Study Material

BUSINESS LAW

CORE COURSE

B.Com

(I&II Semester)

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UNIT – I

Elements of Law Relating to Contract under Indian Contract Act, 1872

- ✓ **Indian Contract Act,1872**

The Indian Contract Act, 1872 is one of the oldest in the Indian law regime, passed by the legislature of pre-independence India; it received its assent on 25th April 1872. The statute contains essential principles for formation of contract along with law relating to indemnity, guarantee, bailment, pledge and agency.

- ✓ **Meaning of a valid Contract:**

An agreement involves an offer or proposal by one person and acceptance of such offer or proposal by another person. If the agreement is capable of being enforced by law then it is a contract. Section 2[h] of Indian Contract Act, 1872 defines the term contract as "an agreement enforceable by law".

According to the terms of Section 10 of the Act, an agreement is a valid contract if it is made by the free consent of the parties competent to contract, for a lawful consideration and with alawful object and are not expressly declared to bevoid.

- ✓ **Essential Elements of a valid Contract**

In order to be a valid contract, in the first place there must be an offer and the said offer must have been accepted. Such offer and acceptance should create legal obligations between parties. This should result in a moral duty on the person who promises or offers to do something. Similarly this should also give a right to the promisee to claim its fulfillment. Such duties and rights should be legal and not merely moral. These elements can be summarized as follows:

1. **Intention to create legal obligation through offer andacceptance:**

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right to the promisee to claim its fulfillment. Such duties and rights should be legal and not merely moral.

2. Free consent of theparties:

The second element is the 'consent' of the parties. 'Consent' means 'knowledge and approval' of the parties concerned. This can also be understood as identity of minds in understanding the term viz consensus ad idem. Further such consent must be free. Consent would be considered as free consent if it is not vitiated by coercion, undue influence, fraud, misrepresentation or mistake. Wherever the consent of any party is not free, the contract is voidable at the option of that party.

3. Competency or capacity to enter intocontract:

Capacity or incapacity of a person could be decided only after reckoning various factors.Section 11 of the Indian Contract Act, 1872 elaborates on the issue by providing that a person who-

a) has not attained the age of majority,

b) is of unsound mind and

c) is disqualified from entering into a contract by any law to which he is subject,

should be considered as not competent to enter into any contract. Therefore, law prohibits (a) Minors (b) persons of unsound mind and (c) person who are otherwise disqualified like an alien enemy, insolvents, convicts etc from entering into any contract.

4. Lawful consideration:

'Consideration' would generally mean 'compensation' for doing or omitting to do an act or deed. It is also referred to as '*quid pro quo'* viz 'something' in return for another thing'. Such a consideration should be a lawful consideration.

5. Lawful object:

The last element to clinch a contract is that the agreement entered into for this purpose must not be which the law declares to be either illegal or void. An illegal agreement is an agreement expressly or impliedly prohibited by law. A void agreement is one without any legal effects. For Example: Threat to commit murder or making/publishing defamatory statements or entering into agreements which are opposed to public policy are illegal in nature.

❖ **Proposal /Offer**

The word 'proposal' and the word 'offer' mean one and the same thing and therefore are used interchangeably. In terms of Section 2(a) of the Act "a person is said to make a proposal when hesignifiestoanotherhiswillingnesstodoorabstainfromdoinganythingwithaviewto

obtaining the assent of that other to such act or abstinence". Hence there are two important ingredients to an offer. Firstly, it must be expressions of willingness to do or to abstain from doing an act. Secondly the willingness must be expressed with a view to obtain the assent of the other party to whom the offer is made.

Classification of offer

Offer can be classified in the following ways:

a. **General offer:** It is an offer made to public at large with or without any time limit. In terms of Section 8 of the Act anyone performing the conditions of the offer can beconsidered to have accepted the offer ..Until the general offer is retracted or withdrawn, it can be accepted by anyone at any time as it is a continuingoffer.

b. **Special/specific offer**: Where an offer is made to a particular and specified person, itis a specific offer. Only that person can accept such specific offer, as it is special and exclusive to him.

c. **Cross offer**: As per section 2(b), when a person to whom proposal (offer) is made signifies his assent, the proposal is said to be accepted. Thus, assent can be only to a 'proposal'. If there was no proposal, question of its acceptance cannot arise. For example, if A makes a proposal to B to sell some goods at a specified price and B, without knowing proposal of A, makes a proposal to purchase the same goods at the price specified in the proposal of A, it is not an acceptance, as B was not aware of proposal made by A. It is only cross proposal (cross offer). And when two persons make offer to each other, it cannot be treated as mutual acceptance. There is no binding contract in such a case.

d. **Counter offer:** Upon receipt of an offer from an offer or, if the offeree instead of accepting it straightway, imposes conditions which have the effect of modifying or varying the offer, he is said to have made a counter offer. Counter offers amount to rejection of originaloffer.

e. **Standing or continuing or open offer**: An offer which is made to public at large and if it is kept open for public acceptance for a certain period of time, it is known as standing or continuing or open offer. Tenders that are invited for supply of materials and goods are classic examples of standingoffer.

Rules relating to offer

Following are the rules for a valid and legal offer:

a. The 'offer' must be with intent to create a legal relationship. Hence if it is accepted, it must result in a validcontract.
b. The offer must be certain and definite. It must not bevague.
c. The offer must be express orimplied.
d. The offer must be distinguished from an invitation tooffer.
e. The offer must be either specific orgeneral.
f. The offer must be communicated to the person to whom it is made. Otherwise the offeree cannot accept theoffer.
g. The offer must be made with a view to obtaining the consent of the offeree.
h. An offer can be conditional but there should be no term in the offer that non-compliance would amount to acceptance. Thus, the offeror cannot say that if non-acceptance is not communicated by a certain time the offer would be treated as accepted.

Invitation to Offer

An offer is definite. It is an intention towards a contract. An invitation to offer is an act precedent to making an offer. It is done with intent to generally to induce and negotiate. An invitation to offer gives rise to an offer after due negotiation and it cannot be per se accepted. In an invitation to offer there is no expression of willingness by the offeror to be bound by his offer. It is only a proposal of certain terms on which he is willing to negotiate. It is not capable of being accepted as it is. When there is advertisement by a person he has a stock of books for sale, it is an invitation to offer and not an offer. This advertisement is made to receive offers and to further negotiate.

Following are instances of invitation to offer to buy or sell:

i. An invitation by a company to the public to subscribe for itsshares.
ii. Display of goods for sale in shopwindows.
iii. Advertising auction salesand
iv. Quotation of prices sent in reply to a query regardingprice.

Acceptance

In terms of Section 2(b) of the Act, " A proposal or offer is said to have been accepted when the person to whom the proposal is made signifies his assent to the proposal to do or not to do something". In short, act of acceptance lies in signifying one's assent to the proposal.

Relationship between offer and acceptance

Acceptance converts the offer into a promise and then it is too late to revoke it. The significance of this is that an offer by itself cannot create any legal relationship but it is the acceptance by the offeree which creates a legal relationship. Once an offer is accepted it becomes a promise and cannot be withdrawn or revoked. An offer remains an offer so long as it is not accepted, but becomes a contract as soon as it is accepted.

Rules governing acceptance

1. Acceptance must be absolute and unqualified: As per Section 7 of the Act, acceptance is valid only when it is absolute and unqualified and is also expressed in some usual and reasonable manner unless the proposal prescribes the manner in which it must be accepted. If the proposal prescribes the manner in which it must be accepted, then it must be accepted accordingly.
2. The acceptance must be communicated: To conclude a contract between the parties, the acceptance must be communicated in some perceptible form. Any conditional acceptance or acceptance with varying or too deviant conditions is no acceptance. Such conditional acceptance is a counter proposal and has to be accepted by the proposer, if the original proposal has to materialize into a contract.
3. Acceptance must be in the prescribed mode: Where the proposal prescribes the mode of acceptance, it must be accepted in that manner. Where the proposal does not prescribe the manner, then it must be accepted in a reasonable manner. If the proposer does not insist on the proposal being accepted in the manner in which it has to be accepted, after it is accepted in any other manner not originally prescribed, the proposer is presumed to have consented to the acceptance. Sometimes the acceptor may agree to a proposal but may insist on a formal agreement, in which case until a formal agreement is drawn up there is no completeacceptance.
4. The acceptance must be given within a reasonable time and before the offerlapses.

5. Mere silence is not acceptance. The acceptor should expressly accept the offer. Acceptance can be implied also. Acceptance must be given only by that person to whom it is made, that too only after knowing about the offer made tohim.

Communication of Offer and Acceptance

One important common requirement for both 'offer' and 'acceptance' is their effective communication. Effective and proper communication prevents avoidable revocation and misunderstanding between parties. The communication part of it assumes importance because parties are separated by and distance. In which case the modes of communication like, post/courier, telegram, fax, email, telephone etc., become very relevant because the method of communication would also decide the 'time' of 'offer' and 'acceptance'. The Indian Contract Act, 1872, gives a lot of importance to "time" element in deciding when the offer and acceptance is complete.

Consideration

The expression 'consideration' has to be understood as a price paid for an obligation. Consideration is "some right, interest, profit or benefit accruing to one party or forbearance, detriment, loss, or responsibility given, suffered or under taken by the other". The judgment thus refers to the position of both the promisor, and the promisee in an agreement. Section 2 (d) of the Act defines consideration as 'when at the desire of the promisor, the promisee or any other person has done or abstained from doing, or does or abstains from doing or promises to do or abstain from doing something, such an act or abstinence or promise is called consideration for the promise".

From the above definition it can be inferred that consideration is doing or not doing something, which the promisor desires to be done or not done.

I. Consideration must be at the desire of thepromisor.
II. Consideration may move from one person to any otherperson.
III. Consideration may be past, present or futureand
IV. Consideration should be real though notadequate

In terms of section 13 of the Act, two or more persons are said to have consented when they agree upon the same thing in the same manner. This is referred to as identity of minds or "consensusad-idem". Absence of identity of minds would arise when there is an error on the part of the partiesregarding

a. nature of transactionor
b. person dealt withor
c. subject matter ofagreement.

In such cases there would be no consent. However cases of fundamental errors have to be distinguished from cases of mutual mistakes.

The consent referred above must be "free consent" as well. Consent is free when it is not caused by coercion, undue influence, fraud, misrepresentation or mistake (Section 14). When the consent is caused by mistake, the agreement is void, but when caused by other factors it is voidable.

1. **Coercion (Section 15):** "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. An agreement induced by coercion is voidable and not void. That means it can be enforced by the party coerced, but not by the party using coercion.
2. **Undue influence (Section 16):** A contract is said to be induced by "undue influence" where the relations subsisting between the parties are such that one of the parties is in a position to dominate the will of the other and uses that position to obtain an unfair advantage of the other. A person is deemed to be in a position to dominate the will of the other, when he holds authority, real or apparent over the other, or when he stands in a fiduciary relation to other. The essential ingredients of undue influence are:

   One of the parties dominates the will of the other and

   a. He has real or apparent authority over theother;
   b. He is in a position to dominate the will of the otherand
   c. The dominating party takes advantage of therelation.

Following are the instances where one person can be treated as in a position to dominate the will of the other.

i. A solicitor can dominate the will of theclient.
ii. A doctor can dominate the will of his patient having protracted illnessand
iii. A trustee can dominate the will of thebeneficiary.

The burden of proof (in situations like the above) that there is no undue influence in an agreement would be on the person who is in a position to dominate the will of theother.

3. **Fraud (Section 17):** Fraud means and includes any of the following act committed by a party to a contract or with his connivance or by his agent with intent to deceive anotherparty.

Types ofContracts:

The following are the main types of contracts:

1. **VoidContract**

A void contract is one which cannot be enforced by a court of law. As per Section 2 (j) "A contract which ceases to be enforceable by law becomes void". For example, a contract becomes void when any of the following happens:

a. Where both parties to an agreement are under a mistake of fact [Section20]
b. When the consideration or object of an agreement is unlawful [Section23],
c. An agreement without consideration [Section25],
d. An agreement in restraint of marriage [Section 26], trade [Section 27], legal proceedings [Section 28] and agreement by way of wager [Section 30] are instances of void contract.

2. **Voidable Contract**

A voidable contract is one where one of the parties to the agreement is in a position or is legally entitled or authorized to avoid performing his part. Such a right might arise from the fact that the contract may have been brought about by one of the parties by coercion, undue influence, fraud or misrepresentation and hence the other party has a right to treat it as a voidable contract. Section 2[i] defines a voidable agreement which is enforceable by law at the option of one or more parties but not at the option of the other or others.

3. **IllegalContracts**

Illegal contracts are those that are forbidden by law. All illegal contracts are hence void also. Because of the illegality of their nature they cannot be enforced by any court of law. Thus, contracts which are opposed to public policy or immoral are illegal. Similarly contracts to commit crime like *supari*contracts are illegalcontracts.

4. **ExpressContracts**

A contract would be an express contract if the terms are expressed by words or in writing. Section 9 of the Act provides that if a proposal or acceptance of any promise is made in words the promise is said to beexpress.

5. **ImpliedContracts**

Implied contracts come into existence by implication which is mostly by law and or by action. Section 9 of the Act contemplates such implied contracts when it lays down that in so far as such proposal or acceptance is made otherwise than in words, the promise is said to be implied. For instance 'A' delivers goods by mistake at the warehouse of 'B' instead of that of 'C'. Here 'B' not being entitled to receive the goods is obliged to return the goods to 'A' although there was no such contract to that effect.

6. **Tacit Contracts**

Tacit contracts are those that are inferred through the conduct of parties. An example of tacit contract is where a contract is assumed to have been entered when a sale is given effect to at the fall of hammer in an auction sale.

7. **Executed Contract**

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

8. **Executory Contract**

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

9. **UnilateralContract**

Unilateral contracts is a one sided contract in which only one party has to perform his dutyor obligation.

10. **BilateralConracts**

A Bilateral contract is one where the obligation or promise is outstanding on the part of both the parties.

Contingent Contracts

In terms of Section 31 of the Act contingent contract is a contract to do or not to do something, if some event collateral to such contract does or does not happen. Contracts of indemnity and

contracts of insurance fall under this category.Forinstance, if 'A' contracts to pay 'B' ` 100000/- if B's house is destroyed by fire then it is a contingentcontract.

Essentials of a contingent contract

1. The performance of a contingent contract would depend upon the happening or non happening of some event or condition. The condition may be precedent orsubsequent.
2. The event referred to is collateral to the contract. The event is not part of the contract. The event should be neither performance promised nor a consideration for apromise.
3. The contingent event should not be a mere 'will' of the promisor. The event should be contingent in addition to being the will of thepromisor.

Rules Relating to Enforcement a Contingent Contract

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

1. *Contingency is the "happening of an event":* Where a contract identifies happening of a future contingent event, the contract cannot be enforced until and unless the event 'happens'. If the happening of the event becomes impossible, then the contingent contract is void.
2. *Contingency is the non-happening of an event*: Where a contingent contract is made contingent on a non-happening of an event, it can be enforced only when its happening becomes impossible.
3. *Contingent on the future conduct of a living person:* A contract would cease to be enforceable if it is contingent upon the conduct of a living person when that living person does something to make the 'event' or 'conduct' as impossible of happening.
4. *Contingent on an impossible event:* A contingent agreement to do a thing or not to do a thing if an impossible event happens is void and hence is not obviously enforceable. The situation would not change even if the parties to the agreement are not aware of such impossibility. 'A' agrees to pay 'B' ` One lakh if Sun rises in the west next morning. This is an impossible event and hencevoid.

Difference between a contingent contract and a wagering contract

1. A wagering agreement is a promise to give money or money's worth with reference toan uncertain event happening or nothappening.
2. A contingent contract is a contract to do or not to do something with reference toa

collateral event happening or not happening.

3. A wagering agreement consists of reciprocal promises whereas a contingentcontract may not contain reciprocalpromises.
4. In a wagering contract the uncertain event is the core factor whereas in acontingent contract the event is collateral.
5. A wagering agreement is essentially contingent in nature whereas a contingentcontract may not be wagering innature.
6. In a wagering agreement, the contracting parties have no interest in the subject matter whereas it is not so in a contingentcontract.
7. A wagering contract is a game, losing and gaining alone matters whereas it is not so ina contingent contract.
8. A wagering agreement is void where as a contingent contract isvalid.

Quasi – Contracts

Even in the absence of a contract, certain social relationships give rise to certain specific obligations to be performed by certain persons. These are known as quasi contracts as they create same obligations as in the case of regular contract. Quasi contracts are based on principles of equity, justice and good conscience.

Salient features of quasi contracts are:

I. In the first place, such a right is always a right to money and generally, though not always, to a liquidated sum of money.

II. Secondly, it does not arise from any agreement of the parties concerned, but it imposed by the law; and

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

Types of Quasi Contract

There are five circumstances which are identified by the Act as quasi contracts. These five circumstances do not result in regular contracts.

1. **Claim for necessaries supplied to persons incapable of contracting**: Any person supplying necessaries of life to persons who are incapable of contracting is entitled toclaim

the price from the other person's property. Similarly where money is paid to such persons for purchase of necessaries, reimbursement can be claimed.

2. **Right to recover money paid for another person:** A person who has paid a sum of money which another is obliged to pay, is entitled to be reimbursed by that otherperson provided the payment has been made by him to protect his owninterest.
3. **Obligation of person enjoying benefits of non-gratuitous act**: In term of section 70 of the Act "where a person lawfully does anything for another person, or delivers anything to him not intending to do so gratuitously and such other person enjoys the benefit thereof, the latter is bound to pay compensation to the former in respect of, or to restore, the thing so done or delivered.
4. **Responsibility of finder of goods:** In terms of Section 71 'A person who finds goods belonging to another and takes them into his custody is subject to same responsibility as if he were abailee'.
5. **Liability for money paid or thing delivered by mistake or by coercion:** In terms of Section 72 of the Act, "a person to whom money has been paid or anything delivered by mistake or under coercion, must repay or return it. Every kind of payment of money or delivery of goods for every type of 'mistake' is recoverable. A payment of municipal tax made under mistaken belief or because of mis- understanding of the terms of lease canbe recovered from municipal authorities.

Performance of Contracts

Performance by all the parties of the respective obligations is the natural and normal mode of termination or discharging of a contract. Section 37 of the Contract Act, states that the parties to a contract must either perform or offer to perform their respective promise under the contract. In case of performance involving personal skill, taste, credit etc., the promisor himself must perform the contract. In case of contract of impersonal nature, the promisor himself or his agent must perform the contract, but in case of death of the promisor before the performance, the liability of performance falls on his legal representative. Section 41 states that if the promisee accepts the performance of the promise from a third party, he cannot afterwards enforce it against thepromisor.

By Whom a Contract may bePerformed

The promise under a contract can be performed by any one of the following:

I. **Promisor himself:** Invariably the promise has to be performed by the promisor where the contracts are entered into for performance of personal skills, or diligence or personal confidence, it becomes absolutely necessary that the promisor performs it himself.

II. **Agent**: Where personal consideration is not the foundation of a contract, the promisor or his representative can employ a competent person to performit.

III. **Representatives:** Generally upon the death of promisor, the legal representatives of the deceased are bound by the promise unless it is a promise for performance involving personal skill or ability of thepromisor.

IV. **Third Person:** Where a promisee accepts performance from a third party he cannot afterwards enforce it against the promisor. Such a performance, where accepted by the promisor has the effect of discharging the promisor though he has neither authorized nor ratified the act of the third party.

V. **Joint promisors**: Where two or more persons jointly promise, the promise must be performed jointly unless a contrary intention appears from the contract.

Termination and Discharge of Contracts

Discharge of a contract implies termination of the contractual relationship between the parties. On the termination of such relationship, the parties are released from their obligations in the contract. In this way the contract comes to an end. In other words, a contract is said to be discharged when the rights and obligations created by the contract are terminated. The contract may be discharged in any one of the following ways which are known as modes of discharging contract.

Modes of Discharge of Contract:

A contract can be discharged in the following ways:

1. Byperformance
2. By mutualagreement
3. By superveningimpossibility

4. By operation oflaw
5. By lapse oftime
6. By materialalteration
7. By breach ofcontract

1. Discharge of Contract byPerformance:

This is the most popular and usual way of discharging the contract. Performance means accomplishing of that which is required by a contract. This may be of two types:

i. *Actual performance:* When both the parties do what they have promised to do, the contract is said to be performed. In this way both parties get released from their obligations in that contract, and the contract comes to an end.

ii. *Attempted performance:* when the promisor is ready and willing to perform his promise, but the promisee refuses to accept the performance, it is known as attempted performance. An attempted performance, to be legally valid, must have the following requirements:

a. It must be unconditional
b. It must be made at reasonable place and time.
c. Reasonable opportunity to ascertain capability.
d. Reasonable opportunity for inspection of goods.
e. It must have been made to the promisee or proper person.

2. Discharge of contract by Mutual agreement:

A contract is formed when the parties mutually agree on a matter. In the same way both the parties of a contract may by mutual agreement discharge the contract.

3. Discharge of contract by superveningimpossibility:

A contract is discharged due to supervening impossibility under the following situations:

i. *Destruction of subject matter ofcontract*
ii. *Non existence or non occurrence of a particular state ofthings*
iii. *Change of law or stepping in of a person with statutoryauthority.*
iv. *Death or personal incapacity of theparty.*
v. *Declaration ofwar.*

4. Discharge of contract by operation of law

A contract may also be discharged by the operation of the law. In these cases, the law comes into force and the parties are released from their obligations in the contract. Following are the instances where the contract is discharged by an operation of law:

i. *Death ofpromisor*
ii. *Insolvency*
iii. *Merger*
iv. *Loss ofevidence*

5. Discharge of contract by lapse oftime

The contract must be performed within a stipulated period of time or a reasonable period of time. If not, the contract will be discharged. Provisions regarding the time factor are provided in the Indian Limitation Act.

6. Discharge of contract by material alterations

A contract is also discharged when the promisee or his agent makes any material alteration, without the consent of the other party, in the document containing the contract and its terms and conditions.

7. Discharge of contract by breach of contract

Breach of contract means refusal of performance on the part of the parties. That means failure of a party to perform his or her obligation under a contract.

Breach of contract can be actual breach or anticipatory breach. Where a person repudiates a contract before the stipulated due date, it is anticipatory breach. In both the events, the party who has suffered injury is entitled for damages. Further he is discharged from performing his part of the contract.

I. Anticipatory Breach of Contract

Where the promisor refuses to perform his obligation even before the specified time for performance and signifies his unwillingness, then there is an anticipatory breach.

II. Actual Breach of Contract

Where one of the parties breaches the contract by refusing to perform the promise on due date, it is known as actual breach of contract. In such a case the other party to contract obtains a right of action against the one who breached thecontract.

╗ Remedies for Breach ofContract

The various types of remedies available to the aggrieved party in the event of breach of a contract are shown as follows:

1. **Rescission of contract:** Where one party breaches the contract, the other partycan treat it as rescinded. In this case the other party is absolved of his obligation and is entitled to compensation for damages which he suffered.
2. Q**uantum Meruit**: The phrase '*quantum meruit'* literally means "*as much as is earned*" or "*according to the quantity of work done*". A person who has begun a civil contract work and has to later stop the work because the other party has made the performance impossible, is entitled to receive compensation on the principle of 'Quantum Meruit'.
3. **Damages:** Another remedy available in the case of breach of contract is damages. Damages may be any of the four types as follows:
    a. **Ordinary**: Damages which arise in the ordinary course of events from the breach of contract are called ordinary damages. These damages constitute the direct loss suffered by the aggrieved party. They are estimated on the basis of circumstances prevailing on the date of the breach of the contract. Subsequent circumstances tending to change the quantum of the damages are ignored.
    b. **Special:** These damages result from the breach of the contract under special circumstances. They constitute the indirect loss suffered by the aggrieved party on account of breach of contract. They can be recovered only when the special circumstances responsible for the special losses, were made known to the party at the time of the making of thecontract.
    c. **Exemplary or vindictive damages:** They are quite heavy in amount and are awarded by way of punishment , when there is a breach of a contract to marry or dishonor of a customer's cheque by the bank without any proper reason. These damages are awarded with the intention of punishing the defaultingparty.

d. **Nominal:** These damages are quite small in amount and are never granted by way of compensation for the loss. In such cases, usually the actual loss may be very negligible. They are awarded simply to recognize the right of the party to claim damages for the breach of thecontract.

4. **Specific Performance:** Courts can, at their discretion, order for the specific performance of a contract according to the provision of the Specific Relief Act. In those cases monetary compensation will not be an adequate remedy or actual damages cannot accurately be assessed. Specific performance of an agreement will not be granted if the agreement has been made without consideration, or the court cannot supervise its execution, or it will be inequitable (that is not fair and just), or if the contract is of a personal nature.
5. **Injunction:** Where a contract is of a negative character, i.e., a party has promised not to do something and he does it and thereby commits a breach of contract, the aggrieved party may, under certain circumstances, seek the protection of the court and obtain an injunction, forbidding the party from committing breach. An injunction is an order of the court instructing a person to refrain from doing some act which has been the subject matter of the contract.
6. **Restitution:** It means an act of restoration. According to Alison, a person who has been unjustly enriched at the expense of another must make compensation to the other.

UNIT – II

Indian Contract Act: Specific Contracts

Special contracts are a species of general contract itself, as such the principles of general contract are applicable to them. Special contracts include contract of indemnity and guarantee, bailment, pledge and agency

❖ Bailment

Sections 148 to 181 of the Indian Contract Act, 1872 (Chapter IX) deal with contracts of bailment and pledge. Bailment is the change of possession of goods from one person to another for some specific purpose. It is defined by Section 148, *as the delivery of goods by one person to another for some purpose, upon a contract that they shall, when the purpose is accomplished, be returned or otherwise disposed off according to the direction of the person delivering them. The person delivering the goods is called the '"Bailor" and the person to whom the goods are delivered is called the "Bailee".* For example, if A delivers his car to B, a mechanic for repairs, then there is a contract of bailment between A and B. Here A is the bailor and B is the bailee.

❖ Characteristics of Bailment

A contract of bailment has the following characteristics:

1. Delivery of goods
2. Agreement
3. Purpose
4. Return of goods

❖ Pledge

Section 72 defines a pledge as *'the bailment of goods as security for payment of debt or performance of a promise'.* The person who delivers the goods as security is called pledgor (pawnor) and the person to whom the goods are so delivered is called pledge (pawnee). The ownership of the goods remains with the pledgor. It is only a qualified property that passes to the pledge. For example, if A borrows Rs. 25000 from B and keeps his gold ornaments as security, a contract of pledge arises. Here, A is the pledgor and B is the pledge. Pledges are a form of

security to assure that a person will repay a debt or perform an act under a contract. In a contract of pledge, one person temporarily gives possession of his property to another party.

❖ Contract ofIndemnity

In ordinary parlance, the term indemnity means to make good any loss or to compensate any person who has suffered some loss. Section 124 of the Act defined a contract of indemnity as a contract by which one party promises to save the other from a loss caused to him by the conduct of the promisor himself, or the conduct of any other person. The person who makes the promise to make good the loss is called the **indemnifier**. The person whose loss is to be made good is called **indemnity holder**.

A contract of indemnity is entered into for compensating losses of the other party that may or may not occur in future. As such, a contact of indemnity is a type of contingent contract. The performance of the contract is dependent on happening or non happening of a contingency which may cause losses to another party.

❖ Contract of Guarantee

A contract of guarantee is a contract to perform the promise made or discharge liability incurred by a third person in case of his default. The contract of guarantee is made to ensure performance of a contact or discharge of obligation by the promisor. In case he fails to do so, the person giving assurance or guarantee becomes liable for such performance or discharge. In a contract of guarantee there are three parties, namely, the principal debtor, creditor and surety. The principal debtor is primarily liable to pay and the surety is the person who gives the guarantee.

❖ Characteristics of contract of guarantee

The following the characteristics of a contract of guarantee:-

1. *Essentials of a valid contract:* It must possess all the essentials of a validcontract.
2. *Concurrence of the party:* To be legally valid, there must be concurrence of all the parties (three, principal debtor, creditor and surety) to a contract of guarantee and to its terms andconditions.
3. *Consideration:* It must be supported by a lawfulconsideration.
4. *Primary liability:* In a contract of guarantee there is a primary liability on the principal debtor to repay or to discharge theobligation.
5. *Implied Indemnity:* In every contract of guarantee, there is an impliedindemnity.

6. *Disclosure of facts:* It is duty of the creditor that he must disclose to the surety all those facts likely to affect the degree of hisresponsibility.
7. *Form of a contract:* According to Section 126 of the Act, the contract of guarantee may be made in writing or by the words ofmouth.

╕╝ Law ofAgency

The contract of agency is a part of the Indian Contract Act, 1872. The terms 'agent' and 'principal' are defined in Section 182 of the Act. According to this section, *an agent is a person employed to do any act for another or to represent another in dealings with third persons. The person for whom such act is done, or who is represented is called the principal.* The contract which creates the relationship of principal and agent is called 'agency'. If A appoints B to act on behalf of him in a situation, there is a contract of agency. Here, A is the principal and B is the agent. The definition given by the Act is very wide and includes servant, employee etc.

❖ Essentials of a Contract of Agency

To constitute a contract of agency, the following essentials are required:

I. *Agreement:* An agreement between the principal and the agent is the first requirement of a contract of agency.
II. *Competency of principal:* Section 183 of the Act states that any person who is of the age of majority and of sound mind can employ an agent.
III. *Consideration not necessary:* No consideration is required to create an agency (Section 185). The agent is remunerated by way of commission for his services rendered.

❖ Termination of Agency

Section 201 provides the circumstances under which an agency can be terminated. According to this, an agency is terminated by the principal revoking his authority, or by the agent renouncing the business of the agency being completed, or by either the principal or the agent dying or becoming of unsound mind, or by the principal being adjudicated an insolvent.

❖ Finder of lost goods and hisposition

In terms of Section 71 'A person who finds goods belonging to another and takes them into his custody is subject to same responsibility as if he were a bailee'.

Thus a finder of lost goods has:

I. To take proper care of the property as men of ordinary prudence wouldtake
II. No right to appropriate the goodsand
III. To restore the goods if the owner isfound.

❖ Rights and Duties of Finder ofGoods

A 'finder of lost goods' is as good as a bailee and he enjoys all the rights and carries all the responsibilities of a bailee.

The bailee has the following rights:

I. To claim compensation for any loss arising from non-disclosure of known defects inthe goods.
II. To claim indemnification for any loss or damage as a result of defective title.
III. To deliver back the goods to joint bailers according to the agreement or directions
IV. To deliver the goods back to the bailor whether or not the bailor has the right to the -- goods
V. To exercise his 'right of lien'. This right of lien is a right to retain the goods and is exercisable where charges due in respect of goods retained have not been paid. The right of lien is a particular lien for the reason that the bailee can retain only these goods for which the bailee has to receive hisfees/remuneration.
VI. To take action against third parties if that party wrongfully denies the bailee of his right to use the goods.

Apart from the above, the 'finder of lost goods' can ask for reimbursement for expenditure incurred for preserving the goods but also for searching the true owner. If the real owner refuses to pay compensation, the 'finder' cannot sue but retain the goods so found. Further where the real owner has announced any reward, the finder is entitled to receive the reward. The right to collect the reward is a primary and a superior right even more than the right to seek reimbursement of expenditure. Lastly the finder though has no right to sell the goods found in the normal course, he may sell the goods if the real owner cannot be found with reasonable efforts or if the owner refuses to pay the lawful charges subject to the followingconditions.

a. When the article is in danger of perishing and losing the greater part of the valueor
b. When the lawful charges of the finder amounts to two-third or more of the value of the articlefound.

UNIT – III

Elements of Law Relating to Sale of Goods under Sale of Goods Act, 1930

The law relating to sale of goods is contained in the Sale of Goods Act, 1930. The Act came into force on 1st July, 1930. Provisions pertaining to the sale of goods were earlier contained in Chapter VII of the Indian Contract Act, 1872. The Act of 1930 extends to whole of India, except Jammu and Kashmir. It deals with provisions relating to passing of ownership of the goods from seller to buyer, duties of seller and buyer, rights of unpaid seller, remedies available to buyer if the goods are not delivered to him etc.

❖ Contract of Sale

The term contract of sale is a generic term and it includes both sale and agreement to sell. Where, under a contract of sale, the property in goods is transferred from seller to the buyer, it is called 'Sale' but where the transfer of property in goods is to take place at a future time or subject to some conditions thereafter to be fulfilled, the contract is called ' agreement to sell'. Section 4 (1) of the Act defines a contract of sale of goods as *a contract whereby the seller transfers or agrees to transfer the property in goods to the buyer for price.*

❖ Essentials of Contract of Sale

The following are the essentials of contract of sale:

1. *Two parties:* There are two distinct parties in a contract of sale – seller and buyer.
2. *Transfer of general property:* 'Property' means the general property in goods and not merely a special property [Section 2(11)].
3. *Goods:* Goods form the subject matter of the contract and must be movable. Goods mean every kind of movable property other than actionable claims and money and include stock and shares, growing crops, grass and things attached to or forming part of land which are agreed to be severed sale or under the contract ofsale.
4. *Price:* The consideration for the contract of sale must be in the form of money and is calledprice.
5. *All essentials of a valid contract:* All the essential elements of a valid contract like agreement, free consent, consideration, etc. must be present in a contract of sale ofgoods.

❖ Sale v/s Agreement to sell

There are a number of distinctions between sale and agreement to sell. Following are the main points of difference between the two:-

Distinction between sale and agreement to sell

Sale	Agreement to sell
1. Sale is an executedcontract.	1. Agreement to sell is an executorycontract.
2. Performance of sale is absolute and without any condition.	2. Performance is conditional and is made infuture.
3. The property of the goods passes from the seller to the buyer immediately and the seller is no longer the owner Of the goods sold.	3. The transfer of property takes place on afuture date, or at times subject to fulfillment of certain conditions.
4. If the goods are lost or destroyed, the loss falls on the buyer, even if they are in the possession of the seller.	4. If the goods are lost or destroyed, the loss falls on seller, even if they are in the possession of the buyer
5. If there is a breach of contract, the seller can sue for the price, even if the goods are in his possession.	5.If the buyer fails to accept the goods, the seller c can only sue for damages and not the price even if the goods are in the possession of the seller.
6. As the property is with the buyer, the seller cannot resell the goods.	6. The property remains with the seller and he can dispose off the goods as he likes.

❖ Conditions andwarranties

Contract of sale of goods will have various terms or stipulations regarding quality of goods, price and mode of payment, delivery of goods and its time and place, etc. All these terms and stipulations are not of equal importance. Some of them may be major terms that go to the very basics or root of the contract and their breach may upset the very purpose of the contract. Certain others are not vital and may not be a breach of contract as such. The major terms, the breach of which may go to the basics of the contract, are known as ‘Conditions’ and the minor terms are

called the 'Warranties'. Section 12[2] and [3] of the Act, deal with conditions and warranties respectively. While conditions are the very basis of a contract of sale, warranty is only of secondary importance.

Condition is defined in Section 12 [2] as a stipulation essential to the main purpose of the contract, the breach of which gives the aggrieved party a right to reject the contract itself. Inaddition, action for damages for losses suffered, if any, due to breach of condition can also be made.

Warranty is defined in Section 12 [3] as stipulation collateral to the main purpose of the contract, the breach of which gives the aggrieved party a right to sue for damages and not to void the contract itself.

Express and Implied conditions and warranties

Conditions may be express or implied. They are express when, at the will of the parties, they are inserted in the contract. They are said to be implied when the law presumes their existence in the contract, even though it has not been put into it in express words. According to Section 62, implied conditions and warranties may be varied by express agreement or by the course of dealing between the parties, or by usage of trade.

Doctrine of Caveat Emptor

The doctrine of *caveat emptor* means 'let the buyer beware'. According to this doctrine , it is the duty of the buyer to be careful while purchasing goods. In the absence of any enquiry from the buyer , the seller is not bound to disclose the defects in the goods. It is the buyer who must examine the goods thoroughly and must see that the goods that he buys are suitable for the purpose of which he want them. If the goods turn out to be defective, the buyer cannot sue the seller, as there is no implied undertaking by the seller that he shall supply goods to suit the buyer's purpose.

Exceptions to caveatemptor

The doctrine of caveat emptor does not apply in the following situations:

a. When the seller makes a representation of fact, whether innocent or fraudulent, regarding theproduct.
b. When the seller actively conceals a defect in the goods which could not be revealed by ordinaryexamination.

c. Where goods are supplied by description and they do not correspond with the description given by theseller.
d. Where goods are supplied by description and they are not of merchantablequality.

Performance of contract ofsale

The performance of a contract of sale implies delivery of goods by the seller and the acceptance of the delivery of goods and payment for them by the buyer, in accordance with the contract. The parties are free to provide any terms they like in their contract about the time, place and manner of delivery of goods, acceptance thereof and payment of the price. But if the parties are silent and do not provide anything regarding these matters in the contract them the rules contained in the Sale of Goods Act are applicable.

Delivery

Delivery of goods means voluntary transfer of possession of goods from one person to another [Sec. 2(2)]. If transfer of possession of goods is not voluntary, that is, possession is obtained under pistol point or by theft, there is no delivery.

Rights of unpaid seller

A seller of the goods is deemed to be an unpaid seller when the whole of the price has not been paid or tendered or a bill of exchange or other negotiable instrument has been received as conditional payment. The unpaid seller has the following rights:

a) *Against the goods*: Against the goods , the unpaid seller has the right of lien, the right of stoppage of goods in transit, and the right of resale. The right of lien can be exercised only for non – payment of the price and not for any other charges. The right of stoppage of goods in transit means the right of stoppage of goods while they are in transit to regain the possession and to retain them till the full price is paid. The right to resale gives the seller the right to resell the goods in the followingcases:

I. When the goods areperishable.
II. When the right is expressly reserved in thecontract.
III. When despite the seller giving a notice to the buyer of the intention to resell, the buyer does not pay or tender the price within a reasonabletime.

b) *Against the buyer personally:* the unpaid seller can file a suit for price, as well as file a suit for damages for non –acceptance.

- **Transfer of Ownership in Goods including Sale by a Non –Owner:**

Transfer of ownership is studied under two heads:

1. *Transfer in specific or ascertainedgoods.*
2. *Transfer in unascertained and futuregoods*

1. Transfer in specific or ascertainedgoods:

Where there is a contract for the sale of specific or ascertained goods the property in them is transferred to the buyer at such time as the parties to the contract intend it to be transferred. For the purpose of ascertaining the intention of the parties regard shall be had to the terms of the contract, the conduct of the parties and the circumstances of the case [Sec. 19 (1) (2)]. Thus, in the case of specific goods, the transfer takes place when the parties intend to pass it. The parties may intend to pass the property at once at the time of making of the contract or when the goods are delivered or when the goods are paid for.

2. Transfer in unascertained and future goods:

The rule relating to transfer of property in unascertained and future goods is contained in Sections 18 and 23. These Sections provide that where goods contracted to be sold are not ascertained or where they are future goods, the property in goods does not pass to the buyer unless and until the goods are ascertained or unconditionally appropriated to the contract so as to bring them in a deliverable state, either by the seller with the assent of the buyer or by the buyer with the assent of the seller. Such assent may be expressed or implied, and may be given either before or after the appropriation is made.

The process of ascertainment or appropriation consists in earmarking or setting apart goods as subject matter of the contract. It involves separating, weighing, measuring, counting or similar acts done in relation to goods with an intention to identify and determine the specific goods to be delivered under the contract.

Transfer of Title/ Sale by a Non – Owner

The general rule relating to transfer of title on sale is that "the seller cannot transfer to the buyer of goods a better title than he himself has." If the title of the seller is defective the buyer's title will also be subject to the same defect. Section 27 also lays down to the same effect and provides that "where goods are sold by a person who is not the owner thereof and who does not sell them under the authority or with the consent of the owner, the buyer acquires no better title to the

goods than the seller had…" This rule is expressed by the maxim, "*nemodet quod habet*", which means *that no one can give what he has not got*.

Thus, a buyer cannot get a good title to the goods unless he purchases the goods from a person who is the owner thereof or who sells them under the authority or with the consent of the owner.

This above general rule as to title is subject to the following exceptions where the buyer gets a better title to the goods than what the seller himself possesses:

1. An unauthorized sale by a mercantileagent.
2. Transfer of tile byestoppels
3. Sale by a jointowner
4. Sale by person in possession under voidablecontract
5. Sale by seller in possession aftersale
6. Sale by buyer in possession after 'agreement to buy'
7. Resale by an unpaid seller
8. Exceptions under other acts

UNIT – IV
PARTNERSHIP LAW

A. Partnership Act,1932

The law of partnership is contained in the Indian Partnership Act of 1932. The Act came into force on 1st October, 1932. This act is based on the English law relating to partnership. Partnership is an association of two or more persons, formed as a result of an agreement to carry on some business, and the agreement must be to share the profits of the business. A partnership will come into existence only where all the above mentioned elements are present.

a. Nature and characteristics of Partnership

Section 4 of the Act defines a partnership as "*the relation between persons who have agreed to share the profits of a business carried on by all or any of them acting for all"*. This definition is also in similar line with the definition provided by Sir F.Pollock. An analysis of the definition provides the essential characteristics of a partnership.

The essential characteristics of a partnership are as follows:

1. *Relation between two or more persons:* Partnership can occur only with a minimum of two persons. The Partnership Act does not mention anything about the maximum number of persons who can be partners in a partnership firm. However, Companies Act, 2013 lays down the limit on the maximum number of partners in a partnership.
2. *Agreement:* Partnership is the result of a contract. It does not arise from status, operation of law, or inheritance. But comes into existence with a mutual agreement between thepartners.
3. *Carrying on business:* The partnership to be called so, the concerned parties must have agreed to carry on a business. The term 'business' has been used in the Act in its widest sense and includes every trade, occupation orprofession.
4. *Sharing of profits*: The agreement to carry on a business must be with the object of making and sharing profits amongst all the partners. The profits (or losses) must be shared among partners in the agreedratio.

5. *Mutual Agency*: The partnership business must be carried on by all partners or any (one or more) of them acting for all. In other sense, there must be mutual agency. Thus, every partner is both an agent and a principal for himself and the otherpartners.
6. *Utmost good faith*: The partners are bound to act in utmost good faith and have to be just and faithful to each other. This assumes greater significance, since partners act both as an agent and a principal for himself and the otherpartners.
7. *Unlimited Liability*: In partnership, the liability of partners is joint as well as unlimited. Each partner is personally and jointly liable to an unlimited extent and each partner's personal property is liable for clearing the debts of the firm, if partnership liabilities cannot be fully discharged our of partnershipproperty.
8. *No separate legal existence*: Partnership firm does not have any separate legal significance or existence, in its own right, other than the persons constituting it jointly.
9. *Restriction on transfer of interest*: In a partnership firm there is a restriction on the transfer of interest. A partner cannot transfer his interest at his own will, it can be done only at the consent of other partners.

b. Registration of Partnership firm

The partnership should be registered as soon as it is formed with the Registrar of Firms in the area. In the absence of registration, the firm will not be able to enforce its legal remedies against outsiders, and the partners also cannot enforce the conditions laid down in the 'partnership deed' through a court of law. The following basic facts must be borne in mind by the persons desirous of entering into an agreement of partnership.

1. A partnership may be formed by oral or by written agreement or an agreement of partnership can be inferred from the conduct of theparties.
2. The successful working of a partnership depends upon mutual confidence and utmost good faith among the partners because each partner is an agent of others and binds them to the fullest extent of theirfortunes.
3. All the essential elements of a valid contract must be present There must be free consent of the parties who must be competent to contract and the object of the partnership should not be forbidden by law or immoral or opposed to publicpolicy.

4. The mutual rights and obligations of partners must be discussed in detail and should be put in black and white in the shape of a 'partnership deed' before the partnership is actuallystarted.

Partnership Deed

The document in which the respective rights and obligations of the members of a partnership are set forth is called a 'partnership deed'. It should be drafted with care and be signed by all the partners. It must be stamped in accordance with the Indian Stamp Act. Each partner should have a copy of the deed. The firm should be registered and copy of the Deed should be filed at the time of registration with the Registrar of Firms because in the absence of such registration, partners cannot enforce the conditions laid down in the Deed through a court of law.

The Deed should cover the following points:

I. The name of business and the names and the addresses of partners who compose it.
II. Nature of business and the town and place where it will be carried on.
III. Date of commencement of partnership.
IV. The duration of partnership.
V. The amount of capital to be contributed by each partner and the methods of raising finance in future if so required.
VI. The ratio of sharing profits or losses.
VII. Interest on partners' capital, partners' loan and interest if any, to be charged on drawings.
VIII. Salaries, commission etc if any, payable to partners and other termsetc.

Duration of Partnership

From the duration point of view the partnership may be classified into the following two categories:

1. **Partnership at will**: Where no provision is made by contract between the partners for the duration of their partnership or for the determination of their partnership, the partnership is 'partnership at will' (Sec. 7). Thus, the essence of a 'partnership at will' is that the partners do not fix any term of partnership and are free to break their relationship at their sweetwill.

2. **Particular partnership:** When a partnership is formed for a *particular period or for a specific venture e.g.,* for working a coal mine or producing a film it is called a 'particular partnership' (Sec. 8). Before such time the partnership would not be dissolved unless all the partners agree to it(Sec.40).

c. Types ofPartners

The different types of partners are the following:

1. **Active or Actual Partners**

Partners who take an active part in the conduct of the partnership business are called 'actual' or 'ostensible' partners. They are full – fledged partners in the real sense of the term. Such a partner must give a public notice of his retirement from the firm in order to free himself from liability for acts after retirement.

2. **Sleeping or Dormant Partners**

A dormant or sleeping partner is one who does not take an active part in the business of the firm. This partner shares profits and losses, has a voice in management, but his relationship with the firm is not disclosed to the general public. He is liable to the third parties for all acts of the firm just like an undisclosed principal. He is however, not required to give public notice of his retirement from the firm.

3. **Silent Partners**

Those who by agreement with other partners have no voice in the management of the partnership business are called 'silent' partners. They share profits and losses, are fully liable for the debts of the firm and may take active part in the conduct of the business.

4. **Partners in Profit only**

A partner who has stipulated with other partners that he will be entitled to a certain share of profits, without being liable for the losses, is known as a 'partner in profits only'. As a rule, such a partner has no voice in the management of the business. However, his liability vis-à-vis third parties will be unlimited.

5. **Partners by Holding out or byEstoppels**

Actually such a person is not a partner in that firm – no agreement, no sharing in profits and losses, no say in the management, may not be a partner , he becomes responsible to outsiders as a partner on the principle of estoppels or holding out. If a person represents to the outside world by words spoken or written or by his conduct or by lending his name, that he is a partner in a certain

partnership firm, he is them stopped from denying his being a partner, and is liable as a partnerin that firm to anyone who has on the faith of such representation granted credit to thefirm.

6. **Nominalpartners**

A nominal partner, as the name suggests, is a partner only in name. Thus, where a person's name is used as if he were a partner of the firm, though actually he is not, he will be known as a 'nominal partner'. Such a partner is not entitled to share the profits of the firm but is liable for all acts of the firm as if he were a realpartner.

7. **Sub –partners**

A sub – partnership comes into existence when one of the partners agrees to share the profits derived by him from the firm with a stranger. That stranger is called a 'sub – partner '. The sub – partner is not a partner in the eyes of the law and, therefore, has no rights against the firm. He is also not liable for the debts of the firm.

8. **Working partners**

A partner, because of his special qualification, may be assigned the management and control of the business. Such a partner is commonly known as a 'working partner'. The working partner normally receives a fixed amount of salary, besides his share in the profits of the firm. Other partners, however, remain liable to the third parties for all his acts.

d. **Incoming Partners and Outgoing Partners**

Incoming Partners: No person can be introduced as a partner into a firm without the consent of all the existing partners. Thus, 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 partners'. An incoming partner does not become liable for any act of the firm done before his admission as a partner. However, where he specifically agreed to bear the past liabilities, he will be liable to the other partners for the same.

Outgoing Partners: A partner who leaves a firm in which the rest of the partners continue to carry on business is called a 'retired' or 'outgoing partner'. Notice to a partner who habitually acts in the business of the firm of any matter relating to the affairs of the firm operates as notice to the firm, except in the case of a fraud on the firm committed by or with the consent of that partner.

e. **Rights and Duties of Partners**

Rights ofPartners

A partner has certain rights as per the provisions of the Partnership Act. They are following:

1. **Right to take part in the conduct of the business:** As per Section 12 [a] of theAct, every partner has the right to take part in the conduct of the business of thefirm.
2. **Right to be consulted:** Every partner has the right to be consulted and heardwith respect to the conduct of the business, before any matter isdecided.
3. **Right of access to books:** Every partner has the right to have access to andinspect and copy of the books of thefirm.
4. **Right to share the profits:** Section 13 [d] of the Act provides every partner, irrespective of the amount of contribution, the right to share equally the profits earned by the firm.
5. **Right to Interest on advances:** Where a partner makes any payment or advances beyond the amount of capital he has agreed to subscribe, he is entitled to receive interest at the rate of 6% per annum.
6. **Right to Indemnity:** As per Section 13 [e], every partner has the right to indemnity from the firm in respect of payments made or liabilities incurred by him.

Duties of Partners

The duties of partners are imposed by law and are not subject to any contract to the contrary. These duties are mandatory in nature and are applicable to all partnerships and cannot be varied by agreement among the partners. The following are some of the duties of partners:

1. **Duty to carry on the business to the greatest common advantages**: According to Section 9 of the Act, every partner is bound to carry on the business of the firm to the greatest common advantage. It implies that every partner must use his knowledge and skill for the benefit of the firm and not for his personalgains.
2. **Duty to be just and faithful**: An ideal partnership is said to be one where there is mutual trust and confidence, and spirit of helpfulness and goodwill among the partners. As such every partner must be just and faithful to his co –partners.
3. **Duty to render true accounts**: Every partner must render true and proper accounts to his co – partners. Each partner must be ready to explain the accounts of the firm and produce vouchers in support of the entries. A partner should not make secret profits at the expense of thefirm.

4. **Duty to provide full information**: All partners must give full information of allmatters affecting the firm to his co – partners. A partner, being an agent of other partners, must not conceal any information concerning the firm from the otherpartners.
5. **Duty to indemnify for loss caused by fraud**: According to Section 10 , if a partner despite acting in a bona fide manner causes loss due to neglect or want of skill or omission, the loss is borne by the firm. When a partner causes loss to the firm due to any fraud committed against a third party, the same must be recovered from the guiltypartner and cannot be shared among all thepartners.
6. **Duty to be liable jointly and severally**: As per Section 25, every partner is liable, jointly and severally, to third parties for all acts of the firm done while he a partner. The liability of all the partners is not only joint and several but also unlimited.
7. **Duty not to assign his interest**: Section 29 states that no partner without the consent of other partners can assign or transfer his partnership interest to any third person so as to make him a partner in the business. He can, however, assign his share of the profit and his share in the assets of the firm. But here the transferee shall not have any right to interfere in the conduct of the business.

f. Implied Authority of a Partner

The firm is also bound by all acts of a partner done within the scope of his implied authority. An implied authority of a partner can be inferred from the circumstances of the case. Generally speaking, such acts of a partner which are incidental to or usually done in the course of the proper conduct of the business come within the scope of his implied or ostensible authority. Sections 19 (1) and 22 define the scope of the implied authority of a partner. Accordingly, for an act to be covered within the implied authority it is necessary that:

i. The act should be done for carrying on the business of the kind carried on bythe firm;
ii. The act should be done in the usual way of such businessand
iii. The act must be done in the firm name or in any other manner expressing or implying an intention to bind thefirm.

Thus, the implied authority of a partner cannot extend to his acts done beyond the scope of the business of the firm. If in a firm of cloth merchants, a partner buys sugar, that will be outside the implied authority of the partner for which the firm cannot be bound. In case of trading or

commercial firm, a partner, in the exercise of his implied authority, can bind the firm by any of the following acts:

i. Buying and selling goods , on behalf of the firm, in which the firmdeals;
ii. Receiving payments of the debts due to the firm and giving valid receipts forthem;
iii. Contracting debts and paying debts on behalf of thefirm;
iv. Settling accounts with persons dealing with thefirm;
v. Employing servants for partnershipfirm;
vi. Drawing cheques, accepting or endorsing bills of exchange and promissory notesin the name of thefirm.
vii. Pledging movable property of the firm;
viii. Suing on behalf of the firm and defending suits in the name of the firm.

g. Modes of Dissolution of Partnership

Sections 39 of the Act deals with dissolution of partnership firm. Section 40 to 44 deal with the various modes of dissolution of a firm. A firm may be dissolved in the following manner:

1. **Dissolution by mutual agreement**: Partnership which is created by an agreement can also be dissolved by mutual agreement.
2. **Compulsory Dissolution:** A firm gets compulsorily dissolved in the following cases:
   - **a.** By the adjudication of all the partners or of all the partners but one is insolvent.
   - **b.** On the happening of any event which makes it unlawful for the business of the firm to be carried on.
   - **c.** If all the partners, or all but one partner, are declared insolvent.
   - **d.** On the happening of any event by which the business being carried on by the partners becomes illegal.
3. **Dissolution on the happening of certain contingencies:** According to Section 42, a firm will be dissolved on the happening of thecontingencies:
   - **a.** If constituted for a fixed term, by the expiry of thatterm.
   - **b.** If constituted to carry out one or more adventures or undertakings, by the completionthereof
   - **c.** By the death of apartner.
   - **d.** By the adjudication of a partner as aninsolvent.

4. **Dissolution by notice of partnership at will :** Where the partnership is at will, the firm may be dissolved by any partner by giving notice in writing to all the other partners of his intention to dissolve thefirm.
5. **Dissolution by the Court:** At the suit of a partner, the court may dissolve a firm on any of the followinggrounds:
   - **a.** If a partner has become of unsoundmind.
   - **b.** Any partner becoming permanently incapable of performing hisduties.
   - **c.** A partner becoming guilty of conduct which is likely to affect prejudicially the carrying on of thebusiness.
   - **d.** If a partner willfully or persistently commits breach of agreements relating to the management of the affairs of the firm.
   - **e.** If a partner has, in any way, transferred the whole of his interest in the firm to a third party.
   - **f.** When the business of the firm cannot be carried on except at a loss.
   - **g.** On any other ground which renders it just and equitable that the firm should be dissolved.

B. Limited Liability Partnership

A. **Salient Features Of Limited Liability Partnership**

Limited liability partnership to be body corporate:

1. A limited liability partnership is a body corporate formed and incorporated under Limited liability partnership Act 2008 and is a legal entity separate from that of its partners.
2. A limited liability partnership shall have perpetual succession like a company has under Companies Act1956.
3. Any change in the partners of a limited liability partnership shall not affect the existence, rights or liabilities of the limited liabilitypartnership.
4. Non-applicability of the Indian Partnership Act, 1932. —Save as otherwise provided, the provisions of the Indian Partnership Act, 1932 (9 of 1932) shall not apply to a limited liabilitypartnership.

5. 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—
    a. he has been found to be of unsound mind by a Court of competent jurisdiction and the finding is inforce;
    b. he is an undischarged insolvent;or
    c. he has applied to be adjudicated as an insolvent and his application ispending.
6. Minimum number ofpartners.
    1. Every limited liability partnership shall have at least two partners and there is no maximumlimit.
    2. 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 reduced to one , 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(one member and business), shall be liable personally for the obligations of the limited liability partnership incurred during that period.

B. **Differences between LLP and Partnership and company**

1. A limited liability partnership has advantages of a Company as well as partnership it is a separate legal entity like a company and are governed by their respective laws and acts viz companies are governed by Companies Act 1956 partnerships are governed by partnership Act 1938 and in the same way Limited liability partnership is governed by Limited liability partnership Act1998.
2. Registration is not important for a partnership whereas registration is important for Companies and LLP with registrar of companies. So far as creation is concerned a partnership is created by contract more specifically a contract of mutual agency where one or few act as agent and another as principal and vice versa. A company is creation of Law and so is a limited liabilitypartnership.

3. A partnership is not a distinct entity in comparison to a company and a limited liability partnership is a distinct entity there by reducing the liability of the owners by mode of separation provided by thelaw.
4. Partnerships are created through mutual agreement between the partners and a nominal fee of agreement is to be incurred where as a LLP is c to be registered and its statutory fee ranges from Rs. 500 to 5000. A partnership firm does not have perpetual succession and its continuity depends upon the will of the partners in comparison to a company where members may come and exit but existence of the company remains un affected. Partnerships do not have a common seal where as a company has to have a common seal and in case of LLP it s the discretion of the partners to have a common seal or not (depends upon the terms of agreement).partnership can sue a third party only if it is registered and a company being a legal entity can be sued and can sue and same is the case with LLP as it has the same characteristics so far as its legal powers are concerned LLP has one more advantage regarding the power to include foreign nationals as its members or subsidiaries and LLP can have foreign individuals as its partners. Partnership can have minimum two and maximum 20 as its members

C. **LLP Agreement**

It is a written agreement between the partners of the limited liability partnership and between the limited liability partnership and its partners which determines the mutual rights and duties of the partners and their rights and duties in relation to that limited liability partnership. It is not necessary to enter into an LLP agreement as per LLP Act, 2008. In the absence of LLP agreement, the mutual rights of partners & in relation to LLP will be determined as per schedule I of the LLP Act,2008.

Due to varied nature of different type of businesses, it may not be practically advisable to have those standard clauses as mentioned in First Schedule. Therefore, it is advisable to have a legally drafted agreement

The First Schedule

[See section 23(4)]

Provisions Regarding Matters Relating to Mutual Rights and Duties of Partners and Limited Liability Partnership and its Partners Applicable in the absence of any Agreement on Such Matters :

1. The mutual rights and duties of the partners and the mutual rights and duties of the limited liability partnership and its partners shall be determined, subject to the terms of any limited liability partnership agreement or in the absence of any such agreement on any matter, by the provisions in thisSchedule.

2. All the partners of a limited liability partnership are entitled to share equally in the capital, profits and losses of the limited liability partnership.

3. The limited liability partnership shall indemnify each partner in respect of payments made and personal liabilities incurred by him—

(a) in the ordinary and proper conduct of the business of the limited liability partnership;or

(b) in or about anything necessarily done for the preservation of the business or property of the limited liability partnership.

4. Every partner shall indemnify the limited liability partnership for any loss caused to it by his fraud in the conduct of the business of the limited liability partnership.

5. Every partner may take part in the management of the limited liability partnership

6. No partner shall be entitled to remuneration for acting in the business or management of the limited liability partnership.

7. No person may be introduced as a partner without the consent of all the existingpartners.

8. Any matter or issue relating to the limited liability partnership shall be decided by a resolution passed by a majority in number of the partners, and for this purpose, each partner shall have one vote. However, no change may be made in the nature of business of the limited liability partnership without the consent of all thepartners.

9. Every limited liability partnership shall ensure that decisions taken by it are recorded in the minutes within thirty days of taking such decisions and are kept and maintained at the registered office of the limited liabilitypartnership.

10. Each partner shall render true accounts and full information of all things affecting the limited liability partnership to any partner or his legalrepresentatives.

11. If a partner, without the consent of the limited liability partnership, carries on any business of the same nature as and competing with the limited liability partnership, he must account for and pay over to the limited liability partnership all profits made by him in thatbusiness.

12. Every partner shall account to the limited liability partnership for any benefit derived by him without the consent of the limited liability partnership from any transaction concerning the limited liability partnership, or from any use by him of the property, name or any business connection of the limited liabilitypartnership.

13. No majority of the partners can expel any partner unless a power to do so has been conferred by express agreement between the partners.

14. All disputes between the partners arising out of the limited liability partnership agreement which cannot be resolved in terms of such agreement shall be referred for arbitration as per the provisions of the Arbitration and Conciliation Act, 1996 (26 of 1996).

D. **Partners and Designated Partners**

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—

(a) he has been found to be of unsound mind by a Court of competent jurisdiction and the finding is in force;

(b) he is an undischarged insolvent; or

(c) he has applied to be adjudicated as an insolvent and his application is pending.

Minimum number of partners.—

(1) Every limited liability partnership shall have at least twopartners.

(2) 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 whilethe

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

(1) 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*. "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.

(2) 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.

(3) 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 beprescribed.

(4) 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 hisappointment.

(5) An individual eligible to be a designated partner shall satisfy such conditions and requirements as may beprescribed.

(6) 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 2668 (both inclusive) of the Companies Act, 1956 (1 of 1956) shall apply mutatis mutandis for the saidpurpose.

8. Liabilities of designatedpartners.—

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

(a) responsible for the doing of all acts, matters and things as are required to be 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

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

9. 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.

10. Punishment for contravention of sections 7, 8 and 9.

(1) If the limited liability partnership contravenes the provisions of sub-section (1) of section 7, the limited liability partnership and its every partner shall be punishable with fine which shall not be less than ten thousand rupees but which may extend to five lakh rupees.

(2) If the limited liability partnership contravenes the provisions of sub-section (4) and sub-section (5) of section 7, section 8 or section 9, the limited liability partnership and its every partner shall be punishable with fine which shall not be less than ten thousand rupees but which may extend to one lakhrupees.

E. **Incorporation Document.**

(1) For a limited liability partnership to be incorporated,—

(a) Two or more persons associated for carrying on a lawful business with a view to profit shall subscribe their names to an incorporationdocument;

(b) The incorporation document shall be filed in such manner and with such fees, as may be prescribed with the Registrar of the State in which the registered office of the limited liability partnership is to be situated;and

(c) there shall be filed along with the incorporation document, a statement in the prescribed form, made by either an advocate, or a Company Secretary or a Chartered Accountant or a Cost Accountant, who is engaged in the formation of the limited liability partnership and by anyone who subscribed his name to the incorporation document, that all the requirements of this Act and the rules made thereunder have been complied with, in respect of incorporation and matters precedent and incidental thereto.

(2) The incorporation document shall

(a) Be in a form as may be prescribed;

(b) State the name of the limited liability partnership;

(c) State the proposed business of the limited liability partnership;

(d) State the address of the registered office of the limited liability partnership;

(e) State the name and address of each of the persons who are to be partners of the limited liability partnership on incorporation;

(f) State the name and address of the persons who are to be designated partners of the limited liability partnership on incorporation;

(g) Contain such other information concerning the proposed limited liability partnership as may be prescribed.

F. Incorporation byregistration.—

(1) When the requirements imposed by clauses (b) and (c) of sub-section (1) of section 11 have been complied with, the Registrar shall retain the incorporation document and, unless the requirement imposed by clause (a) of that sub-section has not been complied with, he shall, within a period of fourteen days— (a) register the incorporation document; and (b) give a certificate that the limited liability partnership is incorporated by the name specifiedtherein.

(2) The Registrar may accept the statement delivered under clause (c) of sub-section (1) of section 11 as sufficient evidence that the requirement imposed by clause (a) of that sub-section has been compliedwith.

(3) The certificate issued under clause (b) of sub-section (1) shall be signed by the Registrar and authenticated by his officialseal.

(4) The certificate shall be conclusive evidence that the limited liability partnership is incorporated by the name specified therein. 13. Registered office of limited liability partnership and changetherein.—

(1) Every limited liability partnership shall have a registered office to which all communications and notices may be addressed and where they shall bereceived.

(2) A document may be served on a limited liability partnership or a partner or designated partner thereof by sending it by post under a certificate of posting or by registered post or by any other manner, as may be prescribed, at the registered office and any other address specifically declared by the limited liability partnership for the purpose in such form and manner as may be prescribed. (3) A limited liability partnership may change the place of its registered office and file the notice of such change with the Registrar in such form and manner and subject to such conditions as may be prescribed and any such change shall take effect only upon such filing. (4) If the limited liability partnership contravenes any provisions of this section, the limited liability partnership and its every partner shall be punishable with fine which shall not be less than two thousand rupees but which may extend to twenty-five thousand rupees.

G. **Effect of registration**.

On registration, a limited liability partnership shall, by its name, be capable of— (a) suing and being sued; (b) acquiring, owning, holding and developing or disposing of property, whether movable or immovable, tangible or intangible; (c) having a common seal, if it decides to have one; and (d) doing and suffering such other acts and things as bodies corporate may lawfully do and suffer.

I. **Name**. — (1) Every limited liability partnership shall have either the words "limited liability partnership" or the acronym "LLP" as the last words of itsname.

II. No limited liability partnership shall be registered by a name which, in the opinion of the Central Government is— (a) undesirable;or

III. identical or too nearly resembles to that of any other partnership firm or limited liability partnership or body corporate or a registered trade mark, or a trade mark which is the subject matter of an application for registration of any other person under the Trade Marks Act, 1999 (47 of1999).

II. **Publication of name and limited liability**.—

(1) Every limited liability partnership shall ensure that its invoices, official correspondence and publications bear the following, namely:— (a) the name, address of its registered office and registration number of the limited liability partnership; and (b) a statement that it is registered with limitedliability.

(2) Any limited liability partnership which contravenes the provisions of sub-section (1) shall be punishable with fine which shall not be less than two thousand rupees but which may extend to twenty-five thousand rupees.

H. **Partners and their relationship**

Eligibility to be partners.—On the incorporation of a limited liability partnership, the persons who subscribed their names to the incorporation document shall be its partners and any other person may become a partner of the limited liability partnership by and in accordance with the limited liability partnership agreement.

I. Relationship of partners.—

(1) Save as otherwise provided by this Act, the mutual rights and duties of the partners of a limited liability partnership, and the mutual rights and duties of a limited liability partnership and its partners, shall be governed by the limited liability partnership agreement between the partners, or between the limited liability partnership and itspartners.

(2) The limited liability partnership agreement and any changes, if any, made therein shall be filed with the Registrar in such form, manner and accompanied by such fees as may be prescribed.

(3) An agreement in writing made before the incorporation of a limited liability partnership between the persons who subscribe their names to the incorporation document may impose obligations on the limited liability partnership, provided such agreement is ratified by all the partners after the incorporation of the limited liabilitypartnership.

(4) In the absence of agreement as to any matter, the mutual rights and duties of the partners and the mutual rights and duties of the limited liability partnership and the partners shall be determined by the provisions relating to that matter as are set-out in the FirstSchedule.

UNIT – V

Elements of Law Relating to Negotiable Instruments under Negotiable Instruments Act, 1881

In India, the law relating to negotiable instruments is contained in the Negotiable Instruments Act, 1881. It deals with Promissory Notes, Bills of Exchange and Cheques, the three kinds of negotiable instruments in most common use. The Act applies to the whole of India and to all persons resident in India, whether foreigners or Indians. The act also applies to 'hundis', other documents such as treasury bills, dividend warrants, bearer debentures, etc. These instruments are also recognised as negotiable instruments, either by mercantile customs or under other act like the Companies Act, 1956.

¬ Definition of Negotiable Instruments

The word meaning of 'negotiable' is being transferable by delivery, and the word 'instrument' means a written document by which a right is created in favour of some person. Thus, negotiable instrument means a written document transferable by delivery. According to Section 13 of the Act, a negotiable instrument means 'a promissory note, bill of exchange or cheque payable either to order or to bearer'. The two main aspects of a negotiable instrument thus are that it is payable to order and is payable to bearer.

1. *Payable to order:* According to this, a note, bill or cheque is payable to order whichis expressed to be 'payable to a particular person or his order'. A document that contains express words prohibiting negotiability is a valid document but they are considered as negotiable instruments since they cannot be negotiated further. However, a cheque is an exception to this. A cheque crossed 'account payee only' is considerednegotiable.
2. *Payable to bearer:* This means 'payable to any person whosoever bears it'. Anote ,bill or cheque is payable to a bearer which is expressed to be so payable.

¬ Elements of Negotiable Instruments

The essential elements of a negotiable instrument are as under:

1. **Negotiability:** The instruments are transferable from one person to anotherwithout any furtherformality.
2. **Transferee can sue in his own name without giving notice:** A bill, note or a cheque represents a debt and implies the right of the creditor to recover it from his debtor. The creditor has the right to either recover this amount himself or he can transfer this right to anotherperson.
3. **Better title to a bonafide transferee for value:** A bonafide transferee of a negotiable instrument gets the instrument free from all defects. He is not affected by any defect of title of the transferor or any priorparty.
4. **Presumptions:** There are certain presumptions that apply to all negotiable instruments, which are contained in Sections 118 and 119. Some of the presumptions are as follows:
    a) Every negotiable instrument was made, drawn, accepted, indorsed or transferred for consideration.
    b) A negotiable instrument bearing a date was made or drawn on the date mentioned.
    c) Every bill of exchange was made and accepted at a reasonable time and before its maturity.
    d) That the holder of a negotiable instrument is a holder in due course.

¬ Types of NegotiableInstruments

The following are the main types of Negotiable instruments:

1. **Promissory Notes:** Section 4 of the Act defines a promissory note as 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.* Any promissory note will have two parties, the maker who makes the promissory note and the payee to whom the payment is to be made. Based on the definition, the essential features of promissory note include thefollowing:

I. It must be inwriting.
II. It must contain a promise or undertaking topay.
III. The promise to pay must beunconditional.
IV. The maker must be a certainperson.
V. They payee must becertain.
VI. The sum payable must becertain.

***2.* Bills of Exchange**

A bill of exchange is an instrument in writing containing an unconditional order signed by the maker directing a certain person to pay a certain sum of money only to , or to the order of, a certain person or to the bearer of the instrument.

¬ Parties to a Bill of Exchange

A bill of exchange will have three parties – the drawer, drawee and payee. The person who makes the bill is called the 'drawer'. The person who is directed to pay is called the 'drawee' and the person to whom the payment is to be made is called the 'payee'. If the bill is endorsed to another person, the endorsee who is in possession of the bill is called the 'holder'. The holder must present the bill to the drawee for his acceptance. When the drawee accepts the bill, by writing the word 'accepted' and then signing it, he is called the'acceptor'.

¬ Essential Characteristics of a Bill ofExchange

An instrument to be considered a valid bill of exchange should comply with the following conditions:

I. It must be in writing.
II. It must be definite and should contain an unconditional order topay.
III. It must be signed by thedrawer.
IV. All the parties must becertain.
V. The sum payable on the instrument must becertain.
VI. It must contain an order to pay moneyonly.
VII. It must also comply with the formalities with respect to date, consideration, stamps etc.

3. Cheque

A cheque is defined as ‘a bill of exchange drawn on a specified banker and not expressed to be payable otherwise than on demand and it includes the electronic image of a truncated cheque and a cheque in the electronic form’. From the definition it can be seen that a cheque is a bill of exchange with two distinctive features:

1. It is always drawn on abank.
2. It is always payable ondemand.

¬ Crossing ofCheques

Cheques may be open cheques or crossed cheques. An open cheque is one that is payable across the counter of a bank. Crossing helps in preventing any probable loss that may occur, in the event of an open cheque getting into the hands of a wrong person. Crossing is a unique feature associated with a cheque that affects a certain obligation of the paying banker and also its negotiable character. Crossing of a cheque is effected by drawing two parallel transverse lines with or without the words ‘and company’ or any abbreviation. If a cheque bears across its face and addition of the words ‘and company’ or any abbreviation between two parallel transverse lines or transverse lines simply, either with or without the words ‘not negotiable’ that shall be deemed a crossing and the cheque shall be deemed to be crossed. Since the payment cannot be claimed across the counter on a crossed cheque, crossing of cheques serves as a measure of safety against theft or loss of cheques intransit.

According to Section 126 of the Act, a cheque can be crossed by any of the following persons:

1. The drawer of a cheque
2. The holder of thecheque
3. Thebanker

¬ Parties to NegotiableInstruments

Holder:

The ‘holder’ of a negotiable instrument means any person entitled to the possession of the instrument in his own name and to receive or recover the amount due thereon from the parties liable thereto (Sec.8). Thus, in order to be called a ‘holder’ a person must satisfy the following two conditions:

I. He must be entitled to the possession of the instrument in his ownname.

II. He must be entitled to receive or recover the amount due thereon from the parties liablethereto.

Holder in due course

The 'holder in due course' means any person who for consideration becomes the possessor of a negotiable instrument if payable to bearer, or the payee or indorsee thereof if payable to order, before the amount mentioned in it became payable, and without sufficient cause to believe that any defect existed in the title of the person from whom he derived his title (Sec. 9). Thus, in order to be called a 'holder in due course' a person must possess the following specifications:

1. *He must be a 'holder'*. i.e., he must be entitled to the possession of the instrument in his own name under a legal title and to recover the amount thereof from the parties liable thereto.
2. *He must be a holder of valuable consideration,* i.e., there must be some consideration to which law attaches value. The consideration, however, need not be adequate.
3. *He must have become the holder of the negotiable instrument before its maturity.*
4. *He must take the negotiable instrument complete and regular on the face ofit.*
5. *He must have become holder in good faith.*

ㅋ Liabilities of parties to Negotiable Instruments

The provisions of law regarding the liability of parties to negotiable instruments are as follows:

1. **Liability of drawer:** The drawer of a bill of exchange or cheque is bound, in case of dishonor by the drawee or acceptor thereof, to compensate the holder, provided due notice of dishonor has been given to, or received by, the drawer as hereinafter provided(Sec.30).Thus,thedrawerofabillorchequeisliabletotheholderonlyof
   (i) the instrument has been dishonored, and (ii) due notice of dishonor has been given to him.
2. **Liability of drawee of cheque (Sec. 31):** The drawee of the cheque (i.e., the paying banker) must pay the cheque when duly presented for payment provided he has sufficient funds to the drawer applicable to the payment of such cheque. If the drawee banker wrongfully dishonors the cheque he can be made liable to pay exemplary damagestothedrawer.Noticethatwhenthebankermakesadefaultheisliablenot

towards the payee or the holder but towards the drawer. This is so because there is no privity of contract between the holder and the banker. The holder has a remedy against the drawer and not against thebanker.

3. **Liability of 'maker' of bill and 'acceptor' of bill (Sec.32):** The maker of a promissory note and the acceptor of a bill of exchange are the principle debtors and hence they are primarily liable for the amount due on the instrument according to its apparent tenor, in the absence of a contract to the contrary. There may be a contract to the contrary, for instance, in the case of an 'accommodation bill' the acceptor may be exempt from liability as percontract.
4. **Liability of endorser (Sec. 35):** When an endorser endorses and delivers a negotiable instrument before maturity he impliedly undertakes to be liable to every subsequent holder for the loss caused to him if the instrument is dishonoured by the party primarily liable thereon. Thus, the endorser stands in the position of a 'drawer' to all the subsequent holders.

- **Liabilities of paying banker**

The paying banker (drawee of the cheque) must pay the cheque when duly presented for payment provided he has sufficient funds to the drawer applicable to the payment of such cheque. If the drawee banker wrongfully dishonors the cheque he can be made liable to pay exemplary damages to the drawer. Notice that when the banker makes a default he is liable not towards the payee or the holder but towards the drawer. This is so because there is no privity of contract between the holder and the banker. The holder has a remedy against the drawer and not against the banker.

- **Dishonor ofinstruments**

A negotiable instrument may be dishonored by (i) non – acceptance or (ii) non – payment. As presentment for acceptance is required only in case of bills of exchange, it is only the bills of exchange which may be dishonored by non – acceptance. Of course any type of negotiable instrument – promissory note, bill of exchange or cheque – may be dishonored by non – payment.

1. **Dishonor by Non – acceptance** *:* A bill of exchange is said to be dishonored by non – payment in the followingcases:

a. When the drawee or one of several drawees (not being partners) makes default in acceptance upon being duly required to accept thebill.
b. Where the presentment for acceptance is excused and the bill is not accepted, i.e., remainsunaccepted.
c. Where the drawee is incompetent tocontract.
d. Where the drawee makes the acceptancequalified.
e. If the drawee is a fictitious person or after reasonable search cannot befound.

2 Dishonor by Non – payment

A promissory note, bill of exchange or cheque is said to be dishonored by non – payment when the maker of the note, acceptor of the bill or drawee of the cheque makes default in payment upon being duly required to pay the same (Sec. 92). Also, a promissory note or bill of exchange is dishonored by non – payment when presentment for payment is excused expressly by the maker of the note or acceptor of the bill and the note or bill remains unpaid at or after maturity (Sec.76).

ㅋ Bouncing of Cheque

A chequeis said to be bounced or dishonored by non – payment when the drawee of the cheque makes default in payment upon being duly required to pay the same. With a view to enhancing the acceptability of cheques in settlement of liabilities, it is necessary that the chequesdrawn are honored and not bounced.

To amend 'the law of dishonor of a cheque', the Negotiable Instrument Act, 1881 has been amended again by the Negotiable Instruments (Amendment and Miscellaneous Provisions) Act, 2002, which has been made effective from February 6, 2003. The Amendment Act, 2002, *inter alia*, has amended Sections 138, 141 and 142 and also inserted five new Sections – Section 143 to 147. The salient features of the provisions of Sections 138 to 147 are discussedbelow:

A drawer of the dishonored cheque shall be deemed to have committed an offence and shall, without prejudice to any other provisions of the Negotiable Instruments Act, be punishable with imprisonment for a term which may extend to two years, or with a fine which may extend to twice the amount of the cheque, or with both. However, before the panel provisions can be invoked against the drawer of a cheque which has bounced, the following requirements should besatisfied:

1. The cheque should have been dishonored due to insufficiency of funds standing to the credit of the account on which the cheque was drawn or for the reason that the amountof cheque drawn on the account exceeds the sanctioned limit ofoverdraft.
2. The cheque should have been issued by the drawer in favour of another person for the discharge of legally enforceable debt or other liability, in whole or in part. Therefore, when any cheque issued for meeting social obligations, such as charity, marriage presents, birthday gifts etc. is dishonored for want of funds the drawer would not be deemed to have committed anoffence.
3. The cheque should have been presented to the bank within a period of six months from the date on which it is drawn or within the period of its validity, whichever isearlier.
4. The payee or holder in due course of the cheque should have made a demand for the payment of the said amount of money by giving a notice in writing to the drawer of the cheque within 30 days of the receipt of the information by him from the bank regarding the return of the cheque as unpaid/bounced.
5. The drawer of such cheque should have failed to make the payment of the said amount of money to the payee or the holder in due course of the cheque within 15 days of the receipt of the said notice of demand. If the drawer does not pay till the expiry of 15 days time, the cause of action arises on the 16th day.