



**BAOU**  
Education  
for All

**DR. BABASAHEB AMBEDKAR  
OPEN UNIVERSITY**

**MBA01C106  
Semester 1**



# BUSINESS LAW

## Message for the Students

Dr. Babasaheb Ambedkar Open (University is the only state Open University, established by the Government of Gujarat by the Act No. 14 of 1994 passed by the Gujarat State Legislature; in the memory of the creator of Indian Constitution and Bharat Ratna Dr. Babasaheb Ambedkar. We Stand at the seventh position in terms of establishment of the Open Universities in the country. The University provides as many as 54 courses including various Certificate, Diploma, UG, PG as well as Doctoral to strengthen Higher Education across the state.



On the occasion of the birth anniversary of Babasaheb Ambedkar, the Gujarat government secured a quiet place with the latest convenience for University, and created a building with all the modern amenities named 'Jyotirmay' Parisar. The Board of Management of the University has greatly contributed to the making of the University and will continue to this by all the means.

Education is the perceived capital investment. Education can contribute more to improving the quality of the people. Here I remember the educational philosophy laid down by Shri Swami Vivekananda:

***“We want the education by which the character is formed, strength of mind is Increased, the intellect is expand and by which one can stand on one’s own feet”.***

In order to provide students with qualitative, skill and life oriented education at their threshold. Dr. Babaasaheb Ambedkar Open University is dedicated to this very manifestation of education. The university is incessantly working to provide higher education to the wider mass across the state of Gujarat and prepare them to face day to day challenges and lead their lives with all the capacity for the upliftment of the society in general and the nation in particular.

The university following the core motto ‘स्वाध्यायः परमम् तपः’ does believe in offering enriched curriculum to the student. The university has come up with lucid material for the better understanding of the students in their concerned subject. With this, the university has widened scope for those students who

are not able to continue with their education in regular/conventional mode. In every subject a dedicated term for Self Learning Material comprising of Programme advisory committee members, content writers and content and language reviewers has been formed to cater the needs of the students.

Matching with the pace of the digital world, the university has its own digital platform Omkar-e to provide education through ICT. Very soon, the University going to offer new online Certificate and Diploma programme on various subjects like Yoga, Naturopathy, and Indian Classical Dance etc. would be available as elective also.

With all these efforts, Dr. Babasaheb Ambedkar Open University is in the process of being core centre of Knowledge and Education and we invite you to join hands to this pious *Yajna* and bring the dreams of Dr. Babasaheb Ambedkar of Harmonious Society come true.



Prof. Ami Upadhyay  
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Ahmedabad.

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**SEMESTER-1**  
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**Dr. Babasaheb Ambedkar Open University**  
(Established by Government of Gujarat)

**BUSINESS LAW**  
**SEMESTER-1**

**BLOCK**

**1**

<b>Unit-1</b>	01
The Indian contract, 1872-I	
<b>Unit-2</b>	29
Indian contract Act, – 1872 – II	
<b>Unit-3</b>	65
Sales of goods Act, 1930- I & II	
<b>Unit-4</b>	95
Indian Partnership Act, 1932 & The limited liability partnership act, 2008	
<b>Unit-5</b>	118
The Negotiable Instruments Act, 1881 I & II	

**BLOCK**

**2**

<b>Unit-6</b>	132
The Information Technology Act, 2000	
<b>Unit-7</b>	150
Intellectual Property Rights (IPR)	
<b>Unit-8</b>	167
Indian Companies Act, 2013	
<b>Unit-9</b>	208
Consumer Protection Act, 1986	
<b>Unit-10</b>	223
Competition Act, 2002	





- 1.0 INTRODUCTION TO LAW**
- 1.1 INTRODUCTION TO CONTRACT LAW**
- 1.2 CLASSIFICATION OF CONTRACTS**
- 1.3 OFFER AND ACCEPTANCE**
- 1.4 CONSIDERATION**
- 1.5 CAPACITY OF PARTIES**
- 1.6 FREE CONSENTS**
- 1.7 LEGALITY OF OBJECT**
- ❖ CHECK YOUR PROGRESS**

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**1.0 INTRODUCTION TO LAW**

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As a social being, man comes into contact with people in different capacities. He comes into contact, for example, with a landlord as a tenant, with Government as a taxpayer. with customers as a seller and with suppliers as a buyer. These contacts or associations are the inevitable consequence of modern civilization. In all these associations, he is expected to observe a code of conduct or a set of rules. The object of these rules is to make human associations possible and conducive to the welfare of the State and its people.

**What is Law ?**

The word 'law' is a general term and has different connotations for different people, e.g.,

- (1) A citizen may think of law as a set of rules which he must obey.
- (2) A lawyer who practices law may think of law as a vocation,
- (3) A legislator may look at law as something created by him.
- (4) A judge may think of law as guiding principles to be applied in making decisions.

Thus, a man's perspective influences his notions about law and as such its meaning. It is, therefore, not possible to give a single, accurate definition of law. It is often preceded by an adjective to give it a more precise meaning, e.g., civil law, criminal law, mercantile law, industrial law, international law. However, in the legal sense with which we are concerned in this book, 'law' includes all the rules and principles which regulate our relations with other individuals and with the State.

The State regulates the conduct of its people by a set of rules. It ordains, directly or indirectly, implicitly or explicitly, a general course of conduct to be followed by the people. Such rules of conduct if recognized by the State and enforced by it on people, are termed as law. In this sense Holland, a jurist, defines law as rules of external human action enforced by the sovereign political authority. i.e., the State.

In the words of Salmond, "Law is the body of principles recognized and applied by the State in the administration of Justice." Woodrow Wilson has defined law as "that portion of the established habit and thought of mankind which has gained distinct and formal recognition in the shape of uniform rules backed by the authority and power of the government.' It represents a code of conduct which is established and enforced by the State. Law, in this sense, has a two-fold aspect: it is an abstract body of rules and also a social machinery for securing order in the community.

Law is not static. As circumstances and conditions in a society change, laws are changed to fit the requirements of the society. As such, law prevailing in a society at any point of time must be in conformity with the general sentiments, customs and aspirations of Its people. It is a living phenomenon having a real existence in relation to the facts of human affairs.

### **Need for the Knowledge of Law**

'Ignorantia Juris not excusat' is a familiar Latin maxim. This means ignorance of law is no excuse. Although it is not possible for a layman to learn every branch of law, yet it is to the advantage of each member of the community to know something of rules and regulations by which he is governed and as such he must acquaint himself with the general principles of the law of the country. This branch of law known as Mercantile or Commercial or Business Law is of particular importance to people engaged in economic and commercial activities. The term 'Mercantile Law' is used to denote that branch of law which is concerned with such matters as are usually the subject of what may be called mercantile transactions, i.e., it deals with contractual situations and the right and obligations arising out of mercantile transactions between mercantile persons A mercantile person may be a single individual, a partnership, or a joint stock company. The term 'Mercantile Law' is also used to denote the aggregate body of those legal rules which are connected with trade, industry and commerce.

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## **1.1 INTRODUCTION TO CONTRACT LAW**

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On a daily basis, we enter into lots of transactions who, from buying toothpaste to paying bills in hotels. To satisfy our daily wants and desires we enter into agreements which may be oral or written, expressed or implied which all results in contracts.

The Indian Contract Act, 1872 is an act which specifies and deals with the principles of the Law of Contract. This Act was enacted on 25th April, 1872 and subsequently came into force on the first day of September 1872. It is important to note here that ever since the enactment of this act in 1872, it has never been amended and thus the law that was made back in 1872 still stands good. The Act was passed by the British Government and is based on the principles of English Common Law.

This Act describes different stages in the formation of a contract, its performance, essential elements, breach of contract and remedies for the breach of contract. The Act deals with a number of limiting principles subject to which the parties to the contract may create certain rights or duties for themselves.

### **Sources of Mercantile Law**

The bulk of the Indian Mercantile Law is based on, and follows, the English Mercantile Law. In the absence of any specific law, usage or custom on a particular point arising before a Court, rules of the English Law, that of justice, equity and good conscience are applied. The Courts in India are, however, selective in the application of the English Law. The sources of the Indian Mercantile law are as follows:

1. **English Mercantile Law:** This is the most important source of the Indian Mercantile Law. The principal source of the English Mercantile Law is the Common Law of England as modified and supplemented by Equity and Statute Law.
2. **Statute Law:** The Contract Act, 1872, the Sale of Goods Act, 1930, the Partnership Act, 1932, the Companies Act, 1956, are instances of the Statute Law. In India, bulk of Mercantile Law is Statute Law based largely on the English Law. The law-making power in India is vested in Parliament and the State Legislatures.
3. **Judicial decisions or the system of precedents:** This is a source of law based upon previous judicial decisions which have to be followed in similar future cases. The system of precedents has been described as a system of law which applies in new combination of circumstances those rules which are derived from earlier judicial decisions.
4. **Customs and usages:** Customs and usages established by long use and constantly put into practice become binding on the parties entering into commercial transactions. A custom in order to be binding on the parties must be ancient, reasonable, certain, definite, consistent with other customs, and uniformly recognised in the ordinary course of business [C.I. & B Syndicate v. Ramachandra, A.I.R- (1968) Mys. 133]. When a custom is accepted by a court and is incorporated in a judicial decision, it becomes a legally recognised custom.

### Object of the law of contract

The law of contract is that branch of law which determines the circumstances in which promises made by the parties to a contract shall be legally binding on them. Its rules define remedies that are available in a court of law against the person who fails to perform his contract, and the conditions under which the remedies are available. It is the most important branch of business Law. It affects all of us in one way or the other. It is, however, of particular importance to people engaged in trade, commerce and industry.

The law contract introduces definiteness in business transactions. Sir William Anson observes in this connection that the law contract is intended to ensure that what a man has been led to expect shall come to pass, and that what he has been promised shall be performed. In simple words, it may be said that the purpose of the law of contract is to ensure the realisation of reasonable expectations of the parties who enter into a contract.

1. **Legal bind:** one of the primary purposes or objectives of law contract is to bind people by the law when they get into any transactions. It determines the circumstances in which promises made by the parties to a contract shall be legally binding on them.
2. **Provides Legal Remedies:** the law of contract provides legal remedies as and when needed by the parties to get into contracts. Every commercial transaction by its very nature is a legal contract and is legally binding onto the parties to it. In case of any breach or violation of the promises made by either of the parties the law can intervene and provide legal solution to the parties if sought so by any of the parties to the contract through the court.
3. **Universal application:** the law of contract is one of the most important branches of business Law and it affects all of us in one way or the other though it is of particular importance to people engaged in trade, commerce and industry. When any person gets into any transaction with another person, they are by default involving this branch of law in it. When one buys a packet of biscuits from a provision store or when a person boards a bus or when one buys or sells in the property, this branch of law is involved.
4. **Definiteness:** the law of contract does not define how a contract should be done but it lists down a few dos and don'ts about every transaction which brings about a definiteness in transactions whether related to business or otherwise.
5. **Social and economic justice:** In our society law serves as a medium of change and as a harbinger of social justice. A great part of law is designed principally to bring about all and the citizens individually and collectively. The law of contracts tries to bring about uniformity in the transaction and the dealings of the people within the society.



## Features of the law of contracts

- (1) **The act is not exhaustive:** The Indian contract act does not provide to be complete and exhaustive code. It deals with the general principles of contract and with some special contracts only. The law of contract differs from other branches of law in an important respect. The law contract does not define precisely to the parties as to, how a contract is to be done. It rather demarcates certain dos and don'ts or which can be defined as limiting factors, within which the parties to a contract are supposed to create a contract. As long as the parties to a contract do not infringe these set of prohibitions, they are free to create any contract and terms of contract as they feel free. This means that the parties to the contract create the laws for themselves. They can make what rules they like in respect of the subject matter of the agreement, and the law will give effect to their decisions.
- (2) **The law off contract is not the whole of agreement nor the whole law obligations:** There are several agreements which do not give rise to legal obligations. They are, therefore, not contracts. Similarly, there are certain obligations which do not necessarily spring from an agreement. For example, civil wrong, quasi-contracts judgements of courts etc. Salmond has rightly observed that the law contract is "not the whole law of agreements, or the whole law obligations. It is the law of those agreements which create obligations, and those obligations which have their sources in agreements." It excludes from its purview all those obligations which are not contractual in nature and agreements which are social in nature.
- (3) **Law of contract creates Jus in Personam, As distinguished from Jus in Rem:** *Jus in Rem* means a right against or in respect of a thing. *Jus in Personam* means a right against court in respect of a specific person. A *Jus in rem* is available against the world at large; *Jus in Personam* is available only against a particular person.
- (4) **Agreement and its enforceability:** If we analyse the definitions of a contract, we find that a contract essentially consists of two elements (1) agreements, and (2) its enforceability by law. An agreement is defined as "every promise and every set of promises, forming consideration for each other." "When the person to whom a proposal is made, signifies his assent there to, the proposal is it to be accepted. A proposal when expected, becomes a promise." This, in other words, means, that an agreement is an accepted proposal. To form an agreement, there must be a proposal or offer by one party and its acceptance by the other.  
To sum up: **Agreement = Offer + Acceptance**
- (5) **Consensus ad idem:** The essence of an agreement is the meeting of the minds of the parties in full and final agreement; there must, in fact, be consensus ad idem. That order could be an agreement between two parties, that must be consensus ad idem. This means that the parties to the agreement must have agreed about the subject matter of the agreement in the same sense, and at the same time. Unless there is consensus ad idem,

there can be no contract.

- (6) **Obligations:** An agreement to become a contract, must give rise to a legal obligation or duty. The term obligation is defined as a legal tie which imposes upon a definite person or persons. The necessity of doing or abstaining from doing a definite act or acts. It may relate to social or legal matters. An agreement which gives rise to a social obligation is not a contract. The rise to a legal obligation in order to become a contract.
- (7) **Agreement is a very wide term:** An agreement may be a social agreement or a legal agreement. If A invites B to a dinner and B accepts the invitation, it is a social agreement. A social agreement does not give rise to contractual obligations and is not enforceable in a court of law. It is only those agreements which are enforceable in a court of law, which are contracts.

To conclude: **Contract = Agreement + Enforceability by law.**

### **Essential Elements of a Valid Contract**

According to section 10 of the contract act, all agreements are contracts if they are made by the *free consent of parties competent* to contract, for a *lawful consideration*, with a *lawful object* and are not expressly *declared to be void*. In order to become a contract, and agreement must have the following essential elements:

- (1) **Offer and Acceptance (Minimum of two Parties):** there must be a minimum of two parties to an agreement, that is, one party making the offer and the other accepting it. The terms of an offer must be definite and the acceptance of the offer must be absolute and unconditional. The acceptance must also be according to the mode prescribed and must be communicated to the offerer.
- (2) **Intention to Create Legal Relationship:** when two parties enter into an agreement, their intention must be to create a legal relationship between them. If there is no such intention on the part of the parties, there is no contract between them. Agreements of social or domestic nature do not contemplate legal relationship and as such they are not contracts.
- (3) **Lawful Consideration:** an agreement to be enforceable by law must be supported by consideration. "Consideration" means an advantage or benefit moving from one party to another. It is the essence of a bargain. In simple words, it means "*something in return*." The agreement is legally enforceable only when both the parties give something and get something in return. A promise to do something, getting nothing in return, is usually not enforceable by law. Consideration need not necessarily be in cash or kind. It may be an act or abstinence or a promise to do or not do something. It may be past, present or future. But it must be real and lawful.

- (4) **Capacity of Parties – Competency:** the parties to the agreement must be capable of entering into a valid contract. Every person is competent to contract if he or she (a) is of the age of majority, (b) is of sound mind, and (c) is not disqualified from contracting by any law to which he is subject. Flaws in capacity to contract may arise from minority, lunacy, idiocy, drunkenness and status. If a party suffers from any flaw in capacity, the agreement is not enforceable, except in some special cases.
- (5) **Free and Genuine Consent:** it is essential to the creation of every contract that there must be a free and genuine consent of the parties to the agreement. The consent of the parties is said to be free when they are of the same mind on all the material terms of the contract. The parties are said to be of the same mind when they agree about the subject matter of the contract in the same sense, and at the same time. There is absence Free Consent if the agreement is induced by coercion, undue influence, fraud, misrepresentation or mistake.
- (6) **Lawful Object:** the object of the agreement must be lawful. In other words, it means that the object must not be (a) illegal, (b) immoral or (c) opposed to public policy. If an agreement suffers from any legal flaw, it would not be enforceable by law.
- (7) **Agreement Not Declared Void:** the agreement must not have been expressly declared void by any law in force in the country.
- (8) **Certainty and Possibility of Performance:** the agreement must be certain and not vague or indefinite. If it is vague and it is not possible to asserting its meaning it cannot be enforced.

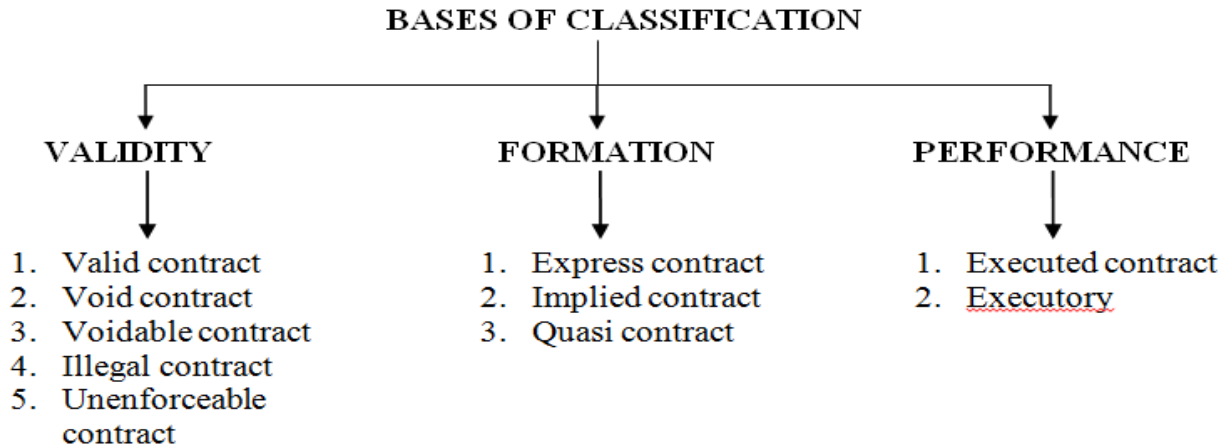
**Legal Formalities:** a contract may be made by words spoken or written. As regards to legal effects, there is no difference between contract in writing and a contract made by word of mouth. It is however, in the interests of the parties that the contract should be writing. There are some other formalities Also, which have to be complied with in order to make an agreement legally enforceable. In some cases, the document in which the contract is incorporated is to be stamped. In some other cases of contract. Besides being written is to be registered. Plus, where there is a statutory requirement that a contract should be made in writing or in the presence of a witness or registered, the required statutory formalities must be complied with.

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## 1.2 CLASSIFICATION OF CONTRACTS

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### ❖ CLASSIFICATION OF CONTRACTS



#### **Classification According to Validity**

According to validity, a contract may be:

1. Valid contract
2. Void contract
3. Voidable contract
4. Illegal contract
5. Unenforceable contract

**1. Valid contract:** According to sec 10, “All agreement(s) are contract if they are made by the free consent of parties competent to contract, for a lawful consideration and with a lawful object and are not hereby expressly declared to be void.” Thus, only a valid contract can create legal obligation.

**2. Void contract:** According to Section 2(f), “A consent which ceases to be enforceable bylaw becomes void when it ceases to be enforceable.”

An agreement which was legal and enforceable when it was entered into may subsequently become void due to –

- ❖ Impossibility of performance, and
- ❖ Change of law

**3. Voidable contract:** According to section 2(i), “An agreement which is enforceable by law at the portion of one or more parties thereto, but not at the option of other or the others, is a voidable contract. A voidable contract remains to be good till it is avoided by the party entitled to do so. Thus, a voidable contract is one, which is enforceable at the option of one of the parties of the contract. If that party does not get it enforced, it may resign it.

**4. Illegal contract:** An illegal agreement is one, which is against law in force in India. Such a contract is one which is criminal in nature or which is immoral or

which is against public policy. An illegal contract is void – *ab-initio*, i.e., legally non-operatable from the beginning itself. For example, a contract to commit dacoity is an illegal contract.

5. **Unenforceable contract:** An unenforceable contract, which, though perfectly valid in all respects, lacks some technical requirements, needed to make it enforceable such as non- registration, want of proper stamp, lack of signature, etc. Such contract can be enforceable in future if these defects are cured.

### Classification According to Formation

According to formation, contract can be

1. Express contract
  2. Implied contract
  3. Quasi contract
1. **Express Contract:** When the offer enumerates express terms, such a contract is called Express Contract. According to section 9, a contract is said to be 'express' when it is entered into by words spoken or written.
  2. **Implied contract:** An implied contract is one which is NOT expressly upon between the parties, but is inferred from the acts or conduct of parties or course of dealings between them or from the surrounding circumstances. For e.g., A takes a public bus of a particular route. I thus, an implied promise results in an implied contract.
  3. **Quasi contract:** A Quasi contract is created by law. Quasi contract does not fulfill all the requirements for the formation of a contract and in the strict sense, is not a contract at all. "These are certain obligations which are not in truth contractual in the sense of resting agreement(s), but which the law treats as if they were". Thus, in quasi contract, the law implies a promise-imposing obligations on one party and conferring rights in favour of the other even when there is no privity of contract between the parties. For example, necessities supplied to persons incapable of contracting minor, lunatics (sec.68) or responsibilities of finder of goods.

### Classification According to Performance

Contract according to performance may be –

1. Executed contract
  2. Executory contract
1. **Executed contract:** An executed contract is one where both the parties have performed their obligations under contract.

**Executory contract:** An executory contract is one where both the parties have yet to perform their obligations. For example, A agrees to deliver a car to B at ₹ 5000 and if A has not delivered the car nor B has paid, the contract is said to be executory contract.



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## **1.3 OFFER AND ACCEPTANCE**

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### **OFFER**

At the Inception of every agreement, there must be a definite offer by one person to another and its unqualified acceptance by the person to whom the offer is made. An offer is a proposal by one party to another to enter into a legally binding agreement with him. A person is said to have made a proposal, when he "signifies to another his willingness to do or to abstain from doing anything, with a view to obtaining the assent of that other to such act or abstinence." [Sec. 2 (a)].

The person making the offer is known as the offeror, proposer, or promisor and the person to whom it is made is called the offeree or proposee. When the offeree accepts the offer, he is called the acceptor or promisee [Sec. 2 (c)].

### **Rules of a Legal Offer**

- 1. Offer must be such as in law is capable of being accepted and giving rise to legal, relationship:** A social invitation, even if it is accepted, does not create legal relations because it is not so intended. An offer, therefore, must be such as would result in a valid contract when it is accepted.
- 2. Terms of-offer must be definite, unambiguous and certain and not loose and vague:** If the terms of an offer are vague or indefinite, its acceptance cannot create any contractual relationship. But if the agreement contains a machinery for ascertaining a vague term, the agreement is not void on the ground of its being vague.
- 3. An offer may be distinguished from:** (i) A declaration of intention and an announcement by person that he intends to do something gives no right of action to another. Such a declaration only means that an offer will be made or invited in future and not that an offer is made now.  
  
(ii) An invitation to make an offer or do business. Display of goods by a shopkeeper in his window, with prices marked on them, is not an offer but merely an invitation to the public to make an offer to buy the goods at the marked prices. Likewise, quotations, catalogues, advertisements in a newspaper for sale of an article, or circulars sent to potential customers do not constitute an offer. They are instead an invitation to the public to make an offer. A person, in case the prices of the goods are marked, cannot force the seller to sell the goods at those prices. He can, at the most, ask the seller to sell the goods to him, in which case he would be making an offer to the seller and it is up to the seller to accept the offer or not.
- 4. Offer must be communicated:** An offer, to be complete, must be communicated to the person to whom it is made. Unless an offer is communicated to the offeree by the offeror or by his duly authorised agent, there can be no acceptance of it. An acceptance of an offer, in ignorance of the offer, is no acceptance and does not confer any bind on the acceptor.

5. **Offer must be made with a view to obtaining the assent:** The offer to do or not to do something must be made with a view to obtaining the assent of the other party addressed and not merely with a view to disclosing the intention of making an offer.
6. **Offer should not contain a term the noncompliance of which may be assumed to amount to acceptance:** Thus, a man cannot say that if acceptance is not communicated by a certain time, the offer would be considered as accepted.
7. **A statement of price is not an offer:** A mere statement of price is not construed as an offer to sell.
8. **Special terms in a contract:** Where any special terms are to be included in a contract, these must be duly brought to the notice of the offeree at the time when the proposal is made. If it is not done and if the contract is subsequently entered into, the offeree will not be bound by them. Also, these terms should be presented in such a manner that a reasonable man can become aware of them before he enters into a contract.

#### ❖ ACCEPTANCE

A contract emerges from the acceptance of an offer. Acceptance is the act of assenting by the offeree to an offer. In other words, it is the manifestation by the offeree of his willingness to be bound by the terms of the offer. It is "to an offer what a lighted match is to a train of gunpowder. It produces something which cannot be recalled, or undone". This means when the offeree signifies his assent, to the offeror, the offer is said to be accepted. An offer when accepted becomes a promise (Sec. 2 (b)). Acceptance may be express or implied. It is express when it is communicated by words spoken or written or by doing some required act. It is implied when it is to be gathered from the surrounding circumstances or the conduct of the parties.

**Acceptance of particular offer:** When an offer made to a particular person, it can be accepted by him alone. If it is accepted by any other person, there is no valid acceptance. The rule of law is clear that if you propose to make a contract with A, B cannot substitute himself for A without your consent.

**Acceptance of general offer:** When an offer is made to world at large, any persons to whom the offer is made can accept it.

#### Rules of Legal Acceptance

1. **It must be absolute and unqualified, i.e., it must conform to the offer:** An acceptance, in order to be binding, must be absolute and unqualified [Sec. 7 (1)] in respect of all terms of the offer, whether material or immaterial, major or minor. If the parties are not ad idem on all matters concerning the offer and acceptance, there is no contract'.

2. **It must be communicated to the offeror:** To conclude a contract between the parties' the acceptance must be communicated in some perceptible form. A mere resolve or mental determination on the part of the offeree to accept an offer, when there is no external manifestation of the intention to do so, is not sufficient. In order to result in a contract, the acceptance must be a 'matter-of fact'.
3. **It must be according to the mode prescribed or usual and reasonable mode:** If the acceptance is not according to the mode prescribed, or some usual and reasonable mode (where no mode is prescribed) the offeror may intimate to the offeree within a reasonable time that the acceptance is not according to the mode prescribed and may insist that the offer must be accepted in the prescribed mode only. If he does not inform the offeree, he is deemed to have accepted the acceptance [Sec. 7 (2)].
4. **It must be given within a reasonable time:** If any time-limit is specified, the acceptance must be, given within that time. If no time limit is specified, it must be given within a reasonable time.
5. **It cannot precede an offer:** There can be no acceptance of an uncommunicated offer. Acceptance cannot precede an offer. A person who has no knowledge of an offer cannot be said to have accepted it merely because he happened to act just by chance in the manner prescribed by the offer.
6. **It must show an intention on the part of the acceptor to fulfil terms of the promise. If no such intention is present, the acceptance is not valid:** Acceptance, in order to be valid, must be made under circumstances which would show that the acceptor is able and willing to fulfil the promise. Acceptance must show an intention on the part of the acceptor to fulfil the promise. If no such intention is present, the acceptance is not valid.
7. **It must be given by the party or parties to whom the offer is made:** If the proposal is made through an agent, it is sufficient if the acceptance is communicated to him.
8. **It must be given before the offer lapses or before the offer is withdrawn:** The acceptance to an offer must be given before the offer was withdrawn. When an offeror has made an offer, he holds the right to withdraw the offer at any time prior to the acceptance. As we've discussed earlier once the acceptance is done the offer turns into a contract, but the offeror can withdraw the offer before the acceptance. Hence, it is important for the offeree to give the acceptance before the lapse of time of the offer (in case where an offer is time bound) or the offer is withdrawn.
9. **It cannot be implied from silence:** The acceptance of an offer cannot be implied from the silence of the offeree or his failure to answer, unless the offeree has by his previous conduct indicated that his silence means that he accepts.

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## 1.4 CONSIDERATION

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Consideration is one of the essential and most important factors of valid contract. It is made compulsory to have consideration to formulate a valid contract. In the law, it is used in the sense of 'quid-pro-quo', i.e., something in return. This something becomes a base or the essence for a contract. a contract is always created for mutual benefits of the parties to it consideration enables the parties to avail such benefits. This something, that is why, must be present into every contract. It is primarily a price at which, the promise of the other is bought for a reciprocal promise. This consideration with a view to satisfy the contract must move from either of the parties to the other. It is the price paid by promisee for the obligation of the promisor.

Sec.2 (d) of the Indian Contract, Act defines consideration as, "When at the behest of the promisor or any other person, the promisee has done or abstained from doing or does or abstains from doing or promises to do or to abstain from doing something, such an act or abstinence or promise is called consideration for the promise.

### Essential Elements of Consideration

1. **It must be moved at the desire of the promisor:** To be a valid consideration, it must move at the desire or request or intention of the promisor himself and none else, if it is moved at the desire not of promisee even though the promisee is benefited from consideration, the reciprocal promise made by him shall not be enforceable in law as such consideration is invalid.
2. **It may move from promisee for, any other person:** In English, law, consideration, while moving at the desire of the promisor, must move from promisee only and none else. Indian law differs in the respect and provides that consideration may move either from the promisee or any other person. According to the law, in the background of Indian circumstances, so long as consideration is present and moved at the desire of the promisor, it is immaterial who has finished it. So, consideration, if present, may move from 3<sup>rd</sup> party also.
3. **Uncertain Form:** The form of the consideration provided in a contract is not fixed or certain. As indicated by Sec.2(d). it may be formed into either an act (doing something) or abstinence (refraining from doing something) or a promise to do or not to do. Any type of consideration is considered as valid by the law and unless in contract, a party cannot insist for a particular form of consideration.
4. **It may be past, present or future:** The words of Sec.2(d) are. "Has done or abstained from doing (past) or does or abstains from doing (present) or promises to do or to abstain from doing (future)." These clearly mean that consideration may not necessarily be present. When a consideration is moved for something which has been done earlier or when a consideration is moved

for a promise to be fulfilled later on, all these are valid consideration.

5. **It need not be adequate:** It is provided by the law that something must be given and obtained by the parties in a contract. This something, however, need not necessarily be adequate or equal to something given. The law is not concerned with adequacy or inadequacy of the consideration. So long as consideration is present, it is moved at the desire of the parties and having some value in the eyes of the law. This value may not be equal for a reciprocal promise. The logic behind such a stand by the law is that it is for the parties to decide and to contemplate regarding consideration and its value at the time of formation of a contract and it is not up to the court to determine when it is sought to be enforced. If the parties are satisfied with an under-value consideration, courts do not have any role to play in the matter. The courts are not here to repair bad bargains of the parties. However, inadequacy of consideration can be treated by the court to determine the free contents of parties in a contract.
6. **It must not be illusory:** If a person is already bound to do some act or abstinence under one's legal or contractual obligation, that act or abstinence would not form a consideration for a fresh promise. That means, as it is the duty of the person to fulfil the obligation, he or she cannot expect another promise from the other party to satisfy one's legal or contractual obligation.
7. **It must be lawful:** In order for a consideration to be enforceable, it must be lawful. If it is unlawful, there shall not be any enforcement. Consideration is unlawful if it is illegal or immoral or opposed to public policy or it is of such a nature to contravene one or more provisions of any law in the country or if permitted it involves a moral turpitude, in such cases, the consideration as well as the contract will not be enforceable.

#### **Exceptions To the Rule 'No Consideration, No Contract.' Or *Nudum Pactum***

Consideration, the most important element of a valid contract, must always be present into a contract to be enforceable. If the consideration is not present into a contract, according to the Sec.25 of the Act, the contract becomes a void agreement, i.e., it is void *ab initio* and no right shall be conferred on either of the parts under the contract. That is why, the saying, 'No Consideration, No Contract' is always applicable in each case. Under the Roman Law, an agreement without consideration is called *nudum pactum* (a naked agreement) and was not enforceable and the action cannot be held to be binding upon the parties. However, applicable in each case this doctrine is also subject to certain exemptions under Sec. 25 and 185, that means if any case comes up under any of the party, these exemptions are all follows:

1. **Natural Love and Affection:** According to Sec.25, if a contract is entered into, in a written form and is registered under the laws of registration of the country between the parties who stand into near relations with each other, on account of natural Love and Affection between them, such a contract shall be enforceable even though it is without consideration. The section gives a list of relations, only which are permitted for these exceptions the list is: Father – Son; Father – Daughter;



Mother – Son; Mother – Daughter. Even though the list is permitted to be taken up, there must be a proof of natural Love and Affection between the parties. The court cannot presume such a state because it is indicated by the section that nearness of relations does not necessarily impact natural Love and Affection between the parties. As such, if it is not proved, the rule of ‘No consideration, No contract’ shall be applicable.

2. **Promise to compensate for a voluntary service:** A promise to compensate, wholly or in part, by another person for any service rendered, act done or abstinence carried on by him in past voluntarily, shall be enforceable even though that promise is not reciprocated by consideration. However, to enforce such promise following conditions must be satisfied:
  - The act or the service or the abstinence must have been made up voluntarily by the promises.
  - The promisor, now promises to compensate the promise.
  - The act done must have been a legal obligation of the promisor.
  - The promisor must be in existence when the act was carried on.
  - The act must have been a lawful one.
  
3. **Promise to pay a time barred debt:** A promise to pay a time barred debt can enforceable by the creditor even though no fresh consideration is provided by him for such a promise. According to Indian Law of limitation, a debt becomes a time-barred debt when it remains unpaid or unclaimed, wholly or part, for successive period of 3 years. On the expiry of 3<sup>rd</sup> year, such debts become legally irrecoverable and the contract between the parties becomes to an end and creditors shall not have any remedy. To enforce such a promise, however, the following conditions must be satisfied:
  - The debt must have been actually a time barred debt
  - The debtor must provide the promise after expiry of period of information.
  - The debt must be a lawful one.
  
4. **Completed gifts:** The concept of ‘No consideration No contract’ does not apply to completed gifts. Completed gift means the gift which have already been executed or given to somebody. In such a case, the person provided the gift cannot recover it form the promises on the ground of want of consideration. However, this exception is not applicable to the gift, which is yet to be executed. Thus, a promise to gift cannot be enforceable.

**Agency:** Creation of agency does not require presence of consideration from either side. According to Sec. (185) the relation between principal and agent is as such in which the principal is bound by acts done by the agent. But agent is not bound in that way. So, principal provides the consideration, the agent does not. Thus, creation of agency is an exception.

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## 1.5 CAPACITY OF PARTIES

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Capacity to contract means competence of a party to bind and to be bound by legal consequences of any transaction made by them. The law gives importance to the capacity of parties to enter into a contract, since in Sec.10 it is stated that all agreements are contract made by parties competent enough. That means a person to enter into a valid contract, must be considered capable to do so by the law. Accordingly, a person who is not capable, in the eyes of law, to contract shall not enforce any legal remedy. Sec.11 of the act further states that, every person is competent to contract if:

1. He is of the age of majority (18 years in India) according to the law to which he is a subject.
2. He is of sound mind.
3. He is not expressly disqualified of contracting by any law to which he is a subject. Thus Sec.11 gives certain criteria for competence to enter into a contract.

Sec.12 further expresses the parties which are considered incompetent to contract, they are as follows:

1. Minor
2. Persons of unsound mind
3. Persons disqualified by any law to which they are subject.

### MINOR

Minority is considered and afforded a special status in the eyes of law. According to Sec. 3 of Indian Majority Act 1875, a person is a minor, who has not attained the age of majority.

Accordingly, a person shall attain age of majority on the completion of 18 years of his age. Until that he is a minor. However, in following two cases a person shall attain age of majority on the completion, not 18 years but 21 years of his age.

1. When a guardian is appointed to administer minors person or property under the Guardians and Wards Act 1890.
2. When management of the property of a minor is taken over by the court of wards. According to above rules any person who is below 18 years or 21 years respectively, is a minor and as such, is incompetent to make a contract.

This criterion of minority and incapacity is a positive criterion. A minor is considered incompetent by the law with vices to regarding interests of minors. The law understands that minors are inexperienced for any commercial transaction and so they are susceptible to pressure from other persons who are more experienced. They may make a contract, harmful to their own interest. It is observed by the law that, for the minors *court is servant, jury is counsellor and the law is guardian*. Therefore, legal position of a minor is very different from

other persons.

### **Legal Rules as To Minority Or Legal Position Of A Minor.**

1. **Agreements with or by minors are void ab initio:** Agreements with or by minors are held by the law to be absolutely void i.e., void ab initio (right from the beginning). They are destitute or having any legal effect since their inception. As a result, no right shall be afforded to the either of the parties under such agreement.
2. **A minor can be beneficiary:** Incapacity of minor, although prevents him to make a contract, does not prove him to be a beneficiary. That means he is prefer to shoulder responsibility but is completely allowed to take benefits of a contract. So, he can enter into a contract only for the benefits of it. Thus, he can be a payee an endorsee or beneficiary under a trust.
3. **No ratification:** Ratification by the minor to his agreement are not allowed by the law. The satisfaction means later on approval. So, if a minor later an approves (after becoming a major) his deeds or acts made during minority. Such ratification shall have on effect. Ratification always has retrospective effect, i.e., effect from the tie when the act approved, was initiated. As the minor agreements are void *ab initio*, as retrospective effect cannot be allowed.
4. **He can plead minority:** A minor has been specifically protected by the law. He can always plead minority in the sense that minority can very well be an excuse for him to escape from any responsibility. Even though he, by misrepresenting his age entered into a contract as major, at the time of fulfilment of obligation he can prove himself to be minor, he can legally escape from responsibility, even if it amounts to some harm or loss to be caused to a 3<sup>rd</sup> party.
5. **No application of restitution:** In the case of minors, the doctrine of restitution does not apply. According to this act under any contract, when it is prematurely restricted for any reason, a party, who has received some benefit under the contract from the other party, most restore it back to the party from whom he has received. This rule is not applicable to a minor and as such he is not liable to restore back any such benefit.
6. **He cannot be a partner:** Partnership is a contract so every party to the partnership must have contractual capacity. A minor does not have that capacity, as such cannot be a partner. However he can be entered into or introduced, with the consent of all other partners, for the benefits of the partnership.
7. **Minor's Liability for Necessaries:** The Indian Contract, Act had provided a valuable exception to all the legal rules applicable to the position of minor. The law suggests that when a contract is made with or by a minor is legally bound to support; the supplier shall have surety of his payment even though such agreements are void *ab initio*. The noted act is that even in such a case a minor is not personally liable but his property or estate is. As such whenever necessaries are supplied to a minor, the supplier can get his payment from the

property of the minor. Sec.23 specifies two matters from the term necessities i.e.,

- **Necessary goods:** However, no specification as to the goods which are termed necessary is laid down, it is suggested that necessary goods do not only mean the good required to maintain a bare existence i.e., bread or cloth, but such good which are considered reasonably necessary regard being had to its actual requirement. Therefore, even a luxurious item may be necessary for a minor. Supplier of such necessities shall have their payments.
- **Necessary services:** The law specifies certain services to be necessities as they are required to enrich the minors life. E.g., Medical, legal, educational, professional, vocational services etc. the provider of such services shall have their payment.

### **PERSONS OF UNSOUND MIND:**

Sec.12 of the Indian Contract Act categorically says that incapacity of a party to make a contract may also arise by unsoundness of mind of that party. The Sec. States that a person is considered to be of an unsound mind if.

- He is not capable to understand the terms of the contract and
  - He is not capable to form a rational judgment as to the consequences of the contract in which he is about to enter.
- Unsoundness of mind may arise from lunacy, idiocy or drunkenness or intoxication of mind.
1. **Lunacy:** Lunacy is of a temporary nature. A person is said to be a lunatic when he is deranged of his mental ability and capacity for some period due to some inherent defect or due to some external shock. There are, as it is of a temporary nature, intermittent interval of sanity and insanity. Contract made during period of sanity stand to be valid and the contract made during period of insanity are absolutely void. The proof is to be presented by respective parties.
  2. **Idiocy:** Idiocy is always of permanent nature. When a person has lost his mental powers permanently, he is said to be an idiot. This period of idiocy does not have any interval. An idiot is even not capable to understand and express an ordinary matter of life. Therefore, any contract with or by such a person is absolutely void.
  3. **State of drunkenness or intoxication:** Owing to the effect of some liquor or some medicine/drug, a person's mind may be in a state of drunkenness or intoxication. He is delirious for some time. This period exists, generally only for a very short time. For such time, any such contract shall be put an end and is void. However, such a person, in order to escape from the responsibility must prove such a state of his mind.

## PERSONS OF PARTICULAR STATUS OR DISQUALIFIED BY LAW

Various laws of the country sometimes disqualify certain persons to make a valid contract. They are given some special status by respective laws to which they are subject and as such are considered incompetent to contract such parties that may be as follows:

1. **Alien Enemy:** An Alien Enemy is the citizen of any such country that India has declared as an enemy country. According to Indian Contract and Indian Penal Code, any contract by citizen of India with an Alien Enemy is not valid but illegal. So, a contract cannot be entered into between citizens of such countries. Thus, an Alien Enemy is considered incapable to contract with the subject of India. More so, the contracts made during the period of war are void in issue, and contracts made before the war, according to their nature, are either suspended or put to an end.
2. **Foreign sovereigns:** Foreign sovereigns means recognized representatives of other countries working in our country. They include ambassadors, diplomats, accredited persons embassy staff, journalists of various foreign agencies and countries. They are given a particular privilege under the constitution of India. Accordingly, they cannot be made subject to the laws of our country. As such the citizen of Indian cannot institute any legal action against such persons according to our laws in our courts. Only if the central government permits, this can be done so. However, they can very well take legal actions against citizen in Indian Courts.
3. **Corporation:** Any corporation, whether established under a special act or under the companies Act, 1956, possesses a juristic personality separate from its members to their perspective or functional are is not governed by law of the nature but either by their memorandum or the companies Act or the special Act. Their authority is limited. Any contract made with or by them goes beyond their authority is limited. Any contract made with or by them goes beyond their authority is *ultra vires* and void. As such they are qualified only to make particular nature of contract and not all.
4. **Insolvents:** According to Indian Insolvency Act, when a person is adjudged insolvent, he or she cannot enter into a valid contract during the period of insolvency. All rights pertaining to property of the insolvent are assigned by the court to an appointed person who can make a contract on behalf of the insolvent. Although, contracts of personal nature are kept out of the realm of this provision.

**Convicts:** According to I.P.C. any person during the period of imprisonment cannot enter into a valid contract. However, if for such period he is on 'Ticket of leave' or 'Parole', he can make a valid transaction. The noted fact is that the perspective of law of limitation is not applicable to a culprit during the period of punishment.



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## 1.6 FREE CONSENTS

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It is essential to the creation of a contract that the parties are *ad idem*, i.e., they agree on the same thing in the same sense at the same time and that their consent is free and real (Sec. 10) also says that “all agreements are contracts if they are made by the free consent of parties ....”

**Consent:** It means acquiescence or act of assenting to an offer. “Two or more persons are said to consent when they agree upon the same thing in the same sense.” (Sec. 13).

**Free consent:** Consent is said to be free when it is not caused by

- (1) Coercion as defined in Sec. 15, or
- (2) Undue influence as defined in Sec. 16, or
- (3) Fraud as defined in Sec. 17, or
- (4) Misrepresentation as defined in Sec. 18, or
- (5) Mistake, subject to the provisions of Secs. 20, 21 and 22 (Sec. 14).

When there is no consent, there is no contract. Salmond describes it as error in consensus. If there is no *consensus ad idem*, there is no contract.

### COERCION

When a person is compelled to enter into a contract by the use of force, by the other party or under a threat, (Including emotional threats or threat to commit suicide) "coercion" is said to be employed. Coercion is the committing, or threatening to commit, any act forbidden by the Indian Penal Code, 1860 or the unlawful detaining, or threatening to detain, any property, to the prejudice of any person whatever, with the intention of causing any person to enter into an agreement. It is immaterial whether the Indian Penal Code, 1860 is or is not in force in the place where the coercion is employed (Sec. 15).

The threat amounting to coercion need not necessarily proceed from a party to the contract. It may proceed even from a stranger to the contract. Likewise, it may be directed against anybody not necessarily the other contracting party. The intention of the person using coercion should, however, be to cause any, person to enter into an agreement.

Coercion includes fear, physical compulsion and menace to goods.

### UNDUE INFLUENCE

Sometimes one party to the contract is compelled to enter into a contract against one's will as a result of unfair persuasion by the other, undue influence is said to be applied. This happens when one party is in domination nature over the other party and uses that domination to obtain an unfair advantage.

Sec. 16 states that a contract is said to be induced by undue influence where relations subsisting between the parties are such that one of the party is in a

position to dominate the will of the other and uses that position to obtain an undue advantage over the other.

A person is deemed to be in a position to obtain an undue advantage over the other.

Sec. 16 prescribes certain relations in which the courts shall have to presume application of undue influence. In such cases, it becomes the duty of the court to ensure that there is no undue influence. Here, not the plaintiff but the defendant has to prove that undue influence was not applied. These relations are:

Parent – Child  
Trustee – Beneficiary  
Solicitor – Client  
Doctor – Patient  
Financer – Financed  
Religious advisor – Disciple  
Guardian – Ward.

Sec.16 however further states that there shall be no presumption of undue influence by the court in following relations:

**Creditor – Debtor Landlord – Tenant Husband – Wife**

**FRAUD**

“Fraud” means and includes any of the following acts committed by a party to a contract, or with his convenience, or by his agent, with intent to deceive any party thereto or his agent, or to induce him to enter into the contract.

- The suggestion, as a fact, of that which is not true by one who does not believe of the fact;
- The active concealment of a fact by one having knowledge or belief of the fact;
- A promise made without any intention of performing it;
- Any other act fitted to deceive;
- Any such act or omission as the law specifically declares to be fraudulent

**Characteristics of Fraud**

1. There must be an assertion or concealment of a material facts
2. Representation must relate to a material fact
3. There must be an intension to induce the other party
4. The other party must be deceived and suffered some loss
5. The assertion may be made by the party or his agent
6. Silence may amount to fraud

**MISREPRESENTATION**

During the course of negotiation, a party asserts something to the other party to induce him into the contract. If the ascertain is wrongly made it becomes a

misrepresentation. If it is made intentionally with a view to deceive the other contracting party, it becomes a fraud. When the representation is a misrepresentation made innocently without any motive to cheat the other contracting party, it is misrepresentation in legal sense.

Misrepresentation is a false statement of facts made innocently and the maker does not believe it to be false or believe it to be true. There is also a misrepresentation when there is a commitment of material facts made intentionally. In misrepresentation there can never be intention to deceive the other party but always has an intention to induce the other party.

Sec.18 defines misrepresentation. It further states that there is a misrepresentation when: a person positively asserts that a fact is true; when his information does not warrant it to be so but he honestly believes it to be true. In all the circumstances, there is however, no intention to defraud the other party. Although it is an assertion of wrong facts, the assertor believes them to be true, although he does not have any ground reality of prove his belief.

### **Features of Misrepresentation**

Remedies on the ground of misrepresentation can be available only if the following features are satisfied and are proved to be there by the plaintiff.

1. The misrepresentation must relate to a fact, which is very essential for the root or substance of the contract. A mere opinion, puffing or commendatory statement, however made to attempt the party, cannot be amounted to a misrepresentation.
2. The misrepresentation must be made before the conclusion of the contract.
3. The misrepresentation must be made with a view to including the other party into the contract.
4. The misrepresentation must be made with the purpose to be acted upon.
5. The other contracting party must have actually acted upon the misrepresentation fact.
6. However, the asserted facts are wrong, the maker does not believe it be wrong.
7. There must be always not be intention to defraud the other contracting party. To be misrepresentation, it need not necessarily to be made directly to the plaintiff.

### **MISTAKE**

Mistake has been provided for in contract act under sections (20) (21) and (22). Mistake although being one of the negative elements of free consent, is completely different, has different ground and different consequence than other negative elements. Whenever any contract is caused due to mistake, unlike consequence of fraud, misrepresentation, coercion and undue influence in which a contract becomes voidable at the option of an aggrieved party, the mistake leads also to the consequences whereby the contract all together become void agreement. As such whenever a mistake is proved, neither of the parties shall have any remedy.

It must be put to an end as it is *void-ab-initio*. Such important consequences follow a mistake.

According to sec.(14) under sec.(20) mistake means erroneous belief as to the subject matter or the terms or the effects of a contract is said to have been induced by mistake when parties to the contract intend to do something eventually ending up doing some other thing under mistaken belief of themselves. This mistake has been classified under different section as follows:

Primarily mistakes are of two types:

1. Mistake of Law, and
2. Mistake of fact

### **Mistake of Law**

1. **Mistake of the law of the land:** It is when a person is under some mistaken belief regarding various aspects of the law of his own country. It is called a mistake of the law of the land. There is a well-settled rule of constitution in that ignorance of the law of the land cannot be an excuse in the court of law. On that line, it is presumed that every citizen must have knowledge of all the laws of his country.
2. **Mistake of the law of a foreign country:** When a person enters into a contract on the basis of his mistaken belief regarding any aspect of the law of a foreign country, such a mistake occurs. A person can be presumed to have knowledge of the law of his own country; however, he cannot be presumed to have the knowledge of the laws of all countries. As such, ignorance of the law can be an excuse to be out of the responsibility of the contract. Such contract becomes void agreement.

### **Mistake of Fact**

When a person makes a mistake as regards some factual matters, it is called a mistake of a fact. It is a real mistake and can be noted by the law as a mistake. Mistake of fact can be **Bilateral**(Mistake by both parties to the contract) or **Unilateral** (Mistake by one party to the contract). A mistake of fact can happen under the following circumstances:

1. Mistake concerning existence of subject matter
2. Mistake concerning the identity of subject matter
3. Mistake concerning quantity of the subject matter
4. Mistake concerning the quality of the subject matter
5. Mistake concerning capacity of performance of a contract
6. Mistake concerning the identity of a person
7. Mistake concerning nature of the contract

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## **1.7 LEGALITY OF OBJECT**

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A contract must not only be based on mutual assent of competent parties but must also have a lawful object. If the object of an agreement is the performance of an unlawful act, the agreement is unenforceable. Sec. 23 declares that the

'object' or the 'consideration' of an agreement is not lawful in certain cases. The words 'object' and 'consideration' in Sec. 23 are not used synonymously. They are distinct in meaning. The word, object means purpose or design. In some cases, consideration for an agreement may be lawful but the purpose for which the agreement is entered into may be unlawful. In such cases the agreement is void. As such, both the object and the consideration of an agreement must be lawful, otherwise the agreement is void.

### **When Consideration or Object is Unlawful (Sec. 23)**

- 1. If it is forbidden by law:** If the object or the consideration of an agreement is the doing of an act forbidden by law, the agreement is void. An act is forbidden by law when it is punishable by the criminal law of the country or when it is prohibited by special legislation or regulations made by a competent authority under powers derived from the Legislature.
- 2. If it is of such a nature that, if permitted, it would defeat the provisions of any law:** If the object or the consideration of an agreement is such that though not directly forbidden by law, it would defeat the provisions of any law the agreement is void.
- 3. If it is fraudulent:** An agreement which is made for a fraudulent purpose is void. Thus, an agreement in fraud of creditors with a view to defeating their rights is void.
- 4. If it involves or implies injury to the person or property of another:** 'Injury' means 'wrong', 'harm', or 'damage'. 'Person' means one's body. 'Property' Includes both movable and immovable property.
- 5. If the Court regards it as immoral:** An agreement, the consideration or object of which is immoral, e.g., an agreement between a husband and wife for future separation, is unlawful. However, agreements for immediate separation between a husband and wife, both in England and in India, are enforceable. The principle underlying this is preservation of the peace and reputation of families. Similarly, agreements in respect of past separation are also valid.

### **An agreement is unlawful for immorality in the following cases**

- (1) Where the consideration is an act of sexual immorality,** e.g., Illicit cohabitation or prostitution. But a promise to compensate a woman who has rendered services in the past, whether immoral or otherwise, forms a good consideration for the contract to compensate her. If the past cohabitation is of an adulterous kind, a promise relating to it cannot be enforced as adultery is an offence punishable under the Indian Penal Code, 1860. Consideration, according to it, which is immoral at the time when it passes, cannot become legal by passage of time.
- (2) Where the object of the agreement is the furtherance of sexual immorality,** e.g., lending money to a prostitute to help her in her trade.

6. Where the Court regards it as opposed to public policy.

### **Unlawful and Illegal Agreements**

An unlawful agreement is one which like a void agreement, is not enforceable by law. It is *void ab initio* and is destitute of legal effects altogether. It affects only the immediate parties and has no further consequences. An illegal agreement, on the other hand, is not only void as between the immediate parties but has this further effect that the collateral transaction to it also become tainted with illegality.

Every illegal agreement is unlawful, but every unlawful agreement is not necessarily illegal. It is sometimes difficult to decide as to whether an act is illegal or unlawful as many of the illegal and the unlawful acts lie on the borderline. It may, however, be observed that illegal acts are those which involve the commission of a crime or contain an element of obvious moral turpitude and where the wicked attribute is reasonably obvious, or are, in some other way, contrary to public policy. A criminal act is one which is both forbidden by law and which is revolting to the moral sentiments of the society. A crime is something more than a mere disobedience to a law. As such illegal agreements include acts opposed to public morals, e.g., an agreement for illicit cohabitation, or an agreement to defraud the revenue or commit a crime, or an agreement which tends to endanger the public safety. On the other hand, unlawful acts are those which are less rigorous in effect and involve a "non-criminal breach of law". These acts do not affect public morals, nor do they result in the commission of a crime. These are simply disapproved by law on some ground of public policy. These include agreements in restraint of trade, marriage or legal proceedings, etc.

### • **CHECK YOUR PROGRESS**

#### **Descriptive Questions**

1. What is a contract? Explain the essential elements of a valid contract.
2. Define in detail the various features of law of contracts
3. Define offer and explain its essential elements.
4. Define acceptance and explain the legal rules as to acceptance.
5. Explain briefly the various types of contracts on the basis of validity, formation and performance.
6. What are considerations? Explain in detail the different elements of consideration.
7. Define in detail the various exceptions to the rule "No Consideration No Contract".
8. Define the legal position of a minor in terms of contracts done with and by a minor.
9. Explain in detail the different people disqualified by law from contracting.
10. Define consents. When are the consents to a contract said to be free?
11. "A contract the object and consideration of which is unlawful is unenforceable by law". Define the statement in the light of the provisions of the contract act.

**Short Notes**

1. Types of contracts based on validity
2. Objects of contract
3. Tender
4. Nudum Pactum
5. Contracts with people of unsound mind
6. Alien Enemy
7. Distinction between Coercion and undue influence
8. Distinction between fraud and misrepresentation
9. Illegal and unlawful agreements

**Multiple Choice Questions**

1. A(n) \_\_\_\_\_ is a proposal by one party to another to enter into a legally binding agreement with him.
  - a. Offer
  - b. Acceptance
  - c. Agreement
  - d. Contract
  
2. Which of the following necessarily needs to be absolute and unconditional?
  - a. Contract
  - b. Offer
  - c. Acceptance
  - d. Agreement
  
3. Which of the following according to the contract act represents the phrase “quid-pro-quo”?
  - a. Acceptance
  - b. Offer
  - c. Free consent
  - d. Consideration
  
4. An agreement can be called *Nudum Pactum* when it is...
  - a. Without Free Consent
  - b. Without Consideration
  - c. With a minor
  - d. Valid
  
5. Contracts can be classified on the basis of ...
  - a. Validity
  - b. Formation
  - c. Performance
  - d. All of the above

**6. According to the the Contract Act, contracts with the following people are void.**

- a. People of unsound mind
- b. Minors
- c. People disqualified by status
- d. All of the above

**7. A Price tag on the goods displayed on the shelves of a showroom is by law**

- a. A proposal
- b. Invitation to offer
- c. Acceptance
- d. None of the above

**8. Which of the following is not a legal rule as to acceptance?**

- a. It must be absolute and unqualified
- b. It need not be communicated to the offerer
- c. It must be according to the mode prescribed
- d. It must be given within a reasonable time

**9. Lunatics, idiots and drunkards are not considered capable to contract due to.**

- a. Status
- b. Mental unsoundness
- c. Age
- d. All the above

**10. Consideration to a contract can be.**

- a. Past
- b. Present
- c. Future
- d. All the above

**11. It is a contract created by the law and not by the mutual consent of the parties.**

- a. Quasi-contracts
- b. contingent contracts
- c. government contracts
- d. void contracts

**12. The consents to a contract are not said to be free when they are obtained under;**

- a. Undue influence
- b. Coercion
- c. Mistake
- d. All of the above



**13. When a person in a contract purposefully misrepresents to the other party to deceive himit amounts to?**

- a) Undue influence
- b) Coercion
- c) Mistake
- d) Fraud

**14. To force someone to get into a contract on the threat to commit suicide amounts to?**

- a) Undue influence
- b) Coercion
- c) Mistake
- d) All of the above

**15. If a contract is made without free consent, the contract turns....**

- (a) Void
- (b) Voidable
- (c) Illegal
- (d) Valid

**MCQ Answer key**

1.	2.	3.	4.	5.	6.	7.	8.	9.	10.	11.	12.	13.	14.	15.
a	c	d	b	d	d	b	b	a	d	a	d	d	b	b

**2.0 DEFINITION & ESSENTIALS OF A VALID CONTRACT**

**2.1 REMEDIES FOR BREACH OF CONTRACT**

**2.2 PERFORMANCE OF CONTRACTS**

**2.3 VOID AGREEMENT**

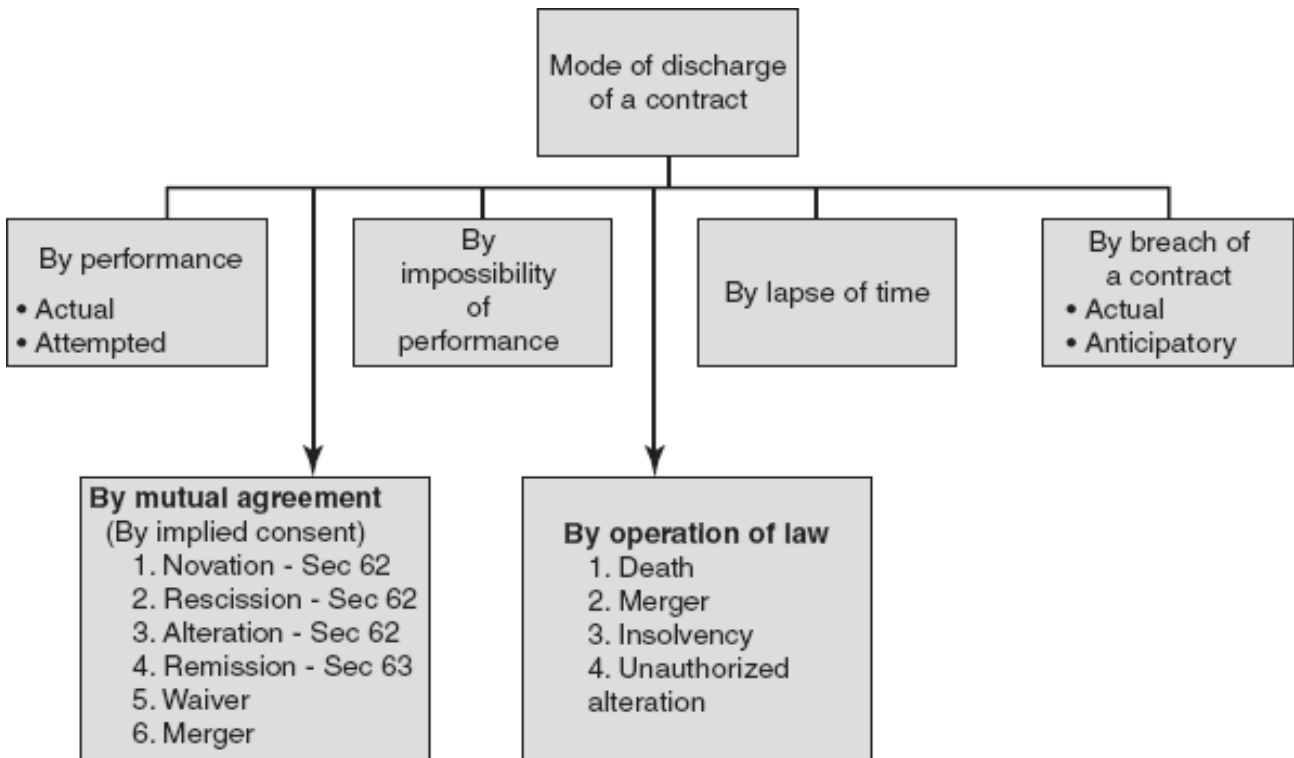
**2.4 QUASI –CONTRACTS**

**2.5 CONTRACT OF AGENCY**

**• CHECK YOUR PROGRESS**

**2.0 DEFINITION & ESSENTIALS OF A VALID CONTRACT**

Discharge of contract means termination of the contractual relationship between the parties. A contract is said to be discharged when it ceases to operate, i.e., when the rights and obligations created by it come to an end. The various modes of discharge of contract can be diagrammatically explained as follows:



**I) Discharge by Performance:**

Discharge by performance takes place when the parties to the contract fulfil their obligations arising under the contract within the prescribed time. This is the most usual mode of discharge of a contract. Performance may be actual performance or attempted performance (i.e., tender).

- (a) **By actual performance:** When both the parties perform their respective promises the contract is discharged. Performance must be complete, precise and according to the terms of the contract.
- (b) **By attempted performance (TENDER):** An offer to perform is called tender or attempted performance. Where the promisor offers to perform his obligation, but the promisee refuses to accept the performance tender is equal to actual performance.

## II) Discharge by Agreement or consent:

As it is the agreement of the parties which binds them, so by their further agreement or consent the contract may be terminated. The rule of the law in this regard is *Eodem modo quo quid constituitur, eodem modo destruitur* (i.e. a thing may be destroyed in the same manner in which it is constituted)

The various cases of discharge of a contract by mutual agreements are as follows:

- (a) Novation
  - (b) Rescission
  - (c) Alteration
  - (d) Remission
  - (e) Waiver
  - (f) Merger
- (a) **Novation (Sec.62):** Novation takes place when a new contract is substituted for an existing one between the same parties or a contract between two parties is rescinded in consideration of a new contract being entered into on the same terms between one of the parties and a third-party novation should take place before the expiry of the time of the performance of the original contract. If it does not, there would be a breach of the contract.
  - (b) **Rescission (Sec.62):** Rescission of a contract takes place when all or some of the terms of the contract are cancelled. It may occur – (i) By mutual consent of the parties or (ii) Where one party fails in the performance of his obligation. In such a case, the other party may rescind the contract without prejudice to his right to claim compensation for the breach of contract
  - (c) **Alteration (Sec.62):** Alteration of a contract may take place when one or more of the terms of the contract is/are altered by the mutual consent of the parties to the contract. In such a case, the old contract is discharged.
  - (d) **Remission-(sec.63):** Remission means acceptance of a lesser fulfillment of the promise made, e.g., acceptance of a lesser sum than what was contracted for, in discharge of the whole of the debt. It is not necessary that there must be some consideration for the remission of the part of the debt.
  - (e) **Waiver:** Waiver takes place when the parties to a contract agree that they shall no longer be bound by the contract. This amounts to a mutual abandonment of rights by the parties to the contract. Consideration is not necessary for waiver
  - (f) **Merger:** Merger takes place when an inferior right accruing to a party under a contract merges into a superior right accruing to the same party under the same or some other contract.

**(III) Discharge by Impossibility of Performance:**

If an agreement contains an undertaking to perform impossibility, it is void ab initio. This rule is based on the following maxims. (i) The law does not recognize what is impossible and (ii) What is impossible does not create an obligation according to section 56 of the Indian Contract Act; impossibility of performance may fall into either of the following categories:

- (a) Impossibility existing at the time of the agreement:** If the parties or unknown to the parties know either. The former is known as absolute impossibility.
- (b) Supervening of impossibility:** A contract is discharged by supervening impossibility in the following cases: (can be an excuse for discharge of contract)
  - i) Destruction of the subject matter of the contract:** When the subject matter of a contract subsequent to its formation is destroyed without any fault of the parties to the contract, the contract is discharged.
  - ii) Non-existence or nonoccurrence of a particular state of things:** Sometimes a contract is entered into between two parties on the basis of a continued existence or occurrence of a particular state of things. If there is any change in the state of things which formed the basis of the contract, or if the state of things which ought to have occurred does not occur, the contract is discharged.
  - iii) Death or incapacity for personal service:** Where the performance of a contract depends on the personal skill or qualification of a party the contract is discharged on the illness or incapacity or death of that party. The man's life is an implied condition of the contract.
  - iv) Change of law:** When subsequent to the formation of a contract, change of law takes place, or the government takes some power under some ordinance or special Act as in the case of the Defence of India Act when the performance of the contract becomes impossible, the contract is discharged
  - v) Outbreak of war:** A contract entered into with an alien enemy during war is unlawful and therefore impossible of performance. Contracts entered into before the outbreak of war are suspended during the war and may be revived after war is over.

Under the following circumstances, a contract is not discharged on the ground of supervening impossibility:

- (a)** Commercial impossibility
- (b)** Difficulty of performance
- (c)** Impossibility due to failure of a third person
- (d)** Strikes, lockouts and civil disturbances
- (e)** Failure of one of the objects

**(IV) DISCHARGE BY OPERATION OF LAW:**

A contract may be discharged independently of the wishes of the parties i.e. by operation of the law under the following circumstances.

- i) **By Death:** In contracts involving personal skill or ability, the contract is terminated on the death of the promisor.
- ii) **By merger:** Merger takes place when an inferior right accruing to a party under a contract merges into a superior right accruing to the same party under the same or some other contract
- iii) **By insolvency:** When a person is adjudged as an insolvent, he is discharged from all the liabilities incurred prior to his adjudication.
- iv) **By unauthorized alteration of terms of contract:** Where a party to a contract makes any material alteration in the contract without the consent of the other party, the other party can avoid the contract.

**(V) DISCHARGE BY LAPSE OF TIME:**

The Limitation Act – 1963 lays down that a contract should be performed within a specified period, called period of limitation. If it is not performed, and if no action is taken by the promised within the period of limitation, he is deprived of his remedy at law. In other words, we may say that the contract is terminated. For example, the price of goods sold without any stipulation as to credit should be paid within three years of the delivery of the goods.

**(VI) DISCHARGE BY BREACH OF CONTRACT:**

Breach of contract means a breaking of the obligation, which a contract imposes. It occurs when a party to the contract without lawful excuse does not fulfil his contractual obligation or by his own act makes it impossible that he should perform his obligation under it. It converts a right of action for damages to the injured party. Breach of contract may be actual or anticipatory.

- i) **Actual Breach of Contract:** It may take place at the time when the performance is due during the performance of the contract.
- (b) **Anticipatory of contract:** It occurs when a party to an executory contract declares his intention of not performing the contract before the performance is due. He may do so by express repudiation or by implied repudiation.

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**2.1 REMEDIES FOR BREACH OF CONTRACT**

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When the contract is broken, the aggrieved (injured) party, i.e., the party who is not in breach has one or more of the following remedies.

- I) Rescission of the contract
- II) Suit for damages
- III) Suit upon Quantum Meruit
- IV) Suit for specific performance of the contract
- V) Suit for injunction

**(I) RESCISSION OF THE CONTRACT:**

When a contract is broken by one party, to the other party may sue to treat the contract as rescinded and refuse further performance. In such a case, he is absolved of all his obligations under the contract.

The court may grant rescission on the following grounds:

- (a) Where the contract is voidable by the plaintiff or
- (b) Where the contract is unlawful for causes not apparent on its face and the defendant is more to blame than the plaintiff.

The court may however refuse rescission on the following grounds:

- (a) Where the plaintiff has expressly or impliedly ratified the contract.
- (b) Where owing to the change of circumstances the parties cannot be restored to their original positions.
- (c) Where third parties have during the subsistence of the contract acquired rights in good faith and for value.
- (d) Where only a part of the contract is sought to be rescinded and such part is not severable from the rest of the contract.

## **(II) DAMAGES:**

Damages are a monetary compensation allowed to the injured party by the court for the loss or injury suffered by him by the breach of a contract. The object of awarding damages for the breach of a contract is to put the injured party in the same position so far as money can do it as if he had not been injured. This is also called the doctrine of restitution.

### **TYPES OF DAMAGES:**

Damages may take any of the following forms:

- i) Ordinary Damages
- ii) Special Damages
- iii) Vindictive or Exemplary Damages
- iv) Nominal Damages
- v) Damages for loss of reputation
- vi) Damages for inconvenience and discomfort Liquidated Damages

**i) Ordinary Damages:** When a contract has been broken, the injured party can recover from the other party such damages as naturally and directly arose in the usual course of things from the breach. This means that the damages must be the approximate consequence of the breach of contract. These damages are known as ordinary damages. Normally ordinary damages in a contract for the sale of goods are the difference between the contract price and the market price of such goods on the date of the breach.

**ii) Special damages:** Damages other than those arising from the breach of a contract may be recovered if such damages may reasonably be supposed to have been in the contemplation of both of the parties as the probable result of the breach of the contract. Such damages are known as special damages. Special damages cannot be claimed as a matter of right. These can be claimed only if the special circumstances, which would result in a special loss in case of breach of a contract, are brought to the notice of the other party.

**iii) Vindictive Damages:** Damages for the breach of a contract are given by way of compensation for loss suffered and not by way of punishment for wrong.

inflicted. Hence vindictive or exemplary damages have no place in the law of contract because they are punitive (involving punishment) by nature. But in the following two grounds the court may award exemplary damages.

- (a) Breach of a promise to marry, and
  - (b) Dishonor of a cheque by a banker wrongfully when the customer possesses sufficient funds to the credit of his account.
- iv) **Nominal Damages:** Where the injured party has not in fact suffered any loss by reason of breach of a contract the damages recoverable by him are nominal, i.e., very small, for example, a rupee. These damages merely acknowledge that the plaintiff has proved his case and won.
- v) **Damages for loss of reputation:** Damages for loss of reputation in case of breach of a contract are generally not recoverable. An exception to this rule exists in the case of a banker who wrongfully refuses to honour a customer's cheque. If the customer happens to be a tradesman, he can recover damages in respect of any loss to his trade reputation by the breach. And the rule of the law is: the smaller the amount of the cheque dishonoured, the larger the amount of the damages awarded.
- vi) **Damages for inconvenience and discomfort:** Damages can be recovered for physical inconvenience and discomfort. The general rule in this connection is that the measure of damages is not affected by the motive or the manner of the breach.
- vii) **Liquidated Damages:** What is a liquidated damage and how far it differs from penalty. Sometimes parties to a contract stipulate at the time of its formation that on the breach of the contract by either of them, a certain specified sum will be payable as damages. Such a sum may amount to either liquidated damages or a penalty. Liquidated damages represent a sum fixed or ascertained by the parties in the contract which is a fair and genuine pre-estimate of the probable loss that might ensue as a result of the breach if it takes place. Penalty is a sum named in the contract at the time of its formation, which is disproportionate to the damage likely to accrue as a result of the breach. Thus, penalty means an amount fixed in terrorem without any regard to the probable loss. The question whether a sum stipulated is a penalty or liquidated damages is a question of construction to be decided upon the terms of the contract and circumstances of each particular case judged of as at the time of making the contract and not as at the time of breach. The sum stipulated is a penalty if: i) It is extravagant or unconscionable (unreasonable) in amount compared with the greatest loss which could conceivably be proved to have flowed from the breach. ii) The breach consists of not paying a sum of money by a certain time and the sum fixed is greater than the sum to be paid.

### (III) QUANTUM MERUIT

The phrase *quantum meruit* literally means 'as much as earned'. A right to sue on quantum meruit arises where a contract, partly performed by one party has become discharged by the breach of the contract by the other party. The right is founded not on the original contract, which is discharged or is void but on an implied promise by the other party to pay for what has been done. When a person has done some work under a contract and the other party repudiates the contract, or some event happens which makes the further

performance of the contract impossible, then the party who has performed the work can claim remuneration for the work he has already done, i.e., so much as the party rendering the service deserves. The right to claim *quantum meruit* does not arise out of contract as the right to damage does. It is a claim on the quasi-contractual obligation, which the law implies in the circumstances. The claim of *quantum meruit* arises in the following cases

- When an agreement is discovered to be void
- When something is done without any intention to do so gratuitously
- When there is an express or implied contract to render service but there is no agreement as to remuneration
- When the completion of the contract has been prevented by the act of the other party to the contract
- When the contract is divisible
- When an indivisible contract is completely performed but badly

**(IV) SPECIFIC PERFORMANCE:**

In certain cases of breach of a contract, damages are not an adequate remedy. The court may in such cases direct the party in breach to carry out his promise according to the terms of the contract. This is a direction by the court for specific performance of the contract at the suit of the party not in breach. Some of the cases in which specific performance of a contract may, in the discretion of the court be enforced are as follows:

When the act agreed to be done is such that compensation in money for its non-performance is not an adequate relief

When there exists no standard for ascertaining the actual damage caused by the non-performance of the act agreed to be done.

When it is probable that the compensation in money cannot be got for the non-performance of the act agreed to be done

**(V) INJUNCTION:**

Where a party is in breach of negative terms of a contract (i.e., where he is doing something which he promised not to do), the court may by issue of an order, and restrain him from doing what he promised not to do. Such an order of the court is known as an ‘injunction’

**2.2 PERFORMANCE OF CONTRACT**

The following persons can perform a valid contract.

- (I) Promisor himself:** If there is something in the contract to show that it was the intention of the parties that the promise should be performed by the promisor himself, such promise must be performed by the promisor (section 40) This means contracts which involve the exercise of personal skill, volition, or diligence of the promisor.
- (II) Agent:** Where personal consideration is not the foundation of a contract, the



promisor or his representative may employ a competent person to perform it (sec.40)

- (III) **Legal representatives:** A contract, which involves the use of personal skill or is founded on personal considerations, comes to an end on the death of the promisor. The rule of law is “action personalize *maritur cum persona*”, i.e., a personal action dies with the person. As regards any other contract, the legal representatives of the deceased promisor are bound to perform it unless a contrary intention appears from the contract. (Sec. 37)
- (IV) **Third persons:** When a promisee accepts performance of the promise from a third person, he cannot afterwards enforce it against the promisor. (Sec.41).
- (V) **Joint Promisor:** (Discuss the „devolution of joint liabilities and rights?) Devolution means passing over from one person to another. When two or more persons have made a joint promise, they are known as joint promisors. Unless a contrary intention appears from the contract, all joint promisors must jointly fulfill the promise. If any of them dies, his legal representative must, jointly with the surviving promisors, fulfill the promise. If all of them die, the legal representatives of all of them must fulfill the promise jointly (sec.42) the following are the rules in this regarding: (a) Any one of the joint promisors may be compelled to perform (sec.43 Para 1) (b) A Joint promisor compelled to perform may claim contribution (sec.43, Para 2). (c) If any one of the joint promisors makes default in the contribution, the remaining joint promisors must bear the loss in equal shares (sec.43, para 3)

## TENDER

Sometimes it so happens that the promisor offers to perform his obligation under the contract at the proper time and place, but the promisee does not accept the performance. This is known as “attempted performance” or “TENDER” (u/s.38). A tender of performance is equivalent to actual performance. It excuses the promisor from further performance and entitles him to sue the promisee for the breach of contract.

### REQUISITES OF A VALID TENDER:

- a. **Tender must be unconditional:** A valid tender must be unconditional. It becomes conditional when it is not in accordance with the terms of the contract.
- b. **Tender must be of whole quantity:** A valid tender must be of whole quantity contracted for or of the whole obligation. A tender of an installment when the contract stipulates payment in full is not a valid tender.
- c. **Tender must be by a proper person:** Tender must be by a person who is in a position and is willing to perform the promise.
- d. **Tender must be made at proper time and place:** It must be made at the proper time and place. A tender of goods after the business hours is not a valid tender.
- e. **Tender must be made to the proper person:** A valid tender must be made to the promisee or to his duly authorized agent in the proper form.
- f. **Tender may be made to one of several joint promisees:** Tender to any one of the several joint promises has the same effect as if the tender was made to all of them.

- g. In case of tender of goods, reasonable opportunity for inspection of goods:** Tender of goods must give a reasonable opportunity to the promisee for the inspection of the goods. A tender of goods at such time when the other party cannot inspect the goods is not a valid tender.
- h. Tender of money must be in Legal Tender Money:** In case of tender of money the debtor must make a valid tender in the legal tender money. If the creditor refuses to accept it, the debtor is not discharged from making the payment.

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### 2.3 VOID AGREEMENT

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It is said that an agreement not enforceable by law is void "[Sec.2 (g)] Therefore, a null agreement does not give rise to any legal consequence and is void ab-initio. Agreement is not an agreement at all from its inception.

An agreement cannot be enforced if it includes illegal considerations or is created by incompetent parties or it violates the basic principles of equity; or is contrary to legal or moral standards are called null agreement.

Void agreements have no legal status at all. An agreement is void if it does not fulfil all the conditions of enforceability. There are few agreements which have been expressly declared void under various sections and they are:

- 1. Agreement by a Minor:** A person who has not completed 18 years of age is a minor. The law acts as guardian of minors and protects their rights. They do not have the ability to judge what is good and what is bad for them. Consequently, when a minor is accused of obligations and the other contracting party seeks to enforce these obligations against the minor, the agreement is considered void.
- 2. Agreement with a Person of Unsound Mind:** A person who does not have a healthy mind or whose mental powers are not fixed or whose mental condition is not under their own control. Any agreement on the part of a sick-minded person is absolutely void because he does not have the capacity to judge, what is good and what is bad for him.
- 3. Agreements in Restraint of Marriage:** Everyone enjoys the freedom to marry and, in accordance with article 26 of the contract law, 'any agreement is the restriction of the marriage of any person, who is not a minor, is null.' The restriction may be general or partial, but the agreement is void, and therefore, an agreement that agrees not to marry at all, or a certain person or, a class of persons, or for a fixed period, is void.
- 4. Agreement in Restraint of Trade:** The constitution of India guarantees the freedom of commerce for each citizen and, therefore, article 27 declares that 'any agreement by which it is restricted to any of exercising a legal profession, trade or business of any kind, is in that sense null.' No person is in livery to deprive himself of the fruit of his work, ability or talent, by any contract he enters.
- 5. Wagering Agreements:** An agreement between two persons under which money or money's worth is payable, by one person to another on the happening or non-happening of a future uncertain event is called a wagering event. Such agreements are chance oriented and therefore, completely uncertain. Betting is

a wagering agreement, as it relies on an uncertain event and only one of the two parties' benefits from it, as such any one gain would the others loss. Hence it defeats the rule of contract and is considered void.

6. **Agreement in restraint of legal proceedings:** Any agreement by which any of its parties has restrictions to enforce their rights under a contract, by the usual legal procedures in the ordinary courts, or that limits the time in which they can assert their rights, is null or void.
7. **Uncertain Agreements:** "Agreements whose meaning is not certain or can be assured are null and void" (Sec-29). Through Sec-29, the law seeks to ensure that the parties to a contract know the precise nature and scope of their mutual rights and obligations under the contract.
8. **Agreement Contingent on Impossible Events:** "Contingent agreements to do or not do anything if an impossible event occurs are null, whether the event's impossibility is known or not by the parties to the agreement at the time it is made." (Sec. 36)
9. **Agreements to do Impossible Act:** "An agreement to do an act impossible in itself is void." Any act that the law or the courts refers to as impossible to perform cannot be contracted. If any person gets into an agreement for such impossible act, it is void.
10. **Agreements made under a mutual mistake of fact (Sec. 20):** A **mutual or bilateral mistake** arises when both the parties to the contract have entered into it on the basis of common mistake on their parts regarding any thing concerning the subject matter and performance of the contract. Bilateral mistake is the real mistake. A bilateral mistake is one where both the parties are under mistake and the mistake relates to some material fact about the subject matter. The material fact related to the subject matter could relate to the existence, identity, quantity, quality of the subject matter or the capacity and identity of the performer. Such agreements are expressly declared void.
11. **Agreements the consideration or object of which is unlawful (Sec. 23):** A contract should not only be based on the mutual consent of the competent parties but should also have a legal purpose. If the object of an agreement is the performance of an unlawful act, the agreement is not enforceable. Sec.23 clears that the 'object' or 'consideration' of an agreement is not legal in certain cases. The words 'object' and 'consideration' in Sec. 23 are not used in same manner, they have different meanings. The word 'object' means purpose or design. In some cases, the consideration of an agreement may be legal, but the purpose for which the agreement is signed may be illegal. In such cases, the agreement is void. As such, both the object and the consideration of an agreement must be legal, otherwise the agreement will be void.
12. **Agreements the consideration or object of which is unlawful in part (Sec. 24):** An agreement must have a lawful objective and a lawful consideration. If the object or consideration of an agreement is the performance of an unlawful act, the agreement is unenforceable and void (Sec. 23)
13. **Agreements made without consideration (Sec. 25):** Consideration is one of the essential and most important factors of a valid contract. It is compulsory to

have consideration to formulate a valid contract. Hence, any agreement without consideration is void. The law is only concerned with the presence of consideration and not the proportion.

- 14. In case of reciprocal promises to do things legal and also other things illegal:** The second set of reciprocal promises is a void agreement (Sec. 57). If an agreement involves two sets of promises one which is legal and the other which is illegal, the entire contract is tainted by illegality; unless and until the illegal portion of the contract is separable or removable.

## 1 CONTINGENT CONTRACT

According to sec.31 of the Indian Contract Act, a contingent contract is a contract to do or not to do something, if some event, collateral (attached) to such contract, does or does not happen. For example, goods sent on approval is a contingent contract. A agrees to sell a certain piece of land to B, in case he succeeds in his litigation concerning that land. This is a contingent contract.

### There are three essential characteristics of a contingent contract:

1. Its performance depends on the happening or non-happening of a futuristic event
  2. The event must be uncertain
  3. The event must be collateral, i.e., incidental to the contract
- Contracts of insurance, indemnity and guarantee are the commonest instances of a contingent contract.

### RULES REGARDING CONTINGENT CONTRACTS:

Following are the important rules regarding contingent contracts:

1. Contingent contracts depend on the happening of an uncertain future event and cannot be enforced until the event has happened. If the event becomes impossible, such contracts become void. (Section 32)
2. Where a contingent contract is to be performed if a particular event does not happen, its performance could be enforced when the happening of that event becomes impossible (section 33)
3. If a contract is contingent on how a person will act at an unspecified time, the event shall be considered to become impossible when such person does anything which renders it impossible that he should so act within any definite time, or otherwise then under further contingencies (section 34.)
4. Contingent contracts as regards doing or not doing anything, if a specified uncertain event happens within a fixed time, become void if the event does not happen or its happening becomes impossible before the expiry of that time. (Sec.35)
5. Contingent agreements as regards doing or not doing anything, in case of an impossible event, are void, whether or not the fact is known to the parties (section 36).

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## 2.4 QUASI-CONTRACTS

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Under certain circumstances, a person may receive a benefit to which the law regards another person as better entitled, or for which the law considers he

should pay to the other person even though there is no contract between the parties. Such relationship is termed as quasi- contracts. This is because although there is no contract or agreement between the parties, they are put in the same position as if there were a contract between them. These relationships are termed as quasi-contracts or constructive contracts. Certain relations resembling those created by contracts are called quasi-contracts. A quasi-contract rests on the ground of equity that a person shall not be allowed to enrich himself unjustly at the expense of another

*Law of quasi-contracts is also known as the law of restitution. Strictly speaking, a quasi- contract is not a contract at all. A contract is intentionally entered into. But law on the other hand creates a quasi-contract.*

### **Kinds of quasi contracts**

Section 68 to 72 of Indian Contract Act deal with five kinds of quasi-contractual obligations. They are as follows.

1. **Supply of necessaries (sec.68):** If a person incapable of entering into a contract or anyone whom he is legally bound to support, is supplied by another with necessaries suited to his condition in life, the person who has furnished such supplies is entitled to be reimbursed from the property of such incapable person.
2. **Payments by an interested person (section.69):** A person, who is interested in the payment of money which another is bound by law to pay and who therefore pays it, is entitled to be reimbursed by the other. However, certain essential requirements should be fulfilled as under the payment made should be bonafide for the protection of one's interest the payment should not be a voluntary one. The payment must be such as the other party was bound by law to pay.
3. **Obligation to pay for non-gratuitous acts (sec.70):** When a person lawfully does anything for another person or delivers anything to him not intending to do so gratuitously and such other person enjoys the benefit thereof, the latter is bound to make compensation to the former in respect of or to restore the thing so done or delivered. However, three conditions must be satisfied: (a) The thing must have been done lawfully. (b) The person doing the act should not have intended to do it gratuitously. (c) The person for whom the act is done must have enjoyed the benefit of the act.
4. **Responsibility of finder of goods (sec.71):** A person, who finds goods belonging to another and takes them into his custody, is subject to the same responsibility as a bailee. He is bound to take as much care of the goods as a man of ordinary prudence would under similar circumstances, take of his own goods of the same bulk, quality and value. He must also take all necessary measures to trace its owner. If he does not do so, he will be guilty of wrongful conversion of the property. Till the owner is found out, the property in goods will vest in the finder and he can retain the goods as his own against the whole world  
The finder can sell the goods in the following cases:
  - (a) When the thing found is in danger of perishing
  - (b) When the owner cannot, with reasonable diligence, be found out
  - (c) When the owner is found, but he refuses to pay the lawful charge of the finder and
  - (d) When the lawful charges of the finder, into respect of the maintenance

of the thing found, amount to two-thirds of the value of the thing found  
**Mistake or Coercion (sec.72):** A person to whom money has been paid, or anything delivered, by mistake or under coercion, must repay or return it to the person who paid it by mistake or under coercion. The word coercion is used in general sense and not as defined in sec.15.

## SPECIAL CONTRACTS

### 1 INDEMNITY AND GUARANTEE

#### 2 CONTRACT OF INDEMNITY

A contract, by which one party promises to save the other from loss caused to him by the conduct of the promisor himself, or by the conduct of any other person, is called a ‘contract of indemnity’ (Sec. 124). The person who promises to make good the loss is called the **indemnifier (promisor)** and the person whose loss is to be made good is called the **indemnified or indemnity-holder (promisee)**. A contract of indemnity is really a class of contingent contracts.

A contract of fire insurance or marine insurance is always a contract of indemnity. But there is no contract of indemnity in case of a contract of life insurance. There may not be a valid contract of indemnity where it is against public policy.

The most common use of the terms *indemnify* and *indemnity* occur in insurance policies. When purchasing an insurance policy, the insurance company agrees to indemnify the policyholder, or another specified party, against losses or damages that may occur.

According to the definition given by Sec. 124 of the Contract Act, a contract of indemnity includes (i) only express promise to indemnify and (ii) cases where loss is caused by the conduct of the promisor himself or by the conduct of any other person. It does not include (a) implied promise to indemnify and (b) cases where the loss is caused by accident or by the conduct of the promisee.

#### Commencement of Indemnifier’s Liability

High Courts have differed in their judgements regarding commencement of indemnifier’s liability. According to High Courts of Calcutta, Madras, Allahabad and Patna indemnity holders when asked to meet a liability, can compel the indemnifiers to put him (indemnity- holder) in a position to meet the liability without waiting until he (indemnity-holder) has actually discharged it. High Courts of Bombay and Nagpur have, however, held that indemnifier can be made liable only when indemnity-holder has incurred an actual loss, i.e., discharged the liability. The former view seems to be more correct and is also in consonance with the English view “to indemnify does not merely mean to reimburse in respect of moneys paid, but to save from loss in respect of liability against which the indemnity has been given...if it be held that payment is a condition precedent to recovery, the contract may be of little value to the person to be indemnified, who may be unable to meet the claim in the first instance.” (Kennedy L.J.) in *Liverpool Insurance Co. case* 84

Thus, we can conclude that if the indemnity holder had incurred an absolute

liability, he has the right to call upon the indemnifier to save him from that liability and pay it off.

### **Rights of Indemnity Holder**

As per the section 125 the rights of indemnity holder are:

- 1. Damages:** In a contract of indemnity the indemnity holder is entitled to recover from the promise and indemnifier all damages for which he may be compelled to pay in any suit as of any matter to which the promise of indemnity applies while acting within the scope of his authority.
- 2. Costs:** Any person with indemnity holder and indemnified or promise is entitled to recover from promisor all costs which he may be compelled to pay in any suit in bringing or defending it if he does not go against the order of the promisor and if he has acted in absence of any contract as would have been prudent for him to do.
- 3. Sums:** An indemnity holder is entitled to recover from indemnified all sums which he has paid under the term of compromise of any suit and compromise was not against the order of the promisor and the compromiser was not against the order of the promisor and the compromise was such that it was to be done (prudent) in absence of any contract of indemnity.

**Explanation of Rights of Indemnity Holder:** It is to be noted that a contract of indemnity being a specie of the general contract and therefore, must satisfy all essentials of a valid contract such as competent parties, free consent, lawful object, etc., otherwise it will not be valid.

### **Duties of the Indemnity Holder**

Even though the duties of the indemnity holder are not mentioned in any section per se, we can say that the indemnity holder has some implied duties. For example, it is the duty of the indemnity holder to comply to the terms and conditions of the contract and any alteration can enable the indemnifier to reject the claim of indemnification.

## **3 CONTRACTS OF GUARANTEE**

A “contract of guarantee” is a contract to perform the promise, or discharge the liability, of a third person in case of his default. The person who gives the guarantee is called the ‘surety’, the person in respect of whose default the guarantee is given is called the ‘principal debtor’, and the person to whom the guarantee is given is called the ‘creditor’. A guarantee may be either oral or written (sec. 126). It may be express or implied and may even be inferred from the course of conduct of the parties concerned.

Example: S requests C to lend Rs. 500 to P and guarantees that if P fails to pay the amount, he will pay. This is a contract of guarantee. S, in this case, is the surety, C, the creditor and P, the principal debtor.

The law of contract defines that for any valid contract there must be a minimum of two parties. A contract of guarantee is one of a kind where it requires a minimum of three parties instead of two for a contract of guarantee to be valid. A contract of guarantee is a tripartite agreement, which contemplates the principal

debtor P, the creditor C, and the surety S. In it, there is a triangular relationship in which the following three collateral contracts may be distinguished:

- 1) As between C and P, there is a contract out of which the guaranteed debt arises.
- 2) As between S and C, there is a contract by which S guarantees to pay to C, P's debt in case of his (P's) default.
- 3) As between S and P, there is a contract that P shall indemnify S in case S pays in the event of a default by P. This contract, if it is not expressed between the parties, is always implied.

### Essentials of a Contract of Guarantee

1. **Concurrence of All the Parties:** All the three parties namely, the principal debtor, the creditor and the surety must agree to make such a contract.
2. **Liability:** In a contract of guarantee, liability of the surety is secondary, i.e., the creditor must first proceed against the debtor and if the latter does not perform his promise, then only he can proceed against the surety.
3. **Existence of a Debt:** A contract of guarantee pre-supposes the existence of a liability, which is enforceable at law. If no such liability exists, there can be no contract of guarantee. Thus, where the debt, which is sought to be guaranteed is already time barred or void, the surety is not liable.
4. **Consideration:** There must be consideration between the creditor and the surety so as to make the contract enforceable. The consideration must also be lawful. In a contract of guarantee, the consideration received by the principal debtor is taken to be the sufficient consideration for the surety. Thus, any benefit received by the debtor is adequate consideration to bind the surety. But past consideration is no consideration for a contract of guarantee. There must be a fresh consideration moving from the creditor.
5. **Writing not Necessary:** A contract of guarantee may either be oral or written. It may be express or implied from the conduct of parties.

**Note:** A Contract of Guarantee is always in writing under English Law.

6. **Essentials of a Valid Contract:** It must have all the essentials of a valid contract such as offer and acceptance, intention to create a legal relationship, capacity to contract, genuine and free consent, lawful object, lawful consideration, certainty and possibility of performance and legal formalities.
7. **No Concealment of Facts:** The creditor should disclose to the surety the facts that are likely to affect the surety's liability. The guarantee obtained by the concealment of such facts is invalid. Thus, the guarantee is invalid if the creditor obtains it by the concealment of material facts.
8. **No Misrepresentation:** The guarantee should not be obtained by misrepresenting the facts to the surety. Though the contract of guarantee is not a contract of *uberrimae fidei* i.e., of absolute good faith, and thus, does not require complete disclosure of all the material facts by the principal debtor or creditor to the surety before he enters into a contract. But the facts, that are likely to affect the extent of surety's responsibility, must be truly represented.
9. **In case co-surety does not join (Sec. 144):** Where a person gives a guarantee upon a contract that the creditor shall not act upon until another person has joined in it as co-surety, the guarantee will be invalid if that other person does not join.



**Example:** A agrees with B to stand as a surety for C for a loan of Rs. 1000 provided D also joins him as surety. D refuses to join. A is not liable as a surety.

### **Kinds of Guarantee**

Contracts of guarantee may be of two types (1) Specific, or (2) Continuing.

1. **Specific guarantee:** Specific guarantee means a guarantee given for one specific transaction. In this case the liability of the surety extends only to a single transaction. Example: A guarantee payment to B of the price of 5 sacks of flour to be delivered by B to C and to be paid in a month. B delivers sacks to C. C pays for them. Afterwards B delivers four sacks to C, which C does not pay. The guarantee given by A was only a specific guarantee and accordingly he is not liable for the price of the four sacks.
2. **Continuing guarantee (Sec. 129):** A continuing guarantee is that which extends to a series of transactions (Sec. 129). It is not confined to a single transaction. Surety can fix up a limit on this liability as to time or amount of guarantee, when the guarantee is a continuing one. The fact that the guarantee is continuing can also be ascertained from the intentions of the parties and the surrounding circumstances.

**Example:** A, in consideration that B will employ C in collecting the rents from B's tenants, promises B to be responsible, to the amount of Rs. 5,0000, for the due collection any payment by C of those rents. This is continuing guarantee.

**Example:** A guarantees payment to B, a tea/dealer to the amount of Rs. 100000, for tea he may from time-to-time supply to C. B supplies C with tea to the extent of the agreed value i.e., Rs. 100000 and C pays B for it. Afterwards, B supplies C with tea to the value of Rs. 200000. C fails to pay. The guarantee given by A was a continuing guarantee, and he is accordingly liable to B to the extent of Rs. 100000.

### **Rights of a surety**

#### **Rights against the Creditor**

1. Sec. 133 – The creditor ought not to change terms of the agreement between the creditor and the principal debtor without the surety's assent. Any such change releases the surety as to transactions ensuing to the difference. However, in the event that the change is for the profit of the surety or does not prefer him or is of an irrelevant character, it might not have the impact of releasing the surety.
2. Sec. 134 – The creditor ought not discharge the principal debtor from his liability under the agreement. The impact of the release of the principal debtor is to release the surety too. Any enactment or exclusion from the creditor which in law has the impact of releasing the principal debtor puts a close to the liability of the surety.
3. Sec. 135 – In the event that an agreement is made between the Creditor and Principal debtor for intensifying the latter's liability or making a guarantee to him growth of time for doing the commitments or swearing up and down to not to beyond any doubt, releases the surety unless he consents to such an agreement.
4. Sec. 139 – the surety is released if the creditor debilitates (weakens) the surety's possible remedy against the principal debtor.

#### **Rights against the Principal Debtor**

1. Right of subrogation – The surety on making good of the debt obtains a right of subrogation (the substitution of one person or group by another in respect of a debt or insurance claim, accompanied by the transfer of any asset).
2. Sec. 140 – the surety can't assert the right of subrogation to the creditor's securities in the event that he has agreed as a security for a part of the contract and security has been procured by the creditor for the complete debt.

#### 4 CONTRACTS OF BAILMENT

The term bailment is derived from French word 'bailor' which means to deliver. Bailment is a delivery of goods on condition that the recipient shall ultimately restore them to the Bailor or dispose of them according to the direction of the Bailee or dispose of them according to the direction of the Bailor.

Bailment etymologically means 'handing over' or 'change of possession'. As per section 148 of the act, bailment is an act whereby goods are delivered by one person to another for some purpose, on a contract, that the goods shall, when the purpose is accomplished, be returned or otherwise disposed of according to the directions of the person delivering them. The person who delivers the goods is called the Bailor and the person to whom the goods are delivered is called the Bailee.

##### Requisites of Bailment

1. **Contract:** A bailment is usually created by agreement between the bailor and the bailee. The agreement may be express or implied. In certain exceptional cases, bailment is implied by law as between a finder of goods and the owner.
2. **Delivery of possession:** A bailment necessarily involves delivery of possession of goods by bailor to bailee. The basic features of possession are control and an intention to exclude others. As such, mere custody of goods does not create relationship of bailor and bailee. A servant who receives certain goods from his master to take to a third party has mere custody of the goods; possession remains with the master and the servant does not become a bailee. Thus, to create bailment, there must be delivery of goods.
3. **Movable goods:** It should be noted that in bailment, only the possession of the goods is transferred not the ownership. Again, only movable goods can be bailed as immovable goods cannot be delivered. It is the main feature of bailment that it is only for the moveable property and not for the immoveable property.
4. **For some purpose:** The delivery of goods from bailor to bailee must be for some purpose. If goods are delivered by mistake to a person, there is no bailment.
5. **Return of specific goods:** It is agreed between the bailor and the bailee that as soon the purpose is achieved, the goods shall be returned or disposed of according to the directions of the bailor. For a transaction of bailment, it is necessary that the same goods must be returned. If the goods are not to be

specifically returned, there is no bailment. But there is a bailment even if the goods bailed are, in the meantime, altered in form, e.g., when a piece of cloth is stitched into a suit. Where money is deposited in a savings bank account or any other account, it is not a transaction of bailment because the bank is not going to return the same currency notes but will return only an equivalent amount. However, where money or valuables are kept in safe custody, it will amount to a transaction of bailment as these will be returned in specie.

- 6. Consideration is not necessary in case of Contract of Bailment:** In case of bailment for mutual benefit of the bailor and bailee, consideration is there for both the parties e.g., A gives his watch for repair to B for Rs. 10. For A, consideration is repair of his watch and for B, consideration is Rs. 10. However, in case of bailment either for the benefit of the bailor or bailee alone, consideration in the form of something in return is not there. In such cases, the detriment suffered by the bailor in parting with the possession of goods is considered as a sufficient consideration to support the promise on the part of the bailee to return the goods.

### Duties of Bailor

- 1. To disclose known faults:** It is the first and foremost duty of the bailor to disclose the known faults about the goods bailed to the bailee. If he does not make such disclosure, he is responsible for any damage caused to the bailee directly from such faults (Sec. 150, Para 1).
- 2. To bear extraordinary expenses of bailment:** The bailee is bound to bear ordinary and reasonable expenses of the bailment but for and extraordinary expenses the bailor is responsible.
- 3. To indemnify bailee for loss in case of premature termination of gratuitous bailment:** A gratuitous bailment can be terminated by the bailor at any time even though the bailment was for a specified time or purpose. But in such a case, the loss accruing to the bailee from such premature termination should not exceed the benefit he has derived out of the bailment. If the loss exceeds the benefit, the bailor shall have to indemnify the bailee (Sec. 159).
- 4. To receive back the goods:** It is the duty of the bailor to receive back the goods when the bailee returns them after the expiry of the term of the bailment or when the purpose for which bailment was created has been accomplished. If the bailor refuses to receive back the goods, the bailee is entitled to receive compensation from the bailor for the necessary expenses of custody.
- 5. To indemnify the bailee:** Where the title of the bailor to the goods is defective and the bailee suffers as a consequence, the bailor is responsible to the bailee for any loss which the bailee may sustain by reason that the bailor was not entitled to make bailment, or to receive back the goods, or to give directions respecting them (Sec. 164).

### Duties of Bailee

1. **To take reasonable care of the goods bailed:** In all cases of bailment the bailee is bound to take as much care of the goods bailed to him as a man of ordinary prudence would, under similar circumstances, take of his own goods of the same bulk, quality and value as the goods bailed (Sec. 151).
2. **Not to make any unauthorized use of goods:** If the bailee uses the goods bailed in a manner which is inconsistent with the terms of the contract, he shall be liable for any loss even though he is not guilty of negligence, and even if the damage is the result of an accident (Sec. 1534).
3. **Not to mix the goods bailed with his own goods:** The bailee must not mix the goods of the bailor with his own goods; but must keep them separate from his own goods. If he mixes the bailor's goods with his own goods.
4. **Not to set up an adverse title (Sec. 117 of the Indian Evidence Act, 1872):** The bailee must hold the goods on behalf of and for the bailor. He cannot deny the right of the bailor to bail the goods and receive them back. If he delivers the goods bailed to a person other than the bailor, he may prove that such person had a right to them as against the bailor.
5. **To return any accretion to the goods:** In the absence of any contract to the contrary, the bailee is bound to deliver to the bailor, or according to his directions, any increase or profit, which may have accrued from the goods, bailed (Sec. 163).
6. **To return the goods:** It is the duty of the bailee to return or deliver, according to the bailor's directions, the goods bailed, without demand, as soon as the time for which they were bailed has expired, or the purpose for which they were bailed has been accomplished (Sec. 160). If he fails to do so, he is responsible to the bailor for any loss (Sec. 161) notwithstanding the exercise of reasonable care on his part.

### **Rights of Bailor**

1. **Enforcement of rights:** The bailor can enforce by suit all the liabilities or duties of the bailee, as his rights.
2. **Avoidance of contract:** The bailor can terminate the bailment if the bailee does, with regard to the goods bailed, any act which is inconsistent with the terms of the bailment (Sec. 153).
3. **Return of goods lent gratuitously:** When the goods are lent gratuitously, the bailor can demand their return whenever he pleases even though he lent them for a specified time or purpose. But if the bailee suffers any loss exceeding the benefit actually derived by him from the use of such goods because of premature return of goods, the bailor shall have to indemnify the bailee (Sec. 159).
4. **Compensation from a wrongdoer:** If a third person wrongfully deprives the bailee of the use or possession of the goods bailed, or does them any injury, the bailor or the bailee may bring a suit against the third person for such deprivation or injury (Sec. 180)

### **Rights of Bailee**

1. **Delivery of goods to one of several joint bailors of goods:** If several joint owners of goods bail them, the bailee may deliver them back to, or according to the directions of, one joint owner without the consent of all, in the absence of any agreement to the contrary (Sec. 165).
2. **Delivery of goods to bailor without title:** If the bailor has no title to the goods, and the bailee, in good faith, delivers them back to, or according to the directions of, the bailor, the bailee is not responsible to the owner in respect of such delivery (Sec. 166).
3. **Right to apply to court to stop delivery:** If a person, other than the bailor, claims goods bailed, the bailee may apply to the Court to stop the delivery of the goods to the bailor, and to decide the title to the goods (Sec. 167).
4. **Right of action against trespassers:** If a third person wrongfully deprives the bailee of the use or possession of the goods bailed to him, he has the right to bring an action against that party. The bailor can also bring a suit in respect of the goods bailed (Sec. 180).
5. **Bailee's lien:** Where the lawful charges of the bailee in respect of the goods bailed are not paid, he may retain the goods. This right of the bailee to retain the goods is known as 'particular lien'. Lien means the right of a person to retain possession of some goods belonging to another until some debt or claim of the person in possession is satisfied. It appertains to the person who has possession of the goods, which belong to another, entitling him to retain them until the debt due to him has been paid.
  - 1) **Particular lien:** A particular lien is one, which is available to the bailee against only those goods in respect of which he has rendered some service involving the exercise of labour or skill. Example: (a) A delivers a rough diamond to B, a jeweler, to be cut and polished. This is accordingly done. B is entitled to retain the finished diamond till he is paid for services he has rendered. (b) A gives a piece of cloth to B, a tailor, to make into a coat. B promises A to deliver the coat as soon as it is finished. B is entitled to retain the coat till he is paid for. Example: A gives a piece of cloth to B, a tailor, to sew it into a coat. B promises A to deliver the coat as soon as it is finished, and to give A three months' credit for the price. B is not entitled to retain the coat.
  - 2) **General lien:** A general lien is a right to retain all the goods or any property (Which is in possession of the holder) of another until all the claims of the holder are satisfied. This is a right to retain the property of another for a general balance of account. Example: if two securities are given to a banker but a loan is taken only against one of the securities, the banker may retain both the securities until his claim is satisfied.

### Termination of Bailment

A contract of bailment is terminated in the following cases:

1. **On the expiry of the period:** When the bailment is for a specific period, it terminates on the expiry of that period.
2. **On the achievement of the object:** When the bailment is for a specific purpose, it terminates as soon as the purpose is achieved.
3. **Inconsistent use of goods:** When the bailee uses the goods in a manner

inconsistent with the terms of the contract, the bailment terminates (Sec. 154).

4. **Destruction of the subject matter:** A bailment is terminated when the subject matter of the bailment (a) is destroyed, or (b) by reason of a change in its nature becomes incapable of use for the purpose of the bailment.
5. **Gratuitous (unjustified) bailment:** It can be terminated any time subject to condition laid down in Sec. 159.
6. **Death of the bailor or bailee:** A gratuitous bailment is terminated by the death either of the bailor or of the bailee (Sec. 162).

## CONTRACTS OF PLEDGE

In pledge, the bailor is called the pledger or pawnor and the bailee is called the pledgee or pawnee (Sec. 172).

A pledge is a bailment for security. It is a special kind of bailment. Example: If A borrows Rs. 200 from B and keeps his watch as security for payment of the debt, the bailment of watch is a pledge. Any kind of movable property, i.e., goods, documents, or valuables may be pledged. Even a Savings Bank Pass Book may be pledged [J. & K. Bank v. Tek Chand, A.I.R. (1959) J. & K. 67]. But delivery is necessary to complete a pledge. The delivery may be actual or constructive. If, because of the bulk of the property or for some other reason, actual delivery is impracticable, a symbolic delivery will suffice (as for example delivery of the keys to a locker in a safe deposit vault).

### Pledge by Non-owners

Ordinarily only a person who is the real owner of the goods can make a valid pledge, but in the following cases pledge made by non-owners will also be valid.

1. **Pledge by a mercantile agent (Sec. 178):** Where a mercantile agent is, with the consent of the owner, a possession of goods or the documents of title to goods, any pledge made by him, when acting in the ordinary course of business of a mercantile agent, shall be as valid as if he were expressly authorised by the owner of the goods to make the same, provided that the pawnee act in good faith and has not at the time of the pledge notice that the pawnor has no authority to pledge.
2. **Pledge by person in possession under voidable contract (Sec. 178 A):** When the pawnor has obtained possession of the goods pledged by him under a contract voidable under Section 19 or Section 19A, but the contract has not been rescinded at the time of the pledge, the pawnee acquired a good title to the goods, provided he acts in good faith and without notice of the pawnor's defect of title.
3. **Pledge where pawnor has only a limited interest (Sec. 179).** Where a person pledges goods in which he had only a limited interest, the pledge is valid to the extent of that interest.
4. **Pledge by a co-owner in possession:** If there are several joint owners of goods and goods are in the sole possession of one of the co-owners with the consent of other co- owners, such a co- owner can make a valid pledge of goods.
5. **Pledge by seller or buyer in possession after sale:** A seller, who has got

possession of goods even after sale, can make a valid-pledge, provided the pawnee acts in good faith.

### **Rights and Duties of Pawnor and Pawnee.**

The rights and duties of pawnor and pawnee are almost similar to those of bailor and bailee. But the rights of the Pawnee and pawnor need a special mention.

#### **Rights of Pawnee**

- 1. Right of retainer:** The pawnee may retain the goods pledged until his dues are paid. He may retain them not only for the payment of the debt or the performance of the promise, but for (a) the interest due on the debt, and (b) all necessary expenses incurred by him in respect of the possession or for the preservation of the goods pledged (sec. 173). He can however exercise only a particular lien over the goods.
- 2. Right of retainer for subsequent advances:** When the pawnee lends money to the same pawnor after the date of the pledge, it is presumed that the right of retainer over the pledged goods extends to subsequent advances also. This presumption can be rebutted only by a contract to the contrary (Sec. 174).
- 3. Right to extraordinary expenses:** The pawnee is entitled to receive from the pawnor extraordinary expenses incurred by him for the preservation of the goods pledged (Sec.175). For such expenses, he has no right to retain the goods; he can only sue to recover them.
- 4. Right against true owner, when the pawnor's title is defective:** When the pawnor has obtained possession of the goods pledged by him under a voidable contract (i.e., by fraud, undue influence, coercion, etc.) but the contract has not been rescinded at the time of the pledge, the pawnee acquires a good title to the goods, provided he acts in good faith and without notice of the pawnor's defect of title (Sec. 178, A).
- 5. Pawnee's rights where pawnor makes default (Sec. 176):** Where the pawnor fails to redeem his pledge, the pawnee can exercise the following rights:
  - a) He may file a suit against the pawnor upon the debt or promise and may retain the goods pledged as a collateral security.
  - b) He may sell the goods pledged after giving the pawnor a reasonable notice of the sale. Of these two rights, while the right to retain or sell the pawned goods are not concurrent, the right to sue and sell are concurrent right, i.e., the pawnee may sue and at the same time retain the goods as concurrent security or sell them after giving reasonable notice of the sale to the pawnor [Haridas Mundra v. National & Grindlays Bank Ltd., A.I.R. (1963) Cal. 132].
  - c) He can recover from the pawnor any deficiency arising on the sale of the goods by him. But he shall have to hand over the surplus, if any, realized on the sale of the goods to the pawnor.

#### **Rights of Pawnor**

- 1. Right to get back goods:** On the performance of promise or repayment of loan and interest, if any, the pawnor is entitled to get back the goods pledged.
- 2. Right to redeem debt:** Quite often a time is stipulated for the payment of the

debt, or performance of the promise, for which the pledge is made. In such a case if the pawnor makes default in payment of the debt or performance of the promise at the stipulated time, he may still redeem the goods pledged at any subsequent time before the actual sale of them; but he must pay additionally, in that case, any expenses that have arisen from his default (Sec. 177).

3. **Preservation and maintenance of the goods:** The pawnor has a right to see that the pawnee, like bailee, preserves the goods pledged and properly maintains them.
4. **Rights of an ordinary debtor:** The pawnor has, in addition to the above rights, the rights of an ordinary debtor, which are conferred on him by various Statutes meant for the protection of debtors.

### **Difference between Bailment and Pledge**

The following are the major differences between Bailment and Pledge:

1. A Bailment is a contract in which goods are transferred from one party to another party for a short period for a specific objective. The Pledge is a kind of Bailment in which goods are pledged as security against payment of debt.
2. A Bailment is defined under section 148 while Pledge is defined under section 172 of the Indian Contract Act, 1872.
3. In bailment, the consideration may or may not be present, but in the case of a pledge, the consideration is always present.
4. The objective of bailment is safe custody or repairing of goods delivered. On the other hand, the sole purpose of delivering the goods is to act as security against the debt.
5. The receiver has no right to sell the goods in case of bailment whereas if Pawnor does not redeem the goods within the reasonable time, the Pawnee can sell the goods after giving notice to him.
6. In bailment, the goods are used by the bailee only for the said purpose. Conversely, in pledge, Pawnee has no right to use the goods.

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## **2.5 CONTRACT OF AGENCY**

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When a person employs another person to do any act for himself or to represent him in dealing with third persons, it is called a 'Contract of Agency'. The person who is so represented is called the 'principal' and the representative so employed is called the 'agent' (Sec. 182). The duty of the agent is to enter into legal relations on behalf of the principal with third parties. But, by doing so he himself does not become a party to the contract to the contract not does he incur any liability under that contract. Principal shall be responsible for all the acts of his agent provided they are not outside the scope of his authority.

The term agent can best be used to denote a relationship that is very different from that between a master and his server, or an employer and his independent contractor.

"Although employees and independent contractors are parties to relationships in which one person acts for another and possesses the ability to involve that other person in responsibility, the nature of the relationship and the type of acts in question are different enough to justify the exclusion of independent servers and contractors from the law relating to the agency, unless a server or independent



contractor is employed as an agent at a given time, when it should be called that way. In other words, the term agent must be restricted to the one who has the power to affect the legal status of his principal by entering into contracts or the disposition of property: but which, incidentally, may affect the legal position of his principal in other ways.

One that represents and acts for another under the contract or agency relationship. The agents are general or special. A general agent is one who is employed in his capacity as professional man or teacher of an art or trade, or to whom the director entrusts all his business or all transactions or functions of a designated class; or is a person who is authorized by his principal to execute all the deeds, sign all contracts or buy all the goods required in a particular trade, business or employment.

### **Definition of Agent**

West's Encyclopedia of American Law "A person who has received the power to act on behalf of another, binding that other person as if he or she were themselves making the decisions." Duhaime's Law Dictionary

A party that has express (oral or written) or implied authority to act for another (the principal) so as to bring the principal into contractual relationship with other parties. An agent is under the control (is obligated to) the principal, and (when acting within the scope of authority delegated by the principal) binds the principal with his or her acts. Additional powers are assigned to agents under the legal concept of 'apparent authority'. The agent, however, does not have title to the principal's goods in his or her possession, except where agent's lien is applicable. In general, advertising agencies do not fall under this definition of an agent, because they act as principals for the services they buy on behalf of their clients.

### **Definition of Principal**

In commercial law, a principal is a person, legal or natural, that authorizes an agent to act to create one or more legal relationships with a third party.

In an agency relationship, the principal is the person who gives authority to another, called an agent, to act on his or her behalf.

Generally, anyone who has the legal capacity to carry out an action can appoint an agent to do it on their behalf. Common types of principal/agent relationships include employer/employee, corporation/officer, client/attorney. It's also possible to create an agent by drawing up a power of attorney to authorize someone to act as one's representative. As long as one has the legal capacity to make decisions.

### **Essentials of relationship of Agency**

There are two essentials of the relationship of agency:

1. **Agreement between the principal and the agent:** The agency depends on the agreement, but not necessarily on the contract. As between the director and third parties, anyone can become an agent. As such, even a minor or a sick-minded person can be an agent. However, the principal is responsible for the acts of said agent.

2. **Intention of the agent to act for the principal:** Whether a person intends to act on behalf of another is a matter of fact. When a person intends to act on behalf of another, the agency may arise even if the contract between the parties stipulates that there is no such relationship.

### Rules of Agency

There are two important rules of agency:

1. **What a person can do personally, can be done through agent:** This rule, of course, is subject to certain well-known exceptions, such as when the act that is performed is of a personal nature (i.e, singing) or is attached to a public office.
2. **He who does an act through another can be dealt by himself:** This means that the acts of an agent, subject to certain conditions, are acts of the principal. Sec. 226 clearly states that the acts and contracts of an agent will have the same legal consequences as if the contracts and acts performed by the director in person had been celebrated.

### Creation of Agency

A person who has the capacity to contract can contract for himself or for another person. If you adopt the first method, it is not about agency. If you adopt the second method, then there arises the concept of an agency. The person who represents another in their dealings with third parties is called an agent and that person who is represented by an agent is called a principle.

The following are different modes of creation of agency.

1. Agency by Express agreement.
  2. Agency by Operation of law.
  3. Agency by Ratification.
  4. Agency by Implied authority.
1. **Agency by Express Agreement:** The authority of an agent can be expressed or implied (Sec. 186). Normally, the authority given by a principal to his agent is an express authority, which allows the agent to bind the principal for acts performed within the scope of his authority. The agent can, in such case, be designated by word of mouth or by means of a written agreement (Sec.187). The usual form of a written agency contract is power (a formal instrument by which one person empowers another to represent it, or act in its place, for certain purposes) on a stamped paper.
  2. **Agency by Implicit (implied) Agreement:** The implied agency arises from the conduct, situation or relationship of the parties. It can be deduced from the circumstances of the case, and the things spoken or written or the ordinary course of the negotiation, can be counted as circumstances of the case (Sec. 187). Examples: A and P are brothers. A lives in Delhi while P lives in Meerut. A with the knowledge of P Leases P lands in Delhi. The income is reported and sent to P. A is the agent of P, although it is not expressly designated as such.

The implied agency arises when the principal addresses the person supposedly the agent or third parties in such a way, as if the director had granted the appointment of that person as agent. It includes:

- a) **Agency for estoppels:** The doctrine of estoppel can be expressed as follows: When a person, by his behavior, or by spoken or written words, voluntarily induces another person to believe that a certain state of affairs exists and induces him to act in accordance with that belief to alter his previous position, it is prevented from subsequently denying the fact of that state of affairs.
  - b) **Agency retaining:** The agency retaining is a branch of the agency by estoppel. In this case, a positive or affirmative prior act by the director is required to establish the agency later.
  - c) **Agency by necessity:** In certain urgent circumstances, the law confers authority on one person to act as agent for the benefit of another, with no opportunity to communicate with that other. Such an agency is called a necessity agency.
3. **Agency for Ratification:** A person can act on behalf of another person without their knowledge or consent. For example, A can act as agent of P even though he does not have prior authority of P. In such a case, P can subsequently accept the act of A or reject it. If he accepts the act of A, done without his consent, it is said that he ratified that act and places the parties exactly in the same position as they would have been if A had the authority of P at the time, he made the contract. In the same way, when an agent exceeds the authority granted by the principal, the principal can ratify the unauthorized act. Ratification can be expressed or implied. In case the adoption of the activity is done through the expression, it is called express ratification. For example, without the address of A, B has purchased goods for the sake of A. After A has given his support (adoption) to the activity of B, it is called Ratification. Now A is Principal and B is agent. Ratification where there is no expression is called implicit ratification. For example: Mr. Q has P's money with him. Without the direction of P, Q has lent that money to R. Thereafter R has paid interest directly to P. Without any debate P has taken that amount of R. This implies that P has given his support to the activity of Q. It is an implicit ratification.

### Duties of Agent

An agent owes a number of duties to his principal which varies in degree according to the nature of agency. These duties are as follows:

1. **To carry out the work given by the director:** In the absence of such instructions, you must act in accordance with the custom that prevails when doing business of the same type in the place where you conduct such business. When acting otherwise, if any loss is sustained, it must be made good for its principal, and if any gain accrues, it must be accounted for (Sec. 211). If the disobedience of the agent is material, the director may even terminate the agency. For example, A, an agent engaged in conducting a P business, in which it is customary to invest from time to time, at interest, the money that may be available, fails to make such investments. A should be good for P the interest generally obtained by such investment.

2. **To carry out the work with care, skill and diligence:** An agent is required to carry out the business of the agency with as much skill as people in similar businesses usually possess, unless the director is aware of his lack of ability. He is always required to act with reasonable diligence, to use the skills he possesses, and to compensate his principal with respect to the direct consequence of his negligence, lack of skill or misconduct. But he is not responsible to his director regarding the loss or damage, which is indirectly or remotely caused by such negligence, lack of skill or misconduct.
3. **To communicate with the director in case of difficulty:** It is the duty of an agent, in cases of difficulty, to use all reasonable diligence to communicate with his principal and seek to obtain his instructions (Section 214).
4. **Do not try on your own:** An agent should not deal with his own account in the business of the agency without first obtaining the consent of the director and familiarizing him with all the material circumstances that he has come to his knowledge.
5. **Pay the sums received by the principal:** An agent is obligated to pay his principal all the sums received in his account (Sec. 218). He may deduct from it all the money that corresponds to him for advances made or expenses incurred by him in carrying out such business and also the remuneration that corresponds to him for acting as agent (Sec. 217).
6. **To protect and preserve the interests of the principal in the event of his death or insolvency:** When the principal expires an agency, the principal is dying or is losing sanity, the agent is obliged to take, on behalf of the representatives of his late director, all reasonable steps for the protection and preservation of the interests that are Trust (Sec. 209).
7. **Not to use information obtained in the course of the agency against the principal:** It is the duty of the agent to transmit any information received in the course of the agency to its director. When one uses such information against the interest of the principal and the principal suffers a loss, one is obligated to compensate the principal. The principal may also prevent the agent from using such information through a court order.
8. **Not to make secret profit from agency:** An agent occupies a fiduciary position. It must not, except with the knowledge and consent of the principal, obtain any benefit beyond the agreed commission or remuneration.
9. **Not to set up an adverse title:** An agent must not set up his own title or the title of a third person (unless he proves a better title in that person) to the goods, which he receives, from the principal as an agent. If he does so, he will be liable for conversion (any act in relation to goods of another person which constitutes an unjustifiable denial of his title to them).
10. **Not to put himself in a position where interest and duty conflict:** An agent has the obligation, in all cases, to act in the interest of the principal. You must not place yourself in a position where your duty to the principal and your personal interest is in conflict unless you have made a full disclosure of your interest to your principal, specifying its exact nature and

obtaining your assent. For example, P hired A, a stockbroker, but with some shares for him. A sold his own shares to P without revealing that the shares belonged to him. Held, P could terminate the contract.

11. **Not to delegate authority:** An agent should not, as a general rule, delegate another person to do what he has committed himself to do. However, this is subject to certain exceptions (Sec. 190).

**Liabilities of Agent:**

Actually, the agents link the principal with their activities, but there are some situations in which the agent finds personal responsibility. Those situations are the following;

- i. **Liabilities regarding damages and misconduct:** In case of breach of contract by an agent, he is responsible for paying the damages. If he is found guilty of misconduct, the principal may delay his remuneration for the part of the business he has mistreated.
- ii. **Personal liability of an agent when it is established by commercial custom or use:** If the commercial custom or use in the business specifies the personal responsibility of an agent, then one will be considered personally responsible for his / her misconduct, until specified otherwise.
- iii. **When an agent expressly accepts being responsible:** When the contract expressly specifies that the agent will be personally responsible in case of breach of contract, then he can be held personally responsible.
- iv. **Liability for their unlawful acts:** An agent takes personal responsibility when acting beyond his authority or commits fraud or misrepresentation.
- v. **Responsibility for the actions of subagents:** When an agent appoints a sub-agent, without having the authority to do so, he will be responsible for all acts of the sub-agent, both for the principal and the third party.

**Rights of Agent.**

An agent has the following rights against the principal:

1. **Right of retainer:** The agent may withhold, from any amount received on account of the principal in the agency's business, all the money owed to him with respect to his remuneration and advances made or expenses incurred by him in conducting such business (Sec. 217).
2. **Right to receive remuneration:** The agent is entitled to his agreed remuneration, or if there is no agreement, to a reasonable remuneration. But in the absence of a special contract, the payment for the performance of any act is not due to the agent until the completion of such act (Sec. 219). Now the question is: when is the act completed? This depends on the terms of the contract.

3. **Right of lien:** In the absence of any contract to the contrary, an agent has the right to retain property, papers and other property, whether movable or immovable, from the principal received by him, up to the amount owed by commission, disbursements and services in connection with the same has been paid or accounted for (Sec. 221). This encumbrance of the agent is a private encumbrance. It is limited to claims that arise in relation to the goods or goods in respect of which the right is claimed. But through a special contract, an agent can have a general lien that extends to all claims arising from the agency.
4. **Right of indemnification:** The agent has the right to be indemnified against The agent has the right to be compensated against the consequences of all legal acts performed by him in the exercise of the authority conferred on him (Sec.222).
5. **Right of compensation:** The agent has the right to be compensated for injuries sustained due to negligence or lack of skill on the part of the director (Section 225). For example, P employs A as a bricklayer in the construction of a house and lifts the scaffolding himself. The scaffolding is misplaced and, consequently, A is injured. P must compensate A.
6. **Right of stoppage in transit:** This right is available to the agent in the following two cases: (1) When you have purchased goods for your principal by incurring personal liability, you have the right to stop in transit against the principal, with respect to the money you have paid or must pay. This right of the agent is similar to that of the unpaid seller.  
  
(2) When he is personally liable to the principal for the price of the goods sold, he is placed in the position of a seller not paid to the buyer and may stop the goods in transit incase of insolvency of the buyer.

### Duties of Principal

The duties of a principal towards his agent are the rights of the agent against the principal. The rights of an agent have already been discussed. The principal owes the following duties to an agent:

1. **To indemnify the agent against the consequences of all lawful acts:** The principal is obliged to indemnify the agent against the consequences of all legal acts performed by said agent in the exercise of the authority conferred on him (section 222).
2. **To indemnify the agent against the consequences of acts done in good faith:** When a person employs another to do an act, and the agent does the act in good faith, the employer is obligated to indemnify the agent against the consequences of that act, even if it causes an injury to the rights of a third party (Sec. 223). However, when a person employs another to perform an act that is criminal, the employer is not liable to the agent, either by an express or implied promise, to indemnify him against the consequences of that act (Section 224).
3. **To indemnify agent for injury caused by principal's neglect:** The principal must compensate his agent regarding an injury caused to that agent

by negligence or lack of skill of the principal (Sec.225).

4. **Duty to Compensate:** An agency relationship can be paid or free. The term of an agency can be established in an agency agreement. If the agreement of the agency does not indicate the terms of the compensation, the principal is obligated to provide the agent with reasonable compensation.
5. **Duty to Reimburse:** The principal must reimburse the agent for a reasonable amount spent in fulfilling the duties. Reasonable refund includes the cost of travel, meals, lodging, incidentals, etc.

### **Right of Principal.**

Rights are legal, social or ethical principles of freedom or right; that is, rights are the fundamental normative rules about what people are allowed or are owed to people, according to some legal system, social convention or ethical theory.

The principal can enforce all the duties of the agent that are indirectly the rights of the principal. When an agent fails in his duty towards the principal, the principal has the following remedies against the agent:

1. **To recover damages:** If the principal suffers a loss because the agent ignores the instructions of the principal, or does not follow the custom of the exchange in the absence of instructions from the principal, or when the principal suffers due to lack of skill, care, or diligence on the part of the agent, he can recover the accumulated damages as a result of the agent.
2. **To obtain an account of secret profits and recover them and resist a claim for remuneration:** If the agent, without the knowledge and assent of the principal, obtains secret profits from the agency, the principal has the right to recover them from the agent. Not only this, the agent also loses his right to any commission with respect to the transaction. When the agent generates a secret benefit, the contract with the third party is not invalidated.
3. **To resist agent's claim for indemnity against liability incurred:** When the principal can demonstrate that the agent has acted as principal and not merely as an agent, he can oppose the agent's claim for compensation against the liability incurred by him in that transaction.

### **Termination of Agency**

After the termination of the agency, the agent is free of any fiduciary obligation to the principal derived from the relationship of the agency. The parties may terminate the agency by mutual agreement. An agency cannot be rescinded by the act of one of the parties and must be done mutually.

An agency relationship will end automatically when certain events occur. Such events include death, insanity or bankruptcy of the principal or agent. A court usually intervenes and terminates the agency relationship if one of the parties refuses to do so.

### **Termination of agency by the operation of law**

The following are the situation where the agency is terminated by the operation of law:

1. **Expiration of time:** sometimes the agency contract can be formed for a particular period. In such case, after the expiration of the agreed period, the termination of the agency occurs.
2. **Fulfilment of the object:** sometimes the agency contract can be found for a particular purpose or to make a particular company. In such case, the termination of the agency takes place after the completion of that company.
3. **Death or madness of either party:** whenever the principal or agent encounters death or insanity, the agency contract ends.
4. **Insolvency of the director:** the director must have the capacity to contract. When the principal becomes insolvent, he renounces the ability to contract and the termination of the agency occurs. But the act is silent with respect to the agent's insolvency. As a minor can also act as an agent, it can be conformed that the insolvent person can act as an agent.
5. **Destruction of matter:** when the object of the contract is destroyed, the contract of the agency comes to an end.
6. **Principal-Alien Enemy:** when the principal is a foreigner and the war breaks out between the countries, the principal becomes a foreign enemy and the contract of the agency is cancelled.
7. **Liquidation of the company:** because of the legal entity, the company can act as principal or agent. Whatever the state, if the company goes into liquidation, the termination of the agency occurs.

### Termination by the act of Parties

The following are the situation where the agency is terminated by the act of parties:

1. **Termination of the agency by the principal:** the principal can terminate the agency contract by notifying the agent. In doing so, if the agent encounters some suffering the principal has to compensate the agent.
2. **Termination of the agency by the agent:** the agent can also terminate the agency's contract by notifying the principal, but in doing so if the principal encounters some suffering, the agent has to compensate.
3. **Termination of the agency by both parties to the contract:** through mutual understanding between the principal and the agent, the contract of the agency may come to an end.

### Termination of sub-agency and substituted agency

The authority of the subagent will end when the main agency is finished. However, the substitute agency will not close automatically if the principal agent's authority is cancelled.

**Personal liability of an agent when it is established by commercial custom or use:** If the commercial custom or use in the business specifies the personal



responsibility of an agent, then one will be considered personally responsible for his / her misconduct, until specified otherwise.

- vi. When an agent expressly accepts being responsible:** When the contract expressly specifies that the agent will be personally responsible in case of breach of contract, then he can be held personally responsible.
- vii. Liability for their unlawful acts:** An agent takes personal responsibility when acting beyond his authority or commits fraud or misrepresentation.
- viii. Responsibility for the actions of subagents:** When an agent appoints a sub-agent, without having the authority to do so, he will be responsible for all acts of the sub-agent, both for the principal and the third party.

### Exercise

#### Descriptive Questions

1. Explain in brief the different types of agreements expressly declared void by the Contract Act 1872.
2. Define in detail what are contingent contracts.
3. Explain in detail the different ways to perform a contract and who can perform?
4. Define the different ways in which the contract can be discharged.
5. When is the consideration and object of an agreement considered to be unlawful?
6. Elaborate the different remedies available to an aggrieved party for the breach of contract.
7. What is a contract of Indemnity? Also explain the rights and duties of and indemnityholder.
8. What is a contract of Guarantee? Explain the essential elements of a contract of guarantee.
9. Define the Contracts of Indemnity and Guarantee and explain in detail the distinction between the two.
10. What are contracts of bailment? Define in detail the requisites of bailment.
11. Define in detail the rights and duties of Bailor and Bailee.
12. What are Contracts of Pledge? Define in detail the rights of Pawnor and Pawnee.
13. Define contracts of bailment and pledge and explain in detail the distinction between them.
14. Define agency. What are the essentials and rules related to agency?
15. Elaborate the different ways in which an agency can be created.
16. Explain in detail the rights and duties of an agent.
17. Explain in detail the rights and duties of principal.
18. Elaborate the different ways in which an agency can be terminated.

#### Short Notes

1. Requisites of a valid tender
2. Wagering agreement
3. Characteristics of contingent contracts
4. The discharge of contract by agreement or mutual consent
5. Impossibility of performance

6. Types of damages awarded for breach of contract
7. Quantum Meruit
8. Kinds of guarantee
9. Rights of surety
10. Termination of Bailment
11. Particular and General Lien
12. Termination of agency by acts of parties
13. Termination of agency by operation of law
14. Creation of agency by ratification
15. Creation of agency by implied agreement
16. Define agent and principal

### Multiple Choice Questions

1. **A contract to do or not to do something, if some event, collateral to such contract does or does not happen is called a...**
  - a. Unenforceable contract
  - b. Quasi Contract
  - c. Contingent contract
  - d. None of the above
  
2. **Under a contract if a promisor offers to attempt performance, but the promisee refuses to accept such an attempt. What does such an attempt to performance amount to?**
  - a. Tender
  - b. Performance
  - c. Void Agreement
  - d. Valid Contract
  
3. **Novation, Rescission, Alteration, Remission, Waiver and Merger are all different ways to discharge contracts by what means?**
  - a. Discharge by Performance
  - b. Discharge by consent
  - c. Discharge by impossibility of performance
  - d. Discharge due to change of law.
  
4. **A supplies B (a minor) with essential necessities for his living. B is not personally liable to pay, but A is entitled for reimbursement from the properties or estate of B. according to the Contract Act 1872 what are such contracts called?**
  - a. Unenforceable contract
  - b. Quasi Contract
  - c. Contingent contract
  - d. Void Contract
  
5. **Where in a contract, partly performed by one party has become discharged by breach of the contract by the other party. As a remedy to breach of contract the aggrieved party is entitled to claim from the other party a consideration for the amount of performance done. What is such a remedy to breach of contract called?**

- a. Quantum Meruit
  - b. Nominal Damages
  - c. Injunction
  - d. Specific Performance
- 6. According to the Contract Act 1872 a 'Wagering Agreement' is a.....**
- a. Valid agreement
  - b. Void agreement
  - c. Contingent agreement
  - d. None of the above
- 7. Which of the following is a method to discharge contract by mutual agreement or consent?**
- a. Novation
  - b. alteration
  - c. recession
  - d. all the above
- 8. Ordinarily, special, vindictive and nominal are all different forms of \_\_\_\_\_**
- a. contracts
  - b. agreements
  - c. Damages
  - d. none of the above
- 9. What type of a contract is a contract of fire insurance?**
- a. Contract of indemnity
  - b. Contract of Bailment
  - c. Contract of Guarantee
  - d. Contract of Pledge
- 10. Which of these has an indemnity holder the right to recover?**
- a. Damages in any suit
  - b. Costs incurred in any suit
  - c. Any sum paid as compromise
  - d. All the above
- 11. Which of the following necessarily has to have three parties to the contract?**
- a. Contract of Indemnity
  - b. Contract of Bailment
  - c. Contract Of Guarantee
  - d. Contract of Pledge
- 12. In a contract of guarantee liability of the surety is...**
- a. Primary
  - b. Secondary
  - c. Contingent
  - d. None of the above

**13. A guarantee that extends to not one but a series of transactions is better known as...**

- a. Specific guarantee
- b. Continuing guarantee
- c. No guarantee
- d. Full guarantee

**14. An act whereby goods are delivered by one person to another for some purpose, on a contract, that the goods shall, when the purpose is accomplished, be returned are called?**

- a. Contract of Indemnity
- b. Contract of Bailment
- c. Contract Of Guarantee
- d. Contract of Pledge

**15. The bailment of goods as security for payment of a debt or performance of a promise is called a...**

- a. Contract of Indemnity
- b. Contract of Bailment
- c. Contract Of Guarantee
- d. Contract of Pledge

**16. A contract of bailment can be made for....**

- a. Movable property only
- b. immovable property only
- c. both movable and immovable property
- d. none of the above.

**17. A contract of bailment can be terminated in which of the following ways?**

- a. On the expiry of the specific period
- b. on destruction of the subject matter
- c. on the achievement of the object
- d. all of the above

**18. What do you call a person who has received the power to act on behalf of another, binding that other person as if he or she were themselves making the decision?**

- a. Principal.
- b. Agent.
- c. Creditor.
- d. Attorney.

**19. What do you call a person who gives authority to another to act on his or her behalf?**

- a. Principal.
- b. Agent.
- c. Creditor.
- d. Attorney.

**20. Which of the following is not a method of terminating an agency relationship by operation of law?**

- a. Bankruptcy of the principal.
- b. Mutual agreement.
- c. Insanity of either the principal or the agent.
- d. Death of either the principal or the agent.

**MCQ Answer key**

1.	2.	3.	4.	5.	6.	7.	8.	9.	10	11	12	13	14	15	16	17	18	19	20
c	a	b	c	a	b	d	c	a	d	c	b	b	b	d	a	d	b	a	b

- 3.0 INTRODUCTION**
  - 3.1 DEFINITION**
  - 3.2 TYPES OF GOODS**
  - 3.3 GENERAL PRINCIPLES**
  - 3.4 ESSENTIALS OF CONTRACT OF SALE**
  - 3.5 TRANSFER OF OWNERSHIP**
  - 3.6 SALE BY NON-OWNERS**
  - 3.7 UNPAID SELLER AND HIS RIGHTS**
  - 3.8 CARRIAGE BY SEA**
  - 3.9 CONDITIONS AND WARRANTIES**
  - 3.10 DOCTRINE OF — CAVEAT EMPTOR**
  - 3.11 AUCTION OF SALE**
- CHECK YOUR PROGRESS**

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### **3.0 INTRODUCTION**

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- The law relating to sale and purchase of goods, prior to 1930 were dealt by the Indian Contract Act, 1872.
- In 1930, Sections 76 to 123 of the Contract Act was repealed and a separate Act known as the Sale of Goods Act, 1930 was passed
- This act lays down special provisions governing the contract of sales of goods. The general law of contract is also applicable to the contracts for the sale of goods unless they are inconsistent with the express provisions of the Sale of Goods Act

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### **3.1 DEFINITIONS**

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1. Buyer: "Buyer means a person who buys or agrees to buy goods." [Sec. 2(1)]  
The definition of buyer is so worded as to include a person who buys as well as one who agrees to buy goods but not a person who has only the option to buy goods.
- (2) Seller: "Seller means a person who sells or agrees to sell goods." [Sec. 2(13)]
- (3) Delivery:\* "Delivery" means voluntary transfer of possession from one person to another" [Sec. 2 (2)]

In the words of Pollock, delivery is "voluntary dispossession in favour of another." Therefore, in case of theft, there is no delivery, though there is a transfer

## SALES OF GOODS ACT, 1930 I & II

of possession. Again, there may be custody without possession, viz. a servant put in charge of his master's goods.

### (4) Deliverable State:\*

"Goods are said to be in a 'deliverable state' when they are in such state that the buyer would under the contract be bound to take delivery of them." [Sec. 2 (3)]

### (5) Documents of Title to Goods:\*

It "includes a Bill of lading, Dock-warrant, Warehouse-keeper's Certificate, Wharfinger's Certificate, Railway Receipt, multimodal transport document Warrant or Order for the delivery of goods and any other document used in the ordinary course of business as proof of the possession or control of goods, or authorising or purporting to authorise, either by endorsement or by delivery, the possessor of the document to transfer or receive goods thereby represented." [Sec. 2 (4)]

The assignment of a bill of lading operates as constructive delivery of the goods. (*Ramdas v. Amerchand*, (1916) 40 Bom. 630 (637). But, as pointed out in *Gurney v. Behrend* ((1854) 118 E.R. 1275) it is not, like a bill of exchange or promissory note, a negotiable instrument which passes by mere delivery to a bonafide transferee for valuable consideration without regard to the title of the parties who made the transfer.

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## 3.2 TYPES OF GOODS

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**Meaning of Goods:** "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 severed before sale or under the contract of sale." [Sec. 2 (7)]

Thus, the term 'goods' includes every kind of movable property except (i) actionable claims and (ii) money; but includes stocks and shares, growing crops, grass, etc. This definition is thus wider than that of the English Sale of Goods Act, for it also includes shares.

**"Movable property"** is defined in the General Clauses Act, 1897, **Section 3 (34)** as property of every description except immovable property.

**"Actionable Claim"** is defined in **Section 3** of the Transfer of Property Act, 1882. The expression used in the English Law is "chose in action". **Section 3** of the Transfer of Property Act defines an actionable claim as "a claim to any debt (except a secured debt) or to any beneficial interest., whether such claim or beneficial interest be existent, accruing, conditional or contingent" Actionable claim is thus something which a person cannot make use of or enjoy, but which can be recovered by him by means of a suit, a money debt, book debts, the interest of a buyer of goods in a contract of "for forward delivery" an option to repurchase property sold, (*Jaffer AU v. Budge & Budge Jute Mills*, 34, Cal. 219.) etc.

**Money** here means legal tender, of money, i.e., the recognised circulation in the country; but not old rare coins. Old coins which are in the nature of curios, e.g., a Jubilee five-pound gold piece, may well come within the definition of goods. So also, foreign money or currency, in a transaction of sale, the contract is between the goods and the money paid for them

The definition further suggests that the term 'Goods' includes stocks and shares, growing crops, grass and things attached to or forming part of land which are agreed to be severed from land before sale. Trees which are ordered to be severed before sale or under the contract of sale are goods. (Badri Prosed v. State of M.P., A.I.R. (1970) S.C. 706)

In other words, things attached to the earth are not movables, but growing crops which can be easily severed from the earth before sale and fruits and mangoes which can be restored from the trees, are included in the definition.

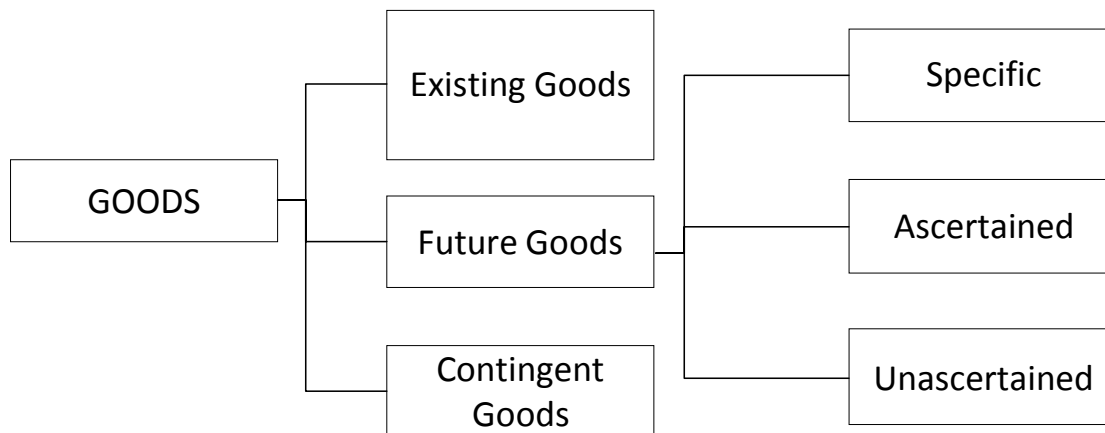
Patents, copyrights, goodwill, trade-marks, are all considered goods which can be the subject-matter of a contract. (CF) Hopper v. Gumm (1867)2 Ch.Ap. 282.)

Copyright in songs has been included in the definition of goods. (Ramiah Asari V. Chindambara Mudaliar (1920) 39 M.L.J. 341) A ship has also been considered to come within the definition of the word "goods". Similarly, water, gas and electricity are included in the definition though some writers doubt if they can be classed among 'goods.' (Rash Behari v. Emperor 1936) Cal. 753) Lottery Tickets are 'goods' and not actionable claims. (Harrison v. Luke(1945) 153 E.R. (423)

**(6) Price: "Price" means the money consideration for a sale of goods.[Sec. 2(10)]**

The 'price' of thing is its value as agreed upon between the parties, and expressed in terms of the currency of the country. No sale can take place without a price. It is this which differentiates a sale from barter or exchange where goods of one kind are given and goods of another variety are taken in return. (Harrison v. Luke (1945) 153 E.R. 423.) But it would appear that a sale may be made in consideration of receiving in return partly goods and partly money or either goods or money in the alternative, (South Australian Insurance Co. v. Randell (1869) 3.P.C. 101) Where there is no consideration given for parting with the goods it becomes a case of gift and the rules relating to sale of goods have no application at all.

**TYPES OF GOODS**





## SALES OF GOODS ACT, 1930 I & II

- **Existing Goods:** These are the goods which are owned or possessed by the seller at the time of sale. Only existing goods can be the subject of a sale. The existing goods may be-
  - (a) **Specific Goods:** Goods identified and agreed upon at the time of making of the contract of sale of goods.
  - (b) **Ascertained Goods:** Goods identified subsequent to the formation of the contract of sale. The terms ascertained and specific, are commonly used for same kind of goods.
  - (c) **Unascertained or generic goods:** Goods not identified or agreed upon at the time of making of the contract of sale. They are the goods defined for description only.  
**Example:** 'A' who wants to buy a television set goes to a showroom where four sets of Janta model of Oscar television are displayed. He sees the performance of a particular set, which he agrees to buy. The set so agreed to be bought is a *specific set*. If after having bought one set he marks a particular set, the set so marked becomes ascertained. Till this all is done all sets are unascertained.
- 2. **Future Goods:** Goods to be manufactured, produced or— acquired after making of the contract are called future goods.  
**Example:** 'A' contract, on 1<sup>st</sup> January, to sell B 50 shares in Reliance Ltd., to be delivered and paid for on the 1<sup>st</sup> March of the same year. At the time of making of the contract, A is not in possession of any shares. The contract is a contract for the sale of future goods.
- 3. **Contingent Goods:** Goods, the acquisition of which by the seller, depends upon an uncertain contingency are called 'contingent goods'. They are also a type of future goods.  
**Example:** 'A' agrees to sell 0 units of an article provided the ship which is bringing them, reasonable safely. This is an agreement for the sale of contingent goods.

## PERISHING OF GOODS

### Perishing of goods before making of the Contract (Sec.7)

Where there is a contract for the sale of specific goods, the contract is void if the goods without the knowledge of the seller have, at the time when the contract was made, perished or become so damaged as no longer to answer to their description in the contract.

#### Illustration:

**Facts:** 'A' agrees to sell to 'B' a certain horse.: It turns out that the horse was dead at the time of bargain, though neither party was aware of the fact. Discuss the validity of the contract.

**Solution:** The agreement is void. In case part of goods is perished, the following rule applies:

- (a) if contract is indivisible, it shall be void; and
- (b) if contract is divisible, it will not be void and the part available in good condition

must be accepted by the buyer

**Goods perishing before sale but after agreement to sell (Sec.8)**

Where there is a contract for the sale of specific goods, the contract is void if the goods without the knowledge of the seller have, at the time when the contract was made, perished or become so damaged as no longer to answer to their description in the contract.

**Illustration**

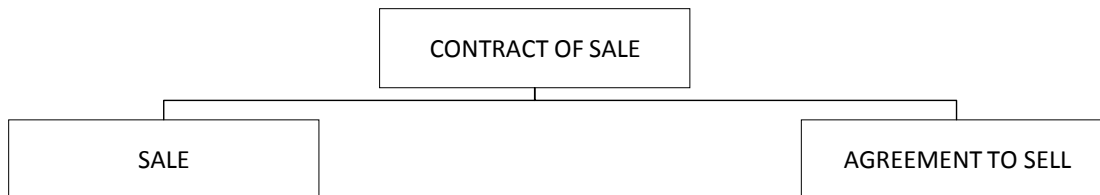
**Facts:** A buyer took a horse on a trial for 10 days on condition that if found suitable for his purpose the bargain would become absolute. The horse died on 5th day without any fault of either party. Discuss the position of both parties.

**Solution:** The contract, which was in the form of an agreement to sell, becomes void and the seller shall bear the loss.

**3.3 GENERAL PRINCIPLES**

**MEANING OF CONTRACT OF SALE**

- According to Section 4 of the Act, a contract of Sale means "a contract where the seller transfers or agrees to transfer the property in goods to the buyer for price"
- Contract of Sale may be of two types



**SALE**

- It is a contract where the ownership in the goods is transferred by seller to the buyer immediately at the conclusion contract

**EXAMPLE:** A sells his house to B for ₹ 10,00,000. It is a sale since the ownership of the house has been transferred from A to B.

**AGREEMENT TO SELL**

- It is a contract of sale where the transfer of property in goods is to take place at a future date or subject to some condition thereafter to be fulfilled.

**EXAMPLE:** A agreed to buy from B a certain quantity of nitrate of soda. The ship carrying the nitrate of soda was yet to arrive. This is 'an agreement to sale'. In this case, the ownership of nitrate of soda is to be transferred to A on the arrival of the ship containing the specified goods (i.e. nitrate of soda) **[Johnson V McDonald**

**SALES OF GOODS ACT, 1930 I & II**

(1842) 9 M &W 600, 60 RR 838]

**DISTINCTION BETWEEN SALE AND AGREEMENT TO SELL**

No.	BASIS	SALE	AGREEMENT TO SELL
1.	Transfer of Property	The property of goods passes from the seller to the buyer immediately. So, the seller is no more owner of the goods sold. It is an executed contract.	The transfer of property of the goods is to take place at a future time or subject to certain conditions to be fulfilled. It is an executor contract.
2.	Type of goods	A sale can only be in case of existing and specific goods only.	An agreement to sell is mostly in case of future and contingent goods (associated or dependent). Although it may refer to uncertain existing goods.
3.	Risk of loss	In a sale if the goods are destroyed, the loss falls on the buyer even though the goods are in the possession of the seller.	In an Agreement to Sell if the goods are destroyed the loss fallson the seller even though the goods are in the possession of the buyer.
4.	Consequen cesof the breach	In a sale the buyer fails to pay the price of goods (or) if there is a breach of contract by the buyer the seller can sue for the price even though the goods are still in his possession	If there is a breach of contract by the buyer the seller can only sue for the damages and not for the price.
5.	Right to re-sell	In a sale the seller cannot re-sell the goods.	The buyer who takes the goods for consideration and without notice of the prior agreement getshim a good 1 title. The original buyer can i only sue the seller for damages.
6.	General and particular property	The sale of contract plus conveyance and creates <i>Jus in rem</i> , i.e., it gives a right to the buyer to enjoy the goods as against the word and large including the seller.	An agreement to sell is merely a contract pure and simple and creates <i>Jus in personam</i> , i.e., it gives a right to the buyer against the seller to sue for the damages.
7.	Insolvency ofbuyer	In a sale if the buyer becomes insolvent before he pays for goods, the seller in the absence of the lien over the goods, must return them to the official receiver or assignee. He can only claim the ratable dividend for the price of the goods.	In an Agreement to Sell, If the buyer becomes insolvent and has not yet paid the price the seller is not bound to part with the goods until he is paid for.

8.	Insolvency of the seller	In a sale the seller becomes insolvent, the buyer being the owner is entitled to recover the goods from the official receiver of the assignee.	If the buyer who has paid the price, finds that the seller has become insolvent he can only claim a ratable dividend and not the goods because property in them has not yet passed to him.
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**3.4 ESSENTIALS OF CONTRACT OF SALE**

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- **Two parties:** There must be two parties—a buyer and a seller to constitute a contract of sale.
- **Goods:** Contract of sale relates to goods, i.e., movable property. Transaction involving purchase and sale of immovable property are out of the purview of the Sale of Goods Act.
- **Transfer of general property:** The object of the contract must be the transfer of general property as distinguished from the special property in the goods by one person to another. The term 'general property' refers to ownership of goods.
- **Price:** The consideration for the contract of sale called price must be money.
- **Essential elements of a valid contract:** All the essential elements of a valid contract must be present in the contract of sale.

**3.5 TRANSFER OF OWNERSHIP**

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- A contract of sale of goods involves transfer of ownership from the seller to the buyer. Transfer of ownership or property in goods is in fact the main object of making a contract of sale.

**IMPORTANCE OF TRANSFER OF OWNERSHIP**

It is important to know the precise moment of time at which the property in goods passes from the seller to the buyer for the following reasons:

1. **Risk prima facie passes with ownership:** In case of destruction of or damage to the goods, it is the owner who has to bear the loss because the general rule is 'res perit domino' risk follows ownership or whosoever is the owner must bear the loss. The payment of the price or possession of goods is immaterial.

**EXAMPLE:** 'A' contracts to purchase 30 tons of apple juice from 'B'. B crushes the apple, puts juice in casks and keeps them ready for delivery. A, however, delays to take the delivery and the juice goes putrid and has to be thrown away, A is liable to pay the price [Demby Hamilton & Co. Ltd. v. Barden (1949) All E R. 435]

2. **Action against third parties:** In case the goods have damaged by a third party, it is the only the owner who can take action against him.
3. **Insolvency of the seller or the buyer:** In the event of insolvency of either the seller or the buyer, the question whether the Official Receiver or Assignee can take over the goods or not depends on whether the property in the goods has passed from the seller to the buyer.

**RULES REGARDING TRANSFER OF OWNERSHIP**

- Goods must be ascertained
- Property passes when intended to pass.

**For Specific Goods (Sec.20 to 22)**

- **Passing of property at the time of contract (Sec.20)**

Where there is an unconditional contract for the sale of specific goods in a deliverable state, the property in the goods passes to the buyer when the contract is made.

Example: B offers A for his horse a sum of ₹. 1000. The horse is to be delivered to B on a fixed day and the price is to be paid on another fixed day. A accepts the offer. The horse becomes B's property as soon as the offer is accepted.

**Passing of property delayed beyond the date of the contract**

- **Goods not in deliverable state (sec.21)**

Where there is a contract for sale of specific goods not in a deliverable state, i.e., the seller has to do something to the goods to put them into the deliverable state, the property does not pass until such thing is done and the buyer has notice of it.

- **When the price of goods is to be ascertained by weighing (Sec.22)**

Where there is a contract for sale of specific goods in a deliverable state, but the seller is bound to weigh, measure, test or do some other act or thing with reference to the goods for the purpose of ascertaining the price, the property does not pass until such act or thing is done and the buyer has notice thereof.

- **For unascertained / 'future' goods Sec.23**

In the case of a contract for a sale of unascertained or future goods by description, property will pass from the seller to the buyer when the goods of the same description, in a deliverable state, are unconditionally appropriated to the contract by one

- **Goods sent on approval or 'sale or return' Sec.24**

When the goods are delivered to the buyer on 'approval' or on 'sale or return' basis, the property in the goods will pass from seller to the buyer, when any of the following conditions are satisfied.

- The buyer accepts the goods, or
- The buyer does something which is similar to his act of accepting the goods, e.g., pledges the goods or sells away the goods, or
- The buyer retains the goods without giving notice of rejection beyond the period fixed or reasonable period if no time is fixed.

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### 3.6 SALE BY NON-OWNERS

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**General Rule :** There is a general rule of law that *nemo dat quod non habet*, i.e., no one can give what he has not got. No one can convey to a transferee a better title than he himself has. This rule, which is also embodied in Sec. 27 of the sale of Goods Act, states that when goods are sold by a person who is not the owner thereof and who does not sell them under the authority or with the consent of the owner, the buyer shall acquire no better title to the goods than what the seller has. For example, if A steals an article and sells it to B, B does not become the owner of the goods. Only the owner can sell the goods and can pass a valid title to the buyer. In case, the seller has no title, the buyer gets none, in spite of the fact the buyer may have acted in good faith and may have paid the value for the goods. Thus, the mere fact of an innocent and bonafide purchaser from a person with no title is no answer to the claim of the true owner. This rule applies equally to movable or immovable goods.

This rule, however, is subject to the exceptions noted in Secs. 27 to 30 of this Act. The idea is to protect innocent purchasers for value from the persons who are in actual possession of the goods with the consent of the real owner. In each of these cases, a person who is not an owner, can still give a transferee a valid title to the goods:

#### 1. Estoppel:

Where the true owner of the goods by his conduct or by his words (acts or omissions) leads the buyer to believe that the seller was the owner of the goods or has the authority to sell and so induces the buyer to buy them in that belief, he shall thereafter be estopped from denying the fact of want of authority or title. (Sec. 27). The buyer in such a case gets a better title than that of the seller. The basis of this is the principle of personal estoppel.

**Example:** A tells B within the hearing of C that he is the owner of certain goods which, in fact, belonged to C. After some time B, buys that property from A. The title of B will be better than A, and C will be precluded from disputing A's title to the goods.

#### 2. Sale by a mercantile agent:

Sale of goods by a "mercantile agent" gives a good title to the purchaser even in cases where the agent acts beyond his authority, provided the following conditions are fulfilled:

- (i) if he is in possession of the goods or of the documents of title to the goods;
- (ii) if the sale is made by him when acting in the ordinary course of business as a mercantile agent; and
- (iii) if the buyer acts in good faith and has no notice of the fact that the seller had no authority to sell. (Sec. 27 proviso)

**[Mercantile Agent:** "Mercantile Agent" means an agent having in the customary course of business as such agent, authority either to sell goods or to consign goods for the purpose of sale, or to buy goods, or to raise money on the security of goods. [Sec.

2 (9)]

Example : A is manufacturing jewellery. B is a person whose business is to travel about the country selling jewellery. A delivers certain articles of jewellery to B upon specific understanding that they should remain the property of A until sold and paid for. B fraudulently pledges them. The pledge is held to be valid. B is a mercantile agent and as such has an ostensible authority to pledge the jewellery. (Weiner v. Haris (1910) 1 K.B. 285)

**3. Sale by one of several joint owners:** "If one of several joint owners of goods has the sole possession of the goods by permission of the co-owners, the property in the goods is transferred to any person who buys them of such joint owner in good faith and has not, at the time of the contract of sale, notice that the seller has no authority to sell" (Sec. 28)

Example: A, B and C own certain cattle in common. A is left by B and C in possession of a cow while he sells to D. D. purchases it bonafide. The property in the cow is transferred to D.

English law is different on this point. A sale by a co-owner without the consent of the other co-owners does not pass the property or title to the innocent buyer. The buyer in such cases, in England, will only get the title of that co-owner who has sold the goods.

**4. Sale of Goods obtained under Voidable Agreement:**

"When the seller of goods has obtained possession thereof under a contract voidable under section 19 or section 19-A of The Indian Contract Act, 1872, but the contract has not been rescinded at the time of the sale, the buyer acquires a good title to the goods, provided he buys them in good faith and without notice of the seller's defect of title." (Sec. 29) Example: A, by a misrepresentation, induces B to sell and deliver to him a horse. A sells the horse to C before B has rescinded the contract. The property in the horse is transferred to C.

It may be noted that the above section applies only when the goods are obtained under a voidable agreement and not under a void or illegal agreement. If a contract under which the seller obtains goods is void, then even innocent purchaser of the goods from such a seller acquires no title to the goods.

Example: If A represents to B that he is acting as agent for C. and B relying on that representation delivers goods to A as buyer, there is not a voidable contract between A and B, but no contract at all. No property passes to A, and he can neither make a valid sale nor a valid pledge. (Hardman v. Booth (1863) L J. Ex. 105)

**5. Sale by the seller in possession of goods after sale:**

"Where a person, having sold goods, continues or is in possession of the goods or of the documents of title to the goods, the delivery or transfer by that person or by a mercantile agent acting for him, of the goods or documents of title under any sale, pledge or other description thereof to any person receiving the same in good faith and without notice of the previous sale shall have the same effect as if the person making

the delivery or transfer were expressly authorised by the owner of the goods to make the same." [Section 30 (1)]

The possession under the section must be possession by the seller as seller. The original buyer in such cases can obtain damages from the seller but cannot recover the goods from the subsequent buyer.

Example: A sells goods to B. B for his own convenience leaves the goods with A. A fraudulently sells the goods to S, who buys them in good faith and without notice of the sale to

B.C gets a good title to the goods. The delivery of the goods by A to C has the same effect as if A was expressly authorised by B to deliver the goods.

'Document of title of goods' includes a bill of lading, dock-warrant warehouse-keeper's certificate, wharfinger's certificate, railway receipt, warrant or order for the delivery of goods and any other document used in the ordinary course of business as proof of the possession or control of goods, or authorising or purporting to authorise, either by endorsement or by delivery the possession of the document to transfer to receive goods thereby represented. [Sec. 2 (4)]

#### **6. Sale by Buyer in Possession After Sale:**

"Where a person, having bought or agreed to buy goods obtains, with the consent of the seller, possession of the goods or the documents of title to the goods, the delivery or transfer by that person or by a mercantile agent acting for him, of the goods or documents of title under any sale, pledge or other disposition thereof to any person receiving the same in good faith and without notice of any lien or other right of the original seller in respect of the goods shall have effect as if such lien or right did not exist." [Sec. 30(2)]

Examples:

- (i) Furniture was delivered to L on hire-purchase basis the ownership to pass on the payment of the last instalment. L sold the furniture to B before the payment of last instalment, B purchased the furniture bonafide. Held, B- having bought in good faith, had obtained a good title to the furniture. (Lee v. Butler (1893) 2. Q.B.318)
- (ii) A shipment of nuts were purchased by A from B and B sent to A, the bill of lading. A handed the said bill of lading to C, and then became insolvent. C in good faith pays the price. B attempted to stop the goods in transit, but C claimed them. Held, that B cannot stop the goods in transit as A could pass a good title to C. (Cahtn v. Pockett's ChannelCo. (1899) 1 Y.B. 643)

#### **7. Sale by an Unpaid Seller:**

Where, an unpaid seller who has exercised his right of lien or stoppage in transit re-sells the goods, the buyer acquires a good title to the goods as against the original buyer [Section 54(3)]



**8. Sale under the Provisions of Other Acts:**

- (i) Sale by an Official Receiver or Liquidator of the Company will give to the purchaser, a valid title.
- (ii) Purchaser of goods from a finder of goods shall be valid under certain circumstances.
- (iii) Sale by a pawnee under default of pawnor will give valid title to the purchaser.

**9. Sale in Market Overt:**

In England, when a person who buys goods in market overt, obtains a good title to the goods. 'Market Overt' means an open, public and legally constituted market' transacting business during specified hours. The buyer, thus, who purchases goods in market overt, will acquire a good title provided.

- (a) the goods are sold in accordance with the usage of the market; and
- (b) the buyer bought the goods in good faith and without notice of any defect or want of title on the part of the seller. In India, this exception is not recognised.

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**3.7 UNPAID SELLER AND HIS RIGHTS**

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**A Seller:** A person who sells the goods or agrees to sell the goods is called seller.

**B. Unpaid:** It means payment is not made or without payment. In simple words, 'unpaid seller' means a person who has sold the goods for a price but price has not been paid to him.

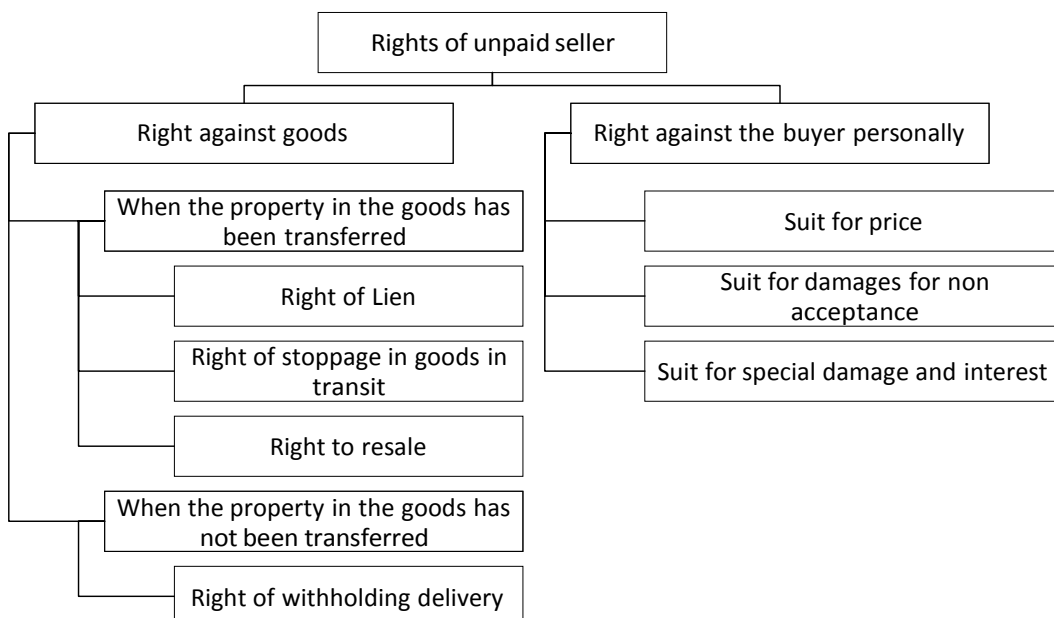
Sales act defines the "unpaid seller" in the following words:

**C. Unpaid Seller Is A Person:**

- i. To whom the whole price has not been paid or tendered.
- ii. And where a bill of exchange or other negotiable instruments has been accepted by him as a condition on which it was received has not been fulfilled by reason of dishonor of the instrument or otherwise.

**EXAMPLE:** Party A sells a car on cash basis to party B and the price has not been received yet.

**RIGHTS OF UNPAID SELLER**



- (a) **Where property in the goods has passed:**  
**The unpaid seller has, by implication of law, the following rights,**

notwithstanding that the property in goods may have passed to the buyer, namely:

- (a) **a lien on the goods for the price while he is in possession of them;**
- (b) **if the buyer becomes insolvent before payment, a right to stop the goods in transit after he has parted with the possession of them;**
- (c) **a right of re-sale (which implies that he is in possession.) as limited by this Act.:[Sec. 46 (1)]**

\*Q: Who is an unpaid seller? State the rights of an unpaid seller against the goods.

- (b) **Where property in the goods has not passed:**

"Where the property in goods has not passed to the buyer, the unpaid seller has, in addition to his other remedies, a right of withholding delivery similar to and co-extensive with his rights of lien and stoppage in transit where the property has passed to the buyer" [Sec. 46(2)]

**A) RIGHT OF LIEN: (SEES. 47-49)**

- (1) The unpaid seller of goods who is in possession of them is entitled to retain possession of them until payment or tender of the price in the following cases:
  - (a) Where the goods have been sold without any stipulation as to credit;
  - (b) Where the goods have been sold on credit, but the term of credit has expired;
  - (c) Where the buyer becomes insolvent. [Sec. 47(1)]
- (2) "The seller may exercise his right of lien notwithstanding that he is in possession of the goods as agent or bailee for the buyer." [Sec. 47(2)]

The lien extends only to the price. It does not extend to warehouse or other charges for keeping the goods, for they are kept against the buyer's will. For these, the seller has a personal remedy against the buyer.

**Termination of lien:**

The unpaid seller of goods loses his lien thereon—

- (a) When he 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
- (b) when the buyer or his agent lawfully obtains possession of the goods
  - (i) A sells to B a lawn-mower. A refuses to deliver it unless paid for. But on request from B, A lends it to him in order that B may cut the grass in the compound. A, thereby does not lose his lien. (See *Knights v. Wiffen* (1870) L.R.. 5 G.B. 660.)

- (c) **By waiver thereof. (S.49'(I))**

The lien may be waived expressly or by implication.

**SALES OF GOODS ACT, 1930 I & II**

**2. RIGHT OF STOPPAGE IN TRANSIT [Sec.50 to 52]**

It means stoppage of goods while they are in transit to take possession until the price is paid (sec.50-52)

- Unpaid seller can stop the goods in transit in the following cases.
  1. While the buyer becomes insolvent.
  2. While the goods are out of actual possession of seller, but have not reached buyer's possession, i.e., goods are in transit with carrier.
  3. The unpaid seller can stop the goods in transit only for payment of the price of the goods and not for any other charges.
- The unpaid seller cannot stop goods in transit in following cases.
  1. When the goods reach the destination
  2. While the buyer or his agent takes possession of delivery even if it is not reached destination,
  3. In case the carrier is agent of the buyer, the transit comes to an end the instance carrier receives the goods and seller cannot stop the transition.
  4. Carrier's wrongful refusal to deliver goods to the buyer

Example: A sells TV set to B. A delivers the TV to the carrier to carry it to B. Later on, A gets the news that B has become insolvent; A can stop delivery. Points of Difference\*

Aspect	Lien	Stoppage in transit
1. Essence	Its essence is to retain possession, i.e., the right of lien can only be exercised on goods which are in actual or constructive possession of the seller.	Its essence is to regain possession, i.e., the right of stoppage in transit can only be exercised when the possession is neither with the seller nor with the buyer but is with a middle-man.
2. Insolvency	The right can be exercised irrespective of whether the buyer is insolvent or not.	The right can be exercised only when the buyer is insolvent.
3. When lost ?	It is lost when the possession is lost.	It is lost when the buyer acquires the possession.
4. Possession	The right subsists so long as the seller holds the possession of the goods.	The right commences when the seller loses the possession of the goods and continues so long as the middleman continues to hold the possession.
5. Begins & Ends	When this right ends, the right of stoppage begins.	This right begins when the right of lien ends.

\*Q: Distinguish between lien and stoppage in transit

**3. Right of Resale (SEC. 54)**

Sec. 54 deals, principally with re-sale by an unpaid seller who has exercised

his right of lien, or has exercised the right of stoppage in transit and resumed possession of the goods. Thus, the unpaid seller can re-sell the goods under the following circumstances:

- (a) Where the goods are of a perishable nature; or
- (b) Where unpaid seller who has exercised his right of lien or stoppage in transit gives notice to the buyer of his intention to resell.
- (c) Where the seller expressly reserves a right of re-sale in case the buyer should make default. If the buyer makes a default the seller can resell the goods and the original contract of sale is thereby rescinded, but without prejudice to any claim which the seller may have for damages.

**If notice given:**

If the unpaid seller gives notice to the buyer of his intention to re-sell, the unpaid seller may, if the buyer does not within a reasonable time, pay or tender the price, re-sell the goods within reasonable time, and

- (i) recover from the original buyer damages for any loss occasioned by his breach of contract, and
- (ii) seller can retain the profits on re-sale.

However, it may be noted, that in case of perishable goods no notice is necessary.

**If notice not given:**

If such notice is not given, then

- (i) the unpaid seller shall not be entitled to recover such damages, and
- (ii) the buyer shall be entitled to the profit, if any on the re-sale.

When an unpaid seller who has exercised his right of lien or stoppage in transit, re-sells the goods, the buyer acquires a good title thereto as against the original buyer, even if no notice of the re-sale has been given to the original buyer.

**[5] RIGHTS OF UNPAID SELLER AGAINST THE BUYER PERSONALLY  
(Secs. 55. to 60)**

The rights discussed below are those rights which are available against the buyer personally. They have no connection with the rights discussed earlier, namely, with the rights of the seller against the goods.

**1. Suit for Price (Sec. 55)**

**(a) Where property has passed: (Sec. 55(1))**

"Where under a contract of sale the property in the goods has passed to the buyer and the buyer wrongfully neglects or refuses to pay for the goods according to the contract, the seller may sue him for the price of goods."

**(b) Where property has not passed:** (Sec. 55(2))

"Where under a contract of sale the price is payable on a certain day irrespective of delivery and the buyer wrongfully neglects or refuses to pay such price, the seller may sue him for the price, although the property in the goods has not passed and the goods have not been appropriated to the contract."

**2. Suit for Damages for Non-acceptance:** (Sec. 56)

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

**3. Repudiation of Contract before due date:** (Sec. 60)

Where the buyer repudiates the contract before the date of delivery, the seller may either treat the contract as subsisting and wait till the date of delivery, or he may treat the contract as rescinded and sue for damages for the breach.

**4. Suit for Interest**

The seller may recover interest or special damages in any case where by law interest or special damages may be recoverable, or to recover the money paid where the consideration for the payment of it has failed.

In the absence of a contract to the contrary, the Court may award interest at such rate as it thinks fit of the amount of the price to the seller in a suit by him for the amount of the price from the date of the tender of the goods or from the date on which the price was payable.

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**3.8 CARRIAGE BY SEA**

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In contract of sale including sea routes, certain special clauses and conditions are to be found. The most important of these contracts are:

- (1) F.O.B. Contracts.
- (2) C.I.F. Contracts.
- (3) Ex-ship Contracts.

**[1] F.O.B. CONTRACTS\***

F.O.B. stands for "free on board". The meaning of these words is, that the seller is to put the goods on board at his own expenses. As soon as the goods are put on board, the property and risk pass to the buyer. When once the goods are put on board the ship, they are at the risk of the buyer. The duty of the seller ends when he delivers the goods at his own expense to the ship at the port of shipment. Such delivery transfers the possession, property and risk to the buyer. But the subsequent expenses are to be borne by the buyer. The only thing that is to be noted is that the seller in such a case has to give such a notice to the buyer as may enable the buyer to insure. If the seller fails to do so, the goods are deemed to be at the seller's risk during the transit. **Position of:**

**(a) The seller:**

- (i) The seller must deliver the goods on board at his own expense. In the absence of any special agreement, the property and risk in the goods do not pass to the buyer until the goods are actually placed on board the ship concerned; (Colley v. Overseas Exporters Ltd. (1921) 3 K, B, 302)
- (ii) to deliver the goods on board a ship at the agreed place of shipment
- (iii) to put the goods on board a ship at his own expense.
- (iv) to give notice to the buyer of shipment in order to enable him to insure the goods during the sea-transit
- (v) to negotiate a reasonable bill of lading and forward it to the buyer

**(b) The buyer:**

- (i) The buyer must name the ship to which goods are to be delivered, or he must authorise the seller to select the ship. If, however, the seller is prevented from putting the goods on board the ship by the failure of the buyer to name a ship, the seller can sue for damages for non-acceptance and not the price. (Colley V. Overseas Exporters Ltd. (1921) 3, K. B. 320)
- (ii) The goods are at buyer's risk, subsequent to the goods being put on board the ship and he is therefore responsible for the freight and subsequent charges including insurance,
- (iii) If the goods are not up to contract quality, the buyer has the right to reject the goods provided he had no reasonable opportunity for examination of the goods until arrival at the port of delivery. (Bragg v. Villanova (1923) 40 T.L.R. 154.)

**[2] C.I.F CONTRACT\***

A contract on c.i.f. terms means a contract at a price to cover 'cost, insurance and freight.' In other words, if R of Ahmedabad agrees to sell 10,000 sq. metres cloth at ₹ 40/- per sq. metre, c.i.f. USA, the sum of ₹ 40/- covers:

- (i) the **price** of goods.
- (ii) the **cost** of insurance and
- (iii) the **freight** up to New York.

A contract of sale C.I.F. is defined as "a contract for the sale of goods to be carried by sea, which is performed by the delivery of certain documents representing the goods, called shipping documents." (Karberg Blythe [1916] 1 K.B. 495.)

One important feature of a C.I.F. contract is that the delivery of the goods is completed by the mere delivery of the complete set of shipping documents.

In the absence of any special provision to the contrary, the seller is bound under an obligation to do the following things. (Refer to the observations of Hamilton J. in Biddell Brothers V E. Cletneus Horst kand Co. (1911) 1 K. B. 214) (1)

- (1) To make out an invoice of the goods, sold (The invoice would normally show the cost of the goods)

## SALES OF GOODS ACT, 1930 I & II

- (2) To ship at the port of shipment, goods of the description contained in the contract
- (3) To procure a contract of affreightment, under which the goods will be delivered at the destination contemplated by the contract
- (4) To arrange for an insurance upon the terms current in the trade which will be available for the benefit of the buyer
- (5) To tender these documents, within reasonable time, after shipment, so that he may be able to obtain delivery of the goods, if they arrive, or recover for their loss if they are lost on the voyage (Narayan Swami v. Soundarajan [1958] A.Mad. 43.)

### [3] EX-SHIP CONTRACT\*

In case of ex-ship contract, the seller has the following duties. (Yang-tze Ins. Ass. v. Lukmanji (1918) A.C. 589.)

- (1) To cause delivery to be made to the buyer from a ship which has arrived at the port of delivery, and has reached a place therein which is usual for delivery of goods of the kind in question;
- (2) to pay the freight or otherwise to release the ship-owner's lien; and
- (3) to furnish the buyer with an effectual direction to the ship to deliver.

Since the goods are at the seller's risk during the voyage, there is no obligation on the part of the seller to insure the goods on behalf of the buyer.

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## 3.9 CONDITIONS AND WARRANTIES

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### MEANING OF CONDITION AND WARRANTY

A stipulation in a contract of sale with reference to goods which are the subject thereof may be a condition or a warranty [Sec. 12(1)].

- **Condition**

A condition is a stipulation essential to the main purpose of the contract, the breach of which gives rise to a right to treat the contract as repudiated. [Sec 12(2)]

- **Warranty**

A warranty is a stipulation collateral to the main purpose of the contract, breach of which gives rise to a claim for damages, but not a right to reject the goods and treat the contract as repudiated. [Sec 12(3)]

- **When condition to be treated as warranty [Sec.13]**

- Where a contract of sale is subject to any condition to be fulfilled by the seller, the buyer may waive the condition or elect to treat the breach of the condition as a breach of warranty, [section 13(1)].
- Where a contract of sale is not severable and the buyer has accepted the goods or part thereof, the breach of any condition to be fulfilled by the seller can only be treated as a breach of warranty, unless there is a term of the contract, express or

- implied, to that effect, [section 13(2)],  
 → Nothing in this section shall affect the case of any condition or warranty fulfillment of which is excused by law by reason of impossibility or otherwise, [section 13(3)].

**DIFFERENCE BETWEEN CONDITION AND WARRANTY**

<b>BASIS</b>	<b>CONDITION</b>	<b>WARRANTY</b>
1. Nature	Condition is of a fundamental nature.	Warranty is of a subsidiary of inferior character.
2. Value	Condition is essential to the main purpose of the contract. The main purpose of the contract cannot be fulfilled without the prior fulfillment of this stipulation.	Warranty is only collateral to in the main purpose of the contract. Fulfillment of the main purpose of the contract does not depend up on the fulfillment of the warranty.
3. Breach	If there is breach of condition, the aggrieved party can repudiate the contract.	In case of breach of warranty, the aggrieved party can claim damages only.
4. Treatment	A breach of condition may be treated as a breach of warranty. This would happen where the aggrieved party is contented with damages only.	A breach of warranty, however, cannot be treated as a breach of condition.
4. Example	X sells food-stuff to Y. The contract between X and Y states that the food to be sold should be fit for consumption and this is the essential term in the contract. So, if it contains any poisonous substance, Y is entitled to reject the food-stuff and to repudiate the contract This essential term is called a condition.	On the other hand, if the contract stipulates that the food-stuff should be packed in 1 kilo box but the seller packs it in half-kilo box, only an auxiliary or minor term of the contract is broken, Y may be able to claim compensation in respect of its breach, but not avoid the contract. Such an auxiliary term is called warranty.

**EXPRESS AND IMPLIED CONDITION AND WARRANTIES**

- Conditions and warranties may be express or implied.

**Express condition and warranties:**

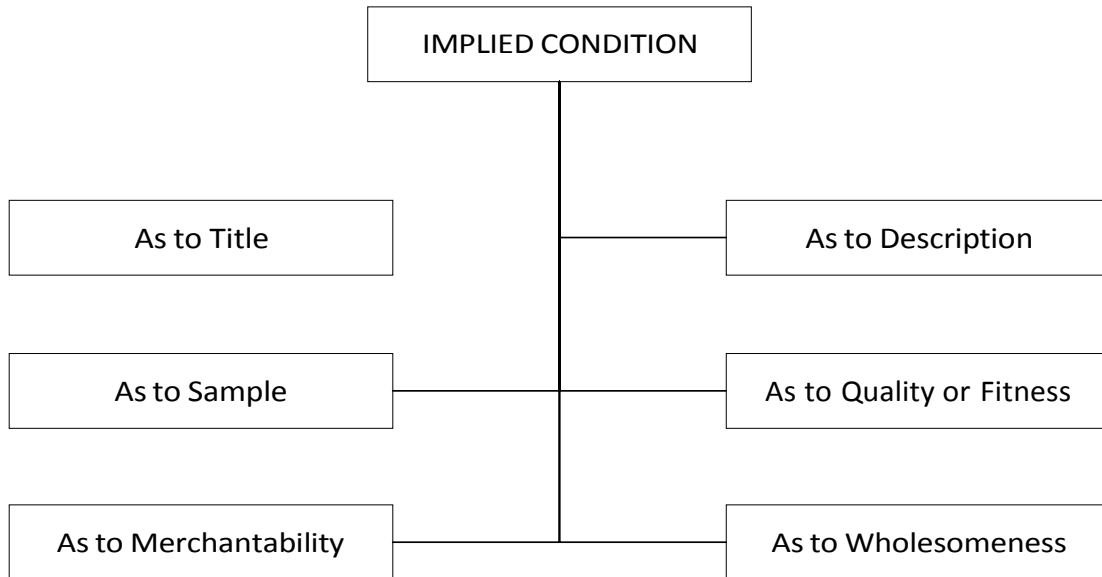
Express condition and warranties are those which have been expressly agreed upon by the parties at the time of contract of sale



**Implied condition and warranties:**

Implied condition and warranties are those which the law incorporates into the contract unless the parties stipulate to the contrary.

**IMPLIED CONDITION (Secs. 14 to 17)**



- **Condition Concerning Title** [Sec. 14(a)]  
In a contract of sale, unless the circumstances of the contract are such as to show a different intention, there is an implied condition on the part of the seller that -
  - a) In the case of a sale, he has a right to sell the goods, and
  - b) In the case of an agreement to sell, he will have a right to sell the goods at the time when the property is to pass.

Example: R bought a car from D and used it for 4 months. D had no title to the car and consequently R had to hand it over to the true owner. Held, R could recover the price paid [Rowland v Divall (1923) 2 K.B. 500]

- **Condition Concerning Description** (Sec. 15)
  - In sale by description there is an implied condition that the goods shall correspond with description.
  - This means "if you contract to sell peas, you cannot oblige the party to take beans."
  - Hence if the description of the article tendered is different then the buyer may not buy the goods.

Example: A wants to sell his typewriter. He says to B, intending a buyer who has not seen the machine, that it is a brand-new machine. B agrees to purchase it. On delivery B finds that the machine is old and repaired. B can repudiate the contract.

- **Condition Concerning Sample (Sec. 17)**

A contract of sale is a contract for sale by sample where there is a term in the contract, express or implied, to that effect.

In a sale by sample, the following are the implied conditions:

1. The bulk shall correspond with the sample in quality;
2. That the buyer shall have a reasonable opportunity of comparing the bulk with the sample; and
3. That the goods shall be free from any defects rendering them unmerchantable, which would not be apparent on

Example: Certain shoes were sold by sample for the French Army. The shoes were found to contain paper not discoverable by ordinary inspection. Held, the buyer was entitled to the refund of price plus damages.

- **Condition as to quality or fitness [Sec, 16 (1)]**

Normally, in a contract of sale there is no implied condition as to quality or fitness of the goods for a particular purpose. The buyer must examine the goods thoroughly before he buys them in order to satisfy himself.

Example: An order was placed for some lorries to be used "for heavy traffic in a hilly area". The lorries supplied ' were unfit and breakdown. There is a breach of condition as to fitness.

- **Condition Concerning Merchantability [Sec. 16(2)]**

→ Where goods are bought by description from a seller who deals in goods of that description there is an implied condition that the goods are of merchantable quality.

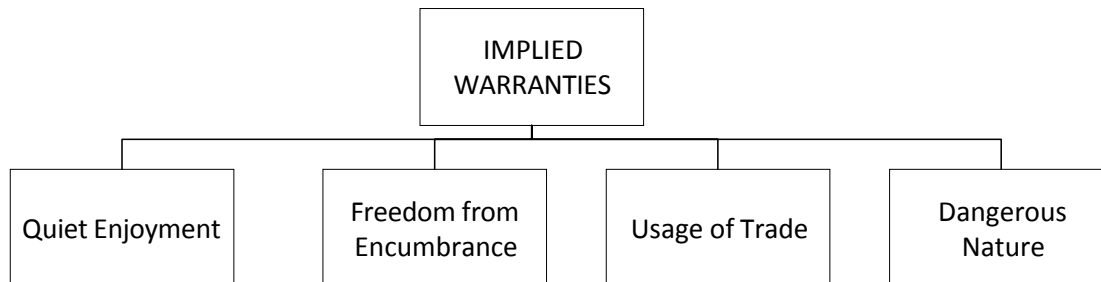
→ This means goods should be such that they are commercially saleable, as per the description by which they are known in the market at their full value.

- **Condition as to wholesomeness**

In the case of eatables and provisions, in addition to the implied condition as to merchantability, there is another implied condition that the good shall be wholesome.

Example: X purchased milk from Y 7a milk dealer. The milk contained typhoid germs. X's wife, on taking the milk, got infection and died. Held, X can be entitled for damages.

**IMPLIED WARRANTIES**



- **Warranty of quiet possession [Sec, 14(b)],**

In a contract of sale, unless there is a contrary intention, there is an implied warranty that the buyer shall have and enjoy quiet possession of the goods. If the buyer is in any way disturbed in the enjoyment of the goods in consequence of seller's defective title to sell, he can claim damages from the seller.

- **Warranty of freedom from encumbrances [Sec, 14(c)]**

The goods are not subject to any change or right in favour of a third party.

- **Warranty as to quality or fitness by usage of trade [Sec,16 (4)]**

An implied warranty as to quality or fitness for a particular purpose may be annexed by the usage of trade.

- **Warranty to disclose dangerous nature of goods**

Where a person sells goods, knowing that the goods are inherently dangerous or they are likely to be dangerous to the buyer and that the buyer is ignorant of the danger, he must warn the buyer of the probable danger, otherwise he will be liable in damages.

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### **3.10 DOCTRINE OF CAVEAT EMPTOR**

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- *Caveat Emptor* is a Latin phrase meaning 'let the buyer beware!'
- Let the buyer beware: the principle that the seller of a product cannot be held responsible for its quality unless it is guaranteed in a warranty.

For example, you buy a used car which you are told is in perfect condition, but it immediately breaks down OR you buy a house, but it has termites.

- Under this doctrine, the buyer takes the risk on an item he purchases and cannot complain of a defect.
- Unless there is either fraud or warranty (guarantee) by the seller, the rule applies to the sale of personal property.
- The buyer and seller have equal access to information about the item and the buyer is able to make personal inspection

Example: Suppose Ram bought 10 cows from a cattle broker. Out of those 10, 2 cows had defects. However, Ram did not know this because he didn't check all 10 cows though he paid for them. Guess what happened? The 2 infected cows died within three days of the purchase. Now, as there was no tacit condition that the cows would be in great health at the time of the sale, Ram cannot hold the cattle broker as responsible or having sold him those infected cows. It was Ram's basic duty to check the health of those cows and not expect the cattle broker to state all the defects.

- **Case study: Jones vs. Padgett**

The buyer bought cloth for making uniforms. However, the seller was not aware of the purpose of buying the cloth. Later, the buyer found that the cloth is not fit for making uniforms. It was, however, fit for other normal purposes. The seller was not found guilty as the principle of 'caveat emptor' applied in this case.

- **EXCEPTION OF CAVEAT EMPTOR**

→ **Implied condition as to quality or fitness**

Where the buyer has made known to the seller the purpose for which he requires the goods and depends on the seller's skill and judgment, there is an implied condition that the seller will supply the goods which are fit for that purpose. Section 16(1)

Example: A buys a black yarn from: B and finds that it has been damaged by white ants. The condition as to merchantable quality is broken and therefore, the doctrine of caveat emptor does not hold good.

→ **Sale of goods by description**

Where the goods are purchased by description from a seller, who deals in such class of goods, there will be an implied condition that the goods shall be of merchantable quality.

Example: English sainfoin seeds, duly exhibited by a sample, are sold. The bulk corresponds to the sample but the seeds supplied are giant sainfoins and not English sainfoin. There is a breach of condition as to description of goods. So the doctrine of caveat emptor is not applicable.

→ **Usage of trade**

An implied condition or warranty as to quality or fitness for a particular purpose may be annexed by the usage of trade and if the seller deviates from that, the rule of caveat emptor does not hold good.

Example: A dealer sells a refrigerator to Mohit. The refrigerator performs all other functions except making ice. This would amount to breach of an implied condition and thus the doctrine of caveat emptor will not work.

→ **Consent by fraud**

When the buyer relies on false representation of the seller and suffers damages, i.e., in a contract where the buyer's consent was obtained by the seller by fraud, the doctrine of caveat emptor will not hold good.

Example: A bought 3000 tins of preserved milk from the U.S.A. The tins were labeled in such a way that they infringed the Nestle's trademark. As a result, they were detained by the custom authorities. To get the clearance certificate from the customs, A had to remove the labels and sell them at a loss. Now, A can hold the seller responsible for fraud and claim damages.

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### 3.11 AUCTION OF SALE

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**Meaning:**

Sale of auction is the public sale where the goods are generally sold to the highest bidder

**Rules of Auction Sale:**

The law on auction sales is contained in Sec.64 of the Sale of Goods Act. According to it, in the case of a sale of auction the following rules apply:

- 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; and, until such announcement is made, any bidder may retract his bid;
- A right to bid may be reserved expressly by or on behalf of the seller and, where such right is expressly so reserved, but not otherwise, the seller or any one person on his behalf may, subject to the provisions hereinafter contained bid at the auction—
- Where the sale is not notified to be subject to a right to bid on behalf of the seller, it shall not be lawful for the seller to bid himself or to employ any person to bid at such sale, or for the auctioneer knowingly to take any bid from the seller or any such person; and any sale contravening this rule may be treated as fraudulent by the buyer;
- The sale may be notified to be subject to a reserved or upset price;
- If the seller makes use of pretended bidding to raise the price, the sale is voidable at the option of the buyer.

### CHECK YOUR PROGRESS

### LONG QUESTIONS

1. Discuss history of Sale of Goods Act **1930**
2. Distinguished between sale and agreement to sale
3. Distinguished between Condition and warranty
4. Discuss Inessentials of contract of sales
5. Discuss types of Goods
6. Write note on perishing goods
7. Write a note on transfer of ownership
8. Define unpaid seller? Discuss Rights of unpaid seller against goods
9. Define unpaid seller? Discuss Rights of unpaid seller against buyer.
10. Define condition. Discuss implied condition.
11. Define condition. Discuss implied warranty.
12. Write a note
  1. Caveat Emptor
  2. FOB Contract
  3. CIF contract
  4. Auction sale

**SHORT QUESTIONS**

1. Define goods
2. Define Buyer
3. Define seller
4. Define Condition
5. Define Warranty
6. Define Title
7. Define Title of Goods
8. Define price

**MULTIPLE CHOICE QUESTIONS**

**1. The Sale of Goods Act, 1930 applies to the whole of India except**

- (a) Jammu and Kashmir
- (b) Dadra and Nagar Haveli
- (c) Goa, Daman and Diu
- (d) All of above

**2. The Sale of Goods Act, 1930 came into force on**

- (a) 1st April, 1930
- (b) 1st May, 1930
- (c) 1st December, 1930
- (d) None

**3. The Sale of Goods Act, 1930 is based on**

- (a) the English Bills of Exchange Act, 1882
- (b) the Transfer of Property Act, 1882
- (c) the English Sale of Goods Act, 1893
- (d) the Indian Contract Act, 1872

**4. In Sale of Goods Act several provisions of the Indian Contract Act have been retained**

- (a) to meet the need of the buyers
- (b) to meet the need of the sellers
- (c) to meet the need of both the buyers and sellers
- (d) to meet special conditions existing in India regarding sale of goods

**5. The term 'buyer', under the Sale of Goods Act, 1930, has**

- (a) been defined under section 2(1)
- (b) been defined under section 2(2)
- (c) been defined under section 2(3)
- (d) not been defined.

**6. The term "goods" in the sale of goods means**

- (a) specific goods only
- (b) Assets
- (c) ownership

## SALES OF GOODS ACT, 1930 I & II

(d) subject matter.

**7. The term 'delivery' has been defined, in the Sale of Goods Act, 1930 under**

- (a) section 2(3)
- (b) section 2(2)
- (c) section 2(1)
- (d) section 2(4).

**8. Under section 2(2) of the Sale of Goods Act, 1930, 'delivery' means**

- (a) gratuitous transfer of possession from one person to another
- (b) involuntary transfer of possession from one person to another
- (c) voluntary transfer of possession from one person to another
- (d) transfer of possession irrespective of whether it is gratuitous, involuntary or voluntary, from one person to another.

**9. 'Delivery' within the meaning of section 2(1) of the Sale of Goods Act, 1930, can be**

- (a) actual
- (b) constructive
- (c) symbolic
- (d) either (a) or (b) or (c).

**10. Which of the following is an instance of constructive delivery of goods**

- (a) the transfer of bill of lading
- (b) attornment by a person in possession of the goods
- (c) both (a) and (b)
- (d) only (b) and not (a). A bill of lading is

**11. A bill of lading is**

- (a) a negotiable instrument like a bill of exchange
- (b) a negotiable instrument like a promissory note
- (c) either (a) or (b)
- (d) neither (a) nor (b)

**12. 'The documents of title to goods' in the Sale of Goods Act, 1930 have been described, under**

- (a) section 2(3)
- (b) section 2(4)
- (c) section 2(1)
- (d) section (2).

**13. Which of the following documents is a document of title to goods**

- (a) bill of exchange
- (b) promissory note
- (c) dock warrant
- (d) all the above.

**14. Which of the following documents is a document of title to 'goods' within the**

**meaning of section 2(4) of the Sale of Goods Act, 1930**

- (a) Warehouse keeper's certificate
- (b) Warfingler's certificate
- (c) both (a) and (b)
- (d) neither (a) nor (b).

**15. Under section 2(4) of the Sale of Goods Act, 1930, which of the following documents is not a document of title**

- (a) pucca delivery order enabling a person to obtain delivery on payment of price
- (b) mate's receipt
- (c) both (a) and (b)
- (d) neither (a) nor (b).

**16. 'Future goods' has been defined, in the Sale of Goods Act, 1930, under**

- (a) section 2(5)
- (b) section 2(6)
- (c) section 2(7)
- (d) section 2(8)

**17. Under section of the Sale of Goods Act, 1930 'future goods' means**

- (a) goods which are not yet in existence
- (b) unascertained goods
- (c) ascertained goods
- (d) specific goods

**18. The term 'goods' has been defined in the Sale of Goods Act, 1930, under**

- (a) section 2(5)
- (b) section 2(6)
- (c) section 2(7)
- (d) section (8)

**19. 'Goods' within the meaning of section 2(7) of the Sale of Goods Act, 1930 not includes**

- (a) actionable claim(s)
- (b) money
- (c) both (a) and (b)
- (d) neither (a) nor (b)

**20. 'Goods' within the meaning of section 2(7) of the Sale of Goods Act, 1930 includes**

- (a) actionable claim(s)
- (b) money
- (c) both (a) and (b)
- (d) neither (a) nor (b)



## SALES OF GOODS ACT, 1930 I & II

- 21. Section 2(7) of the Sale of Goods Act, 1930, the term 'goods' does not include**
- (a) stock and share
  - (b) growing crops
  - (c) grass
  - (d) neither (a) nor (b) nor (c)
- 22. Which of the following are 'goods' within the meaning of section 2(7) of the Sale of Goods Act, 1930**
- (a) things attached to land which are agreed to be severed before sale
  - (b) things forming part of the land agreed to be severed before sale
  - (c) both (a) and (b)
  - (d) neither (a) nor (b)
- 23. Transfer of actionable claim(s) is governed by**
- (a) The Transfer of Property Act, 1882
  - (b) The Sale of Goods Act, 1930
  - (c) The Indian Contract Act, 1872
  - (d) all the above
- 24. 'A person is said to be 'insolvent' who has ceased to pay his debts in the ordinary course of business, or cannot pay his debts as they become due whether he has committed an act of insolvency or not', is the definition of insolvency given in**
- (a) The Indian Partnership Act, 1932
  - (b) The Sale of Goods Act, 1930
  - (c) The Indian Contract Act, 1872
  - (d) all the above
- 25. Who is 'insolvent', has been stated in the Sale of Goods Act, 1930, under**
- (a) section 2(6)
  - (b) section 2(7)
  - (c) section 2(8)
  - (d) section 2(9)
- 26. The Sale of Goods Act, 1930**
- (a) does not define the term mercantile agent defines the term mercantile agent under section 2(9)
  - (b) defines the term mercantile agent under section 2(10)
  - (c) defines the term mercantile agent under section 3
- 27. The question of the insolvency of a buyer, under the Sale of Goods Act, 1930, is of importance in connection with**
- (a) the seller's lien on the goods
  - (b) the right of stoppage in transit
  - (c) both (a) and (b)
  - (d) only (a) and not (b)

**28. "Mercantile agent" means the person**

- (a) who sell goods, or consigns for the purpose of sell, or buy goods or raise money on securityof goods
- (b) who only sell or purchase
- (c) who only consign goods
- (d) who only transfer goods

**29. 'Price' under section 2(10) of the Sale of Goods Act, 1930, means**

- (a) the money consideration
- (b) the consideration given in the form of goods
- (c) partly money consideration and pa; consideration in goods
- (d) either (a) or (b) or (c)

**30. The term 'property' has been defined, in the Sale of Goods Act, 1930 under**

- (a) section 2(9)
- (b) section 2(10)
- (c) section 2(11)
- (d) section 2(12)**Answers**

1A	2D	3D	4D	5 A	6A	7 B	8 C	9 D	10 A
11 B	12 B	13 C	14 C	15 A	16 B	17 A	18 C	19 B	20 A
21 D	22 C	23 B	24 B	25 C	26 B	27C	28A	29B	30 C

- 4.0 INTRODUCTION**
  - 4.1 DEFINITION OF PARTNERSHIP**
  - 4.2 PARTNER AND FIRM**
  - 4.3 ESSENTIAL ELEMENTS OF PARTNERSHIP**
  - 4.4 NATURE AND TYPES OF PARTNERS**
  - 4.5 REGISTRATION OF FIRM**
  - 4.6 THE CONSTITUTION OF THE FIRM (SECTION 17)**
  - 4.7 RELATION OF PARTNERS TO THIRD PARTIES (SEC. 18 TO 30)**
  - 4.8 LEGAL CONSEQUENCES OF PARTNER COMING IN AND GOING OUT(SECTIONS 31 - 38)**
  - 4.9 DISSOLUTION OF PARTNERSHIP**
  - 4.10 DISSOLUTION OF FIRM**
  - 4.11 NATURE OF LIMITED LIABILITY PARTNERSHIP**
  - 4.12 EXTENT AND LIMITATION OF LIABILITY OF LIMITED LIABILITYPARTNERSHIP AND PARTNERS**
  - 4.13 CONVERSION INTO LIMITED LIABILITY PARTNERSHIP**
  - 4.14 WINDING UP AND DISSOLUTION:**
- CHECK YOUR PORGRESS**

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#### **4.0 INTRODUCTION**

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One of the forms in which business can be carried on is partnership, where two or more persons join to form a partnership and run the business. In order to govern and guide partnership, the Indian Partnership Act, 1932, was enacted. In human relations, often misunderstandings crop up. If any misunderstanding crops up in a partnership amongst its partners, the continuity of the partnership may become doubtful. Since, public at large would be dealing with the partnership as customers, suppliers, creditors, lenders, employees or in any other capacity, it is also very important for them to know the legal consequences of their transactions and other actions in relation with the partnership where no one person is the owner of the business and, therefore, exclusively responsible.

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

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#### **4.1 Definition of Partnership**

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Partnership is the relation between persons who have agreed to share the profits of a business carried on by all or any one of them acting for all (Section 4). It, therefore, follows that a partnership consists of three essential elements:

It must be a result of an agreement between two or more persons.

The agreement must be to share the profits of the business.

The business must be carried on by all or any of them acting for all. All these essentials must coexist before a partnership can come into existence.

**Example:** A manager, as a part of his remuneration, may be given a share in profits of the business. He does not thereby become partner.

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## **4.2 PARTNER & FIRM:**

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Persons who have entered into partnership with one another are called individually 'partners' and collectively 'a firm', and the name under which their business is carried on is called the 'firm name'.

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## **4.3 ESSENTIAL ELEMENTS OF PARTNERSHIP**

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

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

Thus, essential elements of relationship of partnership are:

### **1. There must be two or more persons:**

- I. There must be at least two persons to form a partnership. Maximum number of partners, partnership act is silent. But Section 464 Of The Companies Act 2013 specifies it as 50. If number of partners fall below it ceases to be partnership. If it goes beyond 50, it will become an illegal association.
- II. The persons can be natural or artificial. Hence 2 companies can be partners. But a firm cannot enter into a contract for partnership though their partners can become partners.

All such persons must be competent to contract. According to Indian Contract Act every person except the following:

- (i) Minor
  - (ii) Person of unsound mind
2. Person disqualified by any law to which they are subject (alien, insolvents, etc.)
  3. **There must be an agreement**
    - I. A partnership arises only as a result of an agreement. Such an agreement may be express or implied. Implied in the sense that it may be a voluntary act by the persons. Agreement can be oral or in writing but partnership deed must be in writing
    - II. Partnership is thus created by contract; it does not arise by operation of law or from status
    - III. Agreement must be valid

**INDIAN PARTNERSHIP ACT, 1932  
& THE LIMITED LIABILITY PARTNERSHIP ACT, 2008**

Partnership agreement like any other contract, so it must satisfy all the essentials of a valid contract. In other words, the parties must be 'competent', i.e., capable of entering into an agreement, their consent must be free and there should be a lawful consideration and object.

**4. There must be a business:**

- I. The existence of a business is essential in a partnership. 'Business' includes every trade, occupation and profession. If two or more persons join together to form a 'dramatic club' it is not a partnership because there is no business in this case. Similarly, if A and B are co-owners of a building and let it to a tenant for rent and divide the net rents between themselves. A and B are not partners because letting a house is not a business. But if A and B agree to convert the building into a hotel and to share the profits equally, there is a 'business' here and hence A and B are partners in respect of such business.
- II. The business must be lawful.
- III. The business may consist of a single adventure or a single undertaking. Section 8 of the Indian Partnership Act provides:

"A person may become a partner with another person in particular adventures or undertakings."

Example: Two solicitors are engaged for a single case and they agree to share the profits. They would be partners.

**5. Sharing of profits**

- I. The element draws out the most essential feature and basis of partnership. The object of partnership undoubtedly is to earn 'profit'.
- II. Sharing of losses

The agreement to share profit is essential, but it should be noted that an agreement to share the losses is not essential. Where nothing is said as to the sharing of losses, it is implied in a partnership deed.

It may, however, be agreed that as between the partners anyone or more of them shall not be liable for losses. But the reverse is not just possible. So, where persons agree to share the profits of a money-lending business, they become partners,

but where one of them, so called partner is not to receive profits, he is not a partner. Example: A and B agree to work together as carpenters, but that A shall receive all profits and shall pay wages to B, A and B are not partners. When profit is made, it must be distributed (in absence of any agreement) equally, or in the agreed ratio.

- III. A person, who receives the profits of a business, is not necessarily a partner. The persons who receive the profits but are not the partners are referred as under:

**1. Retired partner**

After retirement if the settlement of accounts is not done then the retired partner may get share in profits. But he is not treated as partner.

**2. Money-lenders receiving profits**

A money-lender is a person who lends money on interest. Sometimes, a money-lender receives, in addition to or in place of his interest, a portion of the profits of a business. In such cases, he cannot be said to be a partner only on the ground that he receives the profits of the business.

**3. Employee or agent receiving profits** Sometimes, an employee or an agent of a business agrees to receive, in addition to or in place of his regular remuneration, a portion of the profits of the business. In such cases, he cannot be said to be a partner only on the ground that he receives the profits of the business.

**4. Widow or child of a deceased partner** Sometimes, the widow or a child of deceased partner receives a portion of profits as annuity. In such cases, they cannot be said to be the partners of the firm only on the ground that they receive the profits of the business.

**5. Seller of goodwill**

Sometimes, a person who sells his business along with its goodwill, is given a share in the profits of the business he has sold. In such cases, that person does not become a partner in the business only on the ground that he receives the profits of the business.

**6. Minor:**

Minor receives share in profits but is not considered as partner.

IV. Just because a person is sharing profits, he is not a partner. But if a person is a partner, he will definitely get share in profits.

**5. Agency**

I. This last element is most crucial of partnership. The business of a firm is 'carried on by all or by anyone of them acting for all'. The underlying and fundamental principle herein which constitutes partnership is the idea of 'agency'. The other partners are bound by the acts of one of them only on the principle of agency. This is the cardinal principle of partnership law.

II. It means every partner is a Agent of the firm Principal for other partners acts That is to say, each partner is an agent binding the other partners who are his principals and each partner is again a principal, who in turn, is bound by the acts of the other partners. An act of one partner in the course of business of the firm is in fact an act of all partners.

**Example:**

A, B and C are partners in a business. D is an outsider, who deals with the firm through A. Between A and D, A is the principal. But between A, B and C, A is the agent of B and C. As such A, B and C can all sue D. D can also sue A, B and C. Furthermore, A is accountable to B and C because he is, in this transaction, an agent of B and C.

#### **4.4 NATURE AND TYPES OF PARTNERS**

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Partners can be classified as shown below:

##### **1. Active/Actual Partner**

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

##### **2. Sleeping or Dormant Partner**

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

He is liable for acts of firm.

##### **3. Nominal Partner**

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

##### **4. Partner for profits only**

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

##### **5. Sub-Partner**

- ❖ When a partner agrees to share his profits divided from the firm with a third person, that third person is known as 'sub-partner'. Such a sub-partner is in no way connected with the firm.
- ❖ He cannot represent the firm and bind the firm by his acts. He has no right against the firm nor is he liable for the acts of the firm.

##### **6. Partner by Holding Out or by Estoppel**

1. To hold a person liable as a partner by holding out, it is necessary to establish the following: He represented himself or knowingly permitted

himself to be represented as a partner.

2. Such representation occurred by words spoken or written or by conduct.
3. The other party on the faith of that representation gave credit to the firm.
- ❖ Once he poses himself as a partner, though he is not a partner, he is estopped from saying that he is not a partner in a firm.

❖ **Example:**

X carried on business as RS. & Co. employed a person named RS. to act as manager of the business. It was held that RS. is a partner by the principal of estoppel.

**7. Incoming Partner:**

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

**8. Outgoing Partner:**

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

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**4.5 Registration of Firm**

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

**Procedure:**

1. **Step 1-** Obtain a statement in the form from the office of the Registrar.
2. **Step 2-** State the following information:
  - Name of the firm
  - Principal place of the firm
  - Name of the other places where the firm carries its business
  - Date when each partner joined
  - Name in full and permanent address of each partner
  - Duration of the firm.
3. **Step 3-** Get the statement of duly verified and signed by all the partners or their agents.
4. **Step 4-** File the statement along with prescribed fees
5. **Step 5-** Obtain a certificate or registration from the Registrar.

The registration becomes effective from date of filing of duly signed and verified documents and not from the date of issue since the act of the Registrar in recording an entry of the statement in the firm is only a clerical act.

**Consequences of non-registration:**

1. **The partners cannot file a suit against the firm or other partners:** A partner of an unregistered firm cannot file a suit against the firm or his



**INDIAN PARTNERSHIP ACT, 1932  
& THE LIMITED LIABILITY PARTNERSHIP ACT, 2008**

other present or past partners, for the enforcement of any right arising from a contract or conferred by the Indian Partnership Act. However, this disability may be removed by getting the firm registered before filing the suit.

**2. The firm cannot file a suit against third parties:**

An unregistered firm cannot file a suit against any third party for the enforcement of any right arising from some contract.

This disability of an unregistered firm can be removed by getting the firm registered before filing the suit.

**3. The partner of the firm cannot claim a set-off:**

The term 'set-off' means the adjustment of debts by one party due to him from the other party who files a suit against him. The partners of an unregistered firm or the firm itself cannot claim a set-off, in a suit filed against them or the firm. But the right of set-off is not affected if the claim for setoff does not exceed 359B 100 in value.

**Following are not the disabilities of an unregistered firm:**

4. The third party can file a suit against the firm whether the firm is registered or not. And the firm cannot take the plea of its non-registration.
5. The partners of an unregistered firm can file a suit for the enforcement of the three things, namely,
  - (a) for the dissolution of the firm
  - (b) for the accounts of the dissolved firm, and
  - (c) for realization of the property of the dissolved firm.The right of an unregistered firm to enforce a right which arises otherwise than out of a contract. As a matter of fact, firm's disability is to enforce the contractual rights, and not the others.

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**4.6 THE CONSTITUTION OF THE FIRM (SECTION 17)**

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Before going into rights and duties, we should first know how a change may take place in the constitution of the firm. It may occur in one of the four ways, namely,

- (i) Where a new partner or partners come in,
- (ii) Where some partner or partners go out, i.e., by death or retirement,
- (iii) Where the partnership concerned carries on business other than the business for which it was originally formed,
- (iv) Where the partnership business is carried on after the expiry of the term fixed for the purpose.

➤ **Section 17 lays down the rule:**

- (a) Where a change occurs in the constitution of the firm in any of the first three ways mentioned above, the mutual rights and duties of the partners in the reconstituted firm remain the same as they were before the change as may be.
- (b) Where a firm constituted for a fixed term continues to carry on the business after the expiry of the term, the mutual rights and duties of the partners remain

the same as they were before the expiry, so far as they may be consistent with the incidents of partnership at will. Some provisions have been held to be inconsistent with the incidents of partnership at will, e.g., the provision in the deed that a partner desiring to retire shall give notice of his intention of the same at a certain time before hand.

- (c) Where the firm constituted to carry out one or more ventures or undertakings, carries out other ventures or undertakings, the mutual rights and duties of the partners in respect of the other adventures of the undertaking are the same as of those in respect of the original adventures.

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#### **4.7 RELATION OF PARTNERS TO THIRD PARTIES (SEC. 18 TO 30): Partners as agents of the firm:**

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You may recall that a partnership is the relationship between the partners who have agreed to share the profits of the business carried on by all or any of them acting for all (Section 4). This definition suggests that any of the partners can be the agent of the others. Section 18 clarifies this position by providing that, subject to the provisions of the Act, a partner is the agent of the firm for the purpose of the business of the firm. The partner indeed virtually embraces the character of both a principal and an agent. So far as he acts for himself and in his own interest in the common concern of the partnership, he may properly be deemed a principal: and as far as he acts for his partners, he may properly be deemed an agent. The principal distinction between him and a mere agent is that he has a community of interest with other partners in the whole property and business and liabilities of partnership, whereas an agent as such has no interest in either. The rule that a partner is the agent of the firm for the purpose of the business of the firm cannot be applied to all transactions and dealings between the partners themselves. It is applicable only to the act done by partners for the purpose of the business of the firm.

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#### **4.8 LEGAL CONSEQUENCES OF PARTNER COMING IN AND GOING OUT (SECTIONS 31 - 38)**

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Any change in the relation of partners will result in reconstitution of the partnership firm. Thus, on admission of a new partner or retirement of a partner or expulsion of the partner, or on insolvency of a partner, etc. a firm will be reconstituted:

##### **Introduction of new partner (Section 31):**

As we have studied earlier, subject to a contract between partners and to the provisions regarding minors in a firm, no new partners can be introduced into a firm without the consent of all the existing partners.

**Rights and liabilities of new partner:** The liabilities of the new partner ordinarily commence from the date when he is admitted as a partner, unless he agrees to be liable for obligations incurred by the firm prior to the date. The new firm, including the new partner who joins it, may agree to assume liability for the existing debts of the old firm, and creditors may agree to accept the new firm as their debtor and discharge the old partners. The creditor's consent is necessary in every case to make the transaction operative. Novation is the technical term in a contract for substituted liability, of course, not confined only to case of

**INDIAN PARTNERSHIP ACT, 1932  
& THE LIMITED LIABILITY PARTNERSHIP ACT, 2008**

partnership.

But a mere agreement amongst partners cannot operate as Novation. Thus, an agreement between the partners and the incoming partner that he shall be liable for existing debts will not ipso facto give creditors of the firm any right against him.

**In case of partnership of two partners:** This section does not apply to a partnership of two partners which is automatically dissolved by the death of one of them. In this event there is no partnership at all for any new partner to be introduced into it without the consent of others.

**Retirement of a partner (Section 32):**

**A partner may retire:**

- (i) with the consent of all the other partners;
- (ii) by virtue of an express agreement between the partners; or
- (iii) in the case of a partnership at will, by giving notice in writing to all other partners of his intention to retire.

Such a partner, however, continues to be liable to the third party for acts of the firm after his retirement until public notice of his retirement has been given either by himself or by other partners. But the retired partner will not be liable to any third party if the latter deals with the firm without knowing that the former was partner [Sub-Sections (3) and (4)].

**Right of outgoing partners:**

- (I) An outgoing partner may carry on business competing with that of the firm and he may advertise such business, but subject to contract to the contrary, he cannot use the name of the firm or represent himself as carrying on the business of the firm or solicit customers of the firm he has left [Section 36(1)]. Although this provision has imposed some restrictions on an outgoing partner, it effectively permits him to carry on a business competing with that of the firm. However, the partner may agree with his partners that on his ceasing to be so, he will not carry on a business similar to that of the firm within a specified period or within specified local limits. Such an agreement will not be in restraint of trade if the restraint is reasonable [Section 36(2)]. A similar rule applies to such an agreement of sale of the firm's goodwill [Section 53(3)].
- (II) (A) On the retirement of a partner, he has the right to receive his share of the property of the firm, including goodwill. It has been held that in the absence of evidence of any uniform usage to the contrary, the assets (property) should be taken at their fair value to the firm at the date of the account and not at their value as appearing in the partnership.
- (B) An outgoing partner, where the continuing partners carry on business of the firm with the property of the firm without any final settlement of accounts with him, is entitled to claim from the firm such share of the profits made by the firm, since he ceased to a partner, as attributable to the use of his share of the property of the firm. In the alternative, he can claim interest at the rate of 6% per annum on the amount of his share in firm's property (Section 37).

(III) However, if by a contract between the partners, an option has been given to the surviving or continuing partners to purchase the interest of the outgoing partner and the option is duly exercised, the outgoing partner or his estate will not be entitled to any further share of the profits. If on the other hand, any partner who assumes to act in exercise of the option, does not in all material respects comply with the terms thereof, then he would be liable to account under the provisions contained in Para (a) above (Proviso to Section 37).

**Liabilities of an outgoing partner:**

As we have already stated earlier, a retiring partner continues to be liable to third party for acts of the firm after his retirement until public notice of his retirement has been given either by himself or by any other partner. But the retired partner will not be liable to any third party if the latter deals with the firm without knowing that the former was partner [Sections 32 (3) and (4)].

The liability of a retired partner to the third parties continues until a public notice of his retirement has been given. As regards the liability for acts of the firm done before his retirement, the retiring partner remains liable for the same, unless there is an agreement made by him with the third party concerned and the partners of the reconstituted firm. Such an agreement may be implied by a course of dealings between the third party and the reconstituted firm after he had knowledge of the retirement [Section 32 (2)].

If the partnership is at will, the partner by giving notice in writing to all the other partners of his intention to retire will be deemed to be relieved as a partner without giving a public notice to this effect.

**Expulsion of a partner (Section 33):** A partner may not be expelled from a firm by a majority of partners except in exercise, in good faith, of powers conferred by contract between the partners. It is, thus, essential that:

- (iv) the power of expulsion must have existed in a contract between the partners;
- (v) the power has been exercised by a majority of the partners; and it has been exercised in good faith. If all these conditions are not present, the expulsion is not deemed to be in bona fide interest of the business of the firm.

**The test of good faith as required under Section 33(1) includes three things:**

- (a) that the expulsion must be in the interest of the partnership.
- (b) that the partner to be expelled is served with a notice.
- (c) that he is given an opportunity of being heard.

If a partner is otherwise expelled, the expulsion is null and void. The only remedy, when a partner misconducts in the business of the firm, is to seek judicial dissolution. You should also note that under the Act, the expulsion of partners does not necessarily result in dissolution of the firm. The invalid expulsion of a partner does not put an end to the partnership even if the partnership is at will and it will be deemed to continue as before.

**Example:** A, B and C are partners in a Partnership firm. They were carrying their business successfully for the past several years. Spouses of A and B fought in a ladies club on their personal issue and A's wife was hurt badly. A got angry on the incident and he convinced C to expel B from their partnership firm. B was expelled

**INDIAN PARTNERSHIP ACT, 1932  
&THE LIMITED LIABILITY PARTNERSHIP ACT, 2008**

from partnership without any notice from A and B. Considering the provisions of Indian Partnership Act, 1932 state whether they can expel a partner from the firm. A partner may not be expelled from a firm by a majority of partners except in exercise, in good faith, of powers conferred by contract between the partners. It is, thus, essential that:

- (I) the power of expulsion must have existed in a contract between the partners;
- (II) the power has been exercised by a majority of the partners; and it has been exercised in good faith. If all these conditions are not present, the expulsion is not deemed to be in bona fide interest of the business of the firm.

The test of good faith as required under Section 33(1), Indian Partnership Act, 1932 includes three things:

- (a) that the expulsion must be in the interest of the partnership.
- (b) that the partner to expelled is served with a notice.
- (c) that he is given an opportunity of being heard.

If a partner is otherwise expelled, the expulsion is null and void. Therefore, expulsion of Partner B is not valid.

In this context, you should also remember that provisions of Sections 32 (2), (3) and (4) which we have just discussed, will be equally applicable to an expelled partner as if he was a retired partner.

**Insolvency of a partner (Section 34):** When a partner in a firm is adjudicated an insolvent, he ceases to be a partner on the date of the order of adjudication whether or not the firm is thereby dissolved. His estate (which thereupon vests in the official assignee) ceases to be liable for any act of the firm done after the date of the order, and the firm also is not liable for any act of such a partner after such date (whether or not under a contract between the partners the firm is dissolved by such adjudication).

**Effects of insolvency:**

- (a) The insolvent partner cannot be continued as a partner.
- (b) He will be ceased to be a partner from the very date on which the order of adjudication is made.
- (c) The estate of the insolvent partner is not liable for the acts of the firm done after the date of order of adjudication.
- (d) The firm is also not liable for any act of the insolvent partner after the date of the order of adjudication,
- (e) Ordinarily but not invariably, the insolvency of a partner results in dissolution of a firm; but the partners are competent to agree among themselves that the adjudication of a partner as an insolvent will not give rise to dissolution of the firm.

**Death of a partner (Section 35):**

Where under the contract a firm is not dissolved by the death of a partner, the estate of the deceased partner is not liable for act of the firm after his death.

Ordinarily, the effect of the death of a partner is the dissolution of the partnership, but the rule in regard to the dissolution of the partnership, by death of partner is subject to a contract between the parties and the partners are competent to agree that the death of one will not have the effect of dissolving the partnership as regards the surviving partners unless the firm consists of only two partners. In order that the estate of the deceased partner may be absolved from liability for the future obligations of the firm, it is not necessary to give any notice either to the public or the persons having dealings with the firm.

In relation to Section 35, let us consider a concrete case. X was a partner in a firm. The firm ordered goods in X's lifetime; but the delivery of the goods was made after X's death. In such a case, X's estate would not be liable for the debt; a creditor can have only a personal decree against the surviving partners and a decree against the partnership assets in the hands of those partners. A suit for goods sold and delivered would not lie against the representatives of the deceased partner. This is because there was no debt due in respect of the goods in X's life time. Revocation of continuing guarantee by change in the firm (Section 38):

Section 38 of the Indian Partnership Act provides that a continuing guarantee given to a firm or to third party in respect of the transaction of a firm is, in the absence of an agreement to the contrary, revoked as to future transactions from the date of any change in the constitution of the firm. You should note that the above rule is subject to an agreement to the contrary. The agreement, if any, to the contrary required to displace the effect of Section 38, must be clear.

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#### **4.9 DISSOLUTION OF PARTNERSHIP:**

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The term 'dissolution of partnership' may be defined as a change in the relations of partners, and not the extinction of relationship. In this case, the firm as a whole is not closed down. But only the relations between some of the partners come to an end, and the remaining partners continue to carry on the business of the firm. Thus, the 'dissolution of firm' is different from 'dissolution of partnership.'

Example:

A, B and C were partners in a firm. A retires. Only the partnership between A, B and C is dissolved and a new partnership between B and C comes into existence. The new firm is called the 'reconstituted firm'. Thus, only the relations between the partners are changed on A's retirement.

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#### **4.10 DISSOLUTION OF FIRM:**

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When the firm as a whole is closed down, it is called the dissolution of the firm. Thus, in case of dissolution of the firm, the business of the firm is stopped and the relations between all the partners come to an end.

#### **(A) DISSOLUTION WITHOUT THE INTERVENTION OF COURT**

A firm may be dissolved without the intervention of the court i.e., without going to the Court of Law. The dissolution without the intervention of the court may take place in any of the following ways:

**INDIAN PARTNERSHIP ACT, 1932  
&THE LIMITED LIABILITY PARTNERSHIP ACT, 2008**

**1. Compulsory dissolution:**

In the following cases, the firm is compulsorily dissolved even if there is a contrary contract between the partners, i.e., even if the partners agree that the firm shall not be dissolved in such cases.

**(a) Insolvency/death of all the partners:**

Where all the partners of the firm become insolvent/death, the firm is dissolved. The firm is also dissolved when all the partners except one have become insolvent/died. The reason for the same is that when a partner is declared as insolvent by the court, he ceases to be a partner from the date of the order of insolvency.

**(b) Business of the firm becoming unlawful:**

Where an event happens which makes the business of the firm unlawful, the firm is also dissolved. This includes the cases where the business of the firm is rendered unlawful by the outbreak of war, or where the object for which the firm was formed becomes unlawful or illegal, or where the business remains lawful but it is forbidden to be carried on in partnership.

**2. Optional dissolution:**

**(a) Dissolution by agreement between the partners:**

A firm may also be dissolved in accordance with a contract between the partners in the same way as a firm is formed with the contract between the partners. There may be a separate contract for the dissolution of the firm, or it may also be contained in the partnership deed itself.

**(b) Dissolution by notice:**

A firm can also be dissolved by any partner by giving a notice of dissolution to the other partners where the partnership firm is at will.

**(c) Dissolution on the happening of certain contingencies:**

On the happening of anyone of the following contingencies (i.e., events), the firm is automatically dissolved.

**(i) Expiry of fixed term:**

Where the firm is constituted for a fixed term, the firm is dissolved on the expiry of that term. This is, however, subject to a contract to the contrary i.e., if the contract provides that the firm shall not be dissolved, then it will not be dissolved.

**(ii) Completion of the adventure or undertaking:**

Where the firm is constituted to carry out one or more adventure or undertaking, the firm is dissolved on the completion of such adventure or undertaking. This is also subject to a contract to the contrary.

**(iii) Death of a partner:**

Sometimes, one of the partners of a firm dies during the continuance of the firm. In such cases, the firm is dissolved on the death of the partner. This is subject to contract to the contrary.

**(iv) Insolvency of a partner:**

Sometimes, one of the partners of a firm is declared as insolvent by the court. In such cases the firm is dissolved from the date of the order of insolvency. This is also subject to a contract to the contrary.

**(B) DISSOLUTION WITH THE INTERVENTION OF COURT**

Sometimes, a partner wants that the firm should be dissolved. But the other partners may not agree to the dissolution. In such cases, he can go to Court of Law, and file a suit for dissolution of the firm. A partner may like to have the firm dissolved for various reasons. It may, however, be noted that the court has the discretion to pass an order of dissolution i.e., the court may or may not allow the dissolution of the firm. A partner may file a suit for dissolution of the firm on anyone of the following grounds, and the court may dissolve the firm if it is satisfied about the same:

**1. Insanity of a partner:**

Sometimes, a partner becomes insane i.e., of unsound mind. In such cases, the court may allow the dissolution of the firm. The suit for dissolution of the firm may be filed by anyone of the partners other than the partner who has become insane. The suit may also be filed by the next friend (i.e., legal representative) of the insane partner.

**2. Permanent incapacity of a partner:**

Sometimes, a partner becomes permanently incapable of performing his duties. In such cases also, the court may allow the dissolution of the firm. The suit for dissolution of the firm may be filed by anyone of the partners other than the partner who has become incapable.

**3. Misconduct of a partner:**

Where a partner is guilty of misconduct, the court may allow the dissolution of the firm. The suit for dissolution of the firm may be filed by anyone of the partners other than the partner who is guilty of misconduct.

**4. Persistent breach of agreement:**

Sometimes, a partner willfully or persistently (i.e., frequently) commits a breach of agreements relating to the management of the affairs of the firm, or conducts the partnership business in such a way that the other partners find it difficult to carry on the partnership business with him. In such cases, the court may allow the dissolution of the firm. The suit for dissolution of the firm may be filed by anyone of the partners other than the partner who commits the breach of agreements.



**INDIAN PARTNERSHIP ACT, 1932  
& THE LIMITED LIABILITY PARTNERSHIP ACT, 2008**

Keeping erroneous accounts and not entering receipts, continuing quarrelling between the partners, refusal to meet on matters of business, taking away books of the firm, and misappropriations of income etc., are held to be sufficient ground for dissolution of a firm.

**5. Transfer of interest:**

Where a partner transfers the whole of his interest or share to a third party, the court may allow the dissolution of the firm. The court may also allow the dissolution when the entire share of a partner is attached or sold by an order of the court. The suit for dissolution of the firm may be filed by anyone of the partners other than the partner who has transferred his interest or share.

**6. Perpetual losses in business:**

Where the business of a firm cannot be carried on, except at a loss, the court may allow the dissolution of the firm. The suit for dissolution of the firm may be filed by anyone of the partner. When the court is satisfied that the business of a firm cannot be carried on, except at a loss, it may pass an order of dissolution of the firm.

**7. Other just and equitable grounds:**

A firm may also be dissolved by the court on any 'other just and equitable ground'. A 'just and equitable ground', is a ground which is fair and reasonable according to the opinion of the court.

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**4.11 NATURE OF LIMITED LIABILITY PARTNERSHIP:**

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**Limited liability partnership to be body corporate:**

- (1) A limited liability partnership is a body corporate formed and incorporated under this Act and is a legal entity separate from that of its partners.
- (2) A limited liability partnership shall have perpetual succession. (3) Any change in the partners of a limited liability partnership shall not affect the existence, rights or liabilities of the limited liability partnership.

**Non-applicability of the Indian Partnership Act, 1932:**

As otherwise provided, the provisions of the Indian Partnership Act, 1932 (9 of 1932) shall not apply to a limited liability partnership.

**Partners:**

Any individual or body corporate may be a partner in a limited liability partnership:

Provided that an individual shall not be capable of becoming a partner of a limited liability partnership, if

1. he has been found to be of unsound mind by a Court of competent jurisdiction and the finding is in force;
2. he is an undischarged insolvent; or
3. he has applied to be adjudicated as an insolvent and his application is pending.

**Minimum number of partners:**

- (3) Every limited liability partnership shall have at least two partners.
- (4) If at any time the number of partners of a limited liability partnership is reduced below two and the limited liability partnership carries on business for more than six months while the number is so reduced, the person, who is the only partner of the limited liability partnership during the time that it so carries on business after those six months and has the knowledge of the fact that it is carrying on business with him alone, shall be liable personally for the obligations of the limited liability partnership incurred during that period.

**Designated partners:**

- (5) Every limited liability partnership shall have at least two designated partners who are individuals and at least one of them shall be a resident in India:

Provided that in case of a limited liability partnership in which all the partners are bodies corporate or in which one or more partners are individuals and bodies corporate, at least two individuals who are partners of such limited liability partnership or nominees of such bodies corporate shall act as designated partners.

Explanation—For the purposes of this section, the term ‘resident in India’ means a person who has stayed in India for a period of not less than one hundred and eighty-two days during the immediately preceding one year.

- (6) Subject to the provisions of sub-section (1),
  - (i) if the incorporation document—
    - a. specifies who are to be designated partners, such persons shall be designated partners on incorporation; or
    - b. states that each of the partners from time to time of limited liability partnership is to be designated partner, every such partner shall be a designated partner;
  - (ii) any partner may become a designated partner by and in accordance with the limited liability partnership agreement and a partner may cease to be a designated partner in accordance with limited liability partnership agreement.
- (7) An individual shall not become a designated partner in any limited liability partnership unless he has given his prior consent to act as such to the limited liability partnership in such form and manner as may be prescribed. Every limited liability partnership shall file with the registrar the particulars of every individual who has given his consent to act as designated partner in such form and manner as may be prescribed within thirty days of his appointment.
- (8) An individual eligible to be a designated partner shall satisfy such conditions and requirements as may be prescribed.
- (9) Every designated partner of a limited liability partnership shall obtain a Designated Partner Identification Number (DPIN) from the Central Government and the provisions of sections 266A to 266 (both inclusive) of the Companies Act, 1956 (1 of 1956) shall apply *mutatis mutandis* for the said purpose.

**Liabilities of designated partners:**

Unless expressly provided otherwise in this Act, a designated partner shall be

- 1. responsible for the doing of all acts, matters and things as are required to be

**INDIAN PARTNERSHIP ACT, 1932  
& THE LIMITED LIABILITY PARTNERSHIP ACT, 2008**

done by the limited liability partnership in respect of compliance of the provisions of this Act including filing of any document, return, statement and the like report pursuant to the provisions of this Act and as may be specified in the limited liability partnership agreement; and

2. liable to all penalties imposed on the limited liability partnership for any contravention of those provisions.

**Changes in designated partners:**

A limited liability partnership may appoint a designated partner within thirty days of a vacancy arising for any reason and provisions of sub-section (4) and sub-section (5) of section 7 shall apply in respect of such new designated partner provided that if no designated partner is appointed, or if at any time there is only one designated partner, each partner shall be deemed to be a designated partner.

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**4.12 EXTENT AND LIMITATION OF LIABILITY OF LIMITED LIABILITY PARTNERSHIP AND PARTNERS**

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**Partner as agent:**

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

**Extent of liability of limited liability partnership:**

- (1) A limited liability partnership is not bound by anything done by a partner in dealing with a person if
  - a. the partner in fact has no authority to act for the limited liability partnership in doing a particular act; and
  - b. the partner knows that he has no authority or does not know or believe him to be a partner of the limited liability partnership.
- (2) The limited liability partnership is liable if a partner of a limited liability partnership is liable to any person as a result of a wrongful act or omission on his part in the course of the business of the limited liability partnership or with its authority.
- (3) An obligation of the limited liability partnership whether arising in contract or otherwise, shall be solely the obligation of the limited liability partnership.
- (4) The liabilities of the limited liability partnership shall be met out of the property of the limited liability partnership.
- (5) Extent of liability of partner:

A partner is not personally liable, directly or indirectly for an obligation referred to in sub-section (3) of section 27 solely by reason of being a partner of the limited liability partnership.

- (6) The provisions of sub-section (3) of section 27 and sub-section

(1) of this section shall not affect the personal liability of a partner for his own wrongful act or omission, but a partner shall not be personally liable for the wrongful act or omission of any other partner of the limited liability partnership.

**Holding out:**

- (7) Any person, who by words spoken or written or by conduct, represents himself, or knowingly permits himself to be represented to be a partner in a limited liability partnership is liable to any person who has on the faith of any such representation given credit to the limited liability partnership, whether the person representing himself or represented to be a partner does or does not know that the representation has reached the person so giving credit:

Provided that where any credit is received by the limited liability partnership as a result of such representation, the limited liability partnership shall, without prejudice to the liability of the person so representing himself or represented to be a partner, be liable to the extent of credit received by it or any financial benefit derived thereon.

- (8) Where after a partner's death the business is continued in the same limited liability partnership name, the continued use of that name or of the deceased partner's name as a part thereof shall not of itself make his legal representative or his estate liable for any act of the limited liability partnership done after his death.

**Unlimited liability in case of fraud:**

- (9) In the event of an act carried out by a limited liability partnership, or any of its partners, with intent to defraud creditors of the limited liability partnership or any other person, or for any fraudulent purpose, the liability of the limited liability partnership and partners who 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 limited liability partnership:

Provided that in case any such act is carried out by a partner, the limited liability partnership is liable to the same extent as the partner unless it is established by the limited liability partnership that such act was without the knowledge or the authority of the limited liability partnership.

- (10) here any business is carried on with such intent or for such purpose as mentioned in sub-section (1), every person who was knowingly a party to the carrying on of the business in the manner aforesaid shall be punishable with imprisonment for a term which may extend to two years and with fine which shall not be less than fifty thousand rupees but which may extend to five lakh rupees.
- (11) Where a limited liability partnership or any partner or designated partner or employee of such limited liability partnership has conducted the affairs of the limited liability partnership in a fraudulent manner, then without prejudice to any criminal proceedings which may arise under any law for the time being in force, the limited liability partnership and any such partner or designated partner or employee shall be liable to pay compensation to any person who has suffered any loss or damage by reason of such conduct:

Provided that such limited liability partnership shall not be liable if any such partner or designated partner or employee has acted fraudulently without knowledge of the limited liability partnership.

**Whistle blowing:**

- (12) The Court or Tribunal may reduce or waive any penalty leviable against any partner or employee of a limited liability partnership, if it is satisfied that—
- a. such partner or employee of a limited liability partnership has provided useful information during investigation of such limited liability partnership; or
  - b. when any information given by any partner or employee (whether or not during investigation) leads to limited liability partnership or any partner or employee of such limited liability partnership being convicted under this Act or any other Act.
- (13) No partner or employee of any limited liability partnership may be discharged, demoted, suspended, threatened, harassed or in any other manner discriminated against the terms and conditions of his limited liability partnership or employment merely because of his providing information or causing information to be provided pursuant to sub-section (1).

**Assignment and Transfer of Partnership Rights**

- (1) The rights of a partner to a share of the profits and losses of the limited liability partnership and to receive distributions in accordance with the limited liability partnership agreement are transferable either wholly or in part.
- (2) The transfer of any right by any partner pursuant to sub-section (1) does not by itself cause the disassociation of the partner or a dissolution and winding up of the limited liability partnership.
- (3) The transfer of right pursuant to this section does not, by itself, entitle the transferee or assignee to participate in the management or conduct of the activities of the limited liability partnership, or access information concerning the transactions of the limited liability partnership.

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**4.13 CONVERSION INTO LIMITED LIABILITY PARTNERSHIP**

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**1. Conversion from firm into limited liability partnership**

A firm may convert into a limited liability partnership in accordance with the provisions of this Chapter and the Second Schedule.

**2. Conversion from private company into limited liability partnership:**

A private company may convert into a limited liability partnership in accordance with the provisions of this Chapter and the Third Schedule.

**3. Conversion from unlisted public company into limited liability partnership:**

An unlisted public company may convert into a limited liability partnership in accordance with the provisions of this Chapter and the Fourth Schedule.

**4. Registration and effect of conversion**

The Registrar, on satisfying that a firm, private company or an unlisted public company, as the case may be, has complied with the provisions of the

Second Schedule, the Third Schedule or the Fourth Schedule, as the case may be, shall, subject to the provisions of this Act and the rules made thereunder, register the documents submitted under such Schedule and issue a certificate of registration in such form as the Registrar may determine stating that the limited liability partnership is, on and from the date specified in the certificate, registered under this Act:

Provided that the limited liability partnership shall, within fifteen days of the date of registration, inform the concerned Registrar of Firms or Registrar of Companies, as the case may be, with which it was registered under the provisions of the Indian Partnership Act, 1932 (9 of 1932) or the Companies Act, 1956 (1 of 1956) as the case may be, about the conversion and of the particulars of the limited liability partnership in such form and manner as may be prescribed.

- (1) Upon such conversion, the partners of the firm, the shareholders of private company or unlisted public company, as the case may be, the limited liability partnership to which such firm or such company has converted, and the partners of the limited liability partnership shall be bound by the provisions of the Second Schedule, the Third Schedule or the Fourth Schedule, as the case may be, applicable to them.
- (2) Upon such conversion, on and from the date of certificate of registration, the effects of the conversion shall be such as specified in the Second Schedule, the Third Schedule or the Fourth Schedule, as the case may be.
- (3) Notwithstanding anything contained in any other law for the time being in force, on and from the date of registration specified in the certificate of registration issued under the Second Schedule, the Third Schedule or the Fourth Schedule, as the case may be,
  - (a) there shall be a limited liability partnership by the name specified in the certificate of registration registered under this Act;
  - (b) all tangible (movable or immovable) and intangible property vested in the firm or the company, as the case may be, all assets, interests, rights, privileges, liabilities, obligations relating to the firm or the company, as the case may be, and the whole of the undertaking of the firm or the company, as the case may be, shall be transferred to and shall vest in the limited liability partnership without further assurance, act or deed; and
  - (c) the firm or the company, as the case may be, shall be deemed to be dissolved and removed from the records of the Registrar of Firms or Registrar of Companies, as the case may be.

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#### **4.14 WINDING UP AND DISSOLUTION:**

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The winding up of a limited liability partnership may be either voluntary or by the Tribunal and limited liability partnership, so wound up may be dissolved.

##### **1. Circumstances in which limited liability partnership may be wound up by Tribunal:**

A limited liability partnership may be wound up by the Tribunal,

**INDIAN PARTNERSHIP ACT, 1932  
& THE LIMITED LIABILITY PARTNERSHIP ACT, 2008**

- (a) if the limited liability partnership decides that limited liability partnership be wound up by the Tribunal;
- (b) if, for a period of more than six months, the number of partners of the limited liability partnership is reduced below two;
- (c) if the limited liability partnership is unable to pay its debts;
- (d) if the limited liability partnership has acted against the interests of the sovereignty and integrity of India, the security of the State or public order;
- (e) if the limited liability partnership has made a default in filing with the Registrar the Statement of Account and Solvency or annual return for any five consecutive financial years; or
- (f) if the Tribunal is of the opinion that it is just and equitable that the limited liability partnership be wound up.

**2. Rules for winding up and dissolution**

The Central Government may make rules for the provisions in relation to winding up and dissolution of limited liability partnerships.

❖ **CHECK YOUR PROGRESS**

**1. Answer the following Questions**

- 1. Discuss essential elements of partnership.
- 2. Explain nature of partners.
- 3. Explain types of partners
- 4. Write a note on registration of firm
- 5. Discuss the constitution of the firm (section 17)
- 6. Explain relation of partners to third parties (sec. 18 to 30)
- 7. Write a note on legal consequences of partner coming in and going out (sections 31 - 38)
- 8. Write a note on Introduction of new partner (Section 31)
- 9. Explain Retirement of a partner (Section 32)
- 10. Write a note on Expulsion of a partner (Section 33)
- 11. Discuss Insolvency of a partner (Section 34)
- 12. Explain Death of a partner (Section 35)
- 13. Write a note on Revocation of continuing guarantee by change in the firm (Section 38)
- 14. Explain dissolution of partnership.
- 15. Explain dissolution of partnership firm.
- 16. Discuss nature of limited liability partnership.
- 17. Discuss Limited liability partnership to be body corporate.
- 18. Explain extent and limitation of liability of limited liability partnership and partners.
- 19. Explain assignment and transfer of partnership rights.
- 20. Discuss conversion into limited liability partnership.
- 21. Explain winding up and dissolution.



**2. Answer the following.**

**1. The most important element in partnership is:**

- (a) Business
- (b) Sharing of Profits
- (c) Agreement
- (d) Business to be carried on by all or any of them acting for all.**

**2. A firm is the name of:**

- (a) The Partners
- (b) The minors in the firm.
- (c) The business under which the firm carries on business
- (d) The collective name under which it carries on business**

**3. A partnership at will is one:**

- (a) Which does not have any deed
- (b) Which does not have any partner
- (c) Which does not provide for how long the business will continue**
- (d) Which cannot be dissolved.

**4. Active partner is one who:**

- (a) Takes part in the business of the firm**
- (b) Actively participates in co-curricular activities
- (c) Actively shares the profits
- (d) Makes a show of authority

**5. Every partner has the right to:**

- (a) Take part in the business of the firm**
- (b) To share exclusive profits
- (c) To use the property of the firm for personal purposes
- (d) Pay taxes

**6. Partners are:**

- (a) Principles at well of agents**
- (b) Agents of the firm
- (c) Representatives of the firm
- (d) Co-partners of the firm

**7. A partner can retire on:**

- (a) Reaching the age of superannuation
- (b) On the balance in the capital account reaching a certain amount
- (c) In accordance with the Partnership Deed**
- (d) On the condition of his nominee becoming a partner

**8. A partner can be expelled if:**

- (a) Such expulsion is in good faith**
- (b) The majority of the partner agree on such expulsion
- (c) The expelled partner is given an opportunity to start a business competing with that of the firm
- (d) Compensation is paid

**9. Death of partner has the effect of:**

- (a) Dissolving the firm**



**INDIAN PARTNERSHIP ACT, 1932  
&THE LIMITED LIABILITY PARTNERSHIP ACT, 2008**

- (b) Result in continuance of the business of the firm
- (c) His heirs joining the firm
- (d) Computation of profits up to the date of death

**10. Registration of a firm is:**

- (a) Compulsory
- (b) Optional**
- (c) Occasional
- (d) None of the above

**11. An unregistered firm cannot claim:**

- (a) Set on
- (b) Set off**
- (c) Set on and set off
- (d) None of the above

**12. On dissolution the partners remain liable to till:**

- (a) Accounts are settled
- (b) Partners dues are paid off
- (c) Public notice is given**
- (d) The registrar strikes off the name

**13. The LLP Act, 2008 came into force from:**

- (a) 31st March, 2008
- (b) 31st March, 2009**
- (c) 1st April, 2008
- (d) 1st April, 2009

**14. In case of a LLP, the partners are agents of**

- (a) LLP**
- (b) Other Partners
- (c) Both a) and b)
- (d) None of the above

**15. Minimum designated partners required in a LLP are:**

- (a) 1
- (b) 2**
- (c) 3**
- (d) 0

**16. Common seal is mandatory for**

- (a) Company
- (b) LLP**
- (c) Both the above
- (d) None of the above**

**17. In case of legal non-compliance and penalties under the LLP Act, are responsible.**

- (a) Partners
- (b) Designated Partners**
- (c) LLP
- (d) All the above

**18. Maximum number of partners in a LLP can be:**

- (a) 100
- (b) 200
- (c) 50
- (d) Unlimited**

**MCQ Answer :**

<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>	<b>6</b>	<b>7</b>	<b>8</b>	<b>9</b>	<b>10</b>	<b>11</b>	<b>12</b>	<b>13</b>	<b>14</b>	<b>15</b>	<b>16</b>	<b>17</b>	<b>18</b>
<b>D</b>	<b>D</b>	<b>C</b>	<b>A</b>	<b>A</b>	<b>A</b>	<b>C</b>	<b>A</b>	<b>A</b>	<b>B</b>	<b>B</b>	<b>C</b>	<b>B</b>	<b>A</b>	<b>C</b>	<b>D</b>	<b>B</b>	<b>D</b>

## 5.0 INTRODUCTION

### 5.1 CHARACTERISTICS

### 5.2 ESSENTIAL FEATURES OF NEGOTIABLE INSTRUMENT

### 5.3 PROMISSORY NOTE

### 5.4 BILL OF EXCHANGE

### 5.5 CHEQUE

### 5.6 DIFFERENT TYPES OF CHEQUES

### 5.7 HOLDER & HOLDER IN DUE COURSE

- CHECK YOUR PROGRESS

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## 5.0 INTRODUCTION

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The chief object of the Act is to legalise the system under which negotiable instruments pass from hand to hand in negotiations like ordinary goods. The Act came into force on 1st March, 1882. Documents of a particular type and nature frequently used in commercial transactions and monetary dealings are called Negotiable Instruments. The word ‘negotiable’ connotes that it is transferable from one person to another by delivery in return of consideration. ‘Instrument’ means a written document by which a right accrues in favour of some person. In this sense the term ‘negotiable instrument’ actually means ‘a document transferable from one person to another person by mere delivery or by endorsement and delivery. The person so receiving an instrument is entitled to money thereon and he also gets a right to transfer it.

**Definition of a Negotiable Instrument:\*** A Negotiable instrument is a device of transferring a debt from one person to another. In English Mercantile Law, the term is used in a much wider sense. Thus, under that law, a negotiable instrument is one in which “the true owner could transfer the contract or engagement contained therein by simple delivery of the instrument.” In India, however, it is used in a limited sense. The said law is contained in the Negotiable Instruments Act of 1881, which inter-alia states that,

**“A Negotiable Instrument means a promissory note, bill of exchange or cheque payable either to order or to bearer.”**

**As Thomas has written** A negotiable instrument is one which is by a legally recognized custom of trade or law,

- (1) Transferable by delivery or by endorsement and delivery.
- (2) Without notice to the party liable, in such a way that the holder of it for the time being may sue upon it in his own names and.
- (3) The property in it passes to a *bona fide* transferee for value free from equities and free from any defect in the title of the person from whom he obtained it.”

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### 5.1 CHARACTERISTICS OF A NEGOTIABLE INSTRUMENT\* :

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- (1) Freely Transferable:** The property in negotiable instrument passes from one person to another freely by delivery.
- (2) Title of holder freed from all defects:** If there is any defect in the title of the transferor or of any prior party, the instrument coming in the hands of the holder in due course is cured of all defects in the instruments.
- (3) Recovery:** The holder in due course can sue upon a negotiable instrument in his own name for the recovery of the amount specified in the instrument.
- (4) Presumptions:** Certain presumptions apply in all negotiable instruments unless contrary is proved.

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### 5.2 ESSENTIAL FEATURES OF NEGOTIABLE INSTRUMENTS :

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1. **Writing and signature:** Every negotiable instrument must be reduced to writing and signed by the parties as per the rules relating to Promissory Notes, Bills of Exchange and Cheques.
2. **Money:** Negotiable instruments are payable only by legal tender-money of India (Rupees).
3. **Negotiability:** Negotiable Instruments are easily transferred from one person to another by a simple process.
  - (i) In case of bearer instruments, delivery to the transferee alone is insufficient.
  - (ii) In all other cases (a) Indorsement, and (b) Delivery are necessary to constitute a valid transfer.
4. **Title:** The holder-in-due-course gets a good and clean title to the instrument even if the title of his transferor is defective.
5. **Notice:** Notice of transfer of a negotiable instrument to the party liable to pay is not required to the person liable to pay in respect of the instrument. The transferor can sue in his own name.
6. **Presumption:** Certain presumptions apply to all negotiable instruments.

7. **Special Procedure:** A speedy and special procedure is provided for suits on promissory note and bill of exchange.
8. **Property:** The property and rights in the instrument pass by delivery, with or without indorsements according to circumstances, and no further evidence of the transfer is necessary.
9. **Evidence:** An instrument which is not a negotiable instrument as per the provisions of the Act, is still good as evidence so far as the fact of indebtedness is concerned.

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### 5.3 PROMISSORY NOTE :

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#### **Definition:**

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. (S. 4)

The person who signs the instrument or promises to pay is called the 'Maker'. He is the debtor and must sign the instrument. The person who will receive money ('the creditor') is called 'Payee'.

Essential Elements\*: From the above definition it is apparent that an instrument intended to be a promissory note must fulfil the following essential elements:

- (1) **Writing:** The instrument must be 'in writing'. Mere oral engagement to pay is not enough.
- (2) **Signed by the Maker:** The instrument must be signed by the maker of it, otherwise it is incomplete, and is of no effect. Signature includes a signature in pencil or rubber stamp impression of a facsimile.
- (3) **Promise to pay:** The instrument must contain an undertaking or a promise to pay. Such a promise to pay must be express. It cannot be implied or inferred.
- (4) **Unconditional:** The promise to pay must be unconditional,
- (5) **Definite:** The maker of the instrument must be certain and definite.
- (6) **Stamped:** A promissory note must be duly stamped according to the Indian Stamp Act.
- (7) **Certain sum of money:** The sum of money payable must be certain and not susceptible of contingent additions or subtractions.

**(8) Promise to pay Money only:** The payment must be in the legal tender money of India.”

**(9) Certain person:** The money must be payable to a definite person or, according to his order, the payee may sometimes be misnamed or referred to by his official designation only, but so long as the intention to denote the payee is certain, the note is a valid one. Evidence is admissible to show who the payee really is.

**(10)** The promissory note may be payable on demand or after a definite period of time.

**(11)** The Reserve Bank of India Act prohibits the creation of a promissory note payable on demand to the bearer of the note, except by the Reserve Bank and the government of India.

**Specimen:** Any specific form or style is not necessary for drafting a promissory note as long as it satisfies all the essential elements of a promissory note.

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#### 5.4 BILL OF EXCHANGE \* :

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**Definition:**

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. (Sec. 5)

The maker of a bill of exchange is called the Drawer. The person who is directed to pay is called the Drawee. The person who will receive the money is called the Payee.

The drawer or the payee who is in possession of the bill is called the Holder. It is the holder's duty to present the bill to the drawee for his acceptance. The drawee signifies his acceptance by signing on the bill. The drawee after signing becomes the Acceptor.

**Drawer, Drawee:** The maker of a bill of exchange or cheque is called the drawer; the person thereby directed to pay is called the drawee.

**Acceptor:** After the drawee of a bill has signed his assent upon the bill, or if there are more parts thereof than one, upon one of such parts, and has delivered the same, or given notice of such signing to the holder or to some person on his behalf, he is called the acceptor.

**Acceptor for honour:** When a bill of exchange has been noted or protested for non- acceptance or for better security, and any person accepts it supra protest for honour of the drawer or of any one of the indorsers such, person is called the acceptor for honour.

**Payee:** The person named in the instrument, to whom or to whose order the money is by the instrument directed to be paid, is called the “Payee”. **(Sec. 7)**

**Drawee in case of need:** Besides the parties necessary to a Bill of Exchange another person may be introduced at the option of the drawer who is called the “drawee in case of need”. In other words, the drawer in such a situation inserts in the bill, the name of another person to whom resort may be had “in case of need”, i.e., in the event of the bill being dishonoured by non-acceptance or non-payment.

**Essential Elements:** The following essential elements must be present in every valid bill of exchange:

- (i) The instrument must be in writing
- (ii) The instrument must be signed by the drawer
- (iii) The instrument must contain an order to pay, which is express and unconditional.

The order to pay may be in the form of a request, but it should be imperative. The introduction of the term of gratitude viz. “will be much obliged” etc. does not destroy the promise to pay. (Ruff v. Webb (1794) 5 RR 773) However, merely to give authority to someone to pay the money is not sufficient.

- (iv) The drawer, drawee and the payee must be certain and definite individuals.
- (v) The sum payable must be certain.
- (vi) The payment must be in the legal tender money of India. The instrument must contain an order to pay money and money only.
- (vii) The money must be payable to a definite person or according to his order.
- (viii) A bill of exchange must be properly stamped.
- (ix) The bill may be made payable on demand or after a definite period of time. A bill as originally drawn cannot be made payable to a bearer on demand: No one except the Reserve Bank and the Government of India can draw a bill payable on demand to the bearer of the bill.

In case any of the requirements mentioned above is not fulfilled, the \* document is not a bill of exchange.

**Examples:**

- (1) Ninety days after sight or when realised.
- (2) "A debt that may come into existence at a future date." (Banbury v. Lesset(1744) 2 Stra. 121.)

**Specimen:** A bill of exchange also can be drawn in any form or manner so long as it fulfils all the requirements stipulated above.

Example:

(i)	Ahmedabad, 15-9-2013
₹. 1,000/-	
Six months after date pay Jayant Modi or Order the sum of one thousand rupees for value received.	
	<b>Sd. Jairam Joshi</b>
To Mihir Sen,	

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**5.5 CHEQUE :**

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Cheque is, therefore, such a bill of exchange which is drawn on a specified banker and not expressed to be payable otherwise than on demand.

A cheque being a bill of exchange must possess all the essentials of a bill and should also meet the requirements of S. 6.

**Definition:**

A cheque is a bill of exchange drawn on a specified banker and not expressed to be payable otherwise than on demand. (Sec. 6).

**Banker:** A banker is one, who in the ordinary course of his business, honours cheques drawn upon him by persons and receives money on current accounts. Treasury is not a bank. Therefore, when parties withdraw money from Treasury by issuing orders in the form of cheques, in reality they are in fact issuing a Bill of Exchange and not cheques. (R. Pillai v. 5. Ayyar (1920) 41 Mad. 816.)

**Essential Elements:**

A cheque has the following features:



- (1) A cheque must fulfil all the essential requirements of a bill of exchange.
- (2) A cheque may be payable to bearer or to order but in either case it must be payable on demand.
- (3) A cheque is always on a specified banker.
- (4) The banker named must pay it when it is presented for payment to him at his office during the usual hours of office, provided the cheque is validly drawn and the drawer has sufficient funds to his credit.
- (5) A cheque may be hand-written. But normally banks do provide their customers with printed cheque books containing forms which are to be filled up and signed by the drawer.
- (6) The drawer's signature to a cheque must tally with his specimen signature lying with the bank.
- (7) A cheque must be dated. If the cheque is not so dated, a bank may refuse to make the payment.
- (8) Post-dated cheque, i.e., cheque bearing a future date is valid. It may be noted, however, till the date of the cheque, it is a bill of exchange but becomes the cheque on the day when it becomes payable. However, the payment of such cheque will be made only on or after the date specified.
- (9) If for any reason the cheque remains uncashed for sufficiently long period of time after the date on which it is due for payment, the bank may refuse to honour the cheque. It is a suspicious circumstance and the bank is thus entitled to reject. The time gap, i.e., the period after which a cheque is considered too old or "stale" varies according to custom from place to place. In India, this period is usually taken to be six months.

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#### **5.6 DIFFERENT TYPES OF CHEQUES+ :**

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There are two types of cheques: (a) Open cheque, and (b) Crossed cheque.

- (i) Open cheque:** An open cheque is one which is payable in cash across the counter of the bank to the bearer of the cheque. On the other hand, crossed cheques are not encashable across the counter.

When such an open cheque is in circulation, a great risk attends it. In case the holder loses it, its finder may go to the bank and get payment unless its payment

has been stopped.

It was to prevent the losses incurred by open cheques getting into the hands of wrong parties that the practice of crossing was first introduced.

**Q : Point out the different types of crossing of cheques**

**(ii) Crossed cheque:** A crossed cheque is one which has two short parallel lines with or without the words ‘& Co’ marked across the cheque. A cheque thus marked can be paid only to another banker. Consequently, the payment will not be made across the counter.

**Different modes of crossing:** There are basically two different modes or crossing a cheque: (a) General and (b) Special.

**(a) General Crossing**

Where a cheque bears across its face an addition of the words “and company” or any abbreviation thereof, between two parallel transverse lines or of two parallel transverse lines simply, either with or without the words, “not negotiable”, that addition shall be deemed a crossing, and the cheque shall be deemed to be crossed generally. (Sec. 123)

Effect: The simplest mode of crossing is to put two parallel lines across the face of the cheque. This is normally known as general crossing.

**Payment of cheque crossed generally**

Where a cheque is crossed generally, the banker on whom it is drawn shall not pay it otherwise than to a banker.

Effect: A cheque crossed generally will be paid to any bank through which it is presented. The effect of such a crossing is to make the cheque payable only to a collecting banker, i.e., the paying banker is precluded from paying cash for the cheque across the counter.

**(b) Special Crossing**

Where a cheque bears across its face an addition of the name of a banker, either with or without the words “not negotiable”, that addition shall be deemed a crossing, and the cheque shall be deemed to be crossed specially, and to be crossed to that banker. (S. 124)

**Effect :** When the name of the bank is written between the parallel lines, it is called special crossing. A cheque crossed specially will be paid only when it is presented for collection by the bank named between the parallel lines.

**Payment of cheque crossed specially :**

**“ Where a cheque is crossed specially, the banker on whom it is drawn shall not pay it otherwise than to the banker to whom it is crossed, or his agent for collection.” (S. 126)**

**Effect:** Such crossing affords a greater measure of protection against loss.

**Restrictive crossing :** Besides the cheque may contain certain additional remarks on it, the effect of which is to restrict payment in certain ways. They are :

**“Account Payee” :** This is also-a version of general crossing. The words account payee’ on a cheque are a direction to a banker to credit the proceeds of the cheque to the account of the payee.

**“Not Negotiable” :** A cheque may be crossed generally with the words, “Not negotiable” between parallel lines. This general crossing deprives the cheque of its negotiability. A cheque marked with the words “not negotiable” can be transferred or assigned by the payee.

**Cheque bearing ‘not negotiable’**

A person taking a cheque crossed generally or specially, bearing in either case the words “not negotiable”, shall not have, and shall not be capable of giving a better title to the cheque than that which the person from whom he took it had” (S. 130) Thus, the cheque remains transferable, but “everyone who takes a cheque marked ‘not negotiable’ takes it at his own risk. (Great Western Rly Co. v London & Country Banking Co. (1910) AC. 414 at P. 424.)

Crossing after issue: S. 125 of the Negotiable Instruments Act provides thus. Where a cheque is uncrossed, the holder may cross, it generally or specially. Where a cheque generally, the holder may cross it specially.

**Where a cheque is crossed generally or specially, the holder may add the words ‘not negotiable.’**

Where a cheque is crossed specially the banker to whom it is crossed may again cross it specially to another banker, his agent, for collection.”

**Who can cross?:** A cheque can be crossed by the Drawer, the Holder and Bank (for collection). The holder and the bank can cross the cheque under the circumstances described in S. 125 above. The drawee can cross cheque (generally or specially) before using it.

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**5.7 HOLDER AND HOLDER-IN-DUE-COURSE\***

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Holder (Sec, 8)

The holder of a negotiable instrument means any person

1. entitled in his own name to the possession thereof and

2. to receive or recover the amount due thereon from the parties thereto.

The person legally entitled to receive the money due on the instrument is called the holder. The person who obtains possession of the instrument by illegal means is not a holder.

❖ **CHECK YOUR PORGRESS**

**Example :-**

Discuss with reasons, whether the following persons can be called as a 'holder' under the Negotiable Instruments Act, 1881:

1. X who obtains a cheque drawn by Y by way of gift.
2. A, the payee of the cheque, who is prohibited by a court order from receiving the amount of the cheque.
3. M, who finds a cheque payable to bearer, on the road and retains it.
4. B, the agent of C, is entrusted with an instrument without endorsement by C, who is the payee.
5. B, who steals a blank cheque of A and forges A's signature. (Nov. 2008)

**Answer**

**Person to be called a holder:** As per section 8 of the Negotiable Instruments Act, 1881 'holder' of a Negotiable Instrument means any person entitled in his own name to the possession of it and to receive or recover the amount due thereon from the parties thereto.

On applying the above provision in the given cases-

- (i) Yes, X can be termed as a holder because he has a right to possession and to receive the amount due in his own name.
- (ii) No, he is not a 'holder' because to be called as a 'holder' he must be entitled not only to the possession of the instrument but also to receive the amount mentioned therein.
- (iii) No, M is not a holder of the Instrument though he is in possession of the cheque, so is not entitled to the possession of it in his own name.
- (iv) No, B is not a holder. While the agent may receive payment of the amount mentioned in the cheque, yet he cannot be called the holder thereof because he has no right to sue on the instrument in his own name.
- (v) No, B is not a holder because he is in wrongful possession of the instrument.
- (vi) Holder in due course (Sec, 9)

The holder in due course is a particular kind of holder. The holder of a negotiable instrument is called holder in due course if he satisfies the following conditions:

1. He obtained the instrument for a valuable consideration.

## THE NEGOTIABLE INSTRUMENTS ACT. 1881 I & II

2. He obtained the possession of the negotiable instrument before its maturity, i.e., before the amount mentioned on it became payable.
3. He had no cause to believe that any defect existed in the title of the person from whom he derived his title. In other words, he must have obtained it in good faith.

### Example:

X by inducing Y obtains a Bill of Exchange from him fraudulently in his (X) favour. Later, he enters into a commercial deal and endorses the bill to Z towards consideration to him (Z) for the deal. Z takes the bill as a Holder-in-due-course. Z subsequently endorses the bill to X for value, as consideration to X for some other deal. On maturity the bill is dishonoured. X sues Y for the recovery of the money. With reference to the provisions of the Negotiable Instruments Act, decide whether X will succeed in the case?

### Answer:

The problem stated in the question is based on the provisions of the Negotiable Instruments Act as contained in Section 53. The section provides: 'Once a negotiable instrument passes through the hands of a holder in due course, it gets cleansed of its defects provided the holder was himself not a party to the fraud or illegality which affected the instrument in some stage of its journey. Thus, any defect in the title of the transferor will not affect the rights of the holder in due course even if he had knowledge of the prior defect provided, he is himself not a party to the fraud. (Section 53).

Thus, applying the above provisions, it is clear that X who originally induced Y in obtaining the bill of exchange in question fraudulently, cannot succeed in the case. The reason is obvious as X himself was a party to the fraud.

### Difference between Holder and Holder in due course (Nov 2000)

Holder	Holder in due course
A person becomes a holder even if he obtains the negotiable instrument without any consideration.	A person becomes a holder in due course only if he obtains the negotiable instrument For consideration.
A person becomes a holder even if he obtains the instrument after its maturity.	A person becomes a holder in due course only if he obtains the negotiable instrument before its maturity.
A person becomes a holder, even if he does not obtain the instrument in good faith.	For being a holder in due course, a person must obtain the instrument in good faith.

A holder is not entitled to the privileges,	A holder in due course is entitled to various
which are available to holder in due course.	privileges as specified under the act.
A holder cannot sue all the prior parties.	A holder in due course can sue all the prior parties.

**Long questions (Answer the following in detail)**

1. State the characteristics of a Negotiable Instrument.
2. Define 'Promissory Note' and discuss its essential ingredients
3. Essential Features of a negotiable instrument.
4. Define bill of exchange and discuss the essential ingredients.
5. Define cheque and discuss its essential elements.
6. Define 'Holder' and 'Holder-in-due-course'. Point out the distinction between the two.

**MULTIPLE CHOICE QUESTIONS:**

1. **Person named in the instrument to whom money is directed to be paid—**  
 (a) Drawer (b) Acceptor (c) Maker (d) Payee.2
2. **Maker of a bill of exchange is called —**  
 (a) Drawer (b) Drawee (c) Acceptor (d) Payee
3. **Days of grace provided to the Instruments at maturity is —**  
 (a) 1 day (b) 2 days (c) 3 days (d) 5 days
4. **Parties to a negotiable instrument can be discharged from liability by —**  
 (a) Cancellation (b) Payment (c) Release (d) All of the above
5. **Validity period for the presentment of cheque in bank is —**  
 (a) 3 months (b) 6 months (c) 1 year (d) 2 years
6. **As per the Negotiable Instruments Act, 1881, when the day on which a promissory note or bill of exchange is at maturity is a public holiday, the instrument shall be deemed to be due on the**  
 (a) said public holiday (b) 5 days succeeding public holiday  
 (c) next succeeding business day (d) next preceding business day
7. **Person named in the instrument to whom money is directed to be paid:**  
 (a) Drawer (b) Acceptor (c) Maker (d) Payee
8. **A draw a cheque in favour of M, a minor. M endorses the same in favour of X. The cheque is dishonored by the bank on grounds of inadequate funds. As per the provisions of Negotiable Instruments Act, 1881:**  
 (a) M is liable to X (b) X can proceed against A  
 (c) No one is liable in this case (d) M can proceed against A

**THE NEGOTIABLE INSTRUMENTS ACT. 1881 I & II**

- 9. The Negotiable Instruments Act, came into force on the**  
(a) 1.1.1881 (b) 1.2.1881 (c) 1.4.1881 (d) 1.03.1981
- 10. Person named in the instrument to whom money is directed to be paid is known as \_\_\_\_**  
a) Drawer  
b) Acceptor  
c) Maker  
d) Payee
- 11. Maker of a bill of exchange is called as .....**  
a) Drawer  
b) Drawee  
c) Acceptor  
d) Payee
- 12. Days of grace provided to the Instruments at maturity is.....**  
a) 1 day  
b) 2 days  
c) 3 days  
d) 5 days
- 13. Parties to a negotiable instrument can be discharged from liability by .....**  
a) Cancellation  
b) Payment  
c) Release  
d) All of the above
- 14. Validity period for the presentment of cheque in bank is .....**  
a) 3 months  
b) 6 months  
c) 1 year  
d) 2 years
- 15. Offences committed under the Negotiable Instruments Act can be .....**  
a) Compoundable

- b) Non-compoundable
- c) Non-compoundable and non-bailable
- d) Bailable

**16. A negotiable instrument that is payable to order can be transferred by:**

- a) Simple delivery
- b) endorsement and delivery
- c) endorsement
- d) registered post

**17. A negotiable instrument drawn in favour of minor is**

- a) Void
- b) Void but enforceable
- c) Valid
- d) None of these

**18. Which of the following is not applicable to negotiable instruments?**

- a) It must be in writing
- b) It must be transferable
- c) It must be registered
- d) It must be signed

**19. A promissory note drawn jointly by X, a minor and Y, a major is:**

- a) Void
- b) Valid but not negotiable
- c) Valid but can be enforced only against Y
- d) None of the above

**20. In legal terms, person who takes the instruments bonafide for value before it is overdue, in good faith, is known as:**

- a) Holder in due course
- b) Holder
- c) Holder for value
- d) None of the above

**Ans**

1	D	2	A	3	C	4	D	5	A
6	D	7	D	8	B	9	D	10	D
11	A	12	C	13	D	14	A	15	A
16	B	17	C	18	C	19	C	20	A



**MBA**  
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- 6.0 INTRODUCTION**
- 6.1 DEFINATIONS**
- 6.2 ELECTRONIC GOVERNANCE**
- 6.3 ATTRIBUTION, ACKNOWLEDGMENT AND DESPATCH OF ELECTRONIC RECORDS**
- 6.4 REGULATION OF CERTIFYING AUTHORITIES**
- 6.5 CERTIFYING AUTHORITY TO ISSUE [ELECTRONIC SIGNATURE] CERTIFICATE**
- 6.6 PENALTIES, COMPENSATION AND ADJUDICATION**
- 6.7 CYBER APPELLATE TRIBUNAL**

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**6.1 INTRODUCTION**

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An Act to provide legal recognition for transactions carried out by means of electronic data interchange and other means of electronic communication is commonly referred to as electronic commerce. It involve the use of alternatives to paper-based methods of communication and storage of information, to facilitate electronic filing of documents with the Government agencies and further to amend the Indian Penal Code, the Indian Evidence Act, 1872, the Banker's Books Evidence Act, 1891 and the Reserve Bank of India Act, 1934 and for matters connected therewith or incidental thereto.

Whereas the General Assembly of the United Nations by resolution A/RES/51/162, dated the 30th January, 1997 has adopted the Model Law on Electronic Commerce adopted by the United Nations Commission on International Trade Law;

And whereas the said resolution recommends inter alia, that all States give favourable consideration to the said Model Law when they enact or revise their laws, in view of the need for uniformity of the law applicable to alternatives to paper-based methods of communication and storage of information;

And whereas it is considered necessary to give effect to the said resolution and to promote efficient delivery of Government services by means of reliable electronic records.

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**6.2 DEFINITIONS**

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- 6.2.1 Access: with its grammatical variations and cognate expressions means gaining entry into, instructing or communicating with the logical, arithmetical, or memory function resources of a computer, computer system or computer network;
- 6.2.2 Addressee: means a person who is intended by the originator to receive the electronic record but does not include any intermediary;
- 6.2.3 Appropriate Government: means as respects any matter,

- 6.2.3.1 enumerated in List II of the Seventh Schedule to the Constitution;
- 6.2.3.2 relating to any State law enacted under List III of the Seventh Schedule to the Constitution, the State Government and in any other case, the Central Government;
- 6.2.4 Asymmetric crypto system means a system of a secure key pair consisting of a private key for creating a digital signature and a public key to verify the digital signature;
- 6.2.5 Certifying Authority means a person who has been granted a licence to issue a <sup>1</sup>[electronic signature] Certificate under section 24;
- 6.2.6 computer means any electronic, magnetic, optical or other high-speed data processing device or system which performs logical, arithmetic, and memory functions by manipulations of electronic, magnetic or optical impulses, and includes all input, output, processing, storage, computer software or communication facilities which are connected or related to the computer in a computer system or computer network;
- 6.2.6.1 computer network means the inter-connection of one or more computers or computer systems or communication device through— the use of satellite, microwave, terrestrial line, wire, wireless or other communication media; and
- 6.2.6.2 terminals or a complex consisting of two or more interconnected computers or communication device whether or not the inter-connection is continuously maintained;]
- 6.2.7 computer resource means computer, computer system, computer network, data, computer data base or software;
- 6.2.8 data means a representation of information, knowledge, facts, concepts or instructions which are being prepared or have been prepared in a formalised manner, and is intended to be processed, is being processed or has been processed in a computer system or computer network, and may be in any form (including computer printouts magnetic or optical storage media, punched cards, punched tapes) or stored internally in the memory of the computer;

Digital signature means authentication of any electronic record by a subscriber by means of an electronic method or procedure in accordance with the provisions of section 3

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### 6.3 ELECTRONIC GOVERNANCE

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1. **Legal recognition of electronic records**—Where any law provides such information or any other matter that shall be in writing or in the typewritten or printed form, then, notwithstanding anything contained in such law, such requirement shall be deemed to have been satisfied if such information or matter is—
  - (a) rendered or made available in an electronic form; and
  - (b) accessible so as to be usable for a subsequent reference.
2. **Legal recognition of <sup>1</sup>[electronic signatures**—Where any law provides such information or any other matter that shall be authenticated by affixing the signature or any document shall be signed or bear the signature of any person, then, notwithstanding anything contained in such law, such requirement shall be deemed to have been satisfied, if such information or matter is

## THE INFORMATION TECHNOLOGY ACT, 2000

authenticated by means of <sup>1</sup>[electronic signature] affixed in such manner as may be prescribed by the Central Government.

*Explanation*—For the purposes of this section, signed, with its grammatical variations and cognate expressions, shall, with reference to a person, mean affixing of his hand written signature or any mark on any document and the expression –signature! shall be construed accordingly.

### 3. Use of electronic records and [electronic signatures] in Government and its agencies—

#### (1) Where any law provides for—

- (a) the filing of any form, application or any other document with any office, authority, body or agency owned or controlled by the appropriate Government in a particular manner;
- (b) the issue or grant of any licence, permit, sanction or approval by whatever name called in a particular manner;
- (c) the receipt or payment of money in a particular manner,

Then, notwithstanding anything contained in any other law for the time being in force, such requirement shall be deemed to have been satisfied if such filing, issue, grant, receipt or payment, as the case may be, is effected by means of such electronic form as may be prescribed by the appropriate Government.

#### (2) The appropriate Government may, for the purposes of sub-section (1), by rules, prescribe—

- (a) the manner and format in which such electronic records shall be filed, created or issued;
- (b) the manner or method of payment of any fee or charges for filing, creation or issue any electronic record under clause (a).

### 4. Delivery of services by service provider—

- (1) The appropriate Government may, for the purposes of this Chapter and for efficient delivery of services to the public through electronic means authorised, by order, any service provider to set up, maintain and upgrade the computerised facilities and perform such other services as it may specify, by notification in the Official Gazette.

*Explanation*—For the purposes of this section, service provider so authorised includes any individual, private agency, private company, partnership firm, sole proprietor firm or any such other body or agency which has been granted permission by the appropriate Government to offer services through electronic means in accordance with the policy governing such service sector.

- (2) The appropriate Government may also authorise any service provider authorised under sub- section (1) to collect, retain and appropriate such service charges, as may be prescribed by the appropriate Government for the purpose of providing such services, from the person availing such service.
- (3) Subject to the provisions of sub-section (2), the appropriate Government may authorise the service providers to collect, retain and appropriate service charges under this section notwithstanding the fact that there is no express provision under the Act, rule, regulation or notification under which the

service is provided to collect, retain and appropriate e-service charges by the service providers.

- (4) The appropriate Government shall, by notification in the Official Gazette, specify the scale of service charges which may be charged and collected by the service providers under this section:

Provided that the appropriate Government may specify different scale of service charges for different types of services.]

- 5. Retention of electronic records**—(1) Where any law provides that documents, records or information shall be retained for any specific period, then, that requirement shall be deemed to have been satisfied if such documents, records or information are retained in the electronic form, if—
- i. the information contained therein remains accessible so as to be usable for a subsequent reference;
  - ii. the electronic record is retained in the format in which it was originally generated, sent or received or in a format which can be demonstrated to represent accurately the information originally generated, sent or received;
  - iii. the details which will facilitate the identification of the origin, destination, date and time of dispatch or receipt of such electronic record are available in the electronic record:

Provided that this clause does not apply to any information which is automatically generated solely for the purpose of enabling an electronic record to be dispatched or received.

- (2) Nothing in this section shall apply to any law that expressly provides for the retention of documents, records or information in the form of electronic records.
- 6. Audit of documents, etc., maintained in electronic form**—Where in any law for the time being in force, there is a provision for audit of documents, records or information, that provision shall also be applicable for audit of documents, records or information processed and maintained in the electronic form.]
- 7. Publication of rule, regulation, etc., in Electronic Gazette**—Where any law provides that any rule, regulation, order, bye-law, notification or any other matter shall be published in the Official Gazette, then, such requirement shall be deemed to have been satisfied if such rule, regulation, order, bye-law, notification or any other matter is published in the Official Gazette or Electronic Gazette:

Provided that where any rule, regulation, order, by-law, notification or any other matter is published in the Official Gazette or Electronic Gazette, the date of publication shall be deemed to be the date of the Gazette which was first published in any form.

- 8. Power to make rules by Central Government in respect of <sup>1</sup>[electronic signature]**—The Central Government may, for the purposes of this Act, by rules, prescribe—
1. the type of <sup>1</sup>[electronic signature];
  2. the manner and format in which the <sup>1</sup>[electronic signature] shall be affixed;
  3. the manner or procedure which facilitates identification of the person affixing the [electronic signature];

## THE INFORMATION TECHNOLOGY ACT, 2000

4. control processes and procedures to ensure adequate integrity, security and confidentiality of electronic records or payments; and
5. any other matter which is necessary to give legal effect to <sup>1</sup>[electronic signatures].

**9. Validity of contracts formed through electronic means**—Where in a contract formation, the communication of proposals, the acceptance of proposals, the revocation of proposals and acceptances, as the case may be, are expressed in electronic form or by means of an electronic records, such contract shall not be deemed to be unenforceable solely on the ground that such electronic form or means was used for that purpose.]

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### **6.4 ATTRIBUTION, ACKNOWLEDGMENT AND DESPATCH OF ELECTRONIC RECORDS**

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**(A) Attribution of electronic records**—An electronic record shall be attributed to the originator—

- (a) if it was sent by the originator himself;
- (b) by a person who had the authority to act on behalf of the originator in respect of that electronic record; or
- (c) by an information system programmed by or on behalf of the originator to operate automatically.

**(B) Acknowledgment of receipt**—

(1) Where the originator has not<sup>3</sup> [stipulated] that the acknowledgment of receipt of electronic record be given in a particular form or by a particular method, an acknowledgment may be given by—

- (d) any communication by the addressee, automated or otherwise; or
- (e) any conduct of the addressee, sufficient to indicate to the originator that the electronic record has been received.

(2) Where the originator has stipulated that the electronic record shall be binding only on receipt of an acknowledgment of such electronic record by him, then unless acknowledgment has been so received, the electronic record shall be deemed to have been never sent by the originator.

(3) Where the originator has not stipulated that the electronic record shall be binding only on receipt of such acknowledgment, and the acknowledgment has not been received by the originator within the time specified or agreed or, if no time has been specified or agreed to within a reasonable time, then the originator may give notice to the addressee stating that no acknowledgment has been received by him and specifying a reasonable time by which the acknowledgment must be received by him and if no acknowledgment is received within the aforesaid time limit he may after giving notice to the addressee, treat the electronic record as though it has never been sent.

**(C) Time and place of dispatch and receipt of electronic record**—

(1) Save as otherwise agreed to between the originator and the addressee, the dispatch of an electronic record occurs when it enters a computer resource

- outside the control of the originator.
- (2) Save as otherwise agreed between the originator and the addressee, the time of receipt of an electronic record shall be determined as follows, namely:
    - (a) if the addressee has designated a computer resource for the purpose of receiving electronic records,
      - (i) receipt occurs at the time when the electronic record enters the designated computer resource; or
      - (ii) if the electronic record is sent to a computer resource of the addressee that is not the designated computer resource, receipt occurs at the time when the electronic record is retrieved by the addressee;
    - (b) if the addressee has not designated a computer resource along with specified timings, if any, receipt occurs when the electronic record enters the computer resource of the addressee.
  - (3) Save as otherwise agreed to between the originator and the addressee, an electronic record is deemed to be dispatched at the place where the originator has his place of business, and is deemed to be received at the place where the addressee has his place of business.
  - (4) The provisions of sub-section (2) shall apply notwithstanding that the place where the computer resource is located may be different from the place where the electronic record is deemed to have been received under sub-section (3).

For the purposes of this section,

- 1 if the originator or the addressee has more than one place of business, the principal place of business, shall be the place of business;
- 2 if the originator or the addressee does not have a place of business, his usual place of residence shall be deemed to be the place of business;
- 3 usual place of residence, in relation to a body corporate, means the place where it is registered.

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## 6.5 REGULATION OF CERTIFYING AUTHORITIES

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### (A) Appointment of Controller and other officers—

- (1) The Central Government may, by notification in the Official Gazette, appoint a Controller of Certifying Authorities for the purposes of this Act and may also by the same or subsequent notification appoint such number of Deputy Controllers<sup>3</sup> [, Assistant Controllers, other officers and employees] as it deems fit 3. Subs. by s.12, *ibid.*, for -and Assistant Controllers| (w.e.f. 27-10-2009).

The Controller shall discharge his functions under this Act subject to the general control and directions of the Central Government.

- (2) The Deputy Controllers and Assistant Controllers shall perform the functions assigned to them by the Controller under the general superintendence and control of the Controller.
- (3) The qualifications, experience and terms and conditions of service of Controller, Deputy Controllers<sup>1</sup> [Assistant Controllers, other officers and employees] shall be such as may be prescribed by the Central Government.
- (4) The Head Office and Branch Office of the office of the Controller shall be at such places as the Central Government may specify, and these may be established at such places as the Central Government may think fit.

## THE INFORMATION TECHNOLOGY ACT, 2000

- (5) There shall be a seal of the Office of the Controller.
- (B) Functions of Controller**—The Controller may perform all or any of the following functions, namely:
- i.** exercising supervision over the activities of the Certifying Authorities
  - ii.** certifying public keys of the Certifying Authorities
  - iii.** laying down the standards to be maintained by the Certifying Authorities
  - iv.** specifying the qualifications and experience which employees of the Certifying Authority should possess
  - v.** specifying the conditions subject to which the Certifying Authorities shall conduct their business
  - vi.** specifying the contents of written, printed or visual materials and advertisements that may be distributed or used in respect of a <sup>2</sup>[electronic signature] Certificate and the public key
  - vii.** specifying the form and content of a <sup>2</sup>[electronic signature] Certificate and the key
  - viii.** specifying the form and manner in which accounts shall be maintained by the Certifying Authorities
  - ix.** specifying the terms and conditions subject to which auditors may be appointed and their remuneration to be paid to them
  - x.** facilitating the establishment of any electronic system by a Certifying Authority either solely or jointly with other Certifying Authorities and regulation of such systems
  - xi.** specifying the manner in which the Certifying Authorities shall conduct their dealings with the subscribers
  - xii.** resolving any conflict of interests between the Certifying Authorities and the subscribers;
  - xiii.** laying down the duties of the Certifying Authorities
  - xiv.** maintaining a data base containing the disclosure record of every certifying Authority containing such particulars as may be specified by regulations, which shall be accessible to public

**(C) Licence to issue <sup>1</sup>[electronic signature] Certificates.**—

- (1) Subject to the provisions of sub-section (2), any person may make an application, to the Controller, for a licence to issue <sup>1</sup>[electronic signature] Certificates.
- (2) No licence shall be issued under sub-section (1), unless the applicant fulfils such requirements with respect to qualification, expertise, manpower, financial resources and other infrastructure facilities, which are necessary to issue <sup>1</sup>[electronic signature] Certificates as may be prescribed by the Central Government.
- (3) A licence granted under this section shall—
  - (a) be valid for such period as may be prescribed by the Central Government
  - (b) not be transferable or heritable
  - (c) be subject to such terms and conditions as may be specified by the regulations

**(D) Application for license** —

- (1) Every application for issue of a licence shall be in such form as may be prescribed by the Central Government.



- (2) Every application for issue of a licence shall be accompanied by—
- (a) a certification practice statement
  - (b) a statement including the procedures with respect to identification of the applicant
  - (c) payment of such fees, not exceeding twenty-five thousand rupees as may be prescribed by the Central Government
  - (d) such other documents, as may be prescribed by the Central Government

**(E Renewal of licence—**An application for renewal of a licence shall be

1. in such form; accompanied by such fees, not exceeding five thousand rupees, as may be prescribed by the Central Government and shall be made not less than forty-five days before the date of expiry of the period of validity of the licence.
- 2 **Procedure for grant or rejection of licence—**The Controller may, on receipt of an application under sub-section (1) of section 21, after considering the documents accompanying the application and such other factors, as he deems fit, grant the licence or reject the application:

Provided that no application shall be rejected under this section unless the applicant has been given a reasonable opportunity of presenting his case.

**3. Suspension of licence—**

- (1) The Controller may, if he is satisfied after making such inquiry, as he may think fit, that a Certifying Authority has—
  - i. made a statement in, or in relation to, the application for the issue or renewal of the licence, which is incorrect or false in material particulars;
  - ii. failed to comply with the terms and conditions subject to which the licence was granted;

Contravened any provisions of this Act, rule, regulation or order made thereunder, revoke the licence:

Provided that no licence shall be revoked unless the Certifying Authority has been given a reasonable opportunity of showing cause against the proposed revocation.

- (2) The Controller may, if he has reasonable cause to believe that there is any ground for revoking a licence under sub-section (1), by order suspend such licence pending the completion of any enquiry ordered by him:

Provided that no licence shall be suspended for a period exceeding ten days unless the Certifying Authority has been given a reasonable opportunity of showing cause against the proposed suspension.

- (3) No Certifying Authority whose licence has been suspended shall issue any<sup>1</sup> [electronic signature] Certificate during such suspension.

**(F) Notice of suspension or revocation of licence—**

- (1) Where the licence of the Certifying Authority is suspended or revoked, the Controller shall publish notice of such suspension or revocation, as the case

## THE INFORMATION TECHNOLOGY ACT, 2000

may be, in the data base maintained by him.

- (2) Where one or more repositories are specified, the Controller shall publish notices of such suspension or revocation, as the case may be, in all such repositories:

Provided that the data base containing the notice of such suspension or revocation, as the case maybe, shall be made available through a web site which shall be accessible round the clock:

Provided further that the Controller may, if he considers necessary, publicise the contents of data base in such electronic or other media, as he may consider appropriate.

### **(G) Power to investigate contraventions—**

- (1) The Controller or any officer authorised by him in this behalf shall take up for investigation any contravention of the provisions of this Act, rules or regulations made thereunder.
- (2) The Controller or any officer authorised by him in this behalf shall exercise the like powers which are conferred on Income-tax authorities under Chapter XIII of the Income-tax Act, 1961 (43 of 1961), and shall exercise such powers, subject to such limitations laid down under that Act.
- (3) **Access to computers and data.**—(1) Without prejudice to the provisions of sub-section (1) of section 69, the Controller or any person authorised by him shall, if he has reasonable cause to suspect that<sup>2</sup> [any contravention of the provisions of this Chapter] has been committed, have access to any computer system, any apparatus, data or any other material connected with such system, for the purpose of searching or causing a search to be made for obtaining any information or data contained in or available to such computer system.
- (4) For the purposes of sub-section (1), the Controller or any person authorised by him may, by order, direct any person in charge of, or otherwise concerned with the operation of, the computer system, data apparatus or material, to provide him with such reasonable technical and other assistance as he may consider necessary.

### **(H) Certifying Authority to follow certain procedures—**Every Certifying Authority shall,—

- (a) make use of hardware, software and procedures that are secure from intrusion and misuse;
- (b) provide a reasonable level of reliability in its services which are reasonably suited to the performance of intended functions;
- (c) adhere to security procedures to ensure that the secrecy and privacy of the<sup>1</sup>[electronic signatures] are assured; <sup>3\*\*\*</sup>
- (d) observe such other standards as may be specified by regulations.

**(I) Certifying Authority to ensure compliance of the Act, etc.**—Every Certifying Authority shall ensure that every person employed or otherwise engaged by it complies, in the course of his employment or engagement, with the provisions of this Act, rules, regulations and orders made thereunder.

**(J) Display of license**—Every Certifying Authority shall display its license at a conspicuous place of the premises in which it carries on its business.

**(K) Surrender of licence—**

- (1) Every Certifying Authority whose licence is suspended or revoked shall immediately after such suspension or revocation, surrender the licence to the Controller.
- (2) Where any Certifying Authority fails to surrender a licence under sub-section (1), the person in whose favour a licence is issued, shall be guilty of an offence and shall be punished with imprisonment which may extend up to six months or a fine which may extend up to ten thousand rupees or with both.

**(L) Disclosure—**

- (1) Every Certifying Authority shall disclose in the manner specified by regulations—
  - (a) its <sup>1</sup>[electronic signature] Certificate <sup>2\*\*\*</sup>;
  - (b) any certification practice statement relevant thereto;
  - (c) notice of the revocation or suspension of its Certifying Authority certificate, if any; and
  - (d) any other fact that materially and adversely affects either the reliability of a <sup>1</sup> [electronic signature] Certificate, which that Authority has issued, or the Authority's ability to perform its services.
- (2) Where in the opinion of the Certifying Authority any event has occurred or any situation has arisen which may materially and adversely affect the integrity of its computer system or the conditions subject to which a <sup>1</sup> [electronic signature] Certificate was granted, then, the Certifying Authority shall—
  - (a) use reasonable efforts to notify any person who is likely to be affected by that occurrence; or
  - (b) act in accordance with the procedure specified in its certification practice statement to deal with such event or situation.

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**6.6 Certifying authority to issue [electronic signature] Certificate—**

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- (1) Any person may make an application to the Certifying Authority for the issue of a <sup>1</sup>[electronic signature] Certificate in such form as may be prescribed by the Central Government.
- (2) Every such application shall be accompanied by such fee not exceeding twenty-five thousand rupees as may be prescribed by the Central Government, to be paid to the Certifying Authority:

Provided that while prescribing fees under sub-section (2) different fees may be prescribed for different classes of applicants.

- (3) Every such application shall be accompanied by a certification practice statement or where there is no such statement, a statement containing such particulars, as may be specified by regulations.
- (4) On receipt of an application under sub-section (1), the Certifying Authority may, after consideration of the certification practice statement or the other statement under sub-section (3) and after making such enquiries as it may deem fit, grant the <sup>1</sup> [electronic signature] Certificate or for reasons to be recorded in writing, reject the application:

<sup>3\*\*\*\*\*</sup>

<sup>4</sup>[Provided] that no application shall be rejected unless the applicant has been

given a reasonable opportunity of showing cause against the proposed rejection.

**Representations upon issuance of Digital Signature Certificate—**

A Certifying Authority while issuing a Digital Signature Certificate shall certify that—

- (a) it has complied with the provisions of this Act and the rules and regulations made thereunder;
- (b) it has published the Digital Signature Certificate or otherwise made it available to such person relying on it and the subscriber has accepted it;
- (c) the subscriber holds the private key corresponding to the public key, listed in the Digital Signature Certificate;
1. the subscriber holds a private key which is capable of creating a digital signature; 2 the public key to be listed in the certificate can be used to verify a digital signature affixed by the private key held by the subscriber;
- (d) the subscriber's public key and private key constitute a functioning key pair;
- (e) the information contained in the Digital Signature Certificate is accurate; and
- (f) it has no knowledge of any material fact, which if it had been included in the Digital Signature Certificate would adversely affect the reliability of the representations in clauses (a) to (d).

**Suspension of Digital Signature Certificate—**

- (1) Subject to the provisions of sub-section (2), the Certifying Authority which has issued a Digital Signature Certificate may suspend such Digital Signature Certificate—
  - (a) on receipt of a request to that effect from—
    - (i) the subscriber listed in the Digital Signature Certificate; or
    - (ii) any person duly authorised to act on behalf of that subscriber;
  - (b) if it is of opinion that the Digital Signature Certificate should be suspended in public interest.
- (2) A Digital Signature Certificate shall not be suspended for a period exceeding fifteen days unless the subscriber has been given an opportunity of being heard in the matter.
- (3) On suspension of a Digital Signature Certificate under this section, the Certifying Authority shall communicate the same to the subscriber.

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**6.7 PENALTIES, COMPENSATION AND ADJUDICATION**

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**6.7.1** [Penalty and compensation] for damage to computer, computer system, etc.—

**If any person without permission of the owner or any other person who is in charge of a computer, computer system or computer network—**

- 6.7.2 accesses or secures access to such computer, computer system or computer network <sup>7</sup>[or computer resource];
- 6.7.3 downloads, copies or extracts any data, computer data base or information from such computer, computer system or computer network including information or data held or stored in any removable storage medium;
- 6.7.4 introduces or causes to be introduced any computer contaminant or

- computer virus into any computer, computer system or computer network;
- 6.7.5 damages or causes to be damaged any computer, computer system or computer network, data, computer data base or any other programmes residing in such computer, computer system or computer network;
- 6.7.6 disrupts or causes disruption of any computer, computer system or computernetwork;
- 6.7.7 denies or causes the denial of access to any person authorised to access any computer, computer system or computer network by any means;
- 6.7.8 provides any assistance to any person to facilitate access to a computer, computer system or computer network in contravention of the provisions of this Act, rules or regulations made thereunder;
- 6.7.9 charges the services availed of by a person to the account of another person by tampering with or manipulating any computer, computer system, or computer network;
2. **Penalty for failure to furnish information, return, etc.**—If any person who is required under this Act or any rules or regulations made thereunder to—
- (a) furnish any document, return or report to the Controller or the Certifying Authority fails to furnish the same, he shall be liable to a penalty not exceeding one lakh and fifty thousand rupees for each such failure;
- (b) file any return or furnish any information, books or other documents within the time specified therefor in the regulations fails to file return or furnish the same within the time specified therefor in the regulations, he shall be liable to a penalty not exceeding five thousand rupees for every day during which such failure continues;
- (c) maintain books of account or records, fails to maintain the same, he shall be liable to a penalty not exceeding ten thousand rupees for every day during which the failure continues.

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## 6.8 Cyber Appellate Tribunal

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Cyber Appellate Tribunal has been established under the Information Technology Act under the aegis of Controller of Certifying Authorities (C.C.A.). The first and the only Cyber Appellate Tribunal in the country has been established by the Central Government in accordance with the provisions contained under Section 48(1) of the Information Technology Act, 2000. The Central Government shall also specify, in the notification referred to in sub-section (1), the matters and places in relation to which the Cyber Appellate Tribunal may exercise jurisdiction. The Cyber Appellate Tribunal has, for the purposes of discharging its functions under the I.T. Act, the same powers as are vested in a civil court under the Code of Civil Procedure, 1908. However, the procedure laid down by the Code of Civil Procedure, 1908 applies but at the same time the Tribunal is guided by the principles of natural justice. Initially, the Tribunal consisted of only one person who was referred to as the Presiding Officer who was to be appointed by way of notification by the Central Government. Thereafter, the Act was amended in the year 2008 by which section 49 which provides for the composition of the Cyber Appellate Tribunal has been changed. As per the amended section, the Tribunal shall consist of a Chairperson and such number of other Members as the Central Government may by notification in the Official Gazette appoint. The selection of

## **THE INFORMATION TECHNOLOGY ACT, 2000**

the Chairperson and Members of the Tribunal is made by the Central Government in consultation with the Chief Justice of India. The Presiding Officer of the Tribunal is now known as the Chairperson. Any person aggrieved by an order made by the Controller or by an Adjudicating Officer appointed under the Information Technology Act, 2000 can prefer an appeal before the Tribunal within 45 days of receiving a copy of the order of the Controller or the Adjudicating Officer.

The Central Government may by notification in the Official Gazette appoint a Controller of Certifying Authorities, and also Deputy and Assistant Controllers whose qualifications, experience and terms and conditions of service may be prescribed by the Government, for discharging the functions provided under section 18 of The Act. The Act empowers the Central Government to appoint an officer not below the rank of a Director to the Government of India or an equivalent officer of a State Government to be an adjudicating officer to hold an enquiry as to whether any person has contravened any provisions of the Act or any rule, regulation or direction or order made there under which renders him liable to pay penalty or compensation. The adjudicating officer appointed under the Act can exercise jurisdiction to adjudicate matters in which the claim for injury or damages does not exceed rupees 5 crore. In respect of claim for injury or damage exceeding rupees five crores, the jurisdiction shall vest with the competent court.

### **Establishment of Cyber Appellate Tribunal**

1. The Central Government notifies and establishes appellate tribunals called Cyber Regulations Appellate Tribunal
2. The Central Government also specifies in the notification all the matters and places which fall under the jurisdiction of the Tribunal

### **Composition of Cyber Appellate Tribunal**

- A Cyber Appellate Tribunal shall consist of one person only (hereinafter referred to as the Presiding Officer of the Cyber Appellate Tribunal) to be appointed, by notification, by the Central Government.
- A person shall not be qualified for appointment as the Presiding Officer of a Cyber Appellate Tribunal unless he- is, or has been, or is qualified to be, a Judge of a High Court, or, is or has been a member of the Indian Legal Service and is holding or has held a post in Grade I of that Service for at least three years.
- No order of the Central Government appointing any person as the Presiding Officer of a Cyber Appellate Tribunal shall be called in question in any manner and no act or proceeding before a Cyber Appellate Tribunal shall be called in question in any manner on the ground merely of any defect in the constitution of a Cyber Appellate Tribunal.

### **Staff of the Cyber Appellate Tribunal**

- (1) The Central Government shall provide the Cyber Appellate Tribunal with such officer and employees as that Government may think fit.
- (2) The officers and employees of the Cyber Appellate Tribunal shall discharge their functions under general superintendence of the Presiding Officer.
- (3) The salaries, allowances and other conditions of service of the officers and employees of the Cyber Appellate Tribunal shall be such as may be prescribed

by the Central Government.

### **Term of Office**

*Section 51 (1)* provides a five-year term for the Chairperson or Member of the Cyber Appellate Tribunal. The term states from the date on which he enters upon his office. It will last for five years or until he attains the age of 65 years, whichever is earlier.

### **Resignation and Removal**

1. The Presiding Officer can resign from his office after submitting a notice in writing to the Central Government, provided:
  - he holds office until the expiry of three months from the date the Central Government receives such notice (unless the Government permits him to relinquish his office sooner), Or
  - he holds office till the appointment of a successor, or
  - until the expiry of his office; whichever is earlier.
2. In case of proven misbehaviour or incapacity, the Central Government can pass an order to remove the Presiding Officer of the Cyber Appellate Tribunal. However, this is only after the Judge of the Supreme Court conducts an inquiry where the Presiding Officer is aware of the charges against him and has a reasonable opportunity to defend himself.
3. The Central Government can regulate the procedure for investigation of misbehaviour or incapacity of the Presiding Officer.

### **Appeal to Cyber Appellate Tribunal**

1. Subject to the provisions of sub-section (2), a person not satisfied with the Controller or Adjudicating Officer's order can appeal to the Cyber Appellate Tribunal having jurisdiction in the matter.
2. No appeal shall lie to the Cyber Appellate Tribunal from an order made by an adjudicating officer with the consent of the parties.
3. The person filing the appeal must do so within 25 days from the date of receipt of the order from the Controller or Adjudicating Officer. Further, he must accompany the appeal with the prescribed fees. However, if the Tribunal is satisfied with the reasons behind the delay of filing the appeal, then it may entertain it even after the expiry of 25 days.
4. On receiving an appeal under sub-section (1), the Tribunal gives an opportunity to all the parties to the appeal to state their points, before passing the order.
5. The Cyber Appellate Tribunal sends a copy of every order made to all the parties to the appeal and the concerned Controller or adjudicating officer.
6. The Tribunal tries to expeditiously deal with the appeals received under sub-section (1). It also tries to dispose of the appeal finally within six months of receiving it.

### **Appeal to High Court**

Any person aggrieved by any decision or order of the Cyber Appellate Tribunal may file an appeal to the High Court within sixty days from the date of communication of the decision or order of the Cyber Appellate Tribunal to him on any question of fact or law arising out of such order Provided that the High Court may, if it is satisfied that the appellant was prevented by sufficient cause from

## THE INFORMATION TECHNOLOGY ACT, 2000

filing the appeal within the said period, allow it to be filed within a further period not exceeding sixty days.

### **Procedure and powers of cyber appellate tribunal**

The Code of Civil Procedure 1908 is an Act to consolidate and amend the laws relating to the procedure of the Courts of Civil Judicature. The objective of the section 58 is that the Tribunal is not bound by the procedure laid down by the Code of Civil Procedure 1908 and instead it shall be guided by the principles of natural justice. The principles of natural justice revolve around the premise that the authority should hear the person concerned before passing any decision, direction or order against him.

In *Union of India v. T. R. Verma*, it said that it is the established law that the tribunals should follow law of natural justice requires that a party should have opportunity of adducing all relevant evidence on which he relies. Evidence should be taken in the presence of the parties and the opportunity to cross examination be given.

Further the Cyber Appellant Tribunal shall have powers to regulate its own procedure including the place at which it shall have its sittings. It is an established law that in the absence of any procedure laid down, the provisions of the Code of Civil Procedure should be followed.

### **The Cyber Appellate Court shall have the powers of:**

1. Summoning and enforcing the attendance of any person and examining him on oath,
2. Requiring the discovery and production of documents or other electronic records,
3. Receiving evidence on affidavits,
4. Issuing commissions for the examination of witness or documents,
5. Reviewing its decisions,
6. Dismissing an application for default or deciding it *ex parte*,
7. Any other matter, which may be prescribed.

### **Recovery of Penalty**

A penalty imposed under this Act, if it is not paid, shall be recovered as an arrear of land revenue and the licensee or the Digital Signature Certificate, as the case may be, shall be suspended till the penalty is paid.

### **❖ CHECK YOUR PROGRESS**

#### **A) LONG QUESTIONS**

1. Discuss Provisions of Electronic Governance.
2. Discuss concept of attribution.
3. Discuss process and provisions regarding Acknowledgement and dispatch of Electronic records.
4. Write a note on Certifying Authority to issues digital signature certificate
5. Discuss various provisions regarding computer system and penalties
6. Write a note: The cyber regulation Appellate tribunal



7. DEFFINATIONS
1. Access
2. Addressee
3. Appropriate Government
4. Certifying Authority
5. Computer
6. Computer Network
7. Data

**B. Multiple-choice question**

1. **Any Cyber Crimes comes under Indian Penal Code Which one of the following is an example?**
  - A. Sending Threatening message by E-mail
  - B. Forgery of Electronic Record
  - C. Bogus Website
  - D. All of above
2. **The Information Technology Act 2000 is an Act of Indian Parliament notified on**
  - A. 27th October 2000
  - B. 15th December 2000
  - C. 17th November 2000
  - D. 17th October 2000
3. **Digital Signature Certificate is a \_\_\_\_\_requirement under various applications**
  - A. Statutory
  - B. Legislative
  - C. Governmental
  - D. Voluntary
4. **Assessing Computer without prior authorization is a cybercrime that comes under**
  - A. Section 65
  - B. Section 66
  - C. Section 68
  - D. Section 70
5. **\_\_\_\_\_means a person who has been granted a licence to issue a electronic signaturecertificate.**
  - A. Certifying Authority
  - B. Certifying Private Key Authority
  - C. Certifying system controller
  - D. Appropriate Authority
6. **\_\_\_is a data that has been organized or presented in a meaningful manner.**
  - A process
  - B. Software
  - C. Storage
  - D. Information
7. **\_\_\_\_\_is an application of information and communication technology (ICT) for deliveringGovernment Service.**
  - A. Governance
  - B. Electronic Governance
  - C. Governance and Ethics
  - D. Risk and Governance.
8. **The Altering of data so that it is not usable unless the changes are undone is**

## THE INFORMATION TECHNOLOGY ACT, 2000

- A. Biometrics B. Encryption C. Ergonomics D. Compression

**9. Authentication is \_\_\_\_\_**

- A. To assure identity of user on a remote system  
B. Insertion  
C. Modification  
D. Integration

**10. The following cannot be exploited by assigning or by licensing the rights of others**

- A. Patent B. Design C. Trademark D. All of the above

**11. The investigator has to take the following precautions while collecting evidence (which option is incorrect):**

- A. videotaping the scene, to document the system configuration and the initial condition of the site before arrival  
B. photograph the equipment with its serial number, model number & writing schemes.  
C. seeks Magistrate's permission before investigating a cognizable offence  
D. labelling the evidence

**12. Section 70 - Access or attempt to access by any unauthorized person, a protected computer system as notified by the Government in the Official Gazette where punishment may extend up to 10 yrs. and fine is:**

- A. Cognizable, Bailable  
B. Non-Cognizable, Bailable  
C. Cognizable, Non-Bailable  
D. Non-Cognizable, Non-Bailable

**13. Section 74 – Publication of Digital Signature Certificate for fraudulent purpose, where imprisonment may extend to 2 yrs. or with fine which may extend to Rs. 1 lakh or both is :**

- A. Cognizable, Non-Bailable  
B. Non-Cognizable, Non-Bailable  
C. Cognizable, Bailable  
D. Non-Cognizable, Bailable

**14. When to start investigation:**

- A. after receiving permission from Cyber Cell  
B. after receiving authority from Sr. Inspector of Police  
C. in case of cognizable offence after lodging of the FIR under Section 154 of Cr. P..  
D. as soon as non-cognizable offence is brought to the notice of Police

**15. Hacking means:**

- A. unauthorized attempts to bypass the security mechanisms of an information system or network.  
B. use of information and communication technologies to support deliberate, repeated and hostile behaviour

- C. a form of fraud or cheating of another persons' identity in which someone pretends to besomeone else by assuming that person's identity.
- D. without the permission of the owner to download computer data.

**16. Data theft includes:**

- A. unauthorized attempts to bypass the security mechanisms of an information system or network.
- B. use of information and communication technologies to support hostile behaviour
- C. a form of fraud or cheating of another persons' identity
- D. without the permission of the person who is in charge of the computer, to download, copy orextract any data, computer data base or information from computer.

**17. In the following case the Hon'ble Supreme Court struck down Section 66 A of eh I.T. Act:**

- A. Kartar Singh v/s State of Punjab
- B. Maneka Gandhi v/s UOI
- C. K. A. Abbas v/s UOI
- D. Shreya Singhal v/s UOI

**18. The following laws / sections were amended / passed to combat pornography of an aggravated form:**

- A. Section 134 of the Indian Evidence Act, 1872
- B. Sections 66 A and 66 B of the I.T. (Amendment) Act, 2008
- C. Section 13 of the POCSSO Act, 2012 was passed to deal with such offences
- D. Section 376 of the Indian Penal Code

**19. Prosecution has to give copies of:**

- A. all electronic records relied upon by the prosecution to the Accused
- B. only those copies of the electronic records which are contained external hard disk, pen drives, CD;s, etc.
- C. non-electronic records involved in the case to the Accused
- D. only certain electronic documents to the Accused

**20. The following Section draws a presumption that a secure electronic record has not been altered since the point of time to which the secure status relates:**

- A. Section 85 B of the Indian Evidence Act, 1872
- B. Section 3 of the I.T. Act, 2000
- C. Section 192 of the Indian Penal Code, 1860
- D. Section 200 of Cr. P. C.

**MCQ Answer**

1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20
D	D	A	B	A	D	B	B	A	C	C	C	D	C	A	D	D	B	B	A

**7.0 INTRODUCTION****7.1 COPYRIGHTS****7.2 PATENTS****7.3 TRADEMARKS****7.4 DESIGNS****7.5 GEOGRAPHICAL INDICATORS****CHECK YOUR PROGRESS**

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**7.0 INTRODUCTION**

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Intellectual property (IP) refers to creations of the human mind such as inventions, literary and artistic works, and symbols, names, images and designs used in commerce. Intellectual property is divided into two categories: Industrial property which includes inventions (patents), trademarks, industrial designs, and geographic indications of source; and Copyright which includes literary and artistic work such as novels, poems and plays, films, musical works, artistic works such as drawings, paintings, photographs and sculptures, and architectural designs. Rights related to copyright include those of performing artists in their performances, producers of phonograms in their recordings, and those of broadcasters in their radio and television programs. Intellectual property rights protect the interests of creators by giving them property rights over their creations.

The most noticeable difference between intellectual property and other forms of property, however, is that intellectual property is intangible, that is, it cannot be defined or identified by its own physical parameters. It must be expressed in some discernible way to be protectable. Generally, it encompasses four separate and distinct types of intangible property namely — patents, trademarks, copyrights, and trade secrets, which collectively are referred to as intellectual property. However, the scope and definition of intellectual property is constantly evolving with the inclusion of newer forms under the gambit of intellectual property. In recent times, geographical indications, protection of plant varieties, protection for semi-conductors and integrated circuits, and undisclosed information have been brought under the umbrella of intellectual property.

Intellectual property laws and enforcement vary widely from one jurisdiction to another. There are inter-governmental efforts to harmonise them through international treaties such as the 1994 World Trade Organization (WTO) Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs), while other treaties may facilitate registration in more than one jurisdiction at a time.

With companies, institutions and individuals constantly forging ahead in newer fields and geographical territories and with path breaking inventions becoming

the norm, the field of Intellectual Property Rights has assumed primordial importance, especially in emerging economies like India.

The TRIPS Agreement, which came into effect on 1 January 1995, is to date the most comprehensive multilateral agreement on intellectual property. The areas of intellectual property that it covers are:

- (i) Copyright and related rights (i.e., the rights of performers, producers of soundrecordings and broadcasting organizations)
- (ii) Trademarks including service marks
- (iii) Geographical indications including appellations of origin
- (iv) Industrial designs
- (v) Patents including protection of new varieties of plants
- (vi) The lay-out designs (topographies) of integrated circuits
- (vii) The undisclosed information including trade secrets and test data

### **Intellectual Property System in India (Historic Background)**

Intellectual Property Right (IPR) in India was imported from the west. The Indian Trade and Merchandise Marks Act 1884, was the first Indian Law regarding IPR. The first Indian Patent Law was enacted in 1856 followed by a series of Acts being passed. They are Indian Patents and Designs Act in 1911 and Indian Copyright Act in 1914. Indian Trade and Merchandise Marks Act and Indian Copyright Act have been replaced by Trade and Merchandise Marks Act 1958 and Copyright Act 1957 respectively.

In 1948, the Indian Government appointed the first committee to review the prevailing Patents and Designs legislation. In 1957, Government appointed Justice Rajagobala Ayyangar Committee (RAC) to revise the Patent Law. Rajagobala Ayyangar Committee submitted its report on 1959, the report tried to balance the constitutional guarantee of economic and social justice enshrined in the preamble of the constitution. This report provided the process for Patenting of drugs. This report outlined the policy behind the Indian Patent system.

The theory upon which the patent system is based on, i.e., an opportunity of acquiring exclusive rights in an invention, stimulates technical process in four ways.

1. Encourages research and invention
2. Induces an inventor to disclose his discoveries
3. Offers award for the expenses of developing inventions
4. Provides an inducement to invest capital in new lines of production which might not appear profitable

Based on the Rajagopala Ayyangar Committee Report, a Bill was introduced in the year 1965 and the bill was passed in the Lok Sabha but it lapsed in the Rajya Sabha and once again lapsed in Lok Sabha in the year 1966 due to dissolution of Lok Sabha. But it was reintroduced in 1967 and passed in 1970; the draft rules were incorporated in Patent Act and passed in the year 1971.

The establishment of WTO as a result of institutionalization of international framework of trade calls for harmonization of several aspects of Indian Law relating to Intellectual Property Rights. The TRIPS agreement set minimum standards for protection for IPR rights and also set a time frame within which countries were required to make changes in their laws to comply with the

## INTELLECTUAL PROPERTY RIGHTS (IPR)

required degree of protection. In view of this, India has taken action to modify and amend the various IP Acts in the past few years.

**Patents Act, 1970:** After India became a signatory to the TRIPS agreement forming part of the Agreement establishing the World Trade Organization (WTO) for the purpose of reduction of distortions and impediments to international trade and promotion of effective and adequate protection of intellectual property rights, the Patents Act, 1970 has been amended in the year 1995, 1999, 2002 and 2005 to meet its obligations under the TRIPS agreement.

**Trade Mark Act, 1999:** The law of trademarks is also now modernized under the Trademarks Act of 1999. A trademark is a special symbol for distinguishing the goods offered for sale or otherwise put on the market by one trader from those of another. In India the trademarks have been protected for over four decades as per the provisions of the Trade and Merchandise Mark (TMM) Act of 1958. India became a party to the WTO at its very inception. One of the agreements in that related to the Intellectual Property Rights (TRIPS). In December, 1998 India acceded to the Paris Convention.

**The Designs Act, 2000:** The Designs Act of 1911 has been replaced by the Designs Act, 2000. In view of considerable progress made in the field of science and technology, a need was felt to provide more efficient legal system for the protection of industrial designs in order to ensure effective protection to registered designs, and to encourage design activity to promote the design element in an article of production. In this backdrop, the Designs Act, 2000 has been enacted essentially to balance these interests and to ensure that the law does not unnecessarily extend protection beyond what is necessary to create the required incentive for design activity while removing impediments to the free use of available designs.

**The Geographical Indications of Goods (Registration and Protection) Act, 1999:** Until recently, geographical indications were not registrable in India and in the absence of statutory protection, Indian geographical indications had been misused by persons outside India to indicate goods not originating from the named locality in India. Patenting turmeric, neem and basmati are the instances which drew a lot of attention towards this aspect of the Intellectual property. Mention should be made that under the Agreement on Trade Related Aspects of Intellectual Property Rights (TRIPS), there is no obligation for other countries to extend reciprocal protection unless a geographical indication is protected in the country of its origin. India did not have such a specific law governing geographical indications of goods which could adequately protect the interest of producers of such goods. To cover up such situations it became necessary to have a comprehensive legislation for registration and for providing adequate protection to geographical indications and accordingly the Parliament has passed a legislation, namely, the Geographical indication of Goods (Registration and Protection) Act, 1999.

**Copyright Act, 1957:** Copyright in India is governed by Copyright Act, 1957. This Act has been amended several times to keep pace with the changing times. As per this Act, copyright grants author's lifetime coverage plus 60 years after death. Copyright and related rights on cultural goods, products and services, arise from individual or collective creativity. All original intellectual creations expressed in a reproducible form will be connected as "works eligible for

copyright protections". Copyright laws distinguish between different classes of works such as literary, artistic, musical works and sound recordings and cinematograph films. The work is protected irrespective of the quality thereof and also when it may have very little in common with accepted forms of literature or art.

**The Protection of Plant Varieties and Farmers' Rights Act, 2001:** The concept of Plant Breeders' Rights arises from the need to provide incentives to plant breeders engaged in the creative work of research which sustains agricultural progress through returns on investments made in research and to persuade the researcher to share the benefits of his creativity with society. The issue of enacting a law relating to Plant Varieties Protection and Farmers' Rights in India assumed importance particularly in the wake of TRIPS agreement under WTO which seeks to promote effective protection of Intellectual Property Rights in all fields of technology. Article 27 of TRIPS Agreement defines patentable subject matter and requires member countries to provide for the protection of plant varieties whether by patenting or by an effective *sui generis* system or by any combination thereof.

**The Semi-Conductor Integrated Circuits Layout Design Act, 2000:** Electronics and Information technology is one of the fastest growing sectors that has played a significant role in world economy. This is primarily due to the advancements in the field of electronics, computers and telecommunication. Microelectronics, which primarily refers to Integrated Circuits (ICs) ranging from, Small Scale Integration (SSI) to Very Large-Scale Integration (VLSI) on a semiconductor chip - has rightly been recognized as a core, strategic technology world-over, especially for Information Technology (IT) based society. Design of integrated circuits requires considerable expertise and effort depending on the complexity. Therefore, protection of Intellectual Property Rights (IPR) embedded in the layout designs is of utmost importance to encourage continued investments in R&D to result in technological advancements in the field of microelectronics.

**Trade Secrets:** It may be confidential business information that provides an enterprise a competitive edge. Usually these are manufacturing or industrial secrets and commercial secrets. These include sales methods, distribution methods, consumer profiles, and advertising strategies, lists of suppliers and clients, and manufacturing processes. Contrary to patents, trade secrets are protected without registration.

**Utility Models:** A utility model is an exclusive right granted for an invention, which allows the right holder to prevent others from commercially using the protected invention, without his authorization for a limited period of time. In its basic definition, which may vary from one country (where such protection is available) to another, a utility model is similar to a patent. In fact, utility models are sometimes referred to as 'petty patents' or 'innovation patents'.

The Rules and Laws governing Intellectual Property Rights in India in a nutshell:

1. The Copyright Act, 1957, The Copyright Rules, 1958 and International Copyright Order, 1999
2. The Patents Act, 1970 The Patents Rules, 2003, The Intellectual Property Appellate Board (Patents Procedure) Rules, 2010 and The Patents (Appeals and Applications to the Intellectual Property Appellate Board) Rules, 2011

## INTELLECTUAL PROPERTY RIGHTS (IPR)

3. The Trade Marks Act, 1999, The Trade Marks Rules, 2002, The Trade Marks (Applications and Appeals to the Intellectual Property Appellate Board) Rules, 2003 and The Intellectual Property Appellate Board (Procedure) Rules, 2003
4. The Geographical Indications of Goods (Registration and Protection) Act, 1999 and The Geographical Indications of Goods (Registration and Protection) Rules, 2002
5. The Designs Act, 2000 and The Designs Rules, 2001
6. The Semiconductors Integrated Circuits Layout-Design Act, 2000 and The Semiconductors Integrated Circuits Layout-Design Rules, 2001
7. The Protection of Plant varieties and Farmers' Rights Act, 2001 and The Protection of Plant varieties and Farmers Rights' Rules, 2003
8. The Biological Diversity Act, 2002 and The Biological Diversity Rules, 2004
9. Intellectual Property Rights (Imported Goods) Rules, 2007

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### 7.1 COPYRIGHTS

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Copyright is a right given by the law to creators of literary, dramatic, musical and artistic works and producers of cinematograph films and sound recordings. In fact, it is a bundle of rights including, inter alia, rights of reproduction, communication to the public, adaptation and translation of the work. It means the sole right to produce or reproduce the work or any substantial part thereof in any material form whatsoever (Kartar Singh Giani v. Ladha Singh & Others AIR 1934 Lah 777).

According to Section 14 of the Act, copyright means the exclusive right subject to the provisions of this Act, to do or authorise the doing of any of the following acts in respect of a work or any substantial part thereof, namely:-

**(a) In the case of a literary, dramatic or musical work, not being a computer programme, -**

- (i) To reproduce the work in any material form including the storing of it in any medium by electronic means
- (ii) To issue copies of the work to the public not being copies already in circulation
- (iii) To perform the work in public, or communicate it to the public
- (iv) To make any cinematograph film or sound recording in respect of the work
- (v) To make any translation of the work
- (vi) To make any adaptation of the work
- (vii) To do, in relation to a translation or an adaptation of the work, any of the acts specified in relation to the work in sub-clauses (i) to (vi)

**(b) In the case of a computer programme**

- (i) To do any of the acts specified in clause (a)
- (ii) To sell or give on commercial rental or offer for sale or for commercial rental any copy of the computer programme: Provided that such commercial rental does not apply in respect of computer programmes where the programme itself is not the essential object of the rental.



**(c) In the case of an artistic work**

- (i) To reproduce the work in any material form including depiction in three dimensions of a two-dimensional work or in two dimensions of a three-dimensional work;
- (ii) To communicate the work to the public;
- (iii) To issue copies of the work to the public not being copies already in circulation;
- (iv) To include the work in any cinematograph film;
- (v) To make any adaptation of the work;
- (vi) To do in relation to an adaptation of the work any of the acts specified in relation to the work in sub-clauses (i) to (iv);

**(d) In the case of cinematography and film**

- (i) To make a copy of the film, including a photograph of any image forming part thereof
- (ii) To sell or give on hire, or offer for sale or hire, any copy of the film, regardless of whether such copy has been sold or given on hire on earlier occasions
- (iii) To communicate the film to the public

**(e) In the case of sound recording**

- (i) To make any other sound recording embodying it
- (ii) To sell or give on hire, or offer for sale or hire, any copy of the sound recording regardless of whether such copy has been sold or given on hire on earlier occasions
- (iii) To communicate the sound recording to the public

Explanation: For the purposes of this section, a copy which has been sold once shall be deemed to be a copy already in circulation.

Indian Copyright Act affords separate and exclusive copyright protection to the following 7 clauses of work:

1. Original Literary Work
2. Original Dramatic Work
3. Original Musical Work
4. Original Artistic Work
5. Cinematograph Films
6. Sound recording
7. Computer Programme

**The Criminal Offence**

Any person who knowingly infringes or abets the infringement of the copyright in any work commits criminal offence under Section 63 of the Copyright Act. The minimum punishment for infringement of copyright is imprisonment for six months with the minimum fine of Rs. 50,000/-. In the case of a second and subsequent conviction the minimum punishment is imprisonment for one year and fine of INR one lakh.

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### 7.2 PATENTS

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Patent is a grant for an invention by the Government to the inventor in exchange for full disclosure of the invention. A patent is an exclusive right granted by law to applicants / assignees to make use of and exploit their inventions for a limited period of time (generally

20 years from filing). The patent holder has the legal right to exclude others from commercially exploiting his invention for the duration of this period. In return for exclusive rights, the applicant is obliged to disclose the invention to the public in a manner that enables others, skilled in the art, to replicate the invention. The patent system is designed to balance the interests of applicants / assignees (exclusive rights) and the interests of society (disclosure of invention).

Sec.2(1)(J) –Invention means a **new** product or process involving an inventive step and capable of industrial application

**What is meant by ‘New’?** The invention to be patented must not be published in India or elsewhere, or in prior public knowledge or prior public use with in India or claimed before in any specification in India. A feature of an invention that involves technical advance as compared to the existing knowledge or have economic significance or both and makes the invention not obvious to a person skilled in the art.

#### **Salient Features of the Act**

1. A patent is an exclusive right granted by a country to the owner of an invention to make, use, manufacture and market the invention, provided the invention satisfies certain conditions stipulated in the law.
2. Exclusivity of right implies that no one else can make, use, manufacture or market the invention without the consent of the patent holder.
3. This right is available only for a limited period of time. However, the use or exploitation of a patent may be affected by other laws of the country which has awarded the patent. These laws may relate to health, safety, food, security etc. Further, existing patents in similar area may also come in the way.
4. A patent in the law is a property right and hence, can be gifted, inherited, assigned, sold or licensed.
5. As the right is conferred by the State, it can be revoked by the State under very special circumstances even if the patent has been sold or licensed or manufactured or marketed in the meantime.
6. The patent right is territorial in nature and inventors/their assignees will have to file separate patent applications in countries of their interest, along with necessary fees, for obtaining patents in those countries.
7. A patent is an official document given to an inventor by the government allowing him to exclude anyone else from commercially exploiting his invention for a limited period which is 20 years at present.
8. As per the Supreme Court, the object of Patent Law is to encourage scientific research, new technology and industrial progress. Grant of exclusive privilege to own, use or sell the method or the product patented for a limited period, stimulates new inventions of commercial utility.
9. The price of the grant of the monopoly is the disclosure of the invention at the Patent Office, which, after the expiry of the fixed period of the monopoly, passes into the public domain [M/s Bishwanath Prasad v. Hindustan Metal Industries, AIR1982 SC 1444].

10. By granting an exclusive right, patents provide incentives to individuals, offering them recognition for their creativity and material reward for their marketable inventions. In return for the exclusive right, the inventor has to adequately disclose the patented invention to the public, so that others can gain the new knowledge and can further develop the technology. The disclosure of the invention is thus an essential consideration in any patent granting procedure.

### Types of Patent Applications

1. Ordinary Application
2. Application for Patent of Addition (granted for Improvement or Modification of the already patented invention, for an unexpired term of the main patent).
3. Divisional Application (in case of plurality of inventions disclosed in the main application).
4. Convention application, claiming priority date on the basis of filing in Convention Countries.
5. National Phase Application under PCT.

### Infringement of Patents

Infringement of a patent consists of the unauthorized making, importing, using, offering for sale or selling any patented invention within the India.

### Remedies against infringement of a patented invention

- 1. Interlocutory Injunction:** A patent owner at the start of a trial can request for an interim injunction to restrain the defendant from committing the acts complained of until the hearing of the action or further orders. Permanent injunction is given based on the merits of the case at the end of the trial.
- 2. Relief of damages:** An award of damages focuses on the losses sustained by the claimant. A patent owner is entitled to the relief of damages as compensation to the patentee and not punishment to the infringer.
- 3. Account of profits:** Account of profits focuses on the profits made by the defendant, without reference to the damage suffered by the claimant at the hands of the defendant. The purpose of the account is to prevent the unjust enrichment of the defendant by the use of the claimant's invention. The patent owner may also opt for the account of profits where he has to prove use of invention and the amount of profit derived from such illegal use.

### Penalties

1. Contravention of secrecy provisions relating to certain inventions (Sec.118) - If any person fails to comply with any directions given under section 35 or makes or causes to be made an application in contravention of section 39 he shall be punishable with imprisonment up to 2 years or with fine or with both. (Section 35 deals with secrecy directions relating to inventions relevant for defence purposes and Section 39 deals with residents not to apply for patents outside India without prior permission.
2. Falsification of entries in register, etc. (Sec.119) - If any person makes, or causes to be made, a false entry in any register kept under this Act, he shall be punishable with imprisonment for a term that may extend to 2 years or

with fine or with both.

3. Unauthorized claim of patent rights (Sec.120) - If any person falsely represents that any article sold by him is patented in India or is the subject of an application for a patent in India, he will be punishable with fine that may extend to Rs.1,00,000. The use of words 'patent', 'Patented', 'Patent applied for', 'Patent pending', 'Patent registered' without mentioning the name of the country means they are patented in India or patent applied for in India.
4. Wrongful use of words, 'patent office' (Sec.121) If any person uses on his place of business or any document issued by him or otherwise the words patent office or any other words which reasonably lead to the belief that his place of business is, or is officially connected with, the patent office, he will be punishable with imprisonment for a term that may extend to 6 months, or with fine, or with both.
5. Refusal or failure to supply information (Sec.122) - If any person refuses or fails to furnish information as required under section 100(5) and 146 he shall be punishable with fine, which may go up to Rs.10,00,000/-. If he furnishes false information knowingly, he shall be punishable with imprisonment that may extend to 6 months or with fine or with both.
6. Practice by non-registered patent agents (Sec.123) - Any person practicing as patent agent without registering is liable to be punished with a fine of Rs.1,00,000/- in the first offence and Rs. 5,00,000/- for subsequent offence.
7. Deals with offences by companies (Sec.124) - When offence is committed by a company as well as every person in charge of and responsible to the company for the conducts of its business at the time of the commission of the offence will be deemed to be guilty and will be liable to be proceeded against and punished accordingly. Provided that nothing contained in this sub-section shall render any such person liable to any punishment if he proves that the offence was committed without his knowledge or that he exercised all due diligence to prevent the commission of such offence.

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### 7.3 TRADEMARK

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A trade mark (popularly known as **brand name**) in layman's language is a visual symbol which may be a word signature, name, device, label, numerals or combination of colours used by one undertaking on goods or services or other articles of commerce to distinguish it from other similar goods or services originating from a different undertaking.

1. The selected mark should be capable of being represented graphically (that is in the paper form).
2. It should be capable of distinguishing the goods or services of one undertaking from those of others.
3. It should be used or proposed to be used mark in relation to goods or services for the purpose of indicating or so as to indicate a connection in the course of trade between the goods or services and some person who has the right to use the mark with or without the identity of that person.

Trade Marks are distinctive symbols, signs, logos that help consumer to distinguish between competing goods or services. A trade name is the name of an enterprise which individualizes the enterprise in consumer's mind. It is legally not linked to quality. But, linked in consumer's mind to quality expectation.

### **Key Features of Trademark**

1. Trademark must be Distinctive
2. Trademark must be used in Commerce

### **Types of Trademarks**

1. Trademark
2. Service mark
3. Collective mark
4. Certification mark

### **Functions of Trademark**

Trademark performs four functions

1. It identifies the goods / or services and its origin
2. It guarantees its unchanged quality
3. It advertises the goods/services
4. It creates an image for the goods/ services

### **Offences and Penalties**

There are mainly two classes of Offences relating to Trademarks

1. Falsification of Trademark
2. Falsely applying the trademark to goods or services

The punishment for the above offences shall not be less than 6 months imprisonment which may extend to three years and a fine which shall not be less Rs. 50,000/-, but may extend to INR two lakhs. Wherever the court proposes a lower punishment than the minimum, it has to record, adequate and special reasons for the same.

However, second and subsequent offences shall be more severely punished. There shall be an Imprisonment of not less than one year which may extend to three years and a fine which shall not be less INR one lakh, but may extend to Rupees two lakhs. The court can propose a lower punishment than the minimum, only after recording adequate and special reasons for the same.

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## **7.4 DESIGNS**

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A Design refers to the features of shape, configuration, pattern, ornamentation or composition of lines or colours applied to any article, whether in two or three dimensional (or both) forms. This may be applied by any industrial process or means (manual, mechanical or chemical) separately or by a combined process, which in the finished article appeals to and judged solely by the eye. Design does not include any mode or principle of construction or anything which is mere mechanical device. It also does not include any trade mark or any artistic work.

Industrial designs belong to the aesthetic field, but are at the same time intended to serve as pattern for the manufacture of products of industry or

## INTELLECTUAL PROPERTY RIGHTS (IPR)

handicraft. An industrial design is the ornamental or aesthetic aspect of a useful article, which must appeal to the sense of sight and may consist of the shape and/or pattern and/or colour of article. An industrial design to be protectable, must be new and original. Industrial designs are protected against unauthorised copying or imitation, for a period which usually lasts for five, ten or 15 years.

Textile designs were the first to receive legal protection. As early as in 1787, the first Act for design protection was enacted in the UK for the encouragement of the arts of design. This was an experimental measure extending protection for a limited duration. Shortly thereafter, its life was extended and it was made perpetual. In 1839, the protection under the Act was enlarged to cover "Designs for Printing other woven Fabrics".

An industrial design registration protects the ornamental or aesthetic aspect of an article. Designs may consist of three-dimensional features, such as the shape or surface of an article, or of two-dimensional features, such as patterns, lines or colour. Designs are applied to a wide variety of products of different industries like handicrafts, medical instruments, watches, jewellery, house wares, electrical appliances, vehicles and architectural structures. An industrial design is primarily for aesthetic features.

**The need for registration of Design:** The registration of a design confers upon the registered proprietor the exclusive right to apply a design to the article in the class in which the design has been registered. A registered proprietor of the design is entitled to a better protection of his intellectual property. He can sue for infringement, if his right is infringed by any person. He can license or sell his design as legal property for a consideration or royalty. Registration initially confers this **right for ten years** from the date of registration. It is renewable for a further period of five years. If the fee for extension is not paid for the further period of registration within the period of initial registration, this right will cease. There is provision for the restoration of a lapsed design if the application for restoration is filed within one year from the date of cessation in the prescribed manner.

### **Essential Requirements for Registration of Design** A design should -

1. Be new or original
2. Not be disclosed to the public anywhere by publication in tangible form or by use or in any other way prior to the filing date, or where applicable, the priority date of the application for registration
3. Be significantly distinguishable from known Designs or combination of known designs
4. Not comprise or contain scandalous or obscene matter
5. Not be a mere mechanical contrivance
6. Be applied to an article and should appeal to the eye
7. Not be contrary to public order or morality.

### **Exclusion from Scope of Design**

Designs that are primarily literary or artistic in character are not protected under the Designs Act. These will include:

1. Books, jackets, calendars, certificates, forms-and other documents, dressmaking patterns,greeting cards, leaflets, maps and plan cards, postcards, stamps, medals
2. Labels, tokens, cards, cartoons
3. Any principle or mode of construction of an article
4. Mere mechanical contrivance
5. Buildings and structures
6. Parts of articles not manufactured and sold separately
7. Variations commonly used in the trade
8. Mere workshop alterations of components of an assembly
9. Mere change in size of article
10. Flags, emblems or signs of any country
11. Layout designs of integrated circuits

### **Piracy (Infringement) of Registered Design**

During the existence of copyright over any design, other persons are prohibited from using the design except or with the permission of the proprietor, his licensee or assignee. Piracy of a design means the application of a design or its imitation to any article belonging to the class of articles in which the design has been registered for the purpose of sale or importation of such articles without the written consent of the registered proprietor. Publishing such articles or exposing them for sale with knowledge of the unauthorized application of the design to them also involves piracy of the Design. The following activities are considered to be **infringement**:

1. To apply the design or any fraudulent imitation of it to any article for sale;
2. To import for sale any article to which the design or fraudulent or obvious imitation of it,has been applied;
3. To publish or to expose for sale knowing that the design or any fraudulent or obvious imitation of it has been applied to it.

### **Penalties**

A registered proprietor can institute a suit for injunction as well as recovery of damages against any person engaged in piracy of the registered design. Such legal proceedings can be instituted from the date of registration and till the expiry of copyright. However, in case of reciprocity application, the registered proprietor can claim damages only from the actual date on which the design is registered in India.

If any person commits piracy of a registered design, as defined in Section 22, he shall be liable to pay for a payment of a sum not exceeding Rs. 25,000/- recoverable as contract debt. However, the total sum recoverable in respect of any one design shall not exceed Rs. 50,000/-

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## **7.5 GEOGRAPHICAL INDICATIONS**

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Geographical Indications of Goods are defined as that aspect of industrial property which refers to the geographical indication referring to a country or to a place situated therein as being the country or place of origin of that product. A product's quality, reputation or other characteristics can be determined by where it comes from.

## **INTELLECTUAL PROPERTY RIGHTS (IPR)**

Geographical indications (GIs) are place names (in some countries also words associated with a place) used to identify products that come from these places and have these characteristics (for example, Champagne, Scotch whisky, Tequila, or Roquefort).

Geographical indications serve to recognize the essential role geographic and climatic factors and/or human know-how can play in the end quality of a product. Like trademarks or commercial names GIs are also IPRs, which are used to identify products and to develop their reputation and goodwill in the market. The Agreement on Trade Related Aspects of Intellectual Property (TRIPS), prescribes minimum standards of protection of GIs and additional protection for wines and spirits.

### **What is a Geographical Indication?**

1. It is an indication
2. It originates from a definite geographical territory
3. It is used to identify agricultural, natural or manufactured goods
4. The manufactured goods should be produced or processed or prepared in that territory
5. It should have a special quality or reputation or other characteristics

### **Examples of Indian Geographical Indications -**

1. Solapur Chaddar
2. Solapur Terry Towel
3. Basmati Rice
4. Darjeeling Tea
5. Kanchipuram Silk Saree
6. Alphanso Mango
7. Nagpur Orange

The Object of the Geographical Indications of Goods (Registration and Protection) Act, 1999 is three-fold, firstly by specific law governing the geographical indications of goods in the country which could adequately protect the interest of producers of such goods, secondly, to exclude unauthorized persons from misusing geographical indications and to protect consumers from deception and thirdly, to promote goods bearing Indian geographical indications in the export market.

### **Salient Features Geographical Indications of Goods (Registration and Protection) Act,1999**

The salient features of Geographical Indications of Goods (Registration & Protection) Act,1999 are as under:

1. Definitions and interpretations of several important terms like 'geographical indication', 'goods', 'producers', 'packages', 'registered proprietor', 'authorized user', etc.
2. Provision for the maintenance of a Register of Geographical Indications in two parts-Part A and Part B and use of computers etc. for maintenance of such Register. While Part A will contain all registered geographical indications, Part B will contain particulars of registered authorized users.Registration of geographical indications of goods in specified classes
3. Prohibition of registration of certain geographical indications



4. Provisions for framing of rules by Central Government for filing of application, its contents and matters relating to substantive examination of geographical indication applications
5. Compulsory advertisement of all accepted geographical indication applications and for inviting objections
6. Registration of authorized users of registered geographical indications and providing provisions for taking infringement action either by a registered proprietor or an authorized user
7. Provisions for higher level of protection for notified goods
8. Prohibition of assignment etc. of a geographical indication as it is public property
9. Prohibition of registration of geographical indication as a trademark
10. Appeal against Registrar's decision would be to the Intellectual Property Appellate Board established under the Trade Mark legislation
11. Provision relating to offences and penalties.
12. Provision detailing the effects of registration and the rights conferred by registration
13. Provision for reciprocity powers of the registrar, maintenance of Index, protection of homonymous geographical indications etc.

### **Offences and Penalties**

Chapter VIII of the Act details certain acts as offences punishable by imprisonment or with fine or with both. The legislature has taken a strong view of infringement, piracy, falsification, misrepresentation and has now made them penal offences. The chapter apart from listing penalties for the above-mentioned offences also details the penalty and procedure of prosecution.

#### **The following are the acts deemed as offences:**

In the context of offences, what constitutes the meaning of applying geographical indication has been dealt with in Section 37 and the expression geographical indication has been defined in Section 2 (1) (e). Section 38 lists two kinds of offences namely:

#### **(a) Falsifying a GI and**

#### **(b) Falsely applying a GI**

1. The penalty for falsification of GIs and the circumstances in which a person applies false GI are enumerated in Section 39
2. Selling goods to which false GI is applied as outlined in Section 40
3. Enhanced Penalty for subsequent convictions for the offences of falsifying, falsification of GIs or selling goods with false GIs
4. Falsely representing a GI as registered as listed in Section 42. Misrepresenting the GI as Registered, which has not been actually registered is an Offence
5. Improperly describing a place of business as connected with the GIs Registry as listed in Section 43
6. Falsification of entries in the Register as listed in Section 44
7. No offence in certain cases as provided under Section 45
8. Exemption of certain persons employed in ordinary course of business as provided under Section 46
9. Procedure where invalidity of registration is pleaded by the accused as provided in Section 18

### Infringement of Geographical Indication

A registered geographical indication is infringed if an unauthorized user uses it to indicate or suggests that certain goods originate from a geographical area other than the true place of origin in a manner which misleads the public as to the geographical origin of the goods, or when use of the geographical indication results in unfair competition. This includes passing off in respect of a registered geographical indication, or when the use of another geographical indication results in false representation to the public that goods originate from a territory in respect of which there is a registered geographical indication. The registered proprietor or the authorized users of a registered geographical indication can initiate an infringement action.

### CHECK YOUR PROGRESS

#### Descriptive Questions

1. What are intellectual property rights? Explain the law in India with respect to its salient features.
2. Explain the intellectual property rights law in India in light of its historical background.
3. Explain in detail the laws related to patents and trademarks.
4. Explain in detail the laws related to designs and geographical indications.

#### Short Notes

1. Patents under IPR Act
2. Trademarks under IPR Act
3. Designs under IPR Act
4. Copyrights under IPR Act
5. Geographical Indications under IPR Act

#### Multiple Choice Questions

- 1. The law formed to protect the creations of the human mind like inventions artwork designs etc.**
  - a. Consumer protection act
  - b. Intellectual Property Rights
  - c. Right to information act
  - d. none of the above
- 2. According to the Indian IPR act, creations like books, software and artwork are protected by;**
  - a. Patents
  - b. Copyrights
  - c. Trademarks
  - d. Geographical Indications.
- 3. A brand name is a classic example of;**
  - a. Patents
  - b. Copyrights

- c. Trademarks
- d. Geographical Indications.

**4. Which of the following is an intellectual property as per IPR Laws in India?**

- a. Original literary work
- b. Industrial Design of Maruti800 car
- c. Trademark of Tata company
- d. All the above

**5. A company wishes to ensure that no one else can use their logo.**

- a. Copy rights
- b. Trade mark
- c. Patent
- d. Industrial designs

**6. A singer wishes to assign the rights to reproduce a video she has made of her concert.**

- a. Copy rights
- b. Trade mark
- c. Patent
- d. Industrial designs

**7. A new way to process milk so that there is no fat in any cheese made from it.**

- a. Copy rights
- b. Trade mark
- c. Patent
- d. Industrial designs

**8. Intellectual Property Rights (IPR) protect the use of information and ideas that are of**

- a. Social Value
- b. Moral Value
- c. Commercial Value
- d. Ethical Value

**9. Which of the following is not an intellectual property law?**

- a. Copyright Act, 1957
- b. Trademark Act, 1999
- c. Patent Act, 1970
- d. Customs Act, 1962

**10. Copyright law applies to forms of expression contained in,**

- a. Song lyrics and musical compositions
- b. Sculptures and paintings
- c. Dramatic and literary works
- d. All of the above

## INTELLECTUAL PROPERTY RIGHTS (IPR)

### 11. The term of copyright for an author lasts how long?

- a. The life of the author
- b. The life of the author plus 60 years
- c. 95 years
- d. 75 years

### 12. The rights of a patentee are:

- a. Sell or distribute
- b. License
- c. Assign the property to others
- d. All of the above

### MCQ Answer key

1.	2.	3.	4.	5.	6.	7.	8.	9.	10.	11.	12.
<b>b</b>	<b>b</b>	<b>c</b>	<b>d</b>	<b>b</b>	<b>a</b>	<b>c</b>	<b>c</b>	<b>d</b>	<b>d</b>	<b>b</b>	<b>d</b>

- 8.0 INTRODUCTION**
  - 8.1 FORMATION OF COMPANY**
  - 8.2 MEMORANDUM OF ASSOCIATION**
  - 8.3 ARTICLES OF ASSOCIATION**
  - 8.4 PROSPECTUS**
  - 8.5 SHRECAPITAL**
  - 8.6 COMPANY AUDITOR**
  - 8.7 DIRECTOR**
  - 8.8 GENRAL METTINGS**
  - 8.9 WINDING UP OF COMPANY**
- CHECK YOUR PROGRESS**

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**8.0 INTRODUCTION**

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Originally AOP- Association of Persons who took their meals together. During such gatherings they used to discuss business problems and arrive at feasible solutions Over a period of time they realized business decisions taken as a group were more effective. Hence the concept of Company was born.

The word Company is derived from a Latin roots, *com* 'together' + *pani* 'bread'

**COMPANY****Definition of a company**

According to Lord Justice Lindley,  
A company means

- ❖ An association of many persons
- ❖ Who contribute money or money's worth
- ❖ To a common stock
- ❖ And employ it for a common purpose

**CHARACTERISTICS OF COMPANY**

1. **Separate legal entity**
2. **Artificial person**
3. **Compulsory incorporation**
4. **Separate property**
5. **Common seal**
6. **Perpetual succession**
7. **Separate management**
8. **Transferability of shares**

9. **Diffusion of ownership**
10. **Number of members**
11. **Voting rights**
12. **Tax liability**

### **SEPARATE LEGAL ENTITY**

A company has an individual corporate legal existence. Company and its members are separate. The property of the company and that of the members are separate. Suits (cases) are filed in its own name

### **ARTIFICIAL PERSON**

A company is a juristic person. It has a domicile but it is not treated as a citizen. It is a creation of law, an artificial person, it has no soul, no body, no conscience. It can sue and be sued in its own name

### **COMPULSORY INCORPORATION**

It must be incorporated or *registered* under the Companies Act. Company takes birth due to law and comes to an end by the procedure of law. It comes into existence when ROC–Registrar of Companies, enters its name in the register and issue a certificate of incorporation

### **SEPARATE PROPERTY**

As a company is a legal person distinct from its members, it is capable of owning, enjoying and disposing of property in its own name. Although its capital and assets are contributed by its shareholders, they are not the private and joint owners of its property. The company is the real person in which all its property is vested and by which it is controlled, managed and disposed of.

### **COMMON SEAL**

Company being an artificial person has to work through the agency of human beings such as directors, managers and employees. So, it cannot sign documents for itself. *Official signature* of the company. Of course, signatures of 2 directors as witnesses are necessary in addition to the common seal. The seal is affixed on the contracts, share certificates, documents and day to day transactions of the company

### **PERPETUAL EXISTENCE (OR SUCCESSION)**

Member may come and go but the company can go on forever. It continues to exist even if all its members are dead. The existence of company can be terminated only by law. For example, all members of a private company were killed by a bomb while in a general meeting held, the company continues to exist through the legal heirs of the deceased parties or member.

### **SEPARATE MANAGEMENT**

Company is the only form of business organization where ownership and

management are in two different hands. Shareholders are the people who own and board of directors are the people who manage.

### **TRANSFERABILITY OF SHARES**

A share of a company is a movable property and can be transferable. A member can enjoy a statutory right to sell his shares and get them transferred in the name of the buyer. *Shares are the liquid asset and can be readily converted into cash.* Transferability is subject to the provisions of company law and its articles of association. However, in private company there are certain restrictions on transferability of shares.

### **LIMITED LIABILITY**

In case of the company limited by shares, the liability of the shareholders is limited up to the extent of face value of shares. In case where the company goes into winding up and the shares are fully paid up the shareholder doesn't have any liability but where the shares are partly paid up the shareholders liability will be up to the unpaid value of shares.

In case of the company limited by guarantee, the liability of the shareholder will be limited up to the guaranteed amount agreed upon.

### **DIFFUSION OF OWNERSHIP**

Total capital of a company is divided into small portions / units known as shares.  
 Private company - Finance is contributed through mutual agreement by members  
 Public company - Collects capital from general public by the sale of shares.  
 Ownership of the company is in the hands of a large number of people called shareholders

### **NUMBER OF MEMBERS**

Private company - minimum – 2 and maximum – 200  
 Public company - minimum – 7 and maximum – no limit  
 OPC - one person company - only one member

### **VOTING RIGHTS**

Voting right depends on number of shares.

The members of company can vote as per number of shares they hold.

If they hold more share, they can exercise more control over the management.

### **TAX LIABILITY**

In comparison to sole proprietorship and partnership tax liability is very low in case of a company. Also, there are tax-related incentives as well.

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## **8.1 FORMATION OF COMPANY**

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### **(A) Number of Persons required in formation of a company**

A company may be formed for any lawful purpose by—

- (a) 7 or more persons (Public Company)
- (b) 2 or more persons (Private Company)

- (c) 1 person (One Person Company)

**Types of companies based on liability of members.**

A company formed may be either —

- (a) A company limited by shares
- (b) A company limited by guarantee
- (c) An unlimited company

**(B) SECTION 7 INCORPORATION OF COMPANY**

**1. Documents**

The list of documents is mentioned in detail later and will also be discussed in class.

**2. Certificate of Incorporation**

The Registrar on the basis of documents and information filed shall register all the documents and issue a certificate of incorporation in **Form INC-11** that the proposed company is incorporated under this Act.

**3. COI**

The Certificate of Incorporation shall be issued by the Registrar in **Form No.INC-11** and the Certificate of Incorporation shall mention **PAN number** of the company where if it is issued by the Income-tax Department.

**Allotment of CIN**

On and from the date mentioned in the certificate of incorporation issued, the Registrar shall allot to the company a **CORPORATE IDENTITY NUMBER**, which shall be a distinct identity for the company and which shall also be included in the certificate.

**4. Penalty for providing false information to registrar in the event of Incorporation**

If any person furnishes any **false or incorrect particulars of any information or suppresses any material information**, of which he is aware in any of the documents filed with the Registrar in relation to the registration of a company, he shall be liable for action under **section 447**.

**Punishment for fraud u/s 447 (Mega 447)**

{6 months/3 years} < Imprisonment < {10 years} AND

Fraud Amount (100%) < Penalty < 3 X Fraud Amount (300%)

Where the fraud in question **involves public interest**, the term of imprisonment shall not be less than 3 years

**Punishment for fraud u/s 447 (Mini 447)**

Where the fraud amount < Lower of: (1) Rs. 10 Lacs or (2) 1% of the Turnover.

**AND** does NOT involve Public Interest, Punishment shall be:- Imprisonment < 5



years OR

Fine < **Rs. 50 Lacs** OR (Amendment)

Or BOTH

#### **4. Other Consequences of providing False information to Registrar**

Without prejudice to the above provisions, where a company has been incorporated by furnishing any false or incorrect information or representation or by suppressing any material fact or information in any of the documents or declaration filed or made for incorporating such company or by any fraudulent action, the Tribunal may, on an application made to it, on being satisfied that the situation so warrants—

- (a) Pass such orders, as it may think fit, for regulation of the management of the company including **changes in its memorandum and articles, in public interest or in the interest** of the company and its members and creditors; or
- (b) Direct that liability of the members shall be **unlimited**; or
- (c) Direct **removal of the name** of the company from the register of companies:or
- (d) Pass an order for the **winding up** of the company; or
- (e) Pass such other orders as it may deem fit:

Provided that before making any order under this sub-section—

- 1. The company shall be given a reasonable opportunity of **being heard** in the matter;and
- 2. The tribunal shall take into consideration the **transactions entered** into by the company, including the obligations, if any, contracted or payment of any liability.

#### **(C) CENTRAL REGISTRATION CENTERE (CRC)**

The CRC shall be located at **Indian Institute of Corporate Affairs (IICA)**, Plot No.6,7, 8, Sector 5, IMT Manesar, District Gurgaon (Haryana), Pin Code-122050. Central Registration Centre (CRC) shall have territorial jurisdiction all over India, forcarrying out the following functions: -

- 1) CRC shall carry out the function of processing and disposal of applications for **reservation of names through web service SPICe+ (INC-32)**  
An application for reservation of name shall be made through the web service available at [www.mca.gov.in](http://www.mca.gov.in) by using **web service SPICe+ (INC-32)** and for change of name by using **web service RUN (Reserve Unique Name)**.
- 2) Processing and disposal of e-forms and all related matters pertaining to **registration of companies under section 7 and 8** of the Companies Act,

2013 having territorial jurisdiction all over India.

- 3) The CRC shall **process forms pertaining to registration of companies.**
- 4) CRS shall exercise jurisdiction, processing and approval of name or names proposed in e-Form **number SPICe+ INC - 32** hitherto exercised by the respective Registrar of companies.

The **jurisdictional Registrar of companies**, other than Registrar CRC, within whose jurisdiction the registered office of the company is situated shall continue to have jurisdiction over the companies for all other provisions of the Act.

<b>Purpose</b>	<b>Web-service to be used w.e.f 15.2.2020</b>
<b>Reservation of Name</b>	<b>SPICe+ (INC-32)</b>
<b>Change of Name</b>	<b>RUN</b>
<b>Theory</b>	

**(D) Simplified Proforma for Incorporating Companies electronically Plus (SPICe+)**

**3 massive changes brought about by the CG in the incorporation procedure of the Companies.**

**Unified Single Procedure**

- 1) Establishing **CRC** (Gurugram) for Speedy Incorporation.
- 2) **SPICe+ forms** for incorporating **ALL** companies Form INC-2 & INC-7 has been eliminated now.
- 3) Registration fees exempted for following types of companies:
  - (a) Companies having Nominal Capital of **< Rs. 15 lakhs**
  - (b) Companies not having a share capital whose number of members as stated in the articles of association **< 20 members.**

**Steps for incorporating companies**

**Step 1 - Reservation of Name (w.e.f. 15 February 2020)**

Reserve a Unique Name for **20 days** by using the **SPICe+ (INC-32) Application** on MCA website, which may either be approved or rejected, as the case may be, by the Registrar, Central Registration Centre after allowing re-submission of such web-form within 15 days for rectification of the defects, if any.

**Step 2 - File the following Forms**

File the following Forms **within next 20 days:-**

#	Form No.	Description
(a)	INC-32 (SPICe+)	Incorporation Form
(b)	INC-33	e-Memorandum of Association (e-MOA)
(c)	INC-34	e-Articles of association (e-AOA)
(d)	INC-35 (AGILEPRO)	AGILE PRO (Application for GSTIN, ESI plus EPF, P. Tax Registration and Opening of Bank a/c)
(e)	INC-8	Declaration by <b>Professionals</b> (advocate, CA, CMA or CS in practice) shall be attached.
(f)	INC-9	Declaration shall be submitted by each of the <b>subscribers</b> to the memorandum and each of the <b>first directors</b> named in the articles.
(g)	DIR-12	Particulars of <b>first director</b> of the company and his interest in other firms or bodies corporate along with his <b>consent</b> to act as director of the company shall be filed.
(h)	INC-22	<b>Filing of Registered Office Address</b> A company may furnish verification of its registered office: 1) In Form INC-32 (SPICe+) at the time of incorporation or In Form INC-22 within 30 days of incorporation.

**All Incorporation related documents shall be kept at the registered office only.**

**Step 3 - Issue of COI by Central Registrar**

The Certificate of Incorporation shall be issued by the Registrar in **Form No. INC-11** and the Certificate of Incorporation shall mention

- (a) PAN of the company where if it is issued by the Income-tax Department.
- (b) CIN of the company allotted by Registrar.

**Notes: -**

Theme	Details
Signature	The subscribers and witness or witnesses shall affix their digital signatures to the e-MoA and e-AoA.
> 7 members Or Subscriber outside India	In case of incorporation of a company <b>having more than 7 subscribers or where any of the subscriber to the MOA/AOA is signing at a place outside India</b> , MOA/AOA shall be filed with INC- 32 (SPICe+) in the respective formats as specified in Table A to J in Schedule I <b>without</b> filing form INC-33 and INC- 34.

Upto 3 DIN	Allotment of <b>Director Identification Number (DIN)</b> of Maximum of 3 proposed directors shall be permitted in Form INC-32 (SPICe+).
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**(E) COMMENCEMENT OF BUSINESS (AMENDMENT)****Filing of INC-20A Section 10A(1)**

A company incorporated after the commencement of the Companies (Amendment) Act, 2019 and having a share capital shall not commence any business or exercise any borrowing powers unless—

- a. a declaration in **Form INC-20A certified by CA, CS, CMA in practise** is filed by a director within a period of 180 days of the date of incorporation of the company, with the Registrar that every subscriber to the memorandum has paid the value of the shares agreed to be taken by him on the date of making of such declaration; and
- b. the company has filed with the Registrar a verification of its registered office in SPICe+ (INC-32) at the time of incorporation or INC-22 within 30 days of incorporation.

**Punishment Section 10A(2)**

If any default is made in complying with the requirements of this section, then punishment shall be as follows:

On Company	Fine < Rs. 50,000
On officer in default	Fine of Rs. 1,000 for each day during which such default continues but < Rs. 1,00,000.

**Striking Off by ROC Section 10A(3)**

Where no declaration has been filed with the Registrar within a period of 180 days of the date of incorporation of the company and the Registrar has reasonable cause to believe that the company is not carrying on any business or operations, he may, without prejudice to the provisions of sub-section (2), initiate action for the removal of the name of the company from the register of companies under **Chapter XVIII (Striking Off)**.

**SECTION 11 COMMENCEMENTS OF BUSINESS, ETC****Removal of the ‘Certificate of Commencement of Business’**

**[Omitted via Amendment Act, 2015] - Section 11 of the principal Act, shall be omitted.**

**8.2 MEMORANDUM OF ASSOCIATION (SECTION 4)****Contents of Memorandum of Association**

The memorandum of a company shall state—

1. **Name Clause** - The name of the company with the last word ‘Limited’ in the case of a public limited company, or the last words ‘Private Limited’ in the

case of a private limited company:

2. **Provided that nothing in this clause shall apply to a company registered under section 8**
3. **Situation Clause** - The State in which the registered office of the company is to be situated;
4. **Objects Clause** - The objects for which the company is proposed to be incorporated and any matter considered necessary in furtherance thereof;
5. **Liability Clause** - The liability of members of the company. whether limited or unlimited, and also state—
  - (i) In the case of a company limited by shares, that liability of its members is limited to the amount unpaid, if any, on the shares held by them; and
  - (ii) In the case of a company limited by guarantee, the amount up to which each member undertakes to contribute—
    - (A) To the assets of the company in the event of its being wound- up and
    - (B) To the costs, charges and expenses of winding-up;
6. **Capital Clause** - in the case of a company having a share capital, the amount of share capital with which the company is to be registered and the division thereof into shares;
7. **Subscription Clause** - The number of shares each subscriber to the memorandum intends to take, indicated opposite his name;
8. **Nominee Clause (in case of an OPC)** - in the case of One Person Company. the name of the person who, in the event of death of the subscriber, shall become the member of the company.

#### **Restriction on Undesirable names**

The name stated in the memorandum shall not—

- (a) Be identical with or resemble too nearly to the name of an existing company registered under this Act or any previous company law; or
- (b) Be such that its use by the company—
  - (i) Will constitute an offence under any law for the time being in force; or
  - (ii) Is **UNDESIRABLE** in the opinion of the Central Government.

**See Rule 8 of the Companies (Incorporation) Rules, 2014 - Undesirable names.**

#### **Name of Company not to indicate Government patronage**

A company shall not be registered with a name which contains—

- (a) Any word or expression which is likely to give the impression that the company is in any way connected with, or having the patronage of, the CG, any SG, or any local authority, body corporate; or
- (b) Such word or expression, as may be prescribed, **unless the previous approval of the CG has been obtained** for the use of any such word or expression.

#### **Application to ROC for Reservation of Name**

A person may make an application, in **Form INC-1** to the Registrar for the reservation of a name set out in the application as—

- (a) the name of the proposed company; or

the name to which the company proposes to change its name.

<b>Purpose</b>	<b>Web-service to be used</b>
<b>Reservation of Name</b>	<b>SPICe+ (INC-32)</b>
<b>Change of Name</b>	<b>RUN</b>

**Reservation of Name by ROC**

(i) Upon receipt of an application as above, the Registrar may, on the basis of information and documents furnished along with the application, reserve the name for a period of **20 days** from the date of approval or such other period as may be prescribed.

Provided that in case of an application for reservation of name or for change of its name by an existing company, the Registrar may reserve the name for a period of **60 days** from the date of approval.

(ii) Where after reservation of name, it is found that name was applied by furnishing wrong or incorrect information, then—

**Case I**

If the company has not been incorporated, the reserved name shall be **cancelled** and the person making application in INC-1 shall be liable to a **penalty** which may extend to Rs. 1,00,000.

**Case II**

If the company has been incorporated, the Registrar may, after giving the company an opportunity of being heard—

- (i) Either direct the company to **change its name within a period of 3 months**, after passing an ordinary resolution;
- (ii) Take action for **striking off** the name of the company from the register of companies; or
- (iii) Make a petition for **winding up** of the company.

**Format of Memorandum**

The memorandum of a company shall be in respective forms specified in Tables A, B, C, D and E in Schedule I as may be applicable to such company.

**Exemption-Govt Companies**

In the name of a Government Company, the word ‘Limited’ shall be inserted irrespective of Private/Public.

**Rule 26 - Publication of name by company**

- 1. Every company which has a website for conducting online business or

otherwise, shall disclose/publish its name, address of its registered office, the Corporate Identity Number, Telephone number, fax number if any, email and the name of the person who may be contacted in case of any queries or grievances on the landing /home page of the said website.

2. The CG may as and when required, notify the other documents on which the name of the company shall be printed.

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### **8.3 ARTICLES OF ASSOCIATION (SECTION 5)**

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#### **Articles to contain Regulations for Management**

The articles of a company shall contain the regulations for management of the company.

#### **Provision for Entrenchment Regulations (E.R) in the AOA - Hard to alter E.R.**

The articles may contain provisions for entrenchment to the effect that specified provisions of the articles may be altered only if conditions or procedures as that are more restrictive than Special Resolution, are met or complied with.

#### **Approval required for Introducing**

The provisions for entrenchment referred above shall only be made either on formation of a company, or by an amendment in the articles agreed to by

#### **Entrenchment regulation in the AOA**

- (a) **All the members** of the company in the case of a private company and
- (b) A **Special Resolution** in the case of a public company.

#### **Notice to Registrar for entrenchment**

#### **Rules 10 - Where Articles Contains Entrenchment Provisions**

Where the articles contain the provisions for entrenchment, the company shall give notice to the Registrar of such provisions in **Form No INC-32 (SPICe)** at the time of incorporation of the company or in case of existing companies, the same shall be filed in Form No. MGT.14 within 30 days from the date of entrenchment of the articles.

#### **Articles to be in Respective Form**

The articles of a company shall be in respective forms specified in Tables, F, G, H, I and J in Schedule 1 as may be applicable to such company.

#### **Option for adoption of Table F**

A company may adopt all or any of the regulations contained in Table F.

**Table F shall apply unless they are excluded from the Articles**

In case of any company, which is registered after the commencement of this Act, in so far as the registered articles of such company do not exclude the regulations contained in Table F, then the regulations in Table F shall apply to such Company on matters which are not prescribed in its own AOA.

**Articles registered under Previous Acts**

Nothing in this section shall apply to the articles of a company registered under any previous company law unless amended under this Act.

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**8.4 PROSPECTUS**

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(A) **Prospectus [Section 2(70)]** ‘prospectus’ means any document described or issued as a prospectus and includes a red herring prospectus referred to in section 32 or shelf prospectus referred to in section 31 or any notice, circular, advertisement or other document inviting offers from the public for the subscription or purchase of any securities of a body corporate;

(B) **PUBLIC OFFER & PRIVATE PLACEMENT: (SECTION 23) Issue of Securities by a Public Company**

A public company may issue securities—

- (a) To public through prospectus (herein referred to as ‘Public Offer’)
- (b) Through Private Placement
- (c) Through a Rights/Bonus Issue to its existing shareholder by following

**Companies (Prospectus and Allotment of Securities) Rules, 2014.**

**Note:** Listed company also needs to comply with the provisions of the SEBI Act, 1992 and the rules and regulations made thereunder.

**Issue of Securities by a Private Company**

A private company may issue securities—

- (a) By way of Rights/Bonus issue; or
- (b) Through Private Placement.

Explanation: For the purposes of this Chapter, ‘public offer’ includes Initial Public Offer (IPO) or Further Public Offer (FPO) of securities to the public by a company, or an offer for sale of securities to the public by an existing shareholder, through issue of a prospectus.

(C) **POWER OF SEBI TO ISSUE and TRANSFER SECURITIES Provisions made by SEBI and CG**

The provisions relating to Prospectus and Allotment; Share Capital and Debentures; Non-payment of dividend declared within 30 days:

- (a) in so far as they relate to —



- (i) issue and transfer of securities; and
- (ii) non-payment of dividend,

by listed companies be administered by SEBI by making regulations in this behalf;

- (b) in any other case, be administered by the Central Government (MCA).

**(D) MATTERS TO BE STATED IN PROSPECTUS Expert [Section 2(38)]**

‘Expert’ includes an engineer, a valuer, a CA, a CS, a CMA and any other person who has the power or authority to issue a certificate in pursuance of any law for the time being in force.

**Matters to be contained in the Prospectus**

(1) Every prospectus issued by or on behalf of a public company either with reference to its formation or subsequently, or by or on behalf of any person who is or has been engaged or interested in the formation of a public company, shall be dated and **state such information and set out such reports on financial information as may be specified by the Securities and Exchange Board in consultation with the Central Government:**

**Provided that until the Securities and Exchange Board specifies the information and reports on financial information under this sub-section, the regulations made by the Securities and Exchange Board under the SEBI Act, 1992, in respect of such financial information or reports on financial information shall apply.**

Every prospectus issued by a **PUBLIC COMPANY** shall make a declaration about the compliance of the provisions of this Act, the Securities Contracts (Regulation) Act, 1956 and the Securities and Exchange Board of India Act, 1992 and the rules and regulations made thereunder.

**Registration of Prospectus**

No prospectus shall be issued by company unless on or before the date of its publication, there has been delivered to the Registrar for **filing**, a copy thereof signed by every person who is named therein as a director or proposed director of the company or by his duly authorised attorney.

Registrar of companies shall refuse to register a prospectus:

- a. If it is not dated
- b. Contains statement of an expert who has not signed it
- c. Contains information which is 6 months old

**Expert's written consent needed**

A prospectus may include an expert statement by complying with following conditions:

- 1. Expert is a person who is not, and has not been, engaged or interested in the

formation or promotion or management, of the company and has given his written consent to the issue of the prospectus

2. Expert has not withdrawn such consent before the delivery of a copy of the prospectus to the Registrar for **filing** and
3. A statement regarding above shall be included in the prospectus.

**Disclosure on the face of the Prospectus**

Every prospectus issued shall, on the face of it—

1. State that a copy has been delivered for **filing** to the Registrar; and
2. Specify that any documents required by this section to be attached to the copy so delivered has been attached.

**Validity of prospectus for 90 days.**

No prospectus shall be valid if it is issued more than 90 days after the date on which a copy thereof is delivered to the Registrar.

**Punishment for contravention**

<b>On Company</b>	<b>Rs. 50,000 &lt; Fine &lt; Rs. 3 lacs</b>
<b>On officer in default</b>	<b>Imprisonment &lt; 3 years</b>
	<b>Or</b>
	<b>Rs. 50,000 &lt; Fine &lt; Rs. 3 lacs Or</b>
	<b>Both</b>

**(D) Meaning of Shelf Prospectus**

‘Shelf Prospectus’ means a prospectus in respect of which the securities or class of securities included therein are issued for subscription in one or more issues over a certain period without the issue of a further prospectus.

**Shelf Prospectus having a shelf life of 1 year**

Any class of companies, as the SEBI may provide by regulations, may file a SHELF PROSPECTUS with the Registrar at the stage of the first offer of securities included therein.

- 1) SHELF PROSPECTUS shall indicate a period < 1 year as the period of validity of such prospectus which shall commence from the date of opening of the first offer of securities under that prospectus, and
- 2) In respect of a second/subsequent offer of such securities issued during such 1 year period, no further prospectus is required.

**Changes to be intimated through information Memorandum**

A company filing a shelf prospectus shall be required to file an **Information**

**Memorandum in Form PAS-2 with the Registrar within 1 month prior to the issue of a second or subsequent offer of securities under the shelf prospectus** containing all material facts relating to

- a) New charges created
- b) Changes in the financial position of the company as have occurred between the previous offer of securities and the succeeding offer of securities.

### **Shelf Prospectus + Information Memorandum**

Where an information memorandum is filed, every time an offer of securities is made, such memorandum together with the shelf prospectus shall be regarded as a prospectus.

### **(E) Meaning of Red Herring Prospectus (RHP) (SECTION 32)**

‘Red Herring Prospectus’ means a prospectus which does not include complete particulars of the **quantum** or **price** of the securities included therein.

### **RHP to be issued before issue of a prospectus**

A company proposing to make an offer of securities may issue a red herring prospectus prior to the issue of a prospectus.

### **Filing of RHP with ROC**

A company proposing to issue a red herring prospectus shall file it with the Registrar at least 3 days prior to the opening of the subscription list and the offer.

### **Obligation of RHP to be same as that of Prospectus**

A red herring prospectus shall carry the same obligations as are applicable to a prospectus and any variation between the red herring prospectus and a prospectus shall be highlighted as variations in the prospectus.

### **Filing of Prospectus with ROC**

Upon the closing of the offer of securities, the prospectus stating therein the total capital raised, whether by way of debt or share capital, and the closing price of the securities and any other details as are not included in the red herring prospectus shall be filed with the Registrar and the SEBI.

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## **8.5 SHARECAPITAL**

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### **DEFINITION**

#### **1. Authorised Capital [Section 2(8)]**

‘authorised capital’ or "nominal capital" means such capital as is authorised by the memorandum of a company to be the maximum

**amount of share capital of the company.**

**2. Issued Capital [Section 2(50)]**

‘issued capital’ means such capital as the company issues from time to time for subscription.

**3. Subscribed Capital [Section 2(86)]**

‘subscribed capital’ means such part of the capital which is for the time being subscribed by the members of a company.

**4. Called up Capital [Section 2(15)]**

‘called-up capital’ means such part of the capital, which has been called for Payment. Paid up Share Capital [Section 2(64)]

"paid-up share capital" or "share capital paid-up" means such aggregate amount of money credited as paid-up as is equivalent to the amount received as paid up in respect of shares issued and also includes any amount credited as paid-up in respect of shares of the company, but does not include any other amount received in respect of such shares, by whatever name called.

**KINDS OF SHARECAPITAL**

The share capital of a company limited by shares shall be of 2 kinds, namely:

- (a) Equity Share Capital—
  - (i) with Voting Rights
  - (ii) with Differential Rights as to Dividend, Voting or otherwise, and
- (b) Preference Share Capital

**1. Equity Share Capital [ESC]**

—**Equity Share Capital** means all share capital which is not Preference Share Capital.

**2. Preference Share Capital [PSC]**

**Preference Share Capital** means that part of the issued share capital of the company which carries (or would carry) a Preferential Right with respect to:—

- a) Payment of Dividend; and
- b) Repayment, in the case of a Winding Up or Repayment of Capital.

**3. Exemption – Private Companies**

Section 43 shall not apply where MOA/AOA of the private company so provides.

**4. Conditions to be followed for issuing Shares with Differential rights**

No company limited by shares shall issue equity shares with differential rights as to dividend, voting or otherwise, unless it complies with the following conditions:

1. **Articles of Association** of the company authorizes the issue of shares with Differential Rights.
2. The issue of shares is authorized by an **Ordinary Resolution** passed at a general meeting of the shareholders. (OR by Postal Ballot in case of Listed Company)

**Provided that where the equity shares of a company are listed on a recognized stock exchange, the issue of such shares shall be approved by the shareholders through postal ballot.**

3. The voting power in respect of shares with differential rights of the company shall **not exceed 74% of total voting power** including voting power in respect of equity shares with differential rights issued at any point of time.
4. The company has not defaulted in **filing Financial Statements and Annual Returns** for 3 financial years immediately preceding the financial year in which it is decided to issue such shares.
5. The company has **No Subsisting Default** in the payment of:
  - a. Declared Dividend
  - b. Repayment of its Matured Deposits
  - c. Redemption of its Preference Shares or Debentures
  - d. Payment of the Preference Dividend
  - e. Repayment of Term Loan from a PFI or State Level Financial Institution or Scheduled Bank or Interest payable thereon
  - f. Dues with respect to Statutory Payments relating to its Employees to any authority
  - g. Default in crediting the amount in Investor Education and Protection Fund (IEPF)

**Provided that a company may issue equity shares with differential rights upon expiry of 5 years from the end of the financial Year in which such default was made good.**

6. The company has **Not Been Penalized** by Court or Tribunal during the **last 3 years** of any offence under the **RBI Act, SEBI Act, SCRA, FEMA or any other special Act**, under which such companies being regulated by Sectoral regulators.

#### **Inter-conversion not permissible**

The company shall not convert its existing equity share capital with voting rights into equity share capital carrying differential voting rights and vice-versa.

#### **Rights of Differential shareholders**

The holders of the equity shares with differential rights shall enjoy all other rights such as bonus shares, rights shares etc., which the holders of equity shares are entitled to, **subject to the differential rights** with which such shares have been

issued.

### **Entry in Register of Members**

Where a company issues equity shares with differential rights, the Register of Members maintained u/s 88 shall contain all the relevant particulars of the shares so issued along with details of the shareholders.

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## **8.6 COMPANY AUDITOR**

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### **APPOINTMENT OF AUDITOR (SEC: 139)**

#### **Step 1: AC/BOD recommends the name of the proposed Auditor {Section 139(11)}**

After considering the following parameters, Audit Committee/Board of Directors shall recommend the name of the proposed Auditor before the shareholders for appointment in AGM by passing Ordinary Resolution:

- (1) Qualification
- (2) Experience
- (3) disciplinary proceedings, if any pending against the auditor Explanation: For the purposes of this Chapter, the word 'firm' shall include a limited liability partnership incorporated under the Limited Liability Partnership Act, 2008.

#### **Step 2: Obtaining a certificate from proposed auditor before appointment.**

The auditor appointed shall submit a certificate before his appointment that

- (a) The individual or the firm, as the case may be, is eligible for appointment and is not disqualified for appointment under the Act, the Chartered Accountants Act, 1949 and the rules or regulations made thereunder;
- (b) The proposed appointment is as per the terms provided under the Act
- (c) The proposed appointment is within the limits laid down by or under the authority of the Act {20 Companies u/s 141(3)(g)};
- (d) The list of proceedings against the auditor or audit firm or any partner of the audit firm pending with respect to professional matters of conduct, as disclosed in the certificate, is true and correct.

#### **Step 3: Tenure and Ratification**

The auditor appointed in the annual general meeting shall hold office from the conclusion of that meeting till the conclusion of the 6th AGM, with the meeting wherein such appointment has been made being counted as the 1st meeting.

#### **Step 4: Intimation to Auditor and ROC in Form ADT-1**

The company shall inform the auditor of its appointment, and also file a notice of

such appointment with the Registrar in Form ADT-1 within 15 days of the meeting in which the auditor is appointed.

**Section 139(10):** Where at any annual general meeting, no auditor is appointed or re-appointed, the existing auditor shall continue to be the auditor of the company.

**ROTATION OF AUDITOR AND COOLING PERIOD Section 139(2)(4):**

**Rotation of Auditors**

No listed company or a Prescribed Class of Company shall appoint or re-appoint—

- (a) an individual as auditor for more than one term of 5 consecutive years; and
- (b) an audit firm as auditor for more than 2 terms of 5 consecutive years:

**Prescribed Class of Company:** It means the following classes of companies (excluding one person companies and small companies):

Type of Company	Threshold
Listed Company	NO limit.
All unlisted Public Companies having	PUSC > Rs. 10 crores
All Private Limited Companies having	PUSC > Rs. 50 crores ( <del>20 crores</del> )
All companies having PUSC below 10/50 but having public borrowings from financial institutions, banks or public deposits	Borrowings from FI, Banks or Public Deposits > Rs. 50 crores

**Section 139(2)(4): Cooling period**

Auditors should serve cooling period as follows:

Type of Auditor	Cooling Period
Individual Auditor	5 Years
CA Firm	5 Years

**3 Explanations (Rules)**

**Explanation 1:** As on the date of appointment, no audit firm having a common partner or partners to the other audit firm, whose tenure has expired in a company immediately preceding the financial year, shall be appointed as auditor of the same company for a period of 5 years:

**Explanation 2:** The incoming auditor or audit firm shall not be eligible if such auditor or audit firm is associated with the outgoing auditor or audit firm under the same network of audit firms.

For the purposes of these rules the term ‘same network’ includes the firms operating or functioning, hitherto or in future, under the same brand name, trade name or common control.

**Explanation 3:** If a partner, who is in charge, of an audit firm and also certifies the financial statements of the company, retires from the said firm and joins another

firm of chartered accountants, such other firm shall also be ineligible to be appointed for a period of 5 years.

**Section 139(2) Transitory Provision**

Every company, existing on or before the commencement of this Act which is required to comply with provisions of this sub-section, shall comply with the requirements of this sub-section within 3 years from the date of commencement of this Act.

Provided also that every company, existing on or before the commencement of this Act which is required to comply with the provisions of this sub-section, shall comply with requirements of this sub-section within a period which shall not be later than the date of the first annual general meeting of the company held, within the period specified under Section 96(1), after 3 years from the date of commencement of this Act. [Substituted by Companies (Removal of Difficulties) third Order Dated 30th June, 2016]

**Section 139 (3) Rotation of Audit Partner, Audit Team and JOINT Audit**

Subject to the provisions of this Act, members of a company may resolve to provide that-

- (a) in the audit firm appointed by it, the auditing partner and his team shall be rotated at such intervals as may be resolved by members; or
- (b) the audit shall be conducted by more than one auditor.

**Section 139(9): Re-appointment of the Auditor**

A retiring auditor may be re-appointed at an annual general meeting, if—

- (a) he is not disqualified for re-appointment
- (b) he has not given the company a notice in writing of his unwillingness to be re-appointed
- (c) a special resolution has not been passed at that meeting appointing some other auditor or providing expressly that he shall not be re-appointed

**Section 140(1): Removal of Auditor before AGM (Before the Auditor gives Audit Report) BR + CG + SR**

The auditor may be removed from his office before the expiry of his term only by a SR [Special Resolution] of the company, after obtaining the previous approval of the CG.

- (4) The application to the CG for removal of auditor shall be made in Form ADT-2.
- (5) The application shall be made to the CG within 30 days of the



resolution passed by the Board.

- (6) The company shall hold the general meeting within 60 days of receipt of approval of the CG for passing the Special Resolution.

The CG shall give the auditor a reasonable opportunity of being heard before taking any action as above.

### **Section 140(2)(3): Resignation by the Auditor**

The auditor who has resigned from the company shall file Form ADT - 3 with the company and the ROC within a period of 30 days from the date of resignation, indicating the reasons and other facts as may be relevant with regard to his resignation.

In case of resignation by the Auditor in a Government Company, Auditor shall file Form ADT - 3 with the C & AG, company and the ROC within a period of 30 days from the date of resignation.

**Penalty for non-filing of Form ADT - 3:** If the auditor does not comply above, he or it shall be punishable with

**Minimum Penalty** Rs. 50,000 OR Auditor's Remuneration whichever is less

**Maximum Penalty** Rs. 5,00,000

**Amendment (Ordinance):** If the auditor does not comply with the provisions of sub-section (2), he or it shall be liable to a penalty of Rs. 50,000 or an amount equal to the remuneration of the auditor, whichever is less, and **in case of continuing failure, with further penalty of Rs. 5,000 for each day after the first during which such failure continues**, subject to a maximum of Rs. 5,00,000.

### **Section 140 (4) Removal of Auditor at AGM, i.e., Non-Ratification of Retiring Auditor (Umbrella Diagram)**

#### **Step 1: Requirement of a Special Notice to be received by the Company**

Special notice shall be required for a resolution at an annual general meeting

- (1) appointing as auditor a person other than a retiring auditor, or
- (2) providing expressly that a retiring auditor shall not be re-appointed, except where the retiring auditor has completed a consecutive tenure of 5 years or 10 years, as provided u/s 139.

#### **Step 2: Copy of Special Notice to the retiring auditor**

On receipt of notice of such a resolution, the company shall forthwith send a copy thereof to the retiring auditor.

#### **Step 3: Retiring Auditor's right of Representation**

Where notice is given of such a resolution and the retiring auditor makes a

representation in writing to the company and requests its notification to members of the company, the company shall —

- (a) in any notice of the resolution given to members of the company, state the fact of the representation having been made; and
- (b) send a copy of the representation to every member of the company to whom notice of the meeting is sent, or if it is received late, then the auditor may require that the representation shall be read out at the meeting.

Provided that if a copy of representation is not sent as aforesaid, a copy thereof shall be filed with the Registrar:

Provided further that if the Tribunal is satisfied on an application either of the company or of any other aggrieved person that the rights conferred are being abused by the auditor, then, the copy of the representation may not be sent and the representation need not be read out at the meeting.

**Section 140(5) Fraud by the Auditor and Removal of the Auditor by Tribunal:** The Tribunal either *suo moto* or on an application made to it by the CG or by any person concerned, if it is satisfied that the auditor of a company has, whether directly or indirectly, acted in a fraudulent manner or abetted or colluded in any fraud by, or in relation to, the company or its directors or officers, it may, by order, direct the company to change its auditors.

If the application is made by the CG and the Tribunal is satisfied that any change of the auditor is required, it shall within 15 days of receipt of such application, make an order that he shall not function as an auditor and the CG may appoint another auditor in his place.

#### **Global Ban for 5 years on such Auditor**

An auditor, whether individual or firm, against whom final order has been passed by the Tribunal under this section shall not be eligible to be appointed as an auditor of ANY company for a period of 5 years from the date of passing of the order and the auditor shall also be liable for action under section 447.

#### **Punishment for fraud u/s 447 (Mega 447)**

{6 months/3 years} < Imprisonment < {10 years}

#### **AND**

Fraud Amount (100%) < Penalty < 3 X Fraud Amount (300%)

Where the fraud in question **involves public interest**, the term of imprisonment shall not be less than 3 years

#### **Punishment for fraud u/s 447 (Mini 447)**

Where the fraud amount < Lower of: (1) Rs10 Lacs or

(2) 1% of the Turnover.

**AND** does NOT involve Public Interest, Punishment shall be: Imprisonment < 5

years OR

Fine < Rs. 50 Lacs OR BOTH

## **QUALIFICATION AND DISQUALIFICATION OF AUDITOR**

### **Section 141(1)(2) : Qualification of Auditor**

A person shall be eligible for appointment as an auditor of a company only if he is a chartered accountant.

Provided that a firm whereof majority of partners practising in India are qualified Chartered Accountants may be appointed by its firm name to be auditor of a company.

Where a firm including an LLP is appointed as an auditor of a company, only the partners who are chartered accountants shall be authorised to act and sign on behalf of the firm.

### **Section 141(3) : Disqualification of Auditor**

See Separate Table below.

### **Section 141(4) : Deemed Vacation of the office if disqualification is attracted post appointment**

Where a person appointed as an auditor of a company incurs any of the disqualifications mentioned above after his appointment, he shall vacate his office as such auditor and such vacation shall be deemed to be a casual vacancy in the office of the auditor.

### **Section 141(3) : Disqualification of Auditors**

**Section 141(3) : The following persons shall not be eligible for appointment as an auditor of a company, namely:**

**Section 141(3)(a):** a body corporate other than an LLP

**Section 141(3)(b):** an officer or employee of the company

**Section 141(3)(c):** a person who is a partner, or who is in the employment, of an officer or employee of the company.

**Section 141(3)(d)(i):** a person who, or his relative or partner is holding any security of or interest in the company or its subsidiary, or of its holding or associate company or a subsidiary of such holding company.

Provided that the relative may hold security or interest in the company of face value not exceeding Rs. 1,00,000; [ < Rs. 1,00,000]

Provided further that in the event of acquiring any security or interest by a relative, above Rs. 1, 00,000, the corrective action to maintain the limits shall be taken by the auditor within 60 days of such acquisition or interest.

**Section 141(3)(d)(ii):** a person who, or his relative or partner is indebted to the company, or its subsidiary, or its holding or associate company or a subsidiary of such holding company, in excess of Rs. 5,00,000. [>Rs. 5,00,000]

**Section 141(3)(d)(iii):** a person who, or his relative or partner has given a guarantee or provided any security in connection with the indebtedness of any third person to the company, or its subsidiary, or its holding or associate company or a subsidiary of such holding company, for an amount exceeding Rs. 1,00,000; [ > Rs. 1,00,000]

**Section 141(3)(e):** a person or a firm who, whether directly or indirectly, has business relationship with the company, or its subsidiary, or its holding or associate company or subsidiary of such holding company or associate company of such nature as mentioned below:

The term 'business relationship' shall be construed as any transaction entered into for a commercial purpose, except

- (i) commercial transactions which are in the nature of professional services permitted to be rendered by an auditor or audit firm under the Act and the Chartered Accountants Act, 1949 and the rules or the regulations made under those Acts;
- (ii) commercial transactions which are in the ordinary course of business of the company at arm's length price such as sale of products or services to the auditor, as customer, in the ordinary course of business, by companies engaged in the business of telecommunications, airlines, hospitals, hotels and such other similar businesses.

**Section 141(3)(f):** a person whose relative is a director or is in the employment of the company as a director or key managerial personnel.

**Section 141(3)(g):** a person who is in full time employment elsewhere or a person or a partner of a firm holding appointment as its auditor, if such persons or partner is at the date of such appointment or reappointment holding appointment as auditor of more than 20 companies.

**Exemption Notification dated 5th June 2015 for Section 141 (3) (g)**

- (a) Private Companies having PUSC < Rs. 100 Crores.
- (b) One Person Company u/s 2(62)
- (c) Dormant Company u/s 455
- (d) Small Company u/s 2(85).

**Section 141(3)(h):** a person who has been convicted by a court of an offence involving fraud and a period of 10 years has not elapsed from the date of such conviction.

**Section 141(3)(i):** a person who, directly or indirectly, renders any service referred

toin section 144 to the company or its holding company or its subsidiary company.  
 Explanation: For the purposes of this clause, the term ‘directly or indirectly’ shall have the meaning assigned to it in the Explanation to section 144.

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## **8.7 DIRECTORS**

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### **MEANNING:**

Owners of the company the shareholders are not able to manage the affairs of the company and therefore they appoint their representative called Director to manage the affairs of the company.

Section 2/13 of the Indian company Act 2013 defines director as "Director includesany person occupying the position of director by whatever name called."

### **DIFFERENT TYPES OF DIRECTORS AND MODES OF APPOINTMENTOF DIRECTORS.**

#### **First Director:**

1. Persons named in the articles of association as Directors become the first directorof the company.
2. In absence of the provision in the articles regarding persons to be appointed as firstdirector the subscribers will become the first director as per section 254.

#### **Appointment of Directors:**

1. As per section 255 members at the general meeting will appoint the directors byelection.
2. The Board of Directors will fill up the casual vacancy of Director by nomination.
3. Section 408 states the appointment by nomination by the central government.
4. Appointment of Directors can be done by nomination in statutory corporations.
5. Every public company having 1000 or more shareholders with share value ofRs. 20000 or less may have 1 director out of 3 directors appointed by them.

#### **Other rules regarding appointment of directors are as follows:**

1. Qualification shares
2. Filing of Consent
3. Notice
4. Method of voting
5. Alternative directors
6. Amendment

#### **Disqualifications of Director:**

A person will be disqualified to be a Director of a company under the followingcircumstances.

1. If he is found to be of unsound mind by the court of Law
2. If he is undischarged Insolvent
3. He has applied to be adjudicated as an insolvent and his application is pending
4. He has been convicted by court of any offence
5. He has not paid any call money of the shares of the company held by him personally, or jointly
6. An order has been passed by the court disqualifying him to be the director of the company.

### **REMOVAL OF DIRECTORS:**

The Shareholders, the central government or the court may remove the directors abiding the following rules.

1. Removal by shareholders by passing the ordinary resolution (except the directors appointed by central government u/s 408. In a private company director appointed for life cannot be removed by shareholders resolution direct or appointed by proportional representation cannot be removed by resolution made by the shareholders.
2. Special notice for removal of directors: Special notice must be given to remove a director and a copy of notice must be given to the director concerned.
3. The Director can claim the Remuneration for his premature termination.
4. Central government can make an order for the removal of director if he is not fit or proper person to hold the office.
5. Section 397 and 398 has given power to the court for removal of a director.

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## **8.8 GENERAL MEETINGS**

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### **MEANING**

- A meeting refers to a gathering or assembly or getting together of a number of persons for transacting a lawful business.
- There must be at least 2 persons to constitute a meeting.
- A meeting is an important component of company management.
- Most of the decisions (resolutions) of the company are passed in the meetings.
- Proposal – Motion - Resolution

### **CONDITIONS – REQUISITIES OF A VALID MEETING**

1. Meeting must be duly convened
2. Meeting must be properly constituted
3. Meeting must be properly conducted

### **PROPER AUTHORITY TO CALL THE MEETING**

- Meeting must be convened by Proper Authority.
- Three authorities: BOD, Shareholders and Tribunal.

AOA of a Company empowers BOD to convene general meetings.

- If notice is given without the sanction of BOD it is invalid.
- In certain circumstances, the shareholders or members of the company have the right to insist on calling an EGM.

- In case of any default in holding the AGM, on petition of member, the TRIBUNAL may direct the company to call AGM.

### **PROPER NOTICE**

- A. Notice to Whom – it should be given to every member or shareholder, auditor, legal representative of the deceased member, each of the directors and every such person who is entitled to attend the meeting.
- B. Length Time for Notice – At least 21 clear days' notice must be given to the members. A general meeting may be called after giving a shorter notice if consent is given in writing or by electronic mode by not less than 95% of the members entitled to vote at such meeting
- C. Contents of Notice – The notice for the meeting must specify the place, day and time of the meeting. It must contain the agenda (a statement of business to be transacted at the meeting)
- D. How to Convey the Notice? The notice can be sent by hand, post, courier, fax or E-mail.

### **STATEMENTS TO BE ANNEXED TO NOTICE**

- A statement containing material facts for each item of special business to be transacted at a general meeting shall be annexed to the notice.
- A proxy form must be attached with the notice.
- Any default in following the provisions of notice will hold every promoter, director and manager punishable with fine which may extend to Rs. 50,000 or 5 times the amount of benefit, whichever is more.

### **POSTPONING OR CANCELLING MEETING**

- Meeting conveyed upon due notice shall not be postponed or cancelled.
- If necessary, the Board may reconvene the meeting to transact the same business, after giving 3 days intimation to the members.
- It shall be sent either individually or published in a vernacular newspaper.

### **PROPER CHAIRMAN**

- The chairman is the person who has been designated or elected to preside over and conduct the proceedings of the meeting.
- He is usually a member of the Board.
- The articles designate the chairman of the board of directors to preside over the general meeting of the company.
- If the chairman is absent, the meeting itself can elect a temporary chairman to preside over a meeting.
- The members personally present at the meeting shall elect 1 of them to be the chairman by show of hands.
- Members can also demand poll as per provision of the Act.

### **TYPES OF COMPANY MEETINGS**

#### **Shareholder's Meetings**

##### **1. Statutory Meeting**

- The first general meeting of the members by a public company is called statutory meeting.
  - It should be called within six months from the date on incorporation
- 2. Annual General Meeting (AGM)**
- It is an annual meeting of body of members
  - Every company – Public or Private, having share capital or not, Ltd. Or Unlimited – must hold AGM
  - A company other than OPC has to hold in each year a AGM
  - A company must hold one meeting in each calendar year

**TIME PERIOD**

**For the first AGM**

- It shall be held within 9 months from the date of the closing of the first financial year of the company
- No extension of time can be allowed for first AGM

**Subsequent AGMs**

- AGM must be hold within 6 months from the closing of the financial year
- The gap between 2 AGMs need not be more than 15 months
- Where the first AGM of the company has been held within 9 months from the date of closing its financial year, then it need not to hold another AGM in the year of incorporation
- Registrar may for any reason extend its time not exceeding 3 months within which any AGM shall be held. (this extension is not available for first AGM)
- Day, hour and time of AGM
- Generally during business hours (9 am to 6 pm)
- On any day that is not a national holiday
- Shall be held at the registered office of the company or at some other place within the city, town or village in which the regd. Office of the company is situated

**Power of Tribunal to Call AGM**

If any default is made in holding the AGM of a company, tribunal may, on the application of any member of the company, call or direct the calling of an AGM.

**Provisions for Default in Complying with Provisions**

- If any default is made in holding AGM
- The company and every officer of the company, who is in default, shall be liable



- Fine which may extend to 1 lakh INR and in case of continuing default, further fine of Rs. 5000 every day during which such default continues

### **Business to be Transacted at AGM**

- The term business means major activity to be discussed or major decisions to be taken in the meeting.
- The business to be transacted at AGM may comprise of ordinary business and special business.

### **Ordinary Business**

- The ordinary business is of routine nature. The ordinary business to be transacted at the AGM may include the following items:
  1. Consideration of financial statements and the report of the and auditors.
  2. The declaration of dividend.
  3. The appointment of directors in place of those retiring.
  4. The appointment of and fixing up of the remuneration of auditors.

### **Special Business**

Any business other than mentioned in the ordinary business scheduled to be transacted at the meeting are deemed to be special business.

### **3. Extraordinary General Meeting (EGM)**

- All general meetings other than AGMs shall be called EGMs.
- EGMs are convened by the company at any time
- The business transacted at an EGM comprises anything which cannot be postponed till the next AGM.
- For example, changes in MOA or AOA, reduction or reorganization of share capital, issue of debentures, etc.
- All business transacted at these meetings are special business.

### **EGM may be Called**

- (1) by the BOD on its own accord
- (2) by the directors on the requisition of shareholders
- (3) by the requisitionists (members) themselves
- (4) by the tribunal

#### **(1) By the BOD on its Own Accord**

The board whenever deem fit, call an egm

The meeting is called by giving 21 days clear notice

**(2) By the Directors on the Requisition of Shareholders**

Who can be valid requisitionists?

- (a) in case of company having share capital, such number of members who hold not less than one-tenth of such shares of the paid-up share capital of the company as on that date carries the right of voting
- (b) in case of company not having share capital, such number of members who hold not less than one-tenth of the total voting powers of the all the members having on the said date a right to vote

**Requirements of Requisition**

- The requisition made shall set out the matters for consideration of which the meetings to be called
- It means the requisition must state the objects of meeting
- It must be signed by the requisitionists and sent to the registered office of the company

**(3) By the Requisitionists (Members) Themselves**

- The board must fix a date of calling the meeting –
- Within 21 days from the date of receipt of valid req
- The date of meeting must be fixed on a day not later than 45 days
- If the board fails to fix the date of meeting within the aforesaid period, the meeting may be called by req themselves within a period of 3 months from the date of deposit of req.
- Any reasonable expenses incurred by the req shall be reimbursed by the company

**(4) By the Tribunal**

- If for any other reason, it is impractical to call a meeting of the company, other than an AGM, the tribunal may direct the company to call and hold meeting
  - (1) on its own motion
  - (2) on an application of any director
  - (3) on application of any member, who is entitled to vote at a meeting

**Board Meetings**

Company is an artificial person and so has to act through human intermediaries, who are called directors of the board.

They take active part in the board meetings. Decisions are taken on the basis of majority rule.

**LEGAL PROVISIONS OF BOARD MEETINGS**

- **First Meeting and Subsequent Meeting**  
First board meeting shall be held within 30 days from the date of its

incorporation

So minimum 4 meetings of BOD every year

Subsequent Meeting shall not have more than 120 days interval between two meetings (one in a quarter – one in every 3 months)

### **Manner of Holding Meeting**

- The participation of directors in a meeting may be either in person or through videoconferencing or other audio-visual means
- It must be capable of recording and recognizing the participation of the directors as well as the proceedings of the meetings.

### **Valid Notice for the Board Meeting**

- A meeting of the Board shall be called by giving not less than 7 days notice in writing to every director at his registered address.
- Such notice shall be sent by hand delivery or by post or by electronic means

### **PENALTY FOR DEFAULT IN CONVEYING NOTICE**

Every officer of the company whose duty is to give notice under this section and fails to do so shall be liable to a penalty of Rs. 25,000.

### **QUORUM FOR BOARD MEETING**

- It shall be one-third of the total strength or 2 directors, whichever is higher.
- Any fraction of a number shall be rounded off as one.
- Participation of directors by video conferencing or other audio-visual means shall also be counted for the purpose of quorum
- Due to lack of quorum if meeting couldn't be conducted, the meeting shall stand adjourned to the same day, same time and place in the next week

### **Passing of Resolution by Circulation**

No resolution shall be deemed to have been passed unless it has been approved by a majority of the directors or members who are entitled to vote on the resolution.

### **Defect in Appointment of Directors and Validity of Actions**

No act done by a person as a director shall be deemed to be invalid by reason of any defect or disqualification regarding the appointment of the director, noticed subsequently.

### **Other Meetings**

1. Meetings of the Committees of the Board
2. Meeting of Debenture holders
3. Meeting of Creditors
4. Meeting of Contributories in winding up

### **Meeting of the Committees of the Board**

- The company appoints various committees for various purposes
- Committee Meetings are held individually or the BOD call meeting of all committee members and their chairman

- Committees include – Remuneration Committee, CSR Committee, Audit Committee or Shareholders Relationship Committee, etc.

**MEETING OF DEBENTURE - HOLDERS**

- A company maintains a Register of debenture-holders.
- BOD can call meeting of debenture holders at any time

**MEETING OF CREDITORS**

- Creditors are those persons, organizations and agencies from whom the company has borrowed funds.
- The meeting of creditors is called at the time of 2 events:
  - (a) for purposes other than winding up
  - (b) for winding up

**MEETING OF CONTRIBUTORIES IN WINDING UP**

- Contributories are those persons or agencies who contributed to company’s assets
- At the time of winding up of a company, the liquidator calls the meeting of contributories.

**8.9. WINDING UP COMPANY:**

**INTRODUCTION**

The winding-up of a company is a process which involves ending the life of the company and administering its property for the benefit of its creditors and members. In this process, the assets of the company are collected and realised to the payment of its debt. If after realising the creditors, company finds surplus which is distributed among the members on the other hand if there is any deficit, every member of the company must contribute to the assets of the company.

After completion of these formalities prescribed by the Companies Act, the company is dissolved and its name is removed from the Registrar of Companies.

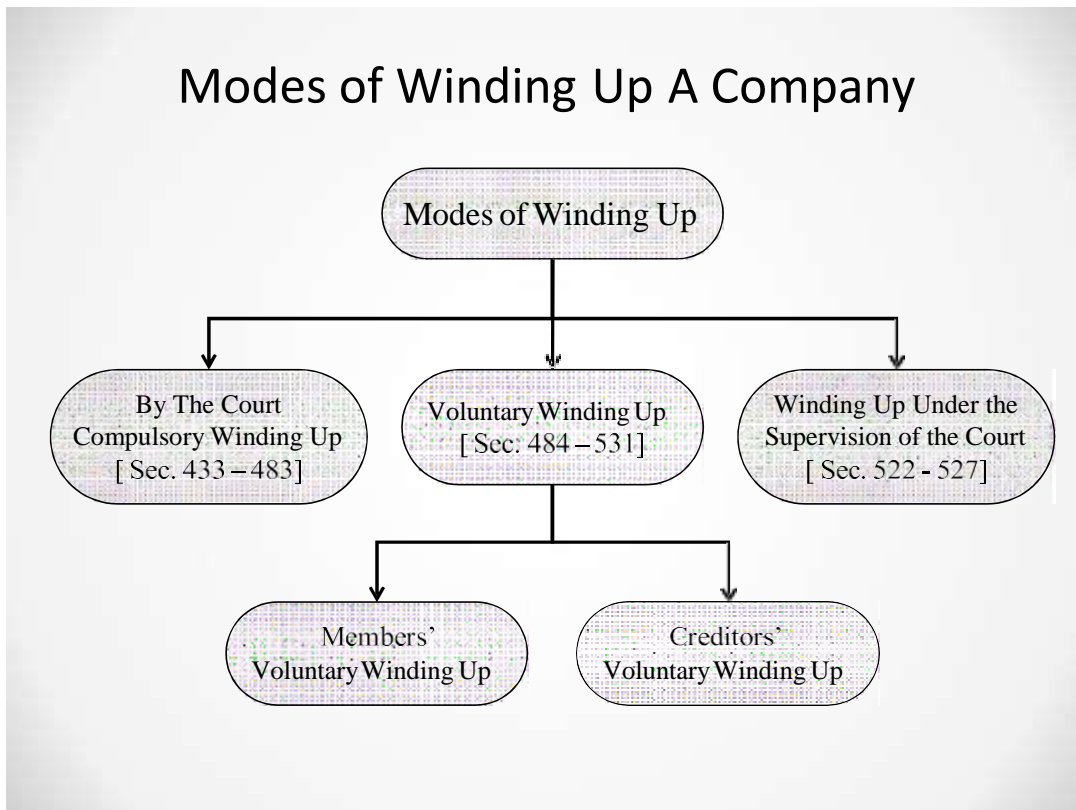
**Winding Up & Dissolution**

Generally, the terms ‘winding up’ and ‘dissolution’ used to mean the same thing, but according to Companies Act, these two terms are quite different by their legal procedures. The differences between them are as below:

<b>Points</b>	<b>Winding Up</b>	<b>Dissolution</b>
Main Feature	The first stage and involves realizing of assets, paying off liabilities and distribution of surplus if any.	The second stage in which a company is finally dissolved.
Proceedings	Carried out by the liquidator Appointed by the company/court.	Order can be issued only by the court.
Liquidator’s Duties	Liquidators represents the company.	Liquidator cannot represent company.

Debt	Creditors can prove their debts.	Creditors can't prove their debts.
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### MODES OF WINDING UP COMPANY:



### Grounds for Compulsory Winding Up

The grounds on which a company can be compulsorily wound up by the court are as follows.

1. If the company itself has passed a special resolution for the winding up by the court.
2. If the statutory report is not filed with the Registrar or company fails to hold the statutory meeting within prescribed time.
3. If the number of members of the company falls below 2 in case of private company and below 7 in case of public company.
4. If company is unable to pay the debts in full.  
A company will be deemed to be unable to pay its debt under the following conditions:
  - a) If it is proved to the court's satisfaction that the company is unable to pay its debts.
  - b) If the process issued on a decree order of a court in favour of a creditor has not been satisfied.
5. If the court is of the opinion that it is just and equitable that the company should be wound up. It should be wound up under the following circumstances:
  - a) When the main object of the company for which it was established was failed.
  - b) When the business of the company becomes illegal.

### **Petition for Winding Up (Section 439)**

A petition for the winding up of a company may be presented to the court by any of the following parties:

1. By a shareholders or contributory can present a petition on the following grounds:
  - a) When No. of members of the company falls below prescribed limit
  - b) When the contributory has paid the calls in arrears
2. By the company itself by passing a special; resolution
3. By the Registrar of the Companies
4. By any creditor or creditors, including any contingent or prospective creditor or creditors
5. By the person authorised by the Central Government
6. By the voluntary liquidator

### **Power of the Court to dispose of Petition of Winding Up**

On hearing a petition for the winding up of the company, the court may take the following steps:

1. It may dismiss the application with or without costs
2. It may adjourn the hearing conditionally/ unconditionally
3. It may dispose of the application in any way it thinks fit
4. It may make an interim order.
5. It may order the winding up of the company with or without costs or make any other orders as it thinks fit.

### **Effects of The Winding Up Order**

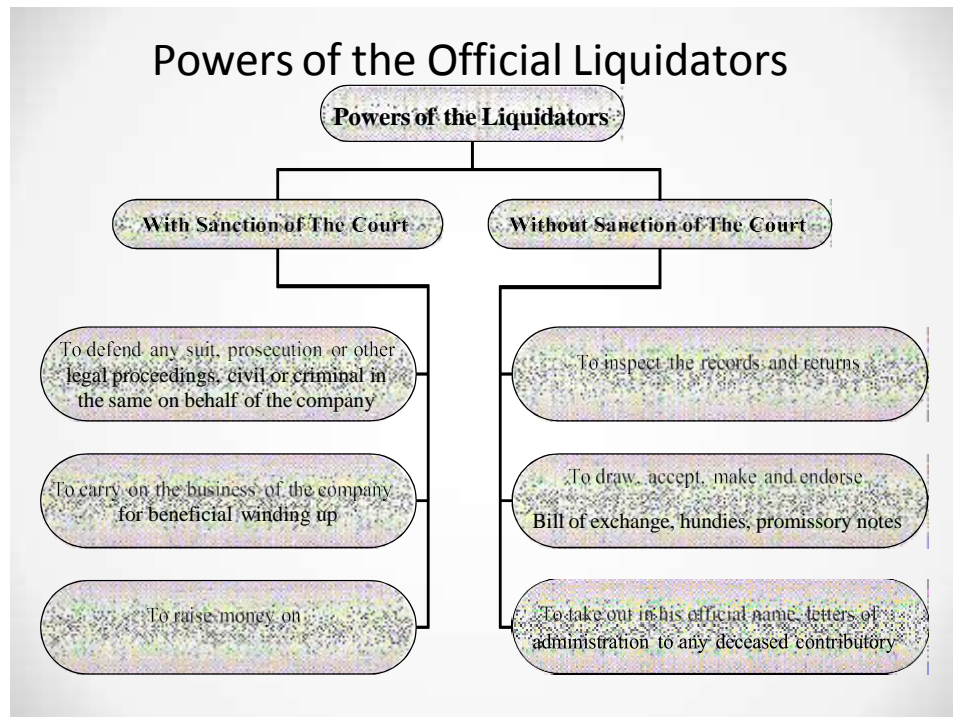
After the order has been made by the court for winding up of the company, its effects will be as follows,

1. No suits or legal proceedings can commence against the company without the permission of the court
2. If a suit or legal proceedings against the company were pending, it cannot be proceeded with or without the permission of the court
3. Suits or legal proceedings by or against the company to be stayed on passing of the order or compulsory winding up
4. The court will appoint the official liquidator for the winding up of the company
5. Powers of the board of directors are terminated and they shall vest in the official liquidator
6. Any debt payable at a future date becomes immediately payable

### **Power of the Court after Winding Up Order**

- To give stay order on receipt of the application for stay order either from auditor or contributor or from the official liquidator
- Directs the contributors who hold partly paid shares to pay the balance on such shares in case of inadequate funds to meet the liabilities and expenses
- Can order dissolution of company when it finds that:
  - (i) it is difficult for the liquidator to proceed with winding up for wants
  - (ii) the affairs of the company are completely wound up

The court has the power to exclude those creditors who fails to prove claims within the stipulated period for the benefit of any distribution to be made on behalf of the company



**Duties of the Official Liquidators**

1. He should take into custody and protect the assets of company
2. He should submit a preliminary report to the court on company affairs
3. He should keep proper books of accounts relating to the company
4. He should keep all the funds of the company in the –Public accounts of India in the RBI.
5. He should obey the court’s order for the disposing of the company’s books.

**Contribution & Proceedings of the Committee of Inspection (Sec.465)**

1. The committee shall not consist of more than 12 members representing the creditors and contributors
2. The committee shall have power to inspect the accounts of the liquidator at any reasonable time
3. The committee shall meet at such time as it may itself decide
4. The quorum of the committee meetings shall be one third or two whichever is higher. Any member of the committee may resign by giving written notice to the liquidator

**Duties of Secretary in case of Compulsory Winding Up**

1. He should assist the directors in preparing the petition for the winding up of the company
2. After the order of winding up passed by the court, the secretary should file with the Registrar within 30 days a certified copy of that order
3. He must submit a statement of affairs of the company to the liquidator within

21 days of the date of winding up order

4. He should furnish information regarding the company which the liquidators may require from time to time

### **Voluntary Winding Up**

When the company winds up itself by surrendering and realising its assets for the payment of debts, it can be called as voluntary winding up:

Two Types of voluntary winding up

1. By Member
2. By Creditors

**Under Section 484 of the Companies Act, a company may wound up voluntarily:**

1. When the period fixed for the duration of the company had expired by the articles. If the company passes a special resolution to wind up the company voluntarily

When an ordinary or special resolution has been passed for the winding up of the company, a notice of the same must be given within 14 days by an advertisement in the official gazette and in the newspaper of district. A voluntary resolution is deemed to commence from the date of the resolution and the company ceases to carry on its business from that date except it may be necessary for the beneficial winding up of such business (Sec. 485 & 486).

### **Declaration of Solvency**

Section 488 of the Companies Act provides that when a company proposed to wind up voluntarily, the majority of the directors make a declaration of solvency must be made:

1. Within five weeks preceding the date of passing the resolution for winding up and delivered to Registrar for registration before the date, along with:
  - The balance sheet made out on the last-mentioned date
  - A statement of the assets and liabilities as on that date

### ***Procedure-Members' Voluntary Winding Up:***

1. Declaration of solvency must be made as per the provision of Section 488 of Companies Act.
2. The next step is to hold a general meeting of the members for passing the special resolution for the winding up.
3. The notice of the same must be given within 14 days by an advertisement in the official gazette and local newspaper.
4. The company can appoint a liquidator and fix his remuneration.
5. On appointment of liquidator, all powers of the Board of directors, managing directors ceases.
6. The liquidator shall exercise all powers of the board & do all such acts necessary for winding up of the company.



***Secretary's Duties-Members' Voluntary Winding Up***

1. To arrange to hold board meetings for the voluntary winding up of the company.
2. To arrange to hold an extraordinary general meeting of the shareholders to pass a special resolution for winding up
3. To file with registrar, a declaration of solvency as per the provisions of Section 488
4. To see that liquidator is properly appointed at fixed remuneration
5. To see that every invoice, order and business letter issued by the company before the words 'under liquidation'.
6. Making arrangement to provide all books, papers and documents as well as movable and immovable properties to the liquidator

***Procedure-Creditors' Voluntary Winding Up***

When no declaration of solvency is made it is considered as a case of creditors' voluntary winding up. Procedure for the same is as follows:

1. The company shall hold a meeting of creditors immediately after the general meeting of the members to pass a resolution for voluntary winding up.
2. The directors must prepare statement of affairs, list of creditors and statement of their claim and present them to the creditors meeting.
3. A liquidator must be nominated by members & creditors at their respective meetings.
4. The creditor's meeting may appoint a committee of inspection constituting not more than 5 members.

***Secretary's Duties-Creditors' Voluntary Winding Up***

1. To call board meeting, to fix the date of general meeting and to hold a creditors' meeting
2. To see that notice of members' meeting and creditors' meeting are issued
3. To see that the notice of creditors meeting is published in the official gazette and a local newspaper

**Provisions Applicable to Both Voluntary Winding Up [Sec.486, 487 &511 to 520]**

1. The voluntary winding up of the company considered to commence when resolution is passed for the same
2. The business of the company ceases on the commencement of the winding up.
3. Even the company's business is ceased the corporate status and power of the company remains continue until it is dissolved.
4. The liquidator has power to prepare contributor's list, to make calls, call general meeting of the company.
5. Any question arising in the winding up of the company the court may approved by the liquidator or any contributor or creditor.

All costs, charges and expenses of winding up including remuneration of liquidator shall be payable by company's assets.

❖ **CHECK YOUR PROGRESS**

**A) LONG QUESTIONS**

- 1 Define company and discuss its characteristics
- 2 Write a note: Memorandum of Association
- 3 Write a note: Article of Association
- 4 Write a note: Prospectus
- 5 Discuss Provisions of Incorporation of Company
- 6 Write a note: Central Registration Centre (CRC)
- 7 Define share capital and discuss various types of share capital
- 8 Write a note on Types of shares
- 9 Define Directors and Discuss various types of Directors.
- 10 State the qualifications and disqualifications of an auditor as per provisions of the company's act 2013.
- 11 Explain the duties of an auditor.
- 12 Explain the provisions of the companies act regarding the Removal of an auditor.
- 13 Rights and Duties of a Company Auditor.
- 14 Appointment and Reappointment of a Company auditor.
- 15 Rules regarding Appointment and removal of Director.
- 16 Qualifications and Disqualifications of a company Director.
- 17 Define Winding up of company.
- 16 Distinguished Winding Up and Dissolution
- 17 Discuss Reasons of Winding Up
- 18 Discuss various modes of winding up of company
- 19 Discuss grounds of compulsory Winding up
- 20 Who can petition of compulsory winding up.
- 21 Discuss effects of The Winding Up Order.
- 22 Duties of Secretary in case of Compulsory Winding Up
- 25 Write a note: Types of Meeting.

**B Multiple-choice Questions.**

1. The minimum number of directors for public company is.....  
(A) 1 (B) 2 (C) 3 (D) 4
2. The minimum number of directors for private company is.....  
(A) 1 (B) 2 (C) 3 (D) 4
- 3.. The maximum number of directors for OPC is.....  
(A) 10 (B) 15 (C) 7 (D) 4
4. What is the paid-up share capital fixed for the appointment of a woman director?  
(A) 100 CR (B) 300CR (C) 500CR (D) NONE
5. The tenure of director appointed by small shareholders shall be....  
(A) Up to date of next AGM (B) 1 year (C) 2 year (D) 3 year
6. The minimum age prescribed for the appointment of Managing Directors  
(A) 18 years (B) 21 Years (C) 30 Years (D) 70 Years

7. If any company appoint more than 15 directors, then they pass.....  
 (A) OR (B) BR (C) UR (D) SR

**8. In Annual General Meeting, which one of the following will be treated as specialbusiness?**

- (a) declaration of any dividend;
- (b) fixing of the remuneration of the auditors;
- (c) appointment of directors in place of those retiring;
- (d) regularization of Director's Appointment;

**9. A section 8 company can call its general meeting by giving a clear at least notice.**

- (a) 7 days
- (b) 14 days
- (c) 21 days
- (d) 27 days

**10. A listed company can call its general meeting by giving a clear at least notice.**

- (a) 7 days
- (b) 14 days
- (c) 21 days
- (d) 27 days

**11. Small Company u/s 2(85) has to fulfil which of the following thresholds:**

- (a) PUSC <Rs. 50 lacs
- (b) Turnover <Rs. 2 crores
- (c) Both (a) and (b)
- (d) Either (a) or (b)

**12. 12Subsidiary company is a company in which > 50 % of the is held by the holding Company u/s 2(87)**

- (a) Total Voting power
- (b) Equity Share Capital
- (c) Equity Share Capital plus Preference Share Capital
- (d) Share in dividends

**13. 13Government company is one in which of the PUSC is held by CG or SG or both u/s 2(45)**

- (a) >50%
- (b) >50%
- (c) >51%
- (d) >51%

**14. 14The minimum number of members in a private company and public company are**

- (a) Three and Seven respectively (3,7)
- (b) Two and seven respectively (2,7)
- (c) Two and nine respectively (2,9)

(d) None of the above

**15. Section 144 of the Companies Act, 2013 does not excludes the statutory auditor of the company to render the services of**

- (a) Investment advisory
- (b) Investment banking
- (c) Branch auditor
- (d) Actuarial**

**16** Bhishm Limited decided to appoint Mr. Rajvir, chartered accountants as the branch auditor for the audit of its Lucknow branch accounts for the year 2017-18. The decision to appoint branch auditor was taken by way of Board Resolution in the meeting of Board of Directors of the company, held in April 2017, subject to shareholders' approval in AGM of the company scheduled to be held in June 2017. Meanwhile, the Principal Auditor of the company raised an objection that the branch auditor cannot be appointed without his consent. Whether the objection raised by company auditor is validRs.?

- (a) The objection raised by company auditor is not valid as per section 143(8) of the companies Act, 2013 / and the Board has authority to appoint branch auditor but should be approved by shareholders in General Meeting.
- (b) The objection raised by company auditor is valid as it is necessary to consult/obtain the consent of Principal Auditor before appointing Branch Auditor.
- (c) The Board of Directors has no authority to appoint Branch Auditor so the objection raised by Principal Auditor is valid.
- (d) The objection raised by company auditor is not valid as it is compulsory to appoint branch auditor as per Sec.139 of the Companies Act, 2013.

**17** ..... appoints Government auditor.

- (A) C& AG (B) Shareholders (C) BOD (D) Government

**18.** ..... appoints First auditor.

- (A) C& AG (B) Shareholders (C) BOD (D) Government

**19.** ..... appoints Statutory auditor.

- (A) C& AG (B) Shareholders (C) BOD (D) Government

20. ....resolution pass in Board Meeting.

- (A) BR (B) OR (C) SR (D) None

21. ....resolution pass in AGM.

- (A) BR (B) OR (C) SR (D) None

22. resolution pass in EGM.

- (A) BR (B) OR (C) SR (D) None

23. \_\_\_ is the representative of the shareholders.

- (A) Company Secretary (B) Company Auditor  
(C) Company Register (D) None of the Above

**MCQ Answers**

1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20	21	22	23
C	B	B	A	A	D	D	B	C	C	A	D	B	D	A	A	A	C	B	A	B	C	B

**9.0 INTRODUCTION****9.1 DEFINITIONS****9.2 RIGHTS OF CONSUMER****9.3 ESSENTIAL REMEDIES AVAILABLE TO CONSUMERS UNDER INDIAN CONSUMER PROTECTIONS ACT****9.4 SCOPE****CHECK YOUR PROGRESS**

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**9.0 INTRODUCTION:**

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The industrial revolution and the development in the international trade and commerce has led the vast expansion of business and trade, as a result of which a variety of consumer goods have appeared in the market to cater to the needs of the consumers and a host of services have been made available to the consumers such as insurance, transport, electricity, housing, entertainment, finance and banking among others. A well organised sector of manufacturers and traders with better knowledge of markets has come into existence, thereby affecting the relationship between the traders and the consumers making the principle of consumer sovereignty almost inapplicable. The advertisements of goods and services in television, newspapers and magazines influence the demand for the same by the consumers though there may be manufacturing defects or imperfections or shortcomings in the quality, quantity and the purity of the goods or there may be deficiency in the services rendered. In addition, the production of the same item by many firms has led the consumers, who have little time to make a selection, to think before they can purchase the best. For the welfare of the public, the glut of adulterated and sub-standard articles in the market has to be checked. In spite of various provisions providing protection to the consumer and providing for stringent action against adulterated and sub-standard articles in the different enactments like Code of Civil Procedure, 1908, the Indian Contract Act, 1872, the Sale of Goods Act, 1930, the Indian Penal Code, 1860, the Standards of Weights and Measures Act, 1976 and the Motor Vehicles Act, 1988, very little could be achieved in the field of Consumer Protection. Though the Monopolies and Restrictive Trade Practices Act, 1969 and the Prevention of Food Adulteration Act, 1954 have provided relief to the consumers yet it became necessary to protect the consumers from the exploitation and to save them from adulterated and sub-standard goods and services and to safeguard the interests of the consumers. In order to provide for better protection of the interests of the consumer, the Consumer Protection Bill, 1986 was introduced in the Lok Sabha on 5<sup>th</sup> December, 1986.

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**9.1 DEFINITIONS:**

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In this Act, unless the context otherwise requires,

**(1) Appropriate Laboratory:**

‘Appropriate laboratory’ means a laboratory or organization-

- (i) recognized by the Central Government
- (ii) recognised by a State Government, subject to such guidelines as may be prescribed by the Central Government in this behalf
- (iii) any such laboratory or organisation established by or under any law for the time-being in force, which is maintained, financed or aided by the Central Government or a State Government for carrying out analysis or test of any goods with a view to determining whether or not such goods suffer from any defect

**(2) Branch Office:**

‘Branch office means,

- (i) any establishment described as a branch by the opposite party,
- (ii) any establishment carrying on either the same or substantially the same activity as that carried on by the head office of the establishment

**(3) Complainant:**

It means,

- (i) a consumer
- (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
- (iii) the Central Government or any State Government
- (iv) one or more consumers, where there are numerous consumers having the same interest, who or which makes a complaint;

**(4) Complaint**

It means any allegation in writing made by a complainant that

- (i) an unfair trade practice or a restrictive trade practice has been adopted by any trader
- (ii) the goods bought by somebody or agreed to be bought by somebody suffer from one or more defects
- (iii) the services hired or availed of or agreed to be hired or availed of by him suffer from deficiency in any respect
- (iv) a trader has charged for the goods mentioned in the complaint a price in excess of the price fixed by or under any law for the time being in force or displayed on the goods or any package containing such goods
- (v) goods which will be hazardous to life and safety when used, are being

offered for sale to the public in contravention of the provisions of any law for the time being in force requiring traders to display information in regard to the contents, manner and effect of use of such goods with a view to obtaining any relief provided by or under this Act.

**(5) Consumer:**

Consumer means any person who

- (i) 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
- (ii) 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.

**(6) 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.

**(7) 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 in force or under any contract, express or implied, or as is claimed by the trader in any manner whatsoever in relation to any goods;

**(8) Deficiency**

It means any fault, imperfection, shortcoming or inadequacy in the quality, nature and manner of performance which is required to be maintained by or under any law for the time being in force or has been undertaken to be performed by a person in pursuance of a contract or otherwise in relation to any service;

**(9) District Forum**

District Forum means a Consumer Disputes Redressal Forum established under clause (a) of section 9;



**(10) Goods**

To be meant as defined in the Sale of Goods Act, 1930(3 of 1930);

**(11) Manufacturer**

Manufacturer 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 others and claims the end product to be goods manufactured by himself; or
- (iii) puts or causes to be put his own mark on any goods made or manufactured by any other manufacturer and claims such goods to be goods made or manufactured by himself.

(Explanation: Where a manufacturer dispatches any goods or part thereof to any branch office maintained by him, such branch office shall not be deemed to be the manufacturer even though the parts so dispatched to it are assembled at such branch office and are sold or distributed from such branch office.

**(12) Member**

Member includes the President and a member of the National Commission or a State Commission or a District Forum, as the case may be;

**(13) National Commission**

National Commission means the National Consumer Disputes Redressal Commission established under clause (c) of section 9;

**(14) Notification**

"notification" means a notification published in the Official Gazette;

**(15) 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, 1860 (22 of 1860) or not

**(16) Prescribed**

It means the rules made by the State Government, or as the case may be, by the Central Government under this Act

**(17) Restrictive Trade Practice**

Restrictive trade practice means any trade practice which requires a consumer to buy, hire or avail of any goods or, as the case may be, services as a condition precedent for buying, hiring or availing of other goods or services;

**(18) Service**

Service means service of any description which is made available to potential users and includes the provision of facilities in connection with banking, financing, insurance, transport, processing, supply of electrical or other energy, board or lodging or both, housing construction, entertainment, amusement or the purveying of news or other information, but does not include the rendering of any service free of charge or under a contract of personal service;

**(19) State Commission**

State Commission means a Consumer Disputes Redressal Commission established in a State under clause (b) of section 9;

**(20) Trader**

Trader in relation to any goods means a person who sells or distributes any goods for sale and includes the manufacturer thereof, and where such goods are sold or distributed in package form, includes the packer thereof;

**(21) Unfair Trade Practice:**

Unfair trade practice means a trade practice which, for the purpose of promoting the sale, use or supply of any goods or for the provision of any service, adopts any unfair method or unfair or deceptive practice including any of the following practices, namely,

- (1)** the practice of making any statement, whether orally or in writing or by visible representation which,
  - (i) falsely represents that the goods are of a particular standard, quality, quantity, grade, composition, style or model
  - (ii) falsely represents that the services are of a particular standard, quality or grade
  - (iii) falsely represents any re-built, second-hand, renovated, reconditioned or old goods as new goods
  - (iv) represents that the goods or services have sponsorship, approval, performance, characteristics, accessories, uses or benefits which such goods or services do not have
  - (v) represents that the seller or the supplier has a sponsorship or approval or affiliation which such seller or supplier does not have

- (vi) makes a false or misleading representation concerning the need for, or the usefulness of, any goods or services
- (vii) gives to the public any warranty or guarantee of the performance, efficacy or length of life of a product or of any goods that is not based on an adequate or proper test thereof:

Provided that where a defence is raised to the effect that such warranty or guarantee is based on adequate or proper test, the burden of proof of such defence shall lie on the person raising such defence;

- (viii) makes to the public a representation in a form that purports to be-
  - (i) a warranty or guarantee of a product or of any goods or services; or
  - (ii) a promise to replace, maintain or repair an article or any part thereof or to repeat or continue a service until it has achieved a specified result, if such purported warranty or guarantee or promise is materially misleading or if there is no reasonable prospect that such warranty, guarantee or promise will be carried out;
- (ix) materially misleads the public concerning the price at which a product or like products or goods or services, have been or are, ordinarily sold or provided, and, for this purpose, a representation as to price shall be deemed to refer to the price at which the product or goods or services has or have been sold by sellers or provided by suppliers generally in the relevant market unless it is clearly the price at which the product has been sold or services have been provided by the person by whom or on whose behalf the representation is made;
- (x) gives false or misleading facts disparaging the goods, services or trade of another person.

Explanation-For the purposes of clause (1), a statement that is-

- (a) expressed on an article offered or displayed for sale, or on its wrapper or container
  - (b) expressed on anything attached to, inserted in, or accompanying, an article offered or displayed for sale, or on anything on which the article is mounted for display or sale
  - (c) contained in or on anything that is sold, sent, delivered, transmitted or in any other manner whatsoever made available to a member of the public, shall be deemed to be a statement made to the public by, and only by, the person who had caused the statement to be so expressed, made or contained
- (2)** permits the publication of any advertisement whether in any newspaper or otherwise, for the sale or supply at a bargain price, of goods or services that are not intended to be offered for sale or supply at the bargain price, or for a period that is, and in quantities that are, reasonable, having regard to the nature of the market in which the business is carried on, the nature and size

of business, and the nature of the advertisement.

**Explanation-** For the purpose of clause (2), 'bargaining price' means-

- (a) a price that is stated in any advertisement to be a bargain price, by reference to an ordinary price or otherwise,
- (b) a price that a person who reads, hears or sees the advertisement, would reasonably understand to be a bargain price having regard to the prices at which the product advertised or like products are ordinarily sold.

**(3) permits**

- (a) the offering of gifts, prizes or other items with the intention of not providing them as offered or creating impression that something is being given or offered free of charge when it is fully or partly covered by the amount charged, in the transaction as a whole; the conduct of any contest, lottery, game of chance or skill, for the purpose of promoting, directly or indirectly, the sale, use or supply of any product or any business interest
- (3A)** withholding from the participants of any scheme offering gifts, prizes or other items free of charge on its closure the information about final results of the scheme. Explanation: for the purpose of this sub clause, the participants of a scheme shall be deemed to have been informed of the final results of the scheme where such results are within a reasonable time published, prominently in the same newspaper in which the scheme was originally advertised)
- (4)** permits the sale or supply of goods intended to be used, or are of a kind likely to be used, by consumers, knowing or having reason to believe that the goods do not comply with the standards prescribed by competent authority relating to performance, composition, contents, design, constructions, finishing or packaging as are necessary to prevent or reduce the risk of injury to the person using the goods;
- (5)** permits the hoarding or destruction of goods, or refuses to sell the goods or to make them available for sale or to provide any service, if such hoarding or destruction or refusal raises or tends to raise or is intended to raise, the cost of those or other similar goods or services.
- (6)** Manufacture of spurious goods or offering such goods for sale or adopting deceptive practices in the provision of services;

Any reference in this Act to any other Act or provision thereof which is not in force in any area to which this Act applies shall be construed to have a reference to the corresponding Act or provision thereof in force in such area.

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## **9.2 RIGHTS OF CONSUMER**

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### **1. Right to Safety**

Means right to be protected against the marketing of goods and services, which are hazardous to life and property. The purchased goods and services availed of should not only meet their immediate needs, but also fulfil long term interests.

Before purchasing, consumers should insist on the quality of the products as well as on the guarantee of the products and services. They should preferably purchase quality marked products such as ISI, AGMARK, etc.

### **2. Right to be Informed**

Means right to be informed about the quality, quantity, potency, purity, standard and price of goods so as to protect the consumer against unfair trade practices.

Consumer should insist on getting all the information about the product or service before making a choice or a decision. This will enable him to act wisely and responsibly and also enable him to desist from falling prey to high pressure selling techniques.

### **3. Right to Choose**

Means right to be assured, wherever possible of access to variety of goods and services at competitive price. In case of monopolies, it means right to be assured of satisfactory quality and service at a fair price. It also includes right to basic goods and services. This is because unrestricted right of the minority to choose can mean a denial for the majority of its fair share. This right can be better exercised in a competitive market where a variety of goods are available at competitive prices

### **4. Right to be Heard:**

Means that consumer's interests will receive due consideration at appropriate forums. It also includes right to be represented in various forums formed to consider the consumer's welfare.

The Consumers should form non-political and non-commercial consumer organizations which can be given representation in various committees formed by the Government and other bodies in matters relating to consumers.

### **5. Right to Seek redressal**

Means right to seek redressal against unfair trade practices or unscrupulous exploitation of consumers. It also includes right to fair settlement of the genuine grievances of the consumer.

Consumers must make complaint for their genuine grievances. Many a time, their

complaint may be of small value but its impact on the society as a whole may be very large. They can also take the help of consumer organisations in seeking redressal of their grievances.

**6. Right to Consumer Education:**

It means the right to acquire knowledge and skill to be an informed consumer throughout life. Ignorance of consumers, particularly of rural consumers, is mainly responsible for their exploitation. They should know their rights and must exercise them. Only then real consumer protection can be achieved with success.

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**9.3 Essential Remedies Available to Consumers Under Indian Consumer Protections Act**

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**1. Removal of Defects**

If after proper testing the product proves to be defective, then the ‘remove its defects’ order can be passed by the authority concerned.

**2. Replacement of Goods**

Orders can be passed to replace the defective product by a new non-defective product of the same type.

**3. Refund of Price**

Orders can be passed to refund the price paid by the complainant for the product.

**4. Award of Compensation**

If negligence of the seller causes tangible or intangible harm or loss to any consumer, then compensation for that loss stands valid.

**5. Removal of Deficiency in Service**

If there is any deficiency in delivery of service, then orders can be passed to remove that deficiency. For instance, if an insurance company makes unnecessary delay in giving final touch to the claim, then under this Act orders can be passed to immediately finalise the claim.

**6. Discontinuance of Unfair/Restrictive Trade Practice**

If a complaint is filed against unfair/restrictive trade practice, then under the Act that practice can be banned with immediate effect. For instance, if a gas company makes it compulsory for a consumer to buy gas stove with the gas connection, then this type of restrictive trade practice can be checked with immediate effect.

**7. Stopping the Sale of Hazardous Goods:**

Products that may prove hazardous for life can be stopped from being sold.

**8. Withdrawal of Hazardous Goods from the Market**

On seeing the serious adverse effects of hazardous goods on the consumers, such goods can be withdrawn from the market. The objective of doing so is that such products should not be offered for sale.

**9. Payment of Adequate Cost**

In the end, there is a provision in this Act that the trader should pay adequate cost to the victim concerned.

**9.4 SCOPE**

**9.5.1 The Central Consumer Protection Council**

- (1) The Central Government shall, by notification, establish with effect from such date as it may specify in such notification, a Council to be known as the Central Consumer Protection Council (hereinafter referred to as the Central Council)
- (2) The Central Council shall consist of the following members, namely:
  - (a) the Minister in charge of the consumer affairs in the Central Government, who shall be its Chairman, and
  - (b) such number of other official or non-official members representing such interests as may be prescribed.

**PROCEDURE FOR MEETINGS OF THE CENTRAL COUNCIL:**

- (3) The Central Council shall meet as and when necessary, but at least one meeting of the Council shall be held every year.
- (4) The Central Council shall meet at such time and place as the Chairman may think fit and shall observe such procedure in regard to the transaction of its business as may be prescribed.

**OBJECTS OF THE CENTRAL COUNCIL:**

The objects of the Central Council shall be to promote and protect the rights of the consumers such as:

- (a) the right to be protected against the marketing of goods and 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, as the case may be so as to protect the

consumer against unfair trade practices

- (c) the right to be assured, wherever possible, access to a variety of goods and services at competitive prices
- (d) the right to be heard and to be assured that consumer's interests 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
- (f) the right to consumer education

**THE STATE CONSUMER PROTECTION COUNCILS:**

- (5) The State Government shall, by notification, establish with effect from such date as it may specify in such notification, a Council to be known as the Consumer Protection Council for the State.
- (6) The State Council shall consist of the following members, namely:
  - (a) the Minister in-charge of consumer affairs in the State Government who shall be its Chairman
  - (b) such number of other official or non-official members representing such interests as may be prescribed by the State Government
  - (c) such number of other official or non-official members, not exceeding ten, as may be nominated by the Central Government
- (7) The State Council shall meet as and when necessary but not less than two meetings shall be held every year
- (8) The State Council shall meet at such time and place as the Chairman may think fit and shall observe such procedure in regard to the transaction of its business as may be prescribed by the State Government

**Objects of the State Council**

The objects of the State Council shall be to promote and protect the rights of the consumers such as

- (a) the right to be protected against the marketing of goods and 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, as the case may be so as to protect the consumer against unfair trade practices
- (c) the right to be assured, wherever possible, access to a variety of goods and services at competitive prices
- (d) the right to be heard and to be assured that consumer's interests 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
- (f) the right to consumer education



**District Consumer Protection Council**

- (9) The State Government shall establish for every district, by notification, a council to be known as the District Consumer Protection Council with effect from such date as it may specify in such notification.
- (10) The District Consumer Protection Council (now referred to as the District Council) shall consist of the following members, namely:
  - (a) the Collector of the district (by whatever name called), who shall be its Chairman; and
  - (b) such number of other official and non-official members representing such interests as may be prescribed by the State Government.
- (11) The District Council shall meet as and when necessary but not less than two meetings shall be held every year.
- (12) The District Council shall meet at such time and place within the district as the Chairman may think fit and shall observe such procedure in regard to the transaction of its business as may be prescribed by the State Government.

**OBJECTS OF DISTRICT COUNCIL:**

The objects of the District Council shall be to promote and protect the rights of the consumers such as

- (a) the right to be protected against the marketing of goods and 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, as the case may be so as to protect the consumer against unfair trade practices
- (c) the right to be assured, wherever possible, access to a variety of goods and services at competitive prices
- (d) the right to be heard and to be assured that consumer's interests 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
- (f) the right to consumer education

**Modes of Complaint**

- (1) A complaint in relation to any goods sold or delivered or agreed to be sold or delivered or any service provided or agreed to be provided may be filed with a District Forum by
  - (a) the consumer to whom such goods are sold or delivered or agreed to be sold or delivered or such service provided or agreed to be provided;
  - (b) any recognised consumer association whether the consumer to whom the goods sold or delivered or agreed to be sold or delivered or service provided

## CONSUMER PROTECTION ACT 1986

or agreed to be provided is a member of such association or not;

- (c) one or more consumers, where there are numerous consumers having the same interest, with the permission of the District Forum, on behalf of, or for the benefit of, all consumers so interested; or
  - (d) the Central Government or the State Government, as the case may be, either in its individual capacity or as a representative of interests of the consumers in general.
- (2) Every complaint filed under sub-section (1) shall be accompanied with such amount of fee and payable in such manner as may be prescribed.
  - (3) On receipt of a complaint made under sub-section (1), the District Forum may, by order, allow the complaint to be proceeded with or rejected:

Provided that a complaint shall not be rejected under this section unless an opportunity of being heard has been given to the complainant:

Provided further that the admissibility of the complaint shall ordinarily be decided within twenty-one days from the date on which the complaint was received.

- (4) Where a complaint is allowed to be proceeded with under sub-section (3), the District Forum may proceed with the complaint in the manner provided under this Act:

Provided that where a complaint has been admitted by the District Forum, it shall not be transferred to any other court or tribunal or any authority set up by or under any other law for the time being in force.

Explanation: For the purpose of this section 'recognised consumer association' means any voluntary consumer association registered under the Companies Act, 1956 or any other law for the time being in force.

### EXERCISE

#### 1. Answer the following Questions

- 1. Explain Rights of Consumer
- 2. Discuss Essential Remedies Available to Consumers Under Indian Consumer Protections Act
- 3. Explain The Central Consumer Protection Council
- 4. Discuss Procedure for Meetings of the Central Council
- 5. Mention Objects of the Central Council
- 6. Write note on the State Consumer Protection Councils
- 7. Mention Objects of the State Council
- 8. Discuss District Consumer Protection Council
- 9. Mention Objects of District Council

**2. Answer the following MCQ**

1. **Rights of consumer are protected under \_\_\_\_\_**
  - A. **Consumer protection Act, 1986**
  - B. Company Act, 1956
  - C. RBI Act, 1934
  - D. SEBI Act, 1992
  
2. **How many rights does a consumer have under the Consumer Protection Act?**
  - A. 8
  - B. **6**
  - C. 4
  - D. 5
  
3. **When the seller manipulates the price, it is known as**
  - A. Caveat Emptor
  - B. Unfair trade practices
  - C. **Restricted trade practices**
  - D. None of the above
  
4. **Consumer Protection Act is significant for**
  - A. Immovable Goods
  - B. Movable Goods
  - C. Particular Goods and Services
  - D. **All Goods and Services**
  
5. **The rights of consumers as per the consumer protection Act does not include the right to be**
  - A. informed
  - B. heard
  - C. safety
  - D. **presented**
  
6. **The term of office for a member is \_\_\_\_\_ years in all redress forum.**
  - A. 5
  - B. **10**
  - C. 7
  - D. 35
  
7. **Which one of the following is not a consumer right?**
  - A. Right to safety
  - B. Right to seek redressal
  - C. Right to get discount
  - D. **Right to be heard**
  
8. **In which year did Consumer Protection Act come into existence?**
  - A. **1986**
  - B. 1999

**CONSUMER PROTECTION ACT 1986**

- C. 1991
- D. 1976

9. **\_\_\_ is one of the redressal agencies for redressing consumer grievances.**

- A. COPRA
- B. **State Commission**
- C. Consumer Organisation
- D. None of these

10. **\_\_\_ mark is used for electrical products.**

- A. **ISI**
- B. FPO
- C. ISO
- D. Agmark

11. **Right to \_\_\_\_\_ is a right to be protected against products which are hazardous to life or health.**

- A. Information
- B. **Safety**
- C. Seek Redressal
- D. Consumer Education

**3. State the following statements are True or False.**

- 1. Right to be informed says that the consumer has the right to acquire knowledge and be well-informed throughout his life.: **False**
- 2. The Consumer Protection Act is applicable throughout India.: **True**
- 3. Buying standardised products is a consumer right.: **False**
- 4. The Central Government can file a complaint under the Consumer Protection Act.: **True**
- 5. Consumer awareness is a campaign for protecting consumer interests.: **False**

**MCQ Answer**

<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>	<b>6</b>	<b>7</b>	<b>8</b>	<b>9</b>	<b>10</b>	<b>11</b>
<b>A</b>	<b>B</b>	<b>C</b>	<b>D</b>	<b>D</b>	<b>B</b>	<b>D</b>	<b>A</b>	<b>B</b>	<b>A</b>	<b>B</b>

**10.0 INTRODUCTION****10.1 WHAT IS THE COMPETITION?****10.2 OBJECTS OF THE COMPETITION ACT, 2002****10.3 DEFINATIONS****10.4 REGULATION OF COMBINATIONS****10.5 FINANCE****10.6 ACCOUNTS AND AUDIT [SECTION 52]****10.7 FURNISHING OF RETURNS, ETC., TO CENTRAL  
GOVERNMENT[SECTION 53]****CHECK YOUR PROGRESS**

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**10.0 INTRODUCTION**

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Given the fact that the structure of world economy and trade has taken rapid strides and undergone vast changes, India has been taking adequate steps for integrating itself with the new changes and challenges. This makes functioning and positioning of the market more effective and competitive. In this regard, Government constituted a High-Level Committee on Competition Policy and Law on September 15, 1999 under the Chairmanship of Mr S.V.S. Raghavan, to recommend a legislative framework relating to Competition Law including mergers and demergers.

The Committee submitted its report on 22nd May 2000. The Government, after considering the report and suggestions from various organizations, institutions and general public, introduced the Competition Bill in the Parliament. This Bill became an Act, i.e., the Competition Act, 2002 after receiving assent from the President on 13th January 2003 and all the sections of the Act have already come into force by virtue of separate Government notifications.

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**10.1 WHAT IS THE COMPETITION?**

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The term “Competition” is not defined in the Competition Act 2002. Chapter 1 of the joint report ‘A Framework for the Design and Implementation of Competition Law and Policy’ by the World Bank and the OECD, broadly defines the competition as,

“A situation in a market in which firms or sellers independently stride for the buyers’ patronage in order to achieve a particular business objective, for example, profit, sales, or market share”.

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**10.2 OBJECTS OF THE COMPETITION ACT, 2002**

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An Act, keeping in view of the economic development of the country (especially

post-economic reforms of 1991), was laid down to provide for an establishment of a Commission with the following objectives:

1. to prevent practices having an adverse effect on competition
2. to promote and sustain competition in markets
3. to protect the interests of consumers
4. to ensure freedom of trade carried on by other participants in markets in India
5. matters connected therewith or incidental thereto

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### 10.3 DEFINITIONS

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#### 1. Acquisition

Acquisition means acquiring or agreeing to acquire by direct or indirect means things such as,

- (i) Shares, voting rights, or assets of any enterprise
- (ii) Control over management or control over assets of any enterprise

#### 2. Agreement

Agreement includes any arrangement or understanding or action in concert

- (i) Whether or not such arrangement, understanding or action is formal or in writing,
- (ii) Whether or not such arrangement, understanding or action is intended to be enforceable by legal proceedings.

#### 3. Cartel

Cartel includes an association of

- i. Producers
- ii. Sellers
- iii. Distributors
- iv. Traders or
- v. Service providers

Who by agreement amongst themselves, limit, control or attempt to control the:

- A. Production, distribution, sale or
- B. Price of or trade in goods or provision of services

#### 4. Goods

Goods means goods as defined in the Sale of Goods Act 1930 and includes:

- i. Products manufactured, processed or mined
- ii. Debentures, stock and shares after allotment
- iii. In relation to goods supplied, distributed or controlled in India, goods imported into India.

#### 5. Consumer

Consumers means any person who:

- i. 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, whether such purchase of goods is for resale or for any commercial

purpose or for personal use

- ii. 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 or partly promised or under any system of deferred payment, when such services are availed of with the approval of the first mentioned person whether such hiring or availing of services is for any commercial purpose or for personal use.

#### **6. Chairperson**

Chairperson means the Chairperson of the Commission appointed under sub-section (1) of section 8;

#### **7. Commission**

Commission means the 'Competition' Commission of India established under sub-section (1) of section 7;

#### **8. Enterprise**

Enterprise means a person or a department of the Government, who or which is, or has been, engaged in any activity, relating to the production, storage, supply, distribution, acquisition or control of articles or goods, or the provision of services, of any kind, or in investment, or in the business of acquiring, holding, underwriting or dealing with shares, debentures or other securities of any other body corporate, either directly or through one or more of its units or divisions or subsidiaries, whether such unit or division or subsidiary is located at the same place where the enterprise is located or at a different place or at different places.

But it does not include any activity of the Government relating to the sovereign functions of the Government including all activities carried on by the departments of the Central Government dealing with atomic energy, currency, defense and space.

#### **9. Person**

It includes

1. An individual, HUF, company body corporate, firm
2. AOP whether incorporated or not, in India or outside India
3. Any co-operative society
4. A local authority
5. Every artificial juristic person

**AAEC** - Appreciable adverse effect on competition

**PSU** – Public Sector Undertaking

**CCI** – Competition Commission of India

**CAT**- Competition Appellate Tribunal

#### **10. Group**

Group means, Two or more enterprise which directly or indirectly

1. Have 26% or more Voting Right in the other Enterprise
2. Ability to appoint more than half of the members of Board of Directors

3. Ability to control the management or affairs of the other enterprise

**11. Price**

Price, in relation to the sale of any goods or to the performance of any services includes every valuable consideration, whether direct or indirect, or deferred, and includes any consideration, which in effect relates to the sale of any goods or to the performance of any services although ostensibly relating to any other matter or thing.

**12. Service**

Service means service of any description which is made available to potential users and includes the provision of services in connection with the business of any industrial or commercial matters such as banking, communication, education, financing, insurance, chit funds, real estate, transport, storage, material treatment, processing, supply of electrical or other energy, boarding, lodging, entertainment, amusement, construction, repair, conveying of news or information and advertising

**13. Statutory Authority**

Statutory authority means any authority, board, corporation, council, institute, university, or any other body corporate, established by or under any Central, State or Provincial Act for the purposes of regulating production or supply of goods or provision of any services or markets therefor or any matter connected therewith or incidental thereto

**14. Trade**

"Trade" means any trade, business, industry, profession, or occupation relating to the production, supply, distribution, storage, or control of goods and includes the provision of any services

**15. Turnover**

Turnover includes the value of sale of goods or services

**16. Control includes**

Controlling the affairs or management by

1. One or more Enterprise Jointly or singularly over another Enterprise
2. One or more Group Jointly or singularly over another group or enterprise

**17. Predatory Pricing**

It means the sale of goods or provision of services, at a price below cost of production to reduce competition or eliminate the competitors. The main objective of such price is to reduce competition or to eliminate the competitors

**18. Anti-Trust law**

The antitrust laws apply to virtually all industries and to every level of business, including manufacturing, transportation, distribution, and marketing. They prohibit a variety of practices that restrain trade [Examples are illegal practices of price-fixing, corporate mergers likely to reduce the competitive vigor of particular markets, and predatory acts designed to achieve or maintain monopoly power]



**19. Monopoly**

A market structure characterized by a single seller, selling a unique product in the market. In a monopoly market, the seller faces no competition, as he is the sole seller of goods with no close substitute

**20. Perfect Competition**

Perfect competition is a market system characterized by many different buyers and sellers. In the classic theoretical definition of perfect competition, there are an infinite number of buyers and sellers. With so many market players, it is impossible for any one participant to alter the prevailing price in the market. If they attempt to do so, buyers and sellers have infinite alternatives to pursue.

**21. Oligopoly**

An oligopoly is similar in many ways to a monopoly. The primary difference is that rather than having only one producer of a good or service, there are a handful of producers, or at least a handful of producers that make up a dominant majority of the production in the market system. While oligopolists do not have the same pricing power as monopolists, it is possible, without diligent government regulation, that oligopolists will collude with one another to set prices in the same way a monopolist would.

**22. Monopolistic competition:**

It is a type of market system combining elements of a monopoly and perfect competition. Like a perfectly competitive market system, there are numerous competitors in the market. The difference is that each competitor is sufficiently differentiated from the others that some can charge greater prices than a perfectly competitive firm. An example of monopolistic competition is the market for music. While there are many artists, each artist is different and is not perfectly substitutable with another artist.

Criteria	Perfect	Monopolistic	Oligopoly	Monopoly
No. of Firms	Very large	Many	Few	one
Type of product	Standard	Differentiated	Std / Diff	Unique
Control of Price	None	Slight	Considerable	Considerable, if not regulated
Entry / Exit	Free	Free	Barriers	Barriers
Example	Agri product like wheat, soybeans, etc.	Restaurants, Retail stores, etc.	Automobiles, airlines, Baby foods etc.	Patented drugs, Electric goods, etc.

**23. Bid Rigging**

Agreement between enterprise or person engaged in similar production or trading of goods or provisions of service which has effect of eliminating or reducing the competition for bid. Prohibition of Certain Agreements, Abuse Of Dominant Position Under the Competition Act 2002, the competition Commission of India is empowered to inquire into anti-competitive agreements (section 3) and instances of abuse of dominant position including predatory pricing (section 4) to declare them void. The Commission is also empowered to regulate the combinations

(sections 5 and 6).

#### **24. Anti-competitive agreements [Section 3]**

It shall be unlawful for any enterprise or association of enterprises or person or association of persons to 'enter' into any agreement in respect of production, supply, storage, distribution, acquisition or control of goods or provision of services, which causes or is likely to cause an appreciable adverse effect on competition within India; and such agreements shall be void.

Anti-competitive agreements referred under the competition Act can be classified into two categories, the first being horizontal agreements (sub-section 3) and second being vertical agreements (sub-section 4).

##### **A. Horizontal anti-competitive agreements**

Any agreement entered into between enterprises or associations of enterprises or persons or associations of persons or between any person and enterprise or practice carried on, or decision taken by, any association of enterprises or association of persons, including cartels, engaged in identical or similar trade of goods or provision of services shall be presumed to have an appreciable adverse effect on competition, if it

- i. Directly or indirectly determines purchase or sale prices
- ii. Limits or controls production, supply, markets, technical development, investment, or provision of services
- iii. Shares the market or source of production or provision of services by way of allocation of the geographical area of market, or type of goods or services, or number of customers in the market or any other similar way
- iv. Directly or indirectly results in bid-rigging or collusive bidding

##### **B. Vertical anti-competitive agreements:**

Any agreement amongst enterprises or persons at different stages or levels of the production chain in different markets, in respect of production, supply, distribution, storage, sale or price of or trade in goods or provision of services shall be a void agreement if it causes or is likely to cause an appreciable adverse effect on competition in India, including:

- a. **Tie-in arrangement** - includes any agreement requiring a purchaser of goods, as a condition of such purchase, to purchase some other goods.
- b. **Exclusive supply agreement** - includes any agreement restricting in any manner the purchaser in the course of his trade from acquiring or otherwise dealing in any goods other than those of the seller or any other person;
- c. **Exclusive distribution agreement**- includes any agreement to limit, restrict or withhold the output or supply of any goods or allocate any area or market for the disposal or sale of the goods;
- d. **Refusal to deal** - includes any agreement which restricts, or is likely to restrict, by any method the persons or classes of persons to whom goods are sold or from whom goods are bought;
- e. **Resale price maintenance** - includes any agreement to sell goods on a condition that the prices to be charged on the resale by the purchaser shall be the prices stipulated by the seller unless it is clearly stated that prices

lower than those prices may be charged.

### **Exception to Section 3**

Any agreement protecting rights conferred under:

1. Copyright Act 1956 (1999)
2. Patent Act 2005
3. Trademarks Act
4. Designs Act
5. Geographical indication Act

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## **10.4 REGULATION OF COMBINATIONS:**

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### **Meaning of Combination:**

The Acquisition of one or more enterprise by way of merger or amalgamation or control over enterprise is regarded as combination.

A Combination is an acquisition of one or more enterprises by one or more persons, merger or amalgamation of enterprises, if it meets the prescribed monetary thresholds and involves:

- Any acquisition of control, shares, voting rights or assets of any enterprise
- Any acquisition of control by a person over an enterprise, where such person already has direct/indirect control over another enterprise in a similar business
- Any merger or amalgamation of enterprises

Combinations above the defined monetary thresholds require filing and prior approval of the CCI before they can be made effective. CCI has powers to investigate combinations and modify/reject them.

No person or enterprise shall enter into a combination which causes or is likely to cause an appreciable adverse effect on competition within the relevant market in India and such a combination shall be void.

### **Notice prior to entering into a combination**

Any person or enterprise, who or which proposes to enter into a combination shall give notice to the commission, as per the manner prescribed under Competition Commission of India (Procedure in regard to the transaction of business relating to combinations) Regulations, 2011, disclosing the details of the proposed combination, within 30 days of board resolution approving merger or amalgamation or execution of any agreement/document for acquisition or acquisition of control, under section 5.

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## **10.5 FINANCE:**

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### **Grants by Central Government [Section 50]**

The Central Government may make grants to the Commission of such sum of money as it thinks fit for being utilised for the purposes of this Act, after due appropriation made by Parliament by law in this behalf.

**Constitution of Fund [Section 51]**

A fund with the name **Competition Fund** shall be constituted

<b>Credit (Sources)(+)</b>	<b>Application(-)</b>
all Government grants received by the Commission; the fees received under this Act; the interest accrued on the amounts referred to above	the salaries and allowances payable to the Chairperson and other Members and the administrative expenses including the salaries, allowances and pension payable to the Director General, Additional, Joint, Deputy or Assistant Directors General, the Registrar and officers, and other employees of the Commission the other expenses of the Commission in connection with the discharge of its functions and for the purposes of this Act

**Notes**

1. Administration - By a committee of such members of the Commission as may be determined by the Chairperson.
2. As per rule 4 of the Competition Commission of India (Form of Annual Statement of Accounts) Rules 2009, every officer of the Commission incurring or authorizing an expenditure from the Competition Fund should be guided by the Standards of financial propriety and other rules of General Financial Rules, 2005.

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**10.6 Accounts And Audit [Section 52]**

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1. The Commission shall maintain proper accounts and other relevant records and prepare an annual statement of accounts in such form and manner as prescribed in Competition Commission of India (Form of Annual Statement of Accounts) Rules 2009 as the case may be.
2. The accounts of the Commission shall be audited by the Comptroller and Auditor-General of India at such intervals as may be specified by him and any expenditure incurred in connection with such audit shall be payable by the Commission. Any other person may be appointed by him in this regard.
3. Comptroller and Auditor-General of India or such other person shall have the same right as they have in connection with the audit of the Government accounts (including the right to demand the production of books, accounts, connected vouchers, and other documents and papers and to inspect any of the offices of the Commission)
4. Audited account along with audit report shall be forwarded annually to the Central Government and same shall be laid before each House of Parliament.

**Note:**

The orders of the Commission, being matters appealable to the Appellate Tribunal or Supreme Court, shall not be subject to audit under this section.

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### 10.7 Furnishing of Returns, Etc., To Central Government[Section 53]

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The Commission shall furnish such returns and statements and such particulars in regard to any proposed or existing measures for the promotion of competition advocacy, creating awareness and imparting training about competition issues, to Central Government, as required from time to time in accordance with Competition Commission of India (Return on Measures for the promotion of competition Advocacy, Awareness and Training on Competition issues) Rules, 2008.

The Commission shall prepare a report once in every year which gives a true and full account of its activities during the previous year, in such form and at such time as may be prescribed in Competition Commission of India (Form and Time of Preparation of Annual Report) Rules, 2008.

#### Note

Copies of such report shall be forwarded annually to the Central Government and same shall be laid before each House of Parliament at the earliest after receipt by the government.

### CHECK YOUR PROGRESS

#### 1. Answer the following Questions:

1. What Is the Competition?
2. Explain Objects of the Competition Act, 2002
3. Discuss Prohibition of Certain Agreements and Abuse of Dominant Position
4. Explain Regulation of Combinations
5. Explain Meaning of Combination
6. Discuss Notice prior to entering into a combination
7. Discuss about Finance
8. Explain Accounts and Audit [Section 52]
9. Discuss Furnishing of Returns, Etc., To Central Government[Section 53]
10. Write a note on Section 52 and section 53

#### 2. Answer the following MCQ:

1. \_\_\_ is a situation in a market in which firms or sellers independently stride for the buyers' patronage in order to achieve a particular business objective, for example, profit, sales, or market share.
  - A. Competition
  - B. Sales
  - C. Purchase
  - D. Customer
  
2. \_\_\_ objective is to prevent practices having an adverse effect on competition.
  - A. Consumer protection Act, 1986
  - B. Company Act, 1956
  - C. RBI Act, 1934
  - D. Competition Act, 2002

3. \_\_\_objective is to promote and sustain competition in markets.
  - A. Consumer protection Act, 1986
  - B. Company Act, 1956
  - C. RBI Act, 1934
  - D. Competition Act, 2002
  
4. \_\_\_objective is to protect the interests of consumers.
  - A. SEBI Act
  - B. Company Act, 1956
  - C. RBI Act, 1934
  - D. Competition Act, 2002
  
5. \_\_\_\_\_objective is to ensure freedom of trade carried on by other participants in markets in India.
  - A. Consumer protection Act, 1986
  - B. Company Act, 1956
  - C. RBI Act, 1934
  - D. Competition Act, 2002
  
6. Full form of AAEC is \_\_\_\_\_
  - A. Appreciable adverse effect on competition
  - B. Public Sector Undertaking
  - C. Competition Commission of India
  - D. Competition Appellate Tribunal
  
7. Full form of PSU is \_\_\_\_\_
  - A. Appreciable adverse effect on competition
  - B. Public Sector Undertaking
  - C. Competition Commission of India
  - D. Competition Appellate Tribunal
  
8. Full form of CCI is \_\_\_\_\_
  - A. Appreciable adverse effect on competition
  - B. Public Sector Undertaking
  - C. Competition Commission of India
  - D. Competition Appellate Tribunal
  
9. Full form of CAT is \_\_\_\_\_
  - A. Appreciable adverse effect on competition
  - B. Public Sector Undertaking
  - C. Competition Commission of India
  - D. Competition Appellate Tribunal
  
10. The acquisition of one or more enterprise by way of merger or amalgamation or control over enterprise is regarded as\_\_\_\_\_.
  - A. Competition
  - B. Combination
  - C. Purchase
  - D. Customer
  
11. Any person or enterprise, who or which proposes to enter into a combination shall give notice to the commission, within \_\_\_\_\_ days of board resolution

approving merger or amalgamation.

- A. 30
- B. 50
- C. 10
- D. 100

**3. State the following statements are True or False.**

- 1. Full form of AAEC is Appreciable adverse effect on competition: **True**
- 2. Competition is a situation in a market in which firms or sellers independently stride for the buyers’ patronage in order to achieve a particular business objective, for example, profit, sales, or market share: **True**
- 3. The Acquisition of one or more enterprise by way of merger or amalgamation or control over enterprise is regarded as Combination: **True**
- 4. Consumer protection Act, 1986 objective is to ensure freedom of trade carried on by other participants in markets in India: **False**
- 5. Any person or enterprise, who or which proposes to enter into a combination shall give notice to the commission, within 100 days of board resolution approving merger or amalgamation.: **False**
- 6. The acquisition of one or more enterprise by way of merger or amalgamation or control over enterprise is regarded as Competition: **False**

**MCQ Answer**

<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>	<b>6</b>	<b>7</b>	<b>8</b>	<b>9</b>	<b>10</b>	<b>11</b>
<b>A</b>	<b>D</b>	<b>D</b>	<b>D</b>	<b>D</b>	<b>A</b>	<b>B</b>	<b>C</b>	<b>D</b>	<b>B</b>	<b>A</b>





## युनिवर्सिटी गीत

स्वाध्यायः परमं तपः

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स्वाध्यायः परमं तपः

शिक्षण, संस्कृति, सद्भाव, दिव्यबोधनुं धाम  
डॉ. बाबासाहेब आंबेडकर ओपन युनिवर्सिटी नाम;  
सौने सौनी पांभ मणे, ने सौने सौनुं आत्म,  
दशे दिशामां स्मित वहे डो दशे दिशे शुभ-लाभ.

अत्मज्ञ रही अज्ञानना शाने, अंधकारने पीवो ?  
कहे बुद्ध आंबेडकर कहे, तुं था तारो दीवो;  
शारदीय अजवाणा पछोंच्यां गुर्जर गामे गाम  
ध्रुव तारकनी जेम झणहणे अकलव्यनी शान.

सरस्वतीना मयूर तमारे इणिये आवी गहेके  
अंधकारने हउसेलीने उजसना झूल महेके;  
बंधन नहीं को स्थान समयना जवुं न घरथी दूर  
घर आवी मा हरे शारदा दैन्य तिमिरना पूर.

संस्कारोनी सुगंध महेके, मन मंदिरने धामे  
सुभनी टपाल पछोंये सौने पोताने सरनामे;  
समाज केरे दरिये हांकी शिक्षण केरुं वडाण,  
आवो करीये आपण सौ  
भव्य राष्ट्र निर्माश...  
दिव्य राष्ट्र निर्माश...  
भव्य राष्ट्र निर्माश

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