction where the value of this claim exceeded rupees twenty lakhs.

(b) Appellate jurisdiction: The National Commission also has the appellate jurisdiction to entertain appeals against the order of any State Commission.

CONSUMER PROTECTION COUNCILS

Consumer protection councils have been set up at national and state levels. Their object is to protect rights of consumers. Provisions with regard to consumer protection councils are contained in the consumer protection act wide section 4 to 8.

II. Central consumer protection Council -

1. Establishment of this council by a notification of the central government.
2. Central government nominates government and private members from different departments and sectors.
3. At present there are 150 members in the council.
4. Chairman of the council is central government food & civil supplies minister.
5. 3 years term of office of council.
6. If any post of the council falls vacant, it shall be filled up by a same cadre member.
7. 3 meetings are compulsory in a year time and place is fixed by chairman.
8. Main object of council is to expand and protect the rights of consumers.
 - Protection against fatal advertisement of goods/for human life services.
 - Protection against improper trade transaction and service.
 - As far as possible, a right of satisfaction about the various qualities.
 - A right of belief and confidence on goods & services.
 - A right of compensation against misbehavior in restricted trade policies.
 - A right of consumer education.

III. State consumer protection council -

1. This council is established by notification of state government.
2. The Chairman of the council is state minister of food and civil supplies.
3. State government nominates government or private members from different sectors.
4. There must be at least two meetings in a year or arrange according to convened any time.
5. Time and place of meetings shall be fixed by the chairman.
6. Object of council is to protect the interest and rights of consumer in the state.



UNIT-V

Company

The word 'company' in its literary sense, conveys the idea of togetherness. In the business world, the word 'company' may be found being used loosely for any large business concern. In the legal sense the word 'company' point towards a very specific form of business set-up, floated and run by more than one person. This is the body corporate form of business organization.

Definition of a Company

Company : sec.3 (1)(i)- " Company means a company formed and registered under this Act or an existing company"

clause (ii) of Sec.3 (1) defines an existing company as follows :

"Existing company" means a company formed and registered under any of the previous companies laws..."

Thus, every such organization would be a company which is registered under the relevant law as a company before or after the enactment of the companies Act, 1956.

Lord Justice Lindley: "A company is an association of persons who contribute money to a common stock and employed in some trade or business and who share the profit and loss arising there from. The common stock so contributed is denoted in money in money and is the capital of the company".

Haney : "A Company is an artificial person created by law having separate entity with a perpetual succession and common seal"

SPECIAL FEATURES OF A COMPANY

1. Incorporated entity
2. Artificial person
3. Separate legal identity
4. Limited liability
5. Perpetual succession
6. Transferable shares
7. Separate property
8. Common Seal
9. Capacity to sue and be sued
10. Governance by majority

LIFTING OR PIERCING CORPORATE VEIL

Lifting of corporate veil is a fiction of law which means disregarding the separate legal entity of a company and identifying the realities which lay behind the legal façade. In applying this doctrine, the court ignores the company and concerns itself directly with the members or directors.

The various cases in which the corporate veil is lifted may be put under two categories:

I. Statutory Exceptions-

1. When the number of members falls below statutory minimum (Sec. 45)
2. Misdescription in prospectus (Sec. 62)
3. Failure to refund application money [Sec.69 (5)]
4. Misdescription representation of name (Sec. 147)
5. Subsidiary company (Sec. 212 & 214)
6. For investigation into affairs of related companies (Sec. 239)
7. for investigation of ownership of a company (Sec. 247)
8. Fraudulent conduct (Sec. 542)
9. Liability for pre-incorporation contracts

II. Judicial Exceptions -

1. Determination of character of company
2. For protection of revenue
3. Prevention of fraud
4. Where the company is acting as the agent of the shareholders
5. Avoidance of welfare laws
6. To punish for contempt of court



KINDS OF COMPANIES

The incorporated bodies or the companies may be put in various classes on the basis of following aspects :

- A. Mode of formation.
- B. Permitted number of members.
- C. Liability of members
- D. Control of management.

A. ON THE BASIS OF MODE OF FORMATION

There are two modes under which a corporate body may be formed; one, through a special Act of parliament, and two, through registration under the Companies Act.

1. **Statutory Companies:** Corporations created under the special legislations of parliament or state legislatures may be called statutory companies; examples: Life Insurance Corporation of India, Food Corporation of India etc. The Acts creating such corporations would include in them all necessary rules and regulations for the corporate bodies so created.
2. **Registered Companies:** A corporate body registered under the Companies Act, 1956 would be called the registered company.

B. ON THE BASIS OF PERMITTED NUMBER OF MEMBERS

1. Private company

Sec. 3 (iii) has defined a private company as follows :

A private company means a company which has a minimum paid-up capital of one lakh rupees or such higher paid-up capital as may be prescribed, and by its articles.

- (a) restricts the right to transfer its shares, if any;
- (b) Limits the number of its members to 50 not including:
 - (i) persons who are in the employment of the company; and
 - (ii) persons who, having been formerly in the employment of the company, were members of the company while in that employment and have continued to be members after the employment ceased.
- (c) Prohibits any invitation to the public to subscribe for any shares in, or debentures of, the company; and
- (d) Prohibits any invitation or acceptance of deposits from persons other than its members, directors or their relatives.

2. Public company

Sec. 3 (1) (iv) has defined a public company as follows :

Public Company ; A public company means a company which –

- (a) is not a private company;
- (b) has a minimum paid-up capital of five lakh rupees or such higher paid-up capital, as may be prescribed;
- (c) is a private company which is a subsidiary of a company which is not a private company.

(C) ON THE BASIS OF LIABILITY OF MEMBERS

- (a) Limited liability companies
 - (i) Limited by shares
 - (ii) Limited by guarantee
- (b) Unlimited companies
 1. **Company limited by shares.** In the matter of members liability, this is the most common type of company. Such a company must have a share capital. The members liability is limited up to the amount of shares held. Sec. 12(2) (a) states that such a company would be:
 2. **Guarantee company.** This is also called a company limited by guarantee. The guarantee is received from the members. Such a company may or may not have share capital. This is also a limited liability company but the amount of members liability is based not on the shares



held but on the guarantee given by the members. Sec. 12(2) (b) states that this is a company having the liability of its members limited by the memorandum to such amount as the members may respectively undertake by the memorandum to contribute to the assets of the company in the event of its being wound up.

3. **Unlimited company.** The unlimited company may or may not have share capital. The members liability being unlimited, the quantum of share capital is not a very crucial matter. If it has share capital, it can be easily increased or reduced by altering the Articles. The restrictions on changes in capital are not relevant for an unlimited liability company. Such a company may purchase its own shares and is free from the restrictions provided by Sec. 77.

(D) ON THE BASIS OF CONTROL OVER MANAGEMENT

A company is supposed to be autonomous in running its affairs but working under the supervision of law. Sometimes, however, a company may exercise control over another company. The former would be called a holding company and the latter its subsidiary company.

1. **Holding company.** A company would be a holding company in relation to another company if it possesses control over the other company. Sec 4(4) states that a company shall be deemed to be the holding company of another if, but only if, that other is its subsidiary.

2. **Subsidiary company.** Sec. 4(1) describes a subsidiary company as follows:

Subsidiary company: A company shall be deemed to be a subsidiary of another if, but only if,

- (a) that other controls the composition of its Board of directors; or
- (b) that other -
 - (i) where the first mentioned company is an existing company in respect of which the holders of preference shares issued before the commencement of this Act have the same voting rights in all respects as the holders of equity shares, exercises or controls more than half of the total voting power of such company;
 - (ii) where the first mentioned company is any other company, holds more than half in nominal value of its equity share capital; or
- (c) the first mentioned company is a subsidiary of any company which is that other's subsidiary.

Company M holds share capital of Rs. 5,00,000 out of Rs. 18,00,000 share capital in company R. Its subsidiary company N holds Rs. 4,50,000 capital in company R. Company R would be the subsidiary of company M since company M and its subsidiary company N together hold a majority share capital in company R.

CERTAIN OTHER KINDS OF COMPANIES

1. Non profit companies or Section 25 companies

It is not uncommon for people to form organizations or associations to pursue non business objectives, such as promotion of art, culture, science and commerce etc. Such associations may or may not be registered. If members do desire registration, then one of the options would be to get the registration under the Companies Act, 1956. Sec. 25 of the Act facilitates the registration of such non business associations as a company under the Act. For this reason, these associations are called Section 25 companies.

2. Government companies

A Government company is such a company registered under the Act in which not less than 50% of the paid-up share capital is held by the Central Government, or by any State Government or Governments, or partly by the Central Government and partly by one or more State Governments, and includes a company which is a subsidiary of a Government company as thus defined (Sec. 617).

3. Foreign companies

Foreign companies are defined in Sec. 59(1) as follows:



Foreign company: Foreign companies are the companies falling under the following two categories:

- (a) Companies incorporated outside India which, after the commencement of this Act, establish a place of business within India; and
- (b) Companies incorporated outside India which have, before the commencement of this Act, established a place of business within India and continue to have an established place of business within India at the commencement of this Act.

4. One-man company

Where almost the entire shareholding in a company is under the ownership of a single person, while a few more members, usually the family members, are there in the company to comply with the requirements of minimum number of members, such a company is commonly called a one-man company or a family company.

PRIVILEGES AND EXEMPTIONS AVAILABLE TO PRIVATE COMPANIES

The following privileges and exemptions are available to a private company:

1. The provisions of Sec. 81 dealing with the further issue of shares do not apply to a private company. So, the shares of a private company, in the event of further issue of capital, need not first be offered to the existing shareholders.
2. A certificate for commencement of business is not necessary for a private company (Sec. 149). It can commence its business as soon as the certificate of incorporation is obtained.
3. A private company need not hold a statutory meeting and file a statutory report [Sec. 165(10)].
4. In case of a private company, under Sec. 179, in a general meeting of the company, a demand for poll on a resolution, may be made by only one member.
5. At the time of getting the company incorporated with the Registrar of companies, the directors of a private company are not required to file with the Registrar their consent in writing to act in that capacity and the undertaking to take up qualification shares.
6. It can proceed to allot shares without having to wait for any such thing as minimum subscription.
7. A life director appointed by a private company on or before April 1, 1952, cannot be removed by the company in general meeting.
8. A private company need not keep an index of members (Sec. 151).
9. Financial assistance to acquire own shares. A private company is not prohibited from giving financial assistance to any one for purchasing or subscribing for its own shares (Sec. 77).
10. Share capital and voting rights. The provisions that there should be only two kinds of share capital i.e. equity share capital and preference share capital, and that voting rights should be proportionate to the capital paid-up, are not applicable to a private company.
11. Provisions as to general meetings. The provisions of sections 171 to 186 relating to the holding of general meetings do not apply on a private company.
12. Managerial remuneration. A private company is exempted from the provisions of Sec. 198 which fixes the overall limit to the managerial remuneration at 11% of net profits.
13. Appointment of firm or body corporate. A private company may appoint a firm or body corporate to any office or place of profit under it for any period.
14. Restriction on disclosure of profit and loss. No person other than a member of the company is entitled to inspect the profit and loss account of a private company in the office of the Registrar (Sec. 220).

Distinction between Private and Public Company

1. **Paid-up capital.** A private company must have a minimum paid-up capital of Rs. 1 lakh whereas the public company should have at least Rs. 5 lakhs.
2. **Minimum number of members.** In the case of a private company, minimum number of persons to form a company is two while it is seven in the case of a public company (Sec. 12).



3. **Maximum number of members.** In case of private company the membership must not exceed 50 whereas there is no such restriction on the maximum number of members for a public company (Sec. 3).
4. **Transferability of shares.** In a private company, the right to transfer shares is restricted, whereas in the case of public company the shares are freely transferable (Secs. 3 and 82).
5. **Prospectus.** A private company cannot issue a prospectus; while a public company may issue a prospectus to invite the general public to subscribe for its shares or debentures.
6. **Statement in lieu of prospectus.** A public company, if it does not issue a prospectus, is required to file a Statement in lieu of prospectus with the Registrar of Companies at least 3 days before allotment. A private company is not required to do this.
7. **Minimum number of directors.** A private company must have at least two directors, whereas a public company must have at least three directors (Sec. 252).
8. **Increase in number of directors.** The number of directors in a private company may be increased to any extent but in case of a public company if the maximum number of directors is more than twelve, then the approval of the Central Government is necessary for any increase in the number of directors (Secs 258 and 259).
9. **Appointment of directors.** Directors of a private company may be appointed by a single resolution, but it is not so in case of a public company where each director is to be appointed by a separate resolution (Sec. 255).
10. **Retirement of directors.** Directors of a private company are not required to retire by rotation, but in case of a public company at least 2/3rds of the directors must retire by rotation at each annual general meeting (Sec. 256).
11. **Quorum for general meetings.** Two members personally present form the quorum in a private company but in a public company the number is five members (Sec. 174).

When does a private company become a public company?

1. **Conversion by default (Sec. 43).** Where a default is made by a private company in complying with the essential requirements of a private company (viz., restriction on transfer of shares, limitation of the number of members to 50 and prohibition of invitation to the public to buy shares or debentures), the company ceases to enjoy the privileges and exemptions conferred on a private company. In such a case, the provisions of the Companies Act apply to it as if it were not a private company.
2. **Conversion by operation of law (deemed public company)** The Companies (Amendment) Act, 1960 introduced a new Sec. 43-A with a view to deal with those private companies which employed public money to a large extent but escaped the restrictions and limitations as to disclosure as apply to public companies]
The Companies (Amendment) Act, 2000 abolished Sec. 43-A with effect from 13th December, 2000.
3. **Conversion by choice or volition (Sec. 44).** If a private company so alters its Articles that they do not contain the provisions which make it a private company, it shall cease to be a private company as on the date of the alteration. It shall then file with the Registrar, within 30 days, either a prospectus or a statement in lieu of prospectus..

A private company which becomes a public company shall also

1. File a copy of the resolution altering the Articles
2. Take steps to raise its membership to at least 7 if it is below that number
3. Alter the regulations contained in the Articles which are inconsistent with those of a public company



Conversion of a public company into a private company

A public company may be converted into a private company by passing a special resolution. The special resolution should be to change the Articles of the company so as to include the conditions as prescribed in Sec. 3 (!) (iii) Which make a company a private company? An alteration made in the Articles which has the effect of converting a public company into a private company shall have effect only when such alteration has been approved by the Central Government. Where the alteration has been approved by the Central Government a printed copy of the Articles as altered shall be filed by the company with the Registrar within 1 month of the date of receipt of approval.

FORMATION OF A COMPANY

The process of formation of a company can be divided and discuss under the following four stages:

1. Promotion;
2. Incorporation or Registration;
3. Capital Subscription;
4. Commencement of Business

Of these stages only the first two are necessary for the formation of a private company, and of a public company not having any share capital. A public company having a share capital has to pass through all the four stages mentioned above before it can commence business or exercise any borrowing powers. (Sec. 149)

PROMOTION

Before a company can be formed, there must be some persons who intended to form a company and who take the necessary steps to carry that intention into operation. Such persons are called promoters. The promotion of a company is a comprehensive terms denoting that process by which a company is incorporated and floated, or established financially as a joint concern, by the issue of a prospectus.

The 'promotion' is the first stage in the formation of a company. Promotion may be defined as "the discovery of business opportunities and the subsequent organisation of funds, property and managerial ability into a business concern for the purpose of making profit there from."

The Promoter

"A person who originates a scheme for the formation of the company, has the memorandum and articles prepared, executed and registered and finds the first directors and settles the terms of the preliminary contracts and prospectus (if any) and making arrangement for advertising and circulating the prospectus and placing the capital is a promoter."

A person may be a promoter even if the undertakes a lesser active role in the formation of a company. Section 62(6) makes it clear that person who acts in a professional capacity is not a promoter, like an advocate, solicitor and auditor.

Who can be a promoter:- A promoter may be a natural person or a company, firm or association of persons, whether a person is or is not a promoter depends upon the nature of the role played by him in the promotion of business.

Functions/Role of a Promoter

1. **To originate the scheme for formation of the company:** Promoter conceives the idea of forming a company after a through study of the business world and identify the business fields which are unexplored or may be explored further.
2. **To secure the cooperation of the required number of persons willing to associate themselves with the project:** In fact, the minimum number of members required to join a private company is two and in case of a public company seven.
3. **Nomenclature:** The promoters have to verify from Registrar of Companies whether the proposed name is available. Promoters usually give three names in order of preference.
4. **To get the documents of the proposed company prepared:** No company can be incorporated unless the M.O.A. and A.O.A. and other documents are not field with the Registrar. Since the company takes birth from the date when certificate of incorporation is issued.



5. To appoint bankers, legal advisors of the company:

6. Arrangement of capital: If a company is to be incorporated as a private company, it has to make arrangement of its capital through private sources as a private cannot invite public to subscribe for its shares.

However, if the company is to be incorporated as a public company and it intends to invite public for subscribing its shares, then the promoters have to prepare the prospectus.

Consent of Directors: Since the first directors are to be appointed by the promoters so they must get the consent of such persons who are to be so appointed.

7. To enter into preliminary Contracts with the Vendors:

8. To arrange for filing of the necessary documents with the Registrar:

Legal Position of Promoters

While the accurate description of a promoter may be difficult, his legal position is quite clear.

A Promoter is neither a trustee nor an agent- The reason is that a person cannot act as an agent or trustee for a person who is non-existent and the company is non-existent at the time when the promoters act for it.

Fiduciary relations with the company: - It does not mean that the promoters do not have any legal relationship with the proposed company. The legal position of a promoter can be correctly described by saying that he stands in a fiduciary position (relationship of trust and confidence) in relation to the company to be promoted.

Duties of Promoters

Since the promoter occupies a position of total trust and confidence in relation to the company promoted by him. The promoters in their fiduciary capacity have the following duties:

1. Duty not to make any secret profit: A promoter cannot make either directly or indirectly any profits at the expenses of the company he promotes, without the knowledge and consent of the company and that if he does so, in disregard of this rule, the company can compel him to account for it.

In case, a promoter makes a secret profit, the company has the following remedies against him:

(a) **Rescission of the contract-** The Company may rescind the contract, in which the promoter has made secret profits.

(b) Order for repayment of secret profits.

2. Duty to make full disclosure to the company of all relevant facts: It is the duty of the promoter to disclose to the company all relevant facts including any profit made from the sale of his own property to the company and his personal interest in a transaction with the company.

Erlanger vs. New Sombrero Phosphate Co. (1878) 3 A.C. 1218.

3. Duty towards future allottees: It is a duty of the promoters to ensure that the real truth is disclosed to those who are induced by the promoters to join the company and the future allottees of the shares.

Liability of Promoters:-

(1) Section 56 lays down matters to be stated and reports to be set out in the prospectus. Promoter may be held liable for the non-compliance of the provisions of this section.

(2) Under section 62, a promoter is liable for any untrue statement in the prospectus to a person who has subscribed for any shares or debentures on the faith of the prospectus.

(3) Section 63 specifies the criminal liabilities for issuing a prospectus which contains untrue statement. The punishment prescribed, is imprisonment for a term which may extend to two years or with fine which may extend to Rs. 50,000 or with both.

(4) A promoter can be held liable if he had mis-applied or retained any of the property of the company or is found guilty of breach of trust or misfeasance in relation to the company.

Remuneration to Promoters:-

The promoters cannot claim as a matter of right any remuneration from the company for the service rendered for a company that is yet in existence. Even where the articles of a company specifically provide that a specified sum may be paid to the promoters for their services, it does not give the promoters a right to claim remuneration or to sue the company for the same.



However, the normal ways of rewarding the promoters for their valuable services are as follows:

- (i) They may be paid a lump sum either in cash or in the form of shares or debentures of the company.
- (ii) They may be given commission on the purchase price of the business taken over by the company.
- (iii) They may be inducted into the Board of Directors.
- (iv) He may be allowed to sell his own property to the company for cash at an inflated price, after he has made a full disclosure about the valuation and the profit earned to an independent Board of Directors.
- (v) The company may give him an option to subscribe for a certain number of the company's unissued shares at par when their market price is higher.

Preliminary Contracts and Pre-incorporation Contracts

The promoters of a company usually enter into contracts to acquire some property or right for the company which is yet to be incorporated, such contracts are called pre-incorporation or preliminary contracts.

Provisional Contracts

The provisional contracts are those contracts which are entered by a public company after incorporation but before the company becomes entitled to commence business.

INCORPORATION OF A COMPANY

"Any seven or more persons or where the company to be formed will be a private company, any two or more persons, associated for any lawful purpose may, by subscribing their name to a memorandum of associations and otherwise complying with the requirement of this Act in respect of registration, form an incorporated company, with or without limited liability." [Sec. 12]

Disqualifications of subscribers of MOA: The 'person' who subscribes to the memorandum of association of the company should not be an infant, an undischarged insolvent, an alien enemy, a lunatic and a person disqualified by law from entering into a contract.

Procedure of Incorporation of a Company

Before proceeding to register a company, the promoters have to decide the following aspects:

(a) Type of company: the promoters must decide whether they want to incorporate a private company or a public company.

(b) Availability of Name: A company is identified by the name with which it is registered.

As per section 13, the memorandum of association of a company should state the name of the company.

Promoters of a company under a proposed name may make an application to Registrar of Companies in e-Form No. 1A, accompanied with a fee of Rs. 500.

Corporate Identity Number: Registrar of Companies is to allot a Corporate Identity Number (CIN) to each company registered on or after Nov. 1, 2000.

Documents to be filed with the Registrar:-

- | | |
|-------------------------------|---|
| 1. Memorandum of Association | 6. Particulars of Directors |
| 2. Articles of Association | 7. Notice of Registered Address |
| 3. Copy of Proposed Agreement | 8. Statutory Declaration |
| 4. Power of Attorney | 9. Filing of Document with the Registrar for Registration |
| 5. Consent of the Directors | |

On registration, the Registrar will issue a certificate of incorporation whereby he certifies that the company is incorporated and in the case of a limited company, that the company is limited. **(Sec. 39)**

- (1)** This certificate contains the name of the company, the date of its issue, and the signature of the Registrar with his seal.



Effect of Certificate of Incorporation

From the date of incorporation mentioned in the certificate of incorporation, such of the subscribers of the memorandum and other persons, as may from time to time be members of the company, shall be a body corporate by the name contained in the memorandum.

Conclusiveness of the Certificate of Incorporation:-

The certificate of incorporation shall be conclusive evidence that:

- (i) all the requirements of the Act have been complied with in respect of registration.
- (ii) The company is duly registered, and
- (iii) that the company has come into existence on the date of the certificate.
- (iv)

CAPITAL SUBSCRIPTION

After being registered and receiving the Certificate of Incorporation, Company is ready for flotation. It can go ahead with raising capital from the public to commence its operation satisfactorily.

Since private company is prohibited from inviting public to subscribe, it can raise the necessary capital from friends and relatives.

Section 70 of the Companies Act requires every public company to take either of the following two steps:

- (i) Issue a Prospectus if public is to be invited to subscribe to its share capital, or
- (ii) File 'A Statute In Lieu of Prospectus', in case capital has been arranged privately.

COMMENCEMENT OF BUSINESS

A private company can commence business immediately after incorporation. However, in the case of companies other than the private company and a company having no share capital, further requirement is to be complied with, namely, obtaining 'a certificate of commencement of businesses before it commence its business.

No public company can commence any business on exercise any borrowing power unless the Certificate to Commence Business is obtained.

Penalty: If any public company having share capital commences business or exercises borrowing power without obtaining the certificate to commence business, then every person at fault shall be liable to fine which may extend to Rs. 5,000 for every day of default. **(Sec. 149 (b))**

It should be noted that the company commences business within one year of its incorporation or otherwise it is liable to be wound up by the Tribunal. **(Sec. 433 (c))**

Procedure for the Incorporation of a Private Company: The procedure for the incorporation of a private company is the same as that of a public limited company with the following charges:

- (a) There should be at least two subscribers in place of seven.
- (b) e-Form No. 29 (relating to consent of directors) need not be prepared and filed.
- (c) Registration of articles of association in compulsory.

MEMORANDUM OF ASSOCIATION

Definition

Memorandum means the memorandum of association of a company as originally framed or as altered from time to time in pursuance of any previous companies law or of this Act.

Palmer,..... It contains the objects for which the company is formed and therefore, identifies the possible scope of its operations beyond which its actions cannot go. It defines as well as confines the powers of the company.

Significance

1. It determines some basic features of the company being formed, such as its name, registered office, capital etc.
2. It determines the area of activity for the company.



3. It lays down the basic parameters to guide the relationship between the company and the outsiders who deal with the company.

Sec. 13 refers to the contents of the Memorandum

1. Name clause :

Every company has to adopt its corporate name carefully. This name has to be stated in the Memorandum. The name of the company as approved by the Registrar would need to be given sufficient display as per the rules, such as outside every office, on the letters, notices etc. In the case of a limited liability company, the word Limited Private limited must be there as the last words of the name.

2. Registered office clause :

This clause requires the mention of the state in which the registered office of the company is to be situate. A company must have a registered office as a stable place for its location and as its domicile.

3. Object clause :

The memorandum must state the objects for which the company is being formed. This clause defines the area of activities for which the company is being formed. Any activity outside the limits defined by this clause would be ultra vires (beyond the powers) for the company and the company can neither do it nor ratify it if it is done by any agent without its sanction.

4. Liability clause :

The nature of liability of the members of the company being formed must be indicated by the memorandum. The memorandum of a company limited by shares or by guarantee shall also state that the liability of its members is limited [Sec. 13(2)]

5. Capital clause :

The capital clause lays down the maximum limit of the capital beyond which the company cannot issue shares. This amount is described as registered capital or authorized capital or nominal capital.

6. Subscription or association clause

This clause contains the declaration by the signatories to the Memorandum about their desire to be formed into a company, about their commitment to acquire the qualification shares, if any, and the personal details about the subscribers with their signatures attested by a witness.

ALTERATION OF MEMORANDUM

(A) Alteration of name clause

A company may, by special resolution and with the approval of the Central Government signified in writing change its name : If a company makes default in complying with any direction given by the government. Shall be punishable with fine which may extend to Rs. 1000 for every day during which the default continues (Sec. 22).

(B) Alteration of registered office clause

(i) Change of office within the same city. The rule contained in Sec. 146(2) implies that a company can make a change in the registered office within the local limits of the same city, town or village through a resolution of the Board of directors. Such a change must be brought to the notice of the Registrar within 30 days of the change.

(ii) Change from one city to another within the same state. This situation attracts the provisions of sec. 17A and Sec. 146. Sec. 146(2) lays down that a change in the registered office from one city to another within the same state would require the passing of a special resolution in the general meeting of the company and filing its copy with the Registrar within 30 days.

(iii) Change of registered office from one state to another.

The office is shifted to the new state and the address notified to the new Registrar within 30 days of shifting to the new office.

(C) Alteration of liability clause

A company can alter its objects clause also, but, since it is a very vital clause in the Memorandum.



- a) passing a special resolution in the general meeting [Sec. 17(1)]
- b) Filing the resolution with the Registrar with 1 month together with the printed copy of the altered Memorandum.

(D) Alternation of liability clause

The liability of members of the company may be altered only to increase it. The liability cannot be decreased. And the liability can be increased only if the members give their consent in writing either before or after the alteration.

This will require the following :

Authorization of the articles of association; (b) A special resolution of the company. (c) A written consent of the affected officer of the company if he was holding the office before the date of alteration.

(E) Alteration of capital clause

The alteration in the capital clause may take many forms :

- (a) Alteration of share capital (Sec. 94,95,97)
- (b) Reduction of share capital (Sec. 100 to 1004)
- (c) Variation of the rights of shareholders (Sec. 106,107)
- (d) Re-arrangement of share capital (Sec. 391).

This alteration requires :

- (i) Authorization by the Articles of Association.
- (ii) An ordinary resolution in the general meeting.
- (iii) No confirmation by court or any other authority.
- (iv) A notice has to be given to the Registrar of the alteration made within 30 days of the resolution.

DOCTRINE OF ULTRA VIRES

The doctrine of ultra vires is one of the most important principles of company law.

The word ultra means beyond, and the word vires means powers. So, the doctrine of ultra vires means that it is beyond a company's powers to do those activities which have been kept outside the scope of the objects clause in the Memorandum. If any such act is undertaken by the company or any of its agents on its behalf, the act shall not be deemed to be done by the company. Even the entire Board or the body of the shareholders cannot approve or ratify it.

Effects of ultra vires Transactions

- (i) Contracts are void ab initial. A contract which is ultra vires the company is void ab initial. Under such a contract, the company cannot sue or be sued upon.
- (ii) Personal liability of directors to the company. If the directors of the company utilize funds of the company in ultra vires transactions, they would be personally liable to compensate the company for any loss suffered by the company.
- (iii) Personal liability of directors to third parties. As the agent of the company, the directors are expected to act within the authority available to them. If they act outside the scope of this authority by presenting themselves to the possessing the authority, this will be a breach of warranty of their authority.
- (iv) Property acquired ultra vires. The funds of the company may be spent in acquiring a property ultra vires. The company's right over the acquired property shall be secure and intact.
- (v) Injunction. In case a company has done is about to do an act ultra vires its Memorandum, any shareholder may seek an order of injunction from the court restraining the company from doing so.

Where the Doctrine does not Apply under some circumstances as mentioned below:

- (i) Where the act is ultra vires only the directors, it may be ratified by the company.
- (ii) Where the act is ultra vires only the Articles of Association, the Articles may be altered to make the action intra vires the articles.
- (iii) Where the act is intra vires but has been done in violation of some bye-laws of the company, the Board or the general meeting may condone it.



ARTICLES OF ASSOCIATION

The Articles of Association is the second important document to be prepared by the promoter and then submitted at the time of registration. The Articles contain the rules and regulations and the bye-laws of the company to govern its internal affairs and functioning.

Definition: According Sec. 2(2) of the Act

“Articles means the articles of association of a company as originally framed or as altered from time to time in pursuance of any previous companies law or of this Act, including, so far as they apply to the company the regulations contained in Table A in Schedule I annexed to this Act”.

A public company limited by shares may either frame its own Articles and get them registered or may adopt Table A of Schedule I as its Articles.

Form

Regarding the form of the articles Sec. 30 states that the Articles shall be printed, be divided into paragraphs numbered consecutively, and be signed by each subscriber of the memorandum of association.

Contents

- 1) Various classes of shares the company shall issue and their rights.
- 2) Procedure for issue of shares and their allotment.
- 3) Procedure for issuing share certificates and share warrants.
- 4) Forfeiture of shares and the procedure for their re-issue.
- 5) Procedure for transfer and transmission of shares.
- 6) Calls on shares.
- 7) Conversion of shares into stock.
- 8) Payment of commission on shares and debentures to underwriters.
- 9) Borrowing powers of directors.
- 10) Rules for adoption for preliminary contracts, if any,
- 11) Re-organization and consolidation of share capital.
- 12) Alteration of shares capital.
- 13) Payment of dividends and creation of reserves.
- 14) General meetings, proxies and polls.
- 15) Voting rights of members.
- 16) Keeping of books of account and their audit.
- 17) Rules regarding use of the Common Seal of the company.
- 18) Appointment, powers, duties, qualifications and remuneration of directors.
- 19) Appointment, powers, duties, remuneration, etc of auditors.
- 20) Appointment, powers, duties, qualifications, remuneration etc of the managing director, manager and secretary, if any.
- 21) Lien on shares.
- 22) Capitalization of profits.
- 23) Board meeting and their proceedings
- 24) Rules as to resolutions.
- 25) Winding up of the company.

ALTERATION OF ARTICLES

According to Sec. 31, the Articles of a company can be altered by a special resolution. A copy of the special resolution which authorized the alteration of Articles must be sent to the Registrar together with the copy of the altered Articles within 30 days of passing of the resolution.

Procedure of Alteration

1. **Where the form of company remain unchanged:** The following procedure is required to be followed for effective alteration of the articles :
 - a. Approval of the Board



- b. Special resolution
- c. Filing resolution with the Registrar

2. Where a private company is converted in to a public company

1. The Board shall approve the draft resolution
2. Special resolution
3. To get the approval of the Central Government to the alteration.
4. File with the Registrar a printed copy of the altered articles. It shall be filled within one month from date of receipt of the order of approval.

Limitations of freedom to alter the Articles

- (i) Alteration must not exceed the scope of or conflict with the Memorandum.
- (ii) The alteration must not be inconsistent with the provisions of the Companies Act or any other law.
- (iii) The Articles cannot be made to include anything which is in itself unlawful or opposed to public policy.
- (iv) The alteration must not seek to undo the alteration made by the CLB or Tribunal in the documents of the company.
- (v) The alteration must be bona fide and for the benefit of the company as a whole.
- (vi) The alteration must not amount to a fraud by majority on the minority.
- (vii) The alteration cannot be done to break a contract with a third party.
- (viii) An alteration would not be complete unless it is followed by the approval of the Central Government wherever necessary.

Distinction between Memorandum and Articles

The memorandum and articles are two important documents for incorporation and governance of a company. The two may, however, be distinguished on the basis of the following points :

- (i) The memorandum contains the basic conditions associated with the incorporation of the company. This includes the name, the maximum capital and the total area of activity of the company etc. The articles however, are the rules governing the internal functioning of the company.
- (ii) The memorandum is a supreme document sub-ordinate to the Companies Act only. The articles is the document sub-ordinate to the memorandum and cannot override it.
- (iii) A memorandum has to be compulsorily registered. The articles may not be registered.
- (iv) The memorandum defines the relationship between the company and the outside world. The articles determine the relationship between the company and the members.
- (v) The alteration in memorandum requires a somewhat difficult procedure. The articles will require a simple procedure for alteration.
- (vi) The acts of the company which are ultra vires the memorandum cannot be made valid through their ratification by the company. However, the acts ultra vires the articles can be made valid through their ratification if they are intra vires the memorandum.

SHARE

Ordinary Shares (Equity Share)

Equity shares capital means all share capital which is not preference share capital. In other words, a share or share capital which does not give the definition of preference shares or preference share capital, is equity share capital.

Equity shareholders receive dividend out of profits as recommended by the Board of directors and as declared by the shareholders in an annual general meeting but after preference shares have been paid their fixed dividend.

Moreover, equity shareholders have a right to vote on every resolution placed in the meeting and the voting right shall be in proportion to the paid up equity capital. Unless a company issue equity shares with differential rights.



Preference Shares

Preference shares with reference to any company limited by shares are those which carry:

- (a) A right to be paid a fixed amount of dividend or the amount of dividend, calculated at a fixed rate, e.g., 10% nominal value of shares and also.
- (b) A right to be paid the amount of capital paid up as such shares in the event of winding up of the company.

The articles share capital is the sum of total of preference shares.

Those of Preference Shares

These may be of the following types:

1. **Cumulative Preference Shares:** These share are entitled to dividend at a fixed rate whether there are profits or not. The company pays dividend if it has sufficient profits. In case the company does not have sufficient profits, dividend on cumulative preference shares will go on accumulating till it is fully paid off, such arrears are carried forward to the next year and are actually paid out of the subsequent years' profits. In the case of winding up of the company, the arrears of dividend on these shares are payable only if the article of association contains express provision in this respect. It may be noted, that all preference shares are presumed to be cumulative unless expressly stated in the articles to be non-cumulative.
2. **Non-cumulative Preference Shares:** Non-cumulative preference shares are those shares on which the arrears of dividend do not accumulate. If in a particular year there are no profits are inadequate, the shareholders shall not get anything or receive a partial dividend and they cannot claim the arrears of dividends in the subsequent year. In simple words, on such shares the unpaid dividends do not accumulate but lapse, i.e., the shareholders lose them forever.
3. **Participating Preference Shares:** The holders of such shares are entitled to receive dividend at a fixed rate and, in addition, they have a right to participate in the surplus profits along with equity shareholders after dividend at a certain rate has been paid to equity shareholders, there are surplus assets, then the holders of such shares shall be entitled to share in the surplus assets as well. Such shares can be issued only if there is a clear provision in the memorandum or articles of association or the terms of issue.
4. **Non-participating Preference Shares:** The holders of such shares are entitled to only a fixed rate of dividend and do not participate further in the surplus profits. If the articles are silent, all preference shares are deemed to be non-participating.
5. **Convertible Preferences Shares:** the holder of such shares have a right to convert these shares into equity shares within a certain period.
6. **Non-convertible Preference Shares:** The preference shares, where the holders have no right to convert their shares into equity shares are known as non-convertible preferences shares. Unless otherwise stated preference shares are assumed to be non-convertible.
7. **Redeemable Preference Shares:** ordinarily, the amounts received by the company on shares is not returned except on the winding up of the company. A company limited by shares, if authorised by its articles, may issue preference shares which are to be redeemed or repaid after a certain fixed period. Thus, the amounts received on such shares can be returned during the life-time of the company. Such shares are termed as redeemable preferences shares.

CLASSES OF CAPITAL

In view of the stages involved in collecting the money on shares, the shares capital of a company may be classified as follow:

- (1) **Authorised Capital:** It is the capital which is stated in company's memorandum of association with which the company intends to be registered. It is called the nominal or registered capital. It is the maximum amount of shares capital which a company is authorised to raise by issuing the shares.
- (2) **Issue Capital:** It is that part of the authorised capital which is actually offered (issued) to the public for subscription. Therefore, the issued capital can never be more than the authorised capital. It can



at the most be equal to the nominal capital. The balance of nominal capital remaining to be issued is called 'unissued capital'.

- (3) **Subscribed Capital:** It is that part of the issued capital which has been actually subscribed by the public. In other words, it is that part of issued capital for which the applications have been received from the public and shares allotted to them.
- (4) **Called-up Capital:** It is that part of nominal value of issued capital which has been called-up or demanded on the shares by the company. Normally, a company does not collect the full amount of shares it has allotted.
- (5) **Paid-up Capital:** It is that part of the called-up capital which has actually been received from the shareholders.
- (6) **Reserve Capital:** It is that part of the uncalled capital which cannot be called by the company except in the event of its winding up.

ISSUE OF SHARES AT PREMIUM

The term 'Securities' has been defined under Section 2(45AA) inserted by Companies (Amendment) Act, 2000. The premium is an amount in excess of par value or nominal value or face value of the securities (shares). Where a company issues securities at a premium whether for cash or for a consideration other than cash, a sum equal to aggregate amount of premiums on these securities shall be transferred to Securities Premium Account. The Securities Premium Account may be applied by the company:

- (a) in paying up unissued shares of the company to be issued to the members of the company as fully paid bonus shares;
- (b) in writing off the preliminary expenses of the company;
- (c) in writing off the expenses of or commission paid or discount allowed on any issue of shares or debentures of the company.
- (d) In providing for the premium payable on the redemption of any redeemable preference shares or any debentures of the company.
- (i) A company may issue shares at a premium, i.e., at a value greater than its face value. Premium so received shall be credited to a separate account called **Securities Premium Account**.

ISSUE OF SHARES AT A DISCOUNT

Discount means a price which is less than nominal value or face value of a share. If share of Rs. 10 is issued at Rs. 8, then, 10-8, i.e., the amount of Rs.2 is discount.

When shares are issued at a price which is lower than market price but not below the face value of the shares, such an issue is not an issue at a discount.

1. A company shall not issue shares at discount except in the Company of a class already issued, if the following conditions are fulfilled, namely:
 - (i) The issue of the shares at a discount is authorised by a resolution passed by the company in general meeting and sanctioned by the company in general meeting and sanctioned by the Company Law Boards;
 - (ii) The resolution specifies the maximum rate of discount at which the share are to be issued;
 - (iii) Not less than one year has at the date of issue elapsed since the date on which the company was entitled to commence business; and
 - (iv) The shares to be issued at discount are issued within two months after the date on which the issue is sanctioned by the Company Law Board or within such extend time as the Company Law Board May allow.
2. Where a company has passed a resolution authorizing the issue of shares at a discount, it may apply to the Company Law Board for an order sanctioning the issue, on such application the Board may make an order if it thinks proper to do so, sanctioning the issue on such terms and conditions as it thinks fit.
3. Every prospectus relating to the issue of shares shall contain particulars of the discount allowed on the issue of shares.



Winding up of a company

Winding up of a company is defined as a process by which the life of a company is brought to an end and its property administered for the benefit of its members and creditors. An administrator, called the liquidator, is appointed and he takes control of the company, collects its assets, pays debts and finally distributes any surplus among the members in accordance with their rights. At the end of winding up, the company will have no assets or liabilities. When the affairs of a company are completely wound up, the dissolution of the company takes place. On dissolution, the company's name is struck off the register of the companies and its legal personality as a corporation comes to an end.

The procedure for winding up differs depending upon whether the company is registered or unregistered. A company formed by registration under the Companies Act, 1956 is known as a registered company. It also includes an existing company, which had been formed and registered under any of the earlier Companies Acts.

Difference between dissolution and winding up

1. Winding Up is first stage where assets/liabilities are realised/paid-off; Dissolution is final stage where company ceases to exist.
2. Winding up is carried on by liquidator appointed by company/court; Order for dissolution is given by court only.
3. Liquidator can represent company during winding up till dissolution; After dissolution liquidator don't represent co.
4. Creditors can prove their debts in winding up but not on dissolution
5. Winding up always don't lead to dissolution

Winding up a Registered Company

The Companies Act provides for two modes of winding up a registered company:

- A. Winding up by the Tribunal
- B. Voluntary Winding Up

A. Winding up by the Tribunal or Grounds for Compulsory Winding Up

The petition for winding up to the Tribunal may be made by:-

- The company, in case of passing a special resolution for winding up.
- A creditor, in case of a company's inability to pay debts.
- A contributory or contributories, in case of a failure to hold a statutory meeting or to file a statutory report or in case of reduction of members below the statutory minimum.
- The Registrar, on any ground provided prior approval of the Central Government has been obtained.
- A person authorized by the Central Government, in case of investigation into the business of the company where it appears from the report of the inspector that the affairs of the company have been conducted with intent to defraud its creditors, members or any other person.
- The Central or State Government, if the company has acted against the sovereignty, integrity or security of India or against public order, decency, morality, etc.

The following circumstances for the winding up of accompany by the court:

- a) If the company has, by a Special Resolution, resolved that the company be wound up by the Tribunal.
- b) If default is made in delivering the statutory report to the Registrar or in holding the statutory meeting. A petition on this ground may be filed by the Registrar or a contributory before the expiry of 14 days after the last day on which the meeting ought to have been held. The Tribunal may instead of winding up, order the holding of statutory meeting or the delivery of statutory report.
- c) If the company fails to commence its business within one year of its incorporation, or suspends its business for a whole year. The winding up on this ground is ordered only if there is no intention to carry on the business and the Tribunal's power in this situation is discretionary.
- d) If the number of members is reduced below the statutory minimum i.e. below seven in case of a public company and two in the case of a private company.
- e) If the company is unable to pay its debts.
- f) If the tribunal is of the opinion that it is just and equitable that the company should be wound up.



- g) Tribunal may inquire into the revival and rehabilitation of sick units. Its revival is unlikely, the tribunal can order its winding up.
- h) If the company has made a default in filing with the Registrar its balance sheet and profit and loss account or annual return for any five consecutive financial years
- i) If the company has acted against the interests of the sovereignty and integrity of India, the security of the State, friendly relations with foreign States, public order, decency or morality.

B. Voluntary Winding Up of a Registered Company

When a company is wound up by the members or the creditors without the intervention of Tribunal, it is called as voluntary winding up. It may take place by:-

- By passing an ordinary resolution in the general meeting if: -
 - (i) the period fixed for the duration of the company by the articles has expired; or
 - (ii) Some event on the happening of which company is to be dissolved, has happened.
- By passing a special resolution to wind up voluntarily for any reason whatsoever.

Within 14 days of passing the resolution, whether ordinary or special, it must be advertised in the Official Gazette and also in some important newspaper circulating in the district of the registered office of the company.

The Act provides two methods for voluntary winding up:-

1. Members' voluntary winding up
2. Creditor's voluntary winding up

1. Members' voluntary winding up

It is possible in the case of solvent companies which are capable of paying their liabilities in full. There are two conditions for such winding up:-

- a) A declaration of solvency must be made by a majority of directors, or all of them if they are two in number. It will state that the company will be able to pay its debts in full in a specified period not exceeding three years from commencement of winding up. It shall be made five weeks preceding the date of resolution for winding up and filed with the Registrar. It shall be accompanied by a copy of the report of auditors on Profit & Loss Account and Balance Sheet, and also a statement of assets and liabilities upto the latest practicable date; and
- b) Shareholders must pass an ordinary or special resolution for winding up of the company.

The provisions applicable to members' voluntary winding up are as follows:-

- a) Appointment of liquidator and fixation of his remuneration by the General Meeting.
- b) Cessation of Board's power on appointment of liquidator except so far as may have been sanctioned by the General Meeting, or the liquidator.
- c) Filling up of vacancy caused by death, resignation or otherwise in the office of liquidator by the general meeting subject to an arrangement with the creditors.
- d) Sending the notice of appointment of liquidator to the Registrar.
- e) Power of liquidator to accept shares or like interest as a consideration for the sale of business of the company provided special resolution has been passed to this effect.
- f) Duty of liquidator to call creditors' meeting in case of insolvency of the company and place a statement of assets and liabilities before them.
- g) Liquidator's duty to convene a General Meeting at the end of each year.
- h) Liquidator's duty to make an account of winding up and lay the same before the final meeting.

2. Creditor's voluntary winding up

It is possible in the case of insolvent companies. It requires the holding of meetings of creditors besides those of the members right from the beginning of the process of voluntary winding up. It is the creditors who get the right to appoint liquidator and hence, the winding up proceedings are dominated by the creditors.

The provisions applicable to creditors' voluntary winding up are as follows:-



- The Board of Directors shall convene a meeting of creditors on the same day or the next day after the meeting at which winding up resolution is to be proposed.
- A statement of position of the company and a list of creditors along with list of their claims shall be placed before the meeting of creditors.
- A copy of resolution passed at creditors' meeting shall be filed with Registrar within 30 days of its passing.
- It shall be done at respective meetings of members and creditors. In case of difference, the nominee of creditors shall be the liquidator.
- A five-member Committee of Inspection is appointed by creditors to supervise the work of liquidator.
- Fixation of remuneration of liquidator by creditors or committee of inspection.
- Cessation of board's powers on appointment of liquidator.

As soon as the affairs of the company are wound up, the liquidator shall call a final meeting of the company as well as that of the creditors through an advertisement in local newspapers as well as in the Official Gazette at least one month before the meeting and place the accounts before it. Within one week of meeting, liquidator shall send to Registrar a copy of accounts and a return of resolutions.

Winding up an Unregistered Company

According to the Companies Act, an unregistered company includes any partnership, association, or company consisting of more than seven persons at the time when petition for winding up is presented. But it will not cover the following:-

- A railway company incorporated by an Act of Parliament or other Indian law or any Act of the British Parliament;
- A company registered under the Companies Act, 1956;
- A company registered under any previous company laws.
- An illegal association formed against the provisions of the Act.

However, a foreign company carrying on business in India can be wound up as an unregistered company even if it has been dissolved or has ceased to exist under the laws of the country of its incorporation.

The provisions relating to winding up of an unregistered company:-

- Such a company can be wound up by the Tribunal but never voluntarily.
- Circumstances in which unregistered company may be wound up are as follows:-
 - If the company has been dissolved or has ceased to carry on business or is carrying on business only for the purpose of winding up its affairs.
 - If the company is unable to pay its debts.
 - If the Tribunal regards it as just and equitable to wind up the company.
- Contributory means a person who is liable to contribute to the assets of a company in the event of its being wound up. Every person shall be considered a contributory if he is liable to pay any of the following amounts:-
 - Any debt or liability of the company;
 - Any sum for adjustment of rights of members among themselves;
 - Any cost, charges and expenses of winding up;
- On the making of winding up order, any legal proceeding can be filed only with the leave of the Tribunal.



UNIT-VI

**Limited Liability Partnership Act, 2008
(LLP Act)**

Introduction

With the growth of Indian economy, the role played by its entrepreneurs as well as its technical and professional manpower has been acknowledged internationally. In this background, a need was felt for a new corporate form that would provide an alternative to the traditional partnership which exposes its partners to unlimited personal liability and a statute based governance structure of limited liability companies.

Need -

At present, under partnership law, the maximum numbers of partners a partnership firm can have is twenty also the partners are liable jointly and severally and most importantly their liability is unlimited which means that the personal property of the partners can also be attached for the satisfaction of the debts, in addition to the capital contributed by the partners in the firm.

This is the principal reason why partnerships firms of professionals have not grown in size to meet the challenges posed today. Not only are the firm's assets completely liquidated under the standard principles of the partnership law, but the partners are also jointly and severally liable for the entire liabilities of the partnership. Thus, the present system acts as a deterrent for the growth and expansion of service based organizations.

Object of Limited Liability Partnership Act, 2008 [LLP] -

Limited Liability Partnership [LLP] is viewed as an alternative corporate business vehicle that provides the benefits of the limited liability but allows its members the flexibility of organizing their internal structure as a partnership based on a mutually arrived agreement. LLP form is expected to enable entrepreneurs, professionals and enterprises providing services of any kind or engaged in scientific and technical disciplines, to form commercially efficient vehicles suited to their requirements.

With this background, Limited Liability Partnership Act, 2008 [LLP Act] was enacted on January 7, 2009. Subsequently, Government of India [GOI] notified various provisions of LLP Act on 31st March 2009. GOI has, on April 1, 2009, also notified the Limited Liability Partnership Rules, 2009 [LLP Rules] in respect of registration and operational aspects under the LLP Act.

The salient features of the Limited Liability Partnership Act, 2008, are as follows:-

- (i) the LLP shall be a body corporate and a legal entity separate from its partners;
- (ii) the mutual rights and duties of the partners of the LLP inter se and those of the LLP and its partners shall be governed by an agreement between the partners inter se or between the LLP and the partners subject to the provisions of the Act. The Act provides flexibility to devise the agreement as per their choice. In the absence of any such agreement, the mutual rights and duties shall be governed by the provisions of the Act;
- (iii) the LLP will be a separate legal entity, liable to the full extent of its assets, with the liability of the partners being limited to their agreed contribution in the LLP. No partner would be liable on account of the independent or unauthorised actions of other partners or their misconduct. The liabilities of the LLP and its partners who are found to have acted with intent to defraud creditors or for any fraudulent purpose shall be unlimited for all or any of the debts or other liabilities of the LLP;
- (iv) every LLP shall have at least two partners and shall also have at least two individuals as Designated Partners, of whom at least one shall be resident in India.
- (v) the LLP shall be under an obligation to maintain annual accounts reflecting true and fair view of its state of affairs. A statement of accounts and solvency shall be filed by every LLP with the Registrar every year. The accounts of LLPs shall also be audited, subject to any class of LLPs being exempted from this requirement by the Central Government;
- (vi) the Central Government shall have powers to investigate the affairs of a LLP, if required, by appointment of competent inspector, for the purpose;
- (vii) the compromise or arrangement including merger and amalgamation of LLPs shall be in accordance with the provisions of the act;



(viii) a firm, private company or an unlisted public company would be allowed to be converted into a LLP in accordance with the provisions of the act.

(ix) the winding up of the LLP may be either voluntary or by the Tribunal to be established under the Companies Act, 1956. Till the Tribunal is established, the power in this regard has been given to the High Court;

(x) the act confers powers on the Central Government to apply provisions of the Companies Act, 1956 as appropriate, by notification with such changes or modifications as deemed necessary. However, such notifications shall be laid in draft before each House of Parliament for a total period of 30 days and shall be subject to any modification as may be approved by both Houses;

(xi) the Indian Partnership Act, 1932 shall not be applicable to LLPs.

KEY DEFINITIONS:-

"Body Corporate" is defined to mean a company as defined under the Companies Act, 1956 and includes LLP, LLP incorporated outside India, a foreign company but does not include a corporation sole, a registered co-operative society and any other body corporate notified by the Central Government (not being a company defined under the Companies Act, 1956 or LLP defined under LLP Act). **[Section 2(1)(d)]**

"Business" includes every trade, profession, service and occupation. **[Section 2(1)(e)]**

"Financial Year", in relation to LLP, means the period from 1st April of a year to the 31st March of the following year. However, in case of LLP incorporated after 30th September, financial year may end on 31st March of the year next following that year. **[Section 2(1)(l)]**

"Foreign Limited Liability Partnership" means a LLP formed, incorporated or registered outside India which establishes a place of business within India. **[Section 2(1)(m)]**

"Limited Liability Partnership" means a partnership formed and registered under LLP Act. **[Section 2(1)(n)]**

"Limited liability partnership" agreement means any written agreement between the partners of LLP or between the LLP and its partners which determines the mutual rights and duties of the partners and their rights and duties in relation to that LLP. **[Section 2(1)(o)]**

"Partner" in relation to LLP means a person who becomes a partner in a LLP in accordance with the LLP agreement. **[Section 2(1)(q)]**

NATURE OF LLP:-

• LLP is a –

— "body corporate" formed and incorporated under LLP Act;

— Legal entity separate from its partners and has perpetual succession. **[Sec. 3(1)]**

• Two or more partners are required to form an LLP. Any individual or a body corporate can be a partner in a LLP.

In case if individual is a partner, he should not be –

— found to be of unsound mind; or

— an undischarged insolvent; or

— a person who has applied to be adjudicated as insolvent and the application is pending

[Sections 5 and 6]

DESIGNATED PARTNERS [SECTION 7]

LLP shall have at least two "designated partners" who are individuals and at least one of them shall be "resident in India". In case one or more of the partners of a LLP are bodies corporate, at least two individuals who are partners of such LLP or nominees of such bodies corporate shall act as "designated partners"

— "Resident in India" means a person who has stayed in India for minimum 182 days during the immediately preceding 1 year.

Designated partner is responsible for compliance with the provisions of LLP Act.

Designated Partner is required to obtain Designated Partner Identification Number [DPIN] from the Central Government.

Application for allotment of DPIN needs to be submitted online on the LLP website along with the necessary



proof duly attested and certified as prescribed.

INCORPORATION OF LLP [SECTIONS 11 TO 21]

Procedure for incorporation of LLP is similar to the procedure for incorporation of a company under the Companies Act, 1956. Applicants are first required to file the application for reservation of name with the Registrar of Companies [ROC]. Once the name applied is approved by the ROC, the documents for incorporation of LLP need to be filed.

Name of every LLP shall end with the words "Limited Liability Partnership" or "LLP".

Name which is undesirable or nearly resembles to that of any other partnership firm or LLP or anybody corporate or trade mark, is not allowed.

Any entity (body corporate/registered partnership firm) which has a name similar to the name of LLP which has been incorporated subsequently may seek change of name of such LLP through ROC within 24 months from date of registration of such LLP.

No person shall carry on business under any name/title which contains the words "Limited Liability Partnership" or "LLP" without duly incorporating it as LLP under the LLP Act.

LLP is required to file with the ROC, the LLP agreement ratified by all the partners within 30 days of incorporation of LLP.

PARTNERS AND THEIR RELATIONS AND EXTENT OF LIABILITY [SEC 22 TO 31]

Mutual rights and duties of partners of a LLP inter se and those of the LLP and its partners shall be governed by an agreement between the partners, or agreement between the LLP and its partners. In absence of any such agreements, the mutual rights and duties shall be governed by the LLP Act.

Every partner of a LLP is, for the purpose of the business of LLP, the agent of LLP, but not of other partners.

LLP, being a separate legal entity, shall be liable to the full extent of its assets whereas the liability of the partners of LLP shall be limited to their agreed contribution in the LLP.

LLP is not bound by anything done by a partner in dealing with a person if –

- the partner in fact has no authority to act for the LLP in doing a particular act; and
- the person knows that he has no authority or does not know or believe him to be a partner of the LLP

LLP is liable if the partner of a LLP is liable to any person for wrongful act/omission on his part in the course of business of LLP/with its authority

Obligation of LLP whether arising in contract or otherwise, shall solely be the obligation of LLP. Liabilities of LLP shall be met out of properties of LLP.

Partner is not personally liable for the obligations of LLP solely by reason of being a partner of LLP.

No partner is liable for the wrongful act or omission of any other partner of LLP, but the partner will be personally liable for his own wrongful act or omission.

The liability of the LLP and partners who are found to have acted with intent to defraud creditors or for any fraudulent purpose shall be unlimited for all or any of the debts or other liabilities of the LLP.

Cessation of a partner on grounds like resignation, death, dissolution of LLP, declaration that a person is of unsound mind, declared/applied to be adjudged as insolvent etc. will not be effective unless –

- The person has notice that the partner has ceased to be so; or
- Notice of cessation has been delivered to ROC.

The notice of cessation may be filed by the outgoing partner if he has reasonable cause to believe that LLP has not filed the said notice.

CONTRIBUTION BY PARTNER [SECTIONS 32 AND 33]

A contribution of a partner to the capital of LLP may consist of any of the –

- tangible, movable or immovable property
- intangible property
- Other benefit to the LLP including money, promissory notes, contracts for services performed or to be performed.

The obligation of a partner for the contribution shall be as per the LLP agreement.



Creditor, which extends credit or acts in reliance on an obligation described in the LLP agreement, without the notice of any compromise made between the partners, may enforce the original obligation against such partner.

AUDIT/FINANCIAL DISCLOSURES [SECTIONS 34 AND 35]

LLP shall maintain the prescribed books of accounts relating to its affairs on cash or accrual basis and according to the double entry system of accounting.

The accounts of every LLP are required to be audited, except in following situations:

- When turnover does not exceed Rs. 40,00,000/- in any financial year; or
- Where contribution does not exceed Rs. 25,00,000/-

Central Government has powers to exempt certain class of LLP from requirement of compulsory audit.

LLP are required to file following documents with the ROC –

- Statement of Account and Solvency, within 30 days from the end of 6 months of the financial year;
- Annual return within 60 days from the end of the financial year.

ASSIGNMENT & TRANSFER OF PARTNERSHIP RIGHTS [SEC.42]

The rights of a partner to a share of the profits and losses of the LLP and to receive distribution in accordance with the LLP agreement are transferable, either wholly or in part. However, such transfer of rights does not cause either disassociation of the partner or a dissolution and winding up of the LLP.

Such transfer of right, shall not, by itself entitle, the assignee or the transferee to participate in the management or conduct of the activities of the LLP or access information concerning the transactions of the LLP.

FOREIGN LLP [SECTION 59 AND RULE 34]

On establishment of a place of business in India, foreign LLP are required to file prescribed documents for registration with ROC within 30 days of the establishment in India.

Any alteration in the constitution documents, overseas principle office address and partner of foreign LLP are required to be filed with the ROC in the prescribed form within 60 days of the close of the financial year.

Any alteration in the certificate of registration of foreign LLP, authorized representative in India and principle place of business in India are required to be filed with the ROC in the prescribed form within 30 days of alteration.

Foreign LLP ceasing to have a place of business in India, are required to give notice to ROC in the prescribed form within 30 days of its intention to close the place of business and from the date of such notice, the obligation of Foreign LLP to file any document with the ROC shall cease, provided it has no other place of business in India and it has filed all the documents due for filing as on the date of the notice.

CONVERSION OF PARTNERSHIP FIRM/PRIVATE COMPANY/UNLISTED PUBLIC COMPANY INTO LLP [SECTIONS 55 TO 58, SECOND, THIRD AND FOURTH SCHEDULES]

GOI has, on May 22, 2009, notified provisions relating to conversion of –

- a partnership firm as defined under the Indian Partnership Act, 1932 into LLP;
- a private limited company into LLP;
- an unlisted public company into LLP.

Second, Third and Fourth Schedules to the LLP Act contain provisions relating to conversion of a partnership firm into LLP, a private limited company into LLP and unlisted public company into LLP, respectively.

Eligibility for conversion:

— Firm into LLP : Firm can be converted into LLP if all the partners of firm become the partners of LLP and no one else.

— Company into LLP : Private limited company/unlisted public company can be converted if and only if -

(a) there is no security interest in its assets subsisting or in force at the time of application for conversion; and

(b) all the shareholders of the company become partners of LLP and no one else.

• For conversion of firm/private limited company/unlisted public company into LLP, the partners of the firm/shareholders of company are required to file a statement and incorporation documents in the prescribed



form with the ROC.

- On receiving the documents for conversion, ROC shall register the documents and issue certificate of registration specifying the date of registration as LLP. Upon registration by ROC, LLP shall intimate Registrar of Firm [ROF]/ROC, as the case may be, about conversion within 15 days of registration.
- On and from the date specified in the certificate of registration issued by ROC -
 - all tangible (movable/immovable) & intangible property, liabilities, interest, obligation etc. relating to the firm/private limited company/unlisted public company and the whole of the undertaking of the firm/private limited company/unlisted public company, shall be transferred to and shall vest in the LLP without further assurance, act or deed.
 - firm/private limited company/unlisted public company shall be deemed to be dissolved and removed from the records of ROF/ROC, as the case may be.
- If any property/rights, etc. of the partnership firm/private limited company/unlisted public company is registered with any authority, LLP shall take steps to notify the authority of the conversion.
- Upon conversion, following things/events in favour of or against the firm/private limited company/unlisted public company on the date of registration may be continued, completed and enforced by or against the LLP:
 - all proceedings, conviction, ruling, order or judgment of any Court, Tribunal or other authority pending in any Court or Tribunal or before any authority on the date of registration
 - every agreement irrespective of whether or not the rights and liabilities there under could be assigned,
 - deeds, contracts, schemes, bonds, agreements, applications, instruments and arrangements
 - every contract of employment
 - appointment in any role or capacity
 - any approval, permit or license issued under any other Act, etc.
- In case of a firm, every partner of a firm which is converted into a LLP shall continue to be personally liable (jointly and severally with LLP) for the liabilities and obligations of the firm incurred prior to the conversion or which arose from any contract entered into prior to the conversion. In case any such partner discharges any such liability or obligation he shall be entitled (subject to any agreement with the LLP to the contrary) to be fully indemnified by LLP in respect of such liability or obligation.
- For a period of 12 months commencing on or before 14 days from the date of registration, LLP shall ensure that every official correspondence of LLP bears the following:
 - a statement that it was, as from the date of registration, converted from a firm/private limited company/unlisted public company into a LLP; and
 - the name and registration number, if applicable, of the firm/a private limited company/an unlisted public company from which it was converted.

GENERAL PARTNERSHIP	LLP
Liability of partners unlimited.	Liability of partners limited to contribution.
Partners jointly and severally liable.	Partners not liable for act of other partners.
Partnership firms are neither body corporate nor do they have perpetual succession and legal entity.	LLP is a body corporate having perpetual succession and legal entity.
Registration of partnership is not mandatory.	Incorporation of LLP is mandatory.
Partnership cannot have more than 20 partners.	LLP can have more than 20 partners.



COMPANY	LLP
Incorporation procedure comparatively complex than LLP.	Incorporation procedure relatively simple and expeditious.
Management structure usually complex – shareholders do not ordinarily participate in day to day management.	Flexible management structure – Partners are entitled to participate in management.
Capital structure relatively less flexible than LLP.	Flexible capital structure.
Elaborate provision relating to redressal in case of oppression and mismanagement.	No provision relating to redressal in case of oppression and mismanagement.
Complex statutory compliance requirements.	Limited statutory compliances as compared to Companies.

COMPROMISE, ARRANGEMENT OR RECONSTRUCTION OF LLPS

[SECTION 60]

Provisions have been made in the LLP Act for allowing a compromise and arrangement including mergers and amalgamations.

Compromise and arrangement can be between LLP and its creditors or between LLP and its partners.

If majority representing 3/4th in value of creditors or partners, at the meeting, agree to compromise or arrangement shall, if sanctioned by National Company Law Tribunal [NCLT] be binding on all the creditors, all the partners and LLP. NCLT to pass order subject to disclosure of all material facts/latest financial position and pendency of investigation proceedings.

NCLT order shall be filed with the ROC within 30 days, in order to be effective.

In case of scheme of the amalgamation, NCLT shall pass order only on receipt of report from the ROC that the affairs of the LLP (transferor LLP) have not been conducted in the manner prejudicial to the interest of the partner/public.

WINDING-UP OF LLP [SECTIONS 63 AND 64]

LLPs may be wound-up either voluntarily or by NCLT. LLP may be wound up by NCLT if –

- LLP decides to wound up by NCLT;
- Number of partners is reduced below 2 for a period of more than 6 months;
- LLP is unable to pay its debts;
- LLP has acted against the interests of the sovereignty and integrity of India, the security of the State or public order;
- LLP has defaulted in filing Statement of Account and Solvency or annual return with the ROC for 5 consecutive financial years; or
- NCLT is of the opinion that it is just and equitable that the LLP be wound up.

In January 2010, MCA had notified that certain provisions relating to winding-up of a company under the Companies Act, 1956 will also be applicable to a LLP. The notification also provides details of modification in the provisions of the Companies Act relating to winding up for its applicability to winding up of LLP under the LLP Act. Subsequently, on 30 March 2010, issued Limited Liability Partnership (Winding up and Dissolution) Rules, 2010.

MISCELLANEOUS PROVISIONS



The Central government has been empowered to apply any of the provisions of the Companies Act, 1956 to LLPs with suitable changes or modification. [Section 67]

ROC may strike off the name of LLP from the register of LLP if LLP is not carrying on business or its operation, in accordance with the provisions of LLP Act in the manner prescribed. [Section 75]

Forms/documents required to be filed under the LLP shall be filed in electronic form online on the LLP portal duly authenticated by the partner/designated partner with a digital signature and further attested by the practicing chartered accountant/company secretary/cost accountant whenever required. [Section 68]

Presently all the provisions of the LLP Act, other than those relating to winding-up and dissolution of LLP and appellate provisions to be exercised by NCLT and National Company Law Appellate Tribunal [NCLAT], have been brought into force.

Till the constitution of NCLT and NCLAT under the Companies Act, 1956, the powers of NCLT and NCLAT will be exercised by the Company Law Board or High Court as is specified in the LLP Act. [Section 81]

Unless specifically provided, the provisions of the Indian Partnership Act, 1932 are not applicable to LLPs. [Section 4]

Merits of LLP

- 1) Renowned and accepted form of business worldwide in comparison to Company.
- 2) Easy to form or easy to establish and low cost of formation.
- 3) Body Corporate (Separate Legal Entity)
- 4) Limited Liability
- 5) Perpetual Succession
- 6) Flexible to manage i.e. easy to manage and run.
- 7) Easy transferable ownership
- 8) Capacity to sue
- 9) Lesser compliances
- 10) No requirement of any minimum capital contribution.
- 11) No restrictions as to maximum number of partners.
- 12) LLP & its partners are distinct from each other.
- 13) Partners are not liable for Act of partners.
- 14) Less Compliance level.
- 15) No exposure to personal assets of the partners except in case of fraud.
- 16) Less requirement as to maintenance of statutory records.
- 17) Less Government Intervention.
- 18) Easy to dissolve or wind-up.
- 19) Professionals can form Multi-disciplinary Professional LLP, which was not allowed earlier.
- 20) Audit requirement only in case of contributions exceeding Rs. 25 lakh or turnover exceeding Rs. 40 lakh.

Demerits of LLP

- 1) Any act of the partner without the other partner, may bind the LLP
- 2) Under some cases, liability may extend to personal assets of partners.
- 3) Cannot raise money from Public.

Conclusion

The LLP will act as an engine of growth for economic development of the country and would lead to the growth of professional services in the country. With the liberalisation and globalisation of Indian economy, the LLP, as an alternate mode of carrying business, will encourage joint ventures and would make Indian service sectors globally competitive. LLP structure will enable Small & Medium Enterprises and family partnerships to expand as they will be able to admit outsiders with capital or skill as partners. The hybrid structure of LLP will facilitate entrepreneurs, service providers and professionals to organize and operate in an innovative and efficient manner for effectively competing in the global market.