Ahmednagar Jilha Maratha Vidya Prasarak Samaj's

NEW LAW COLLEGE

Ahmednagar

LL.M I Semester II[2014 Pattern]

LAW OF CONTRACT-

GENERAL PRINCIPLES

Asst.Prof.Punam Umesh Vaddepalli
B.A.,LL. M.(SET)

Semester II

Papers of Business Law Cluste r

(Paper -8)

Compulsory Paper **Credits:4**

LAW OF CONTR ACTS- GENERAL PR INCIPLES

Topics for Study:

1. **INTRODUCTION**
   a) Proposal
   b) Acceptance
   c) Agreement & Contract
   d) Tenders
   e) Standard form contracts
   f) E-contracts
   g) Government contracts
2. **CONSIDERATION**
   a) Definition
   b) Privity of contract and of consideration
   c) Exceptions to consideration
3. **FREE CONSENT**
   a) Vitiating factors and their effect
   b) Coercion
   c) Undue influence
   d) Misrepresentation
   e) Fraud
   f) Mistake

4. PERFORMANCE & DISCHARGE OF CONTRACT

a) Modes of discharge

b) Discharge by performance

c) Discharge by agreement

d) Discharge by frustration

e) Discharge by breach

5. REMEDIES FOR BREACH OF CONTRACT

a) Damages

b) Specific performance & Injunction

c) Limitation of actions

d) Restitution

6. SALE OF GOODS

a) Sale and agreement to sell

b) Conditions and warranties

c) Effects of the con tract of sale

d) Performance of contract

e) Rights of an unpaid seller

f) Suits for breach of contract

g) Auction Sales

7. PARTNERSHIP

a) Nature of Partnership

b) Relations of partners to one another

c) Relations of partners to third parties

d) Incoming and outgoing partners

e) Dissolution of firms

f) Registration of firms

Topic No.1

INTRODUCTION

Introduction to Indian Contract Act

The law relating to contracts in India is contained in the **Indian Contract Act, 1872.**The Act was passed by British India and is based on the principles of English common law. It is applicable to all the states of India except the state of Jammu & Kashmir. It determines the circumstance in which promise made by the parties to a contract shall be legally binding on them. All of us enter into a number of contracts everyday knowingly or unknowingly. Each contract creates some rights and duties on the contracting parties. Hence this legislation, the Indian Contract Act 1872, being of skeletal nature, deals with the enforcement of these rights and duties on the parties in India.

History of Indian Contract Act

It was enacted mainly with a view to ensure reasonable fulfillment of expectation created by the promises of the parties and also enforcement of obligations prescribed by an agreement between the parties. The Third law commission of British India formed in 1861 under the stewardship of chairman Sir John Romilly, with initial members as Sir Edward Ryan, R. Lowe, J.M. Macleod, Sir W. Erle (Succeeded by Sir, W .M. James) and justice Wills (succeeded by J. Henderson) , had presented the report on contract law for India as Draft Contract law (1866) . The Draft Law was enacted as The Act 9 of Indian Contract Act, 1872 on 25 April 1872 and the Indian Contract Act, 1872 came into force with effect from 1 September 1872.

Role of East India Company

Before the enactment of the Indian Contract Act, 1872, there was no codified law governing contracts in India. In the Presidency Towns of Madras, Bombay and Calcutta law relating to the contract was dealt with the Charter granted in 1726 by King George I to the East India Company. Thereafter in 1781, in the Presidency Town, Act of Settlement passed by the British Government came into force.

Act of settlement required the Supreme court of India that questions of inheritance and succession and all matters of contract and dealing between party and party should be determined in case of Hindu as per Hindu law and in case of Muslim as per Muslim law and when parties to a suit belonged to different persuasions, then the law of the defendant was to apply . In outside Presidency Towns matters with regard to the contract was mainly dealt with through English Contract Laws: the principle of justice, equity and good conscience was followed.

Nature of Contract

What is Contract?

According to section 2 (h) of the India Contract Act,'' An agreement enforceable by law is a contract '.

Thus for the formation of a contract, there must be –

- An agreement, and
- The agreement should be enforceable by law.

All agreements are not enforceable by law and therefore, all agreements are not contracts. Some agreement not enforceable by law.

For example- An agreements to sell a radio set any be a contract, but an agreement to go to see a movie may be a mere agreement not enforceable by law.

Illustration – if the agreement between the farmer and the tractor owner is given force under the law, then it becomes a contract.

Agreement

According to section 2 (e) defines agreement as, "Every promise and every set of promise, forming the consideration for each other, is an agreement."
In agreement, there is a promise from both sides. For example, A promises to deliver his watch

to B and in return B promises to pay a sum of Rs. 2000 to A, there is said to be an agreement between A and B.

A promise is a result of an offer (proposal) by one person and its acceptance by the other. For example – when A makes a proposal to sell his watch to B for Rs. 2,000 and B accept his proposal, it results from a promise between the two persons.

Illustration – Such a promise between the tractor owner and the farmer which involves a consideration of an Rs. 1000 is called an agreement.

The promise in the Indian Contract Act

According to section 2 (b) defines promise as, When the person to whom the proposal is made, signifies his assent thereto, the proposal is said to be accepted. A proposal, when accepted, becomes a promise.''

Thus, when there is a proposal from one side and the acceptance of that proposal by the other side, it results in a promise. This promise from the two parties to one another is known as an agreement. The person who makes the proposal is called the promisor. The person who accepts such a promise is called the promise.

Illustration – if in the given example, the farmer accepts the proposal of the tractor owner to transport his produce from the farms to the market, the proposal then becomes a promise.

"All contracts are agreements but all agreements are not contracts" , because agreements of moral, religious or social nature e.g.., a promise to lunch together at a friend's house or to take a walk together are not contracts because they are not likely to create a duty enforceable by law for the simple reason that the parties never intended that they should be attended by legal consequences.

In business agreements the presumption is usually that the parties intend to create legal relation for e.g. An agreement to buy certain specific goods at an agreed price e.g.., 10 bags of wheat at Rs. 500 per bag is a contract because it gives rise to a duty enforceable by law , and in case of default on the part of either party an action for breach of contract could be enforced through a

court provided other essential elements of a valid contract as laid down in Section 10 are present, namely, if the contract was made by free consent of the parties competent to contract, for a lawful consideration and with a lawful object.

The various agreements may be classified into two categories :

- **Agreement not enforceable by law (**Any essential of a valid contract is not available **)**
- **An agreement enforceable by law(**All essentials of a valid contract are available **)**

Conclusion

Thus we see that an agreement may be or may not be enforceable by law, and so all agreement does not contract. Only those agreements are contracts, which are enforceable by law, In short.

Contracts = Agreement = Enforceability by law

Hence, we can conclude "All contracts are agreement, but all agreements are not contracts ."

Essentials of contract

According to of section 10, as All agreement are contracts if they are made by the free consent of parties competent to contract, for a lawful consideration and with a lawful object, and are not hereby expressly declared to be void. Nothing herein contained shall affect any law in force in India, and not hereby expressly repealed, by which any contract is required to be made in writing or in the presence of witnesses, or any law relating to the registration of documents.

ESSENTIALS OF VALID CONTRACT

Offer + Acceptance = Promise + Consideration = Agreement +Enforceability by law Contract

The essential elements of a valid contract are as follows :

- **Lawful offer and Acceptance**

These must be a ‘ lawful offer ‘ and a ‘ lawful acceptance ‘ of the offer, thus resulting in an agreement. The adjective ‘ lawful ‘ implies that the offer and acceptance must satisfy the requirements of the Indian Contract Act in relation thereto.

- **Intention to create legal relation**

There must be intention among the parties that the agreement should be attached by legal consequences and create legal obligations. Agreements of social or domestic nature do not contemplate legal relations, and as such, they do not give rise to a contract.

For example:

1. An agreement to dine at a friend’s house is not an agreement intended to create legal relations and therefore is not a contract.
2. An agreement between husband and wife also lack the intention to create a legal relationship and thus do not result in a contract.
3. Suraj promises his wife Megha to get her jewelry if she will make a special dish. Megha made a dish but Suraj did not bring the jewelry for her. Megha cannot bring an action in a court to enforce the agreement as it lacked the intention to create legal relation.

CASE LAW: BALFOUR V/S BALFOUR

Where the defendant was a civil servant stationed in Ceylon. He and his wife were enjoying leave in England. When the defendant was due to return to Ceylon, his wife could not accompany him because if her health. The defendant agreed to send her Rs. 300 a month as maintenance expenses during the time they were thus forced to live apart. She sued for breach of this agreement. Her action was dismissed on the ground that no legal relation had been contemplated and therefore, there was no contract.

- **Lawful consideration**

The third essential element of a valid contract is the presence of consideration. Consideration has been defined as “the price paid by one party for the promise of the other.” An agreement is

legally enforceable only when each of the parties to it gives something and gets something. The something given or obtained is the price for the promise and is called 'consideration'. But only those considerations are valid which 'lawful'.

According to Section 23, the consideration is unlawful if:

1. Law forbids it;
2. It is fraudulent;

- Involves or implies injury to the person or property of another;

1. It is of such a nature that, if permitted it would defeat the provision of any law;
2. Is immoral or is opposed to public policy.

- **Capacity of parties**

The parties to an agreement must be competent to contract; otherwise, it cannot be enforced by a court of law. In order to be competent to contract according to section 11 the parties must be :

1. Of the age of majority;
2. Of sound mind:

- Must not be disqualified from contracting by any law to which they are subject.

Thus, if any of the parties to the agreement suffers from minority, lunacy, idiocy, drunkenness, etc.

- **Free consent**

Consent' means that the parties must have agreed upon the same thing in the same sense (section 13). Free consent of all the parties to an agreement is another essential element of a valid contract.

There is an absence of 'free consent'. If the agreement is induced by any of the following factors:

1. Coercion
2. Undue influence,
3. Fraud
4. Misrepresentation, or
5. Mistake

If the agreement is vitiation by any of the first four factors, the contract would be voidable and cannot be enforced by the party guilty of coercion, under influence, etc. The other party (i.e., the aggrieved party) can either reject the contract or accept it, subject to the rules laid down in the act. But, if the agreement were induced by mutual mistake that is material to the agreement, it would be void.

- **Lawful object**

For the formation of a valid contract, it is also necessary that the parties to an agreement must agree for a lawful object.

The object for which the agreement has been entered into must be fraudulent or illegal or immoral or opposed to public policy or must not imply injury to the person or property of another (section 23).

If the object is unlawful for one or the other of the reason mentioned above the agreement is void.

For example – When a landlord knowingly lets a house to a prostitute to carry on prostitution, he cannot recover the rent through a court of law.

- **Oral, Writing and Registration**

According to the Indian contract act, a contract may be oral or in writing. But in certain special cases, it lays down that the agreement, to be valid, must be in writing or/ and registered.

For example – under section 25 of the act – It requires that an agreement to pay a time-barred debt must be in writing and an agreement to make a gift for natural love and affection must be in writing and registered.

Similarly, certain other cats also require writing or/and registration to make the agreement enforceable by law, which must be observed.

Illustration – The agreement for a sale of immovable property must be in writing and registered under the Transfer of Property Act, 1882 before they can be legally enforced.

- **Certainty**

Section 29 of the contract act provided that, 'Agreement', the meaning of which is not certain, or capable of being made certain, are void.''

In order to give rise to a valid contract, the terms of the agreement must not be vague or uncertain. It must be possible to ascertain the meaning of the agreement, for otherwise, it cannot be enforced.

Illustration- A agrees to sell B "a hundred tons of oil". There is nothing whatever to show what kind of oil was intended. The agreement is void for uncertainty.

- **Possibility of performance**

Another essentials feature of a valid contract is that must be capable of performing.

Section 56 lays down that, "An agreement to do an act impossible in itself is void." If the act is impossible in itself, physically or legally, the agreement cannot be enforced at law.

Illustration- Ajay agrees with Vijay to discover treasure by magic. The agreement is not enforceable because it is physically impossible to perform.

- **Not expressly declared a void agreement**

The agreement must not have been expressly declared to be void under the Indian Contract Act. Section 24 – 30 specify certain types of agreements, that have been expressly declared to be void.

For example-

- An agreement in restraint of marriage, (section 26)
- An agreement in restraint of trade, and (section 27)
- An agreement by way of the wager (section 30)

Has been expressly declared void agreement.

Types Of Contracts in India

There are four types of contracts:-

1. On the basis of creation
2. On the basis of validity
3. On the basis of execution
4. On the basis of liability

CONTRACTS ON THE BASIS OF CREATION

- Express contract:- A contract made by the word spoken or written. According to Sec. 9 in so far as the proposal or acceptance of any promise is made words, the promise is said to be express.

Example – A says to B ‘ will you purchase my bike for Rs. 20,000?’’ B says to A ‘’yes’’.

- Implied contract: A contract inferred by
- The contract of a person or
- The circumstance of the case.

By implied contract means implied by law _(i.e.,) the law implied a contract through parties never intended. According to sec. 9 in so far as such proposed or acceptance is made otherwise than in words, the promises are said to be implied.

Example: A stops a taxi by waving his hand and takes his seat. There is an implied contract that A will pay the prescribed fare.

Tacit contract:- A contract is said to be tacit when it has to be inferred from the conduct of the parties.

Example- obtaining cash through automatic teller machine, sale by fall hammer of an auction sale.

- Quasi-contracts are contracts which are created:-

-Neither by the word was spoken

-Nor written

-Nor by the conduct of the parties.

-But these are created by the law.

Example- If Mr A leaves his good at Mr B's shop by mistake, then it is for Mr B to return the goods or to compensate the price. In fact, these contracts depend on the principle that nobody will be allowed to become rich at the expenses of the other.

- E-contracts:- An e-contract is one, which is entered into between two parties via the internet.

2. 0N THE BASIS OF VALIDITY

- Valid contracts:- An agreement which satisfies all the requirements prescribed by law on the basis of creation.

(According to sec. 10)

- Void contracts: The word 'void' means 'not binding in law'. Accordingly, the term 'void contract' implies a useless contract that has no legal effect at all. a contract which ceases to be enforceable by law because void, when of, ceased to be enforceable. (Acc. Section 2 (j)).
- Voidable contracts: According to section 2 (i) "an agreement, which is enforceable by law at the option of one or more of the parties thereto, but not at the option of the other of others, is a voidable contract." Thus, a voidable contract is one that is enforceable by law at the option of one of the parties. Until it is avoided it is a valid contract.
- Unenforceable contracts: where a contract is good in substance but because of some technical defect i.e., absence in writing barred by imitation etc one or both the parties cannot sue upon but is described as an unenforceable contract.

Example-Writing registration or stamping.

- Illegal contracts: It is a contract which the law forbids to be made. All illegal agreement is void but all void agreement or contracts are not necessarily illegal.

A contract that is immoral or opposed to public policy is illegal in nature.

- Unlike the illegal agreement, there is no punishment for the parties to avoid agreement.
- The illegal agreement is void from the very beginning but sometimes valid contracts may subsequently become void.

3. CONTRACTS ON THE BASIS OF EXECUTION

- Executed contracts: A contract in which both the parties have fulfilled their obligations under the contract.

Example- A contract to buy a car from B by paying cash, B instantly delivers his cart.

- Executory contracts: A contract in which both the parties have still to fulfil their obligations.

Example- D agrees to buy V's cycle by promising to pay cash on 15th July. V agrees to deliver the cycle on 20th July.

- Partly executed and partly executor: A contract in which one of the parties has fulfilled his obligation but the other party is yet to fulfil his obligation.

Example- A sells his car to B and A has delivered the car but B is yet to pay the price. For A, it is executed contract whereas it is executor contract on the part of B since the price is yet to be paid.

4. CONTRACTS ON THE BASIS OF LIABILITY FOR PERFORMANCE

- Bilateral contracts: A contract in which both the parties commit to performing their respective promises is called a bilateral contract.

Example- A offers to sell his fiat car to B for Rs. 1,00,000 on acceptance of A's offer by B, there is a promise by A to sell the car and there is a promise by B to purchase the car there are two promises.

- Unilateral contracts: A unilateral contract is a one-sided contract in which only one party has to perform his promises or obligation party has to perform his promise or obligation to do or forbear.

Example: A wants to get his room painted. He offers Rs. 500 to B for this purpose B says to A "if I have spare time next Sunday I will paint your room". There is a promise by A to pay Rs. 500 to B. If B is able to spare time to paint A's room. However, there is no promise by B to paint the house. There is only one promise.

TOPIC NO.2

CONSIDERATION

Presence of consideration is one of the essentials of a valid contract. The subject of certain exception, the general rule in India is that "an agreement, without consideration, is void".

MEANING

1. (a) Consideration is a quid pro quo, i.e., something in return, it may be –

(i)something benefit right, interest, loss or profit that may accrue to one party or,

(ii)some forbearance, detriment, loss or responsibility suffered on undertaken by the other party (Currie V Mussa)

(b) According to Sir Frederick Pollock, "consideration is the price for which the promise of the other is bought and the promise is thus given for value is enforceable".

2. Definition 2 (d): when at the desire of the Promisor, the promise or any other person.

(a) has done or abstained from during, or (Past consideration)

(b) does or abstained from doing, or (Present consideration)

(c) promise to do or abstain from doing something (future consideration) such act or abstinence or promise is called a consideration for the promise.

3. Example

(i) 'P' aggress to sell his car to 'Q' for Rs.50,000 Here 'Q' s promise to pay Rs .50,000 is the consideration for 'P's promise and 'P's promise to sell the car is the consideration for 'Q's promise to pay Rs.50,000.

(ii) 'A' promise his debtor 'B' not to file a suit against him for one year on 'A' s agreeing to pay him Rs.10,000 more. Here the abstinence of 'A' is the consideration for 'B's promise to pay.

LEGAL RULES FOR VALID CONSIDERATION

1. IT MUST MOVE AT THE DESIRE OF THE PROMISOR

It is essential that the consideration must have been at the desire of the promisor, rather than merely voluntarily or at the instance of the same third party. Simply, the act of abstinence forming the consideration must be done at the desire of or request of the promisor. Thud acts done or services given at the desire of the third party, will not amount to valid consideration.

ILLUSTRATION

1. Anita sees Mudita house on fire and help in extinguishing the fire. He cannot demand payment for his services because the media never asked her to come for help.

Example:

D constructed a market at the instance of the district collector. Occupants of shops promised to pay D a commission on articles sold through their shops. Held, there was no consideration because money was not spent by the plaintiff at the request of the defendants, but an instance of a third person viz. the collector and, thus the contract was void. Durga Prasad v. Baldeo

2. It may move from the promise or any other person who is not a party to the contract

According to Indian law, the promise or any other person may give consideration . in India there is a possibility that consideration for the promise may move not only from the promisee but also from a third person, who is not a party to the contract.

ILLUSTRATION:

1. A promise to give his watch to B and consideration of Rs.200000

For the same is given to A by X and not by B. Such a contract will be valid in India as sec. 2 (d) clearly provided that at the promisor, the promise or any other person may provide consideration.

CASH LAW: A owed Rs.20000 to B. A persuaded C to sign a pro notes in favor of B. C promised B that he would pay the amount . on the faith of promise by C, B Credited the amount to A's account. held, the discharge of A's account was consideration by C's promise. NATIONAL BANK UPPER INDIA V.BANSIDHAR

What is meant by privity of contract:

Stranger to contract cannot sue: The doctrine of privity of contract means only those person who is parties to the contract can enforce the same. A stranger to the contract enforce a contract even though the contract may have been entered into for his benefit.

For e.g., if in a contract between A and B some benefit has been conferred upon X, X cannot file a suit to enforce the contract because A and B are the only parties to the contract whereas X is stranger to the contract.

The principle of privity of contract is generally applicable in India, with the effect that only a party to the contract is entitled to enforce the same.

ILLUSTRATIONS:

1. Where Manish mortgages his property to Sanjay in consideration of Sanjay's promise to Manish that he shall pay Manish debt to Shanu,

Shanu cannot file a suit against Sanjay to enforce his promise because Shanu was not a party to the contract between the Manish and Sanjay.

CAN 'STRANGER TO CONSIDERATION' SUE

Yes, a stranger to consideration can sue: the rule that a stranger to contract cannot sue has to be distinguished from the rule discussed above that in Indian a person who is stranger to consideration can sue. It has been noted above that a person may not have himself given any

consideration but he can enforce the contract if he is a party to the contract, because according to the Indian law consideration may be given either by the promise or a third party. That does not affect the rule of privity of contract.

A LEADING CASE DECIDED ON IT IS:

CASE 1: Chinayya v. Ramayya

In this case A, an old lady, by deed of gift, made over certain property to her daughter R, with a direction that the daughter should pay an annuity to A's brother C, as has been done by A . according ,on the same day, R, the daughter, executed a writing in the favor of her maternal uncle agreeing to pay the annuity. Afterward, she declined to say that no consideration had moved from her uncle i.e. promise. The court held that though the uncle was stranger to the consideration (as consideration indirectly moved from the sister) and there was a separate contract between him and R, the daughter, was entitled to get the annuity. The maternal uncle could not have sued on the basis of 'gift deed' executed by A in favor of R because he was not a party to that contract i.e. he is stranger to that contract. thus, A person may be a stranger to the consideration but he should not be a stranger to the contract because 'privity of contract' is essential for enforcing any of the right arising out of the contract. It is a fundamental principle of the law of contract that 'a stranger to a contract cannot sue, only a person who is a party to a contract can sue on it.'

ARE THERE ANY EXCEPTION TO RULE STRANGER TO CONTRACT CANNOT SUE

The above rule that stranger to contract cannot sue is subject to the following exception:

(i) Where an express on implied trust is created :

In case of a trust, the beneficiary can sue in his own right under the trust, though he was not a party to the contract between the settler and the trustee.

ILLUSTRATION:

1. An addressee of an insured article is entitled to sue that post office become a trustee in law for the addressee.
2. Raja transfers his property to check to be held by Chetek in trust for the benefit of Ruchi. Ruchi can enforce the agreement i.e. trust.

(ii) Family settlement:

Where a provision is made in a partition or family settlement for maintenance or marriage expenses of the female member, such persons even though not party to contract can sue if not maintained.

ILLUSTRATION:

1. An entry into a contract with his father that he will maintain his mother and sister and the property of the father will be conveyed to him. In such case even though the mother and sister are strangers to the contract she can sue her son if he denies maintaining her.

(iii) Where the defendant constitutes himself, as the agent of the third party:

ILLUSTRATION:

1. Anu received some money from vase to be paid over Nitin and he admits of this receipt to Nitin, then Nitin can recover this amount from Anu who shall be regarded as an agent of Nitin.

(iv) In case of assignment of right under a contract in favor of a third party either voluntarily or by operation of law: the assignee can enforce the benefits of the contract.

ILLUSTRATION:

The assignee of an insurance policy or the official assignee on the insolvency of a person can sue on the contract even though originally they were not parties to the contract.

3. Consideration may be past, present, and future:

Whether the consideration is past, executed or executor, it is essential that is much have been given "at the desire of the promisor."

- Past consideration

As noted above, the Indian contract ACT recognizes past consideration. it means that the consideration for any promise was given earlier and the promise is made thereafter. Simply, when something is done before the date of the agreement, at the desire of the promise, it is called 'past consideration'.

ILLUSTRATION:

1. Sanjana teaches the son of Sudhir at Sudhir,s request in the month April, and in May he promises to pay Sanjana a sum of Rs.1000 for his services. The services of Sanjana will be past consideration.

- Present consideration

The consideration that moves simultaneously with the promise i.e., if both parties have done their part under the contract it is called 'present consideration'.

ILLUSTRATION:

1. A makes an offer of reward of Rs.100 and anyone who find out the lost dog and delivers the same to A. When B does so, that amounts to both the acceptance of the offer, which results in a binding contract under which A is bound to pay Rs.100 to B, and also simultaneously giving consideration for the contract.
2. A sells his pen to B and B pays its price immediately.

(C) Executory or future consideration

When one person makes a promise in exchange for the promise by the other side, the performance of the obligation by each side to be made subsequent to the making of the contract, the consideration is known as the executor.

ILLUSTRATION: A agrees to supply certain goods to B on a future date i.e., 5 January and B agree to pay for them on the same day this is a case of executor consideration.

- Under English law, Past consideration is no consideration.
- Present consideration: cash sale
- Future or executor consideration: A promises to B to deliver him 100 bags of sugar at a future date, B promise to pay first on delivery.

4. Consideration should be real and not illusory, Illusory consideration renders the transaction void consideration is not valid if it is.

- Physically impossible
- Legally not permissible
- Uncertain
- Illusory (Fulfillment of a pre-existing obligation)

5. Must be legal:

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

6. Consideration need not be adequate. A contract is not void merely became of the fact that the consideration is inadequate. The law simply requires that contract should be supported by consideration. So long as consideration exists and it is some value, courts are not required to consider its adequacy:

Example: A agreed to sell a watch worth Rs .500 for Rs. 20, A's consent to the agreement was freely given. The consideration, though inadequate. Will not affect the validity of the contract. However, the inadequacy of the consideration can be considered in order to know whether the consent of the promise was free or not.

7. The performance of an act what one is legally bound to perform is not a consideration for the contract mean's something other than the promisor's existing obligation:

Ex. Nudo Pacto non-oritur,i.e, an agreement without consideration is void.

The exception to the Rule "No consideration. No contract".

1. **Written and registered agreement arising out of love and affection: 25 (1)**

- Expressed in writing and registered under law for the time being in force for registration of the document
- Natural love and affection
- Between parties standing in a near relation to each other.

Example:- An elder brother, on account of natural love and affection, promised to pay the debt of his younger brother. The agreement was put to writing and registered. Held, the agreement was valid.

Exception: Rajlukhy Dabee v/s Bhootnath Mukharjee

2. **Promise to compensate 25(2)**

- Promise to compensate wholly or in part
- Who has already voluntarily done something for the promisor
- Something which the promisor was legally compellable to do.

Example- A finds B's purse and give to him. B promise to give A Rs. 500. This is a valid contract.

3. **Promise to pay a time-barred debt.25(3)**

- A debt barred by limitation cannot be recovered. Hence, a promise to pay such a debt is without any consideration.
- Can be enforced only when – in writing and sighed by the debtor or his authorized agent.

Example- A owes B Rs. 10,000 but the debt is barred by Limitation Act. A signs a written promise to pay B Rs. 8,000 on account of debt. This is a valid contract.

4. **Completed gift:**

A gift (which is not agreement) does not require it in order to be valid. In such a case, it is not necessary that there should be natural love and affection or nearness of relationship between the donor and done.

5. **Agency(185):**

According to the Indian Contract Act. No consideration is necessary to create an agency.

6. **Bailment (148):**

Consideration is not necessary to effect a valid bailment of goods. It is called Gratuitous Bailment.

7. **Charity:** If a person promises to contribute to a charity and on this faith, the promises undertake a liability to the extent not exceeding the promised subscription, the contract shall be valid.

TOPIC NO.3

CAPACITY TO CONTRACT

PARTIES UNABLE TO ENTER INTO A CONTRACT

- Minor
- A person of unsound mind
- A person disqualified by law

1. Who is competent to make a contract:

Section 11. Every person is competent to contract who is of the age of majority according to the law to which he is subject, who is of sound mind and not is disqualified from contracting by any law to which he is subject.

Age of majority: According to section 3 of Indian majority act -1875 every person domiciled in Indian attains a majority on the completion of 18 years of age.

Exception: 21 year – in the following cases.

1890. Where a guardian of a minor's person or property is appointed under the guardian and ward act, 1890.

1891. Where minor's property has passed under the superintendence of court of words.

Position of agreements by minor:

1. Validity: an agreement with a minor is void-ab-initio (Mohoribibee vs. Dharmodas Ghose)

Example:

Mr. D, a minor, mortgaged his house Rs. 20000 to a money – lender, but the mortgagee, i.e, the money- lender, paid him a sum of Rs. 8000. Subsequently, the minor sued for setting aside the

mortgage. Held that the contract was void, as Mr. D. Was minor and therefore he is not liable to pay anything to the lender.

2. A minor has received any benefit under a void contract, he cannot be asked to return the same.
3. If a minor has received any benefit under a void contract, he cannot be asked to return the same.
4. Fraudulent representation by a minor- no difference in the status of the agreement. The contract remains void.
5. A minor with the consent of all the partners, be admitted to the benefits of an existing partnership.
6. Contracts entered into by minors are void – ab – initio. Hence no specific performance can be enforced for such contracts.
7. Minor ‘s parent/guardians are not liable to a minor’s creditor for the breach of contract by the minor.
8. A minor can act as an agent but not personally liable. But he cannot be principal.
9. A minor cannot become a shareholder of the company except when the shares are fully paid up and transfer by share.
10. A minor cannot be adjudicated as insolvent.
11. Can enter into contracts of Apprenticeship, Services, Education, etc:

- A minor can enter into the contract of apprenticeship, or for training or instruction in a special art, education, etc.
- These are allowed because it generates benefits to the minor.

12. Guarantee for and by minor

A contract of guarantee. This is because the surety is ultimately liable under a contract of guarantee whereas a minor can never be held personally liable.

13. Minor as a trade union member

Any person who has attained the age of fifteen years may be a member for the registered trade union, provided the rules of the trade union allow so. Such a member will enjoy all the rights of a member.

EXCEPTION

- The contract for the benefit of a minor
- Contract by Guardian

The benefit of a minor by his guardian or manager of his estate.

1. Within the scope of the authority of the guardian.
2. Is for the benefit of the minor.

- A contract for the supply of Necessaries.

Minor being incapable of entering into the contract if is supplied by another person with necessaries suited to his life, the person who has furnished such supplies is entitled to be reimbursed from the property of this minor but the minor himself is not liable to the supplier.

Example-

Food , clothes, bed, shelter, shoes, medicines and similar other things required for the maintenance of his life or for the life of his dependents, expenses for instruction in grade or arts; expenses for moral religions or intellectual education, funeral expenses of his deceased family members, ,marriage expenses of a dependent female member in the family; expenses incurred in the protection of life. However, things like earring for a male, spectacles for a blind person or a wild animal cannot be considered as necessaries.

Liability for tort: A minor is liable for a tort, i.e, civil wrong committed by him.

- A ‘tort’ is a civil wrong for which the ordinary remedy is damage. A minor is liable for his tort, unless the tort is, in reality, a breach of contract. In a case, thus, were a minor hired a horse for riding and injured it by overriding, he was not held liable. The court

observed in that case, "if an infant in the course of doing what he is entitled to do under the contract is guilty of negligence, he cannot be made liable in tort if he is not liable on the contract".

- But if the wrongful action is of a kind not contemplated by the contract, the minor may be held liable for the tort. Thus, where a minor hired a horse for riding under express instruction not to jump, he was held liable when he lent the horse to one of his friends who jumped it, whereby it was injured and ultimately died.
- The court observed, it was a bare trespass, not within the object and purpose of the hiring, for which the defendant was liable.

Example:

14 –year—old boy drives a car carelessly and injuries B. He is liable for the accident i.e, tort.

2. A person of unsound mind

- **Lunatic**
- **Idiot**
- **Drunken and Intoxicated**

Person of Unsound Mind

A person who usually minds, but occasionally of sound mind can make a contract when he is of sound mind. Similarly, a Person who is usually of sound mind, but occasionally of unsound mind, may not make a contract when he is of unsound mind. (According to sec. 12)

- At the time of entering into a contract, a person must be a sound mind. Law presumes that every person is of sound mind unless otherwise it is proved before the court. An agreement by a person of unsound mind is void. The following are categories of a person considered a person of an unsound mind.
- An idiot

An idiot is a person who is congenital (by birth) unsound mind. His incapacity is permanent and therefore he can never understand the contract and make a rational judgment as to its effects

upon his interest. Consequently, the agreement of an idiot is absolutely void ab initio. He is not personally liable even for the payment of necessaries of life supplied to him.

- Delirious persons

A person delirious from fever is also not capable of understanding the nature and implications of an agreement. Therefore, he cannot enter into a contract so long as delirium lasts.

- Hypnotized persons

Hypnotized produces temporary incapacity until a person is under the effect of artificially induced sleep.

- Mental decay

There may be mental decay or senile mind the to old age or poor health. When such a person is not capable of understanding the contract and its effect upon his interest, he cannot enter into a contract.

- Drunken person

An agreement made by an intoxicated person is void.

3. Person Disqualified by law

- Alien enemy
- An ‘alien’ is a person who is a foreigner to the land. He may be either an ‘ alien friend’ or an ‘ alien enemy. If the sovereign or state of the alien is at peace with the country of his stay, he is an alien friend. And if a war is declared between the two countries he is termed as an alien enemy.
- During the war, a contract can be entered into with alien enemy with the permission of the central government.

- Foreign sovereigns, diplomatic staff, and representative of foreign staff can enter into a valid contract. However, a suit cannot be filed against them, in the Indian counts without the prior sanction of the central government.

- Convict can't enter into a contract while he is undergoing imprisonment. But he can enter into a contract with permission of the central government while undergoing imprisonment. After the imprisonment is over, he becomes capable of entering into the contract. Thus the incapacity is only during the period of sentence.

- Body corporate or company or corporation

The contractual capacity of a company is determined by the object clause of its memorandum of association. Any act done in excess of power given is ultra- vires and hence void.

- Insolvent

When any person is declared as an insolvent, his property vests in the receiver and therefore, he can 't enter into a contract relating to his property. Again he becomes capable to enter into contract when he is discharged by the court.

FREE CONSENT

One of the essentials of a valid contract mentioned in section 10 is that the parties should enter into the contract with their 'Free consent'.

According to section 13. Two persons are said to have consented when they agree upon the same thing in the same sense.

In English law, this is called 'consensus–ad-idem'.

Effect of absence of consent:

- Where there is no consent at all, the agreement is 'void-ab–inito'.

It is not enforceable at the option of either party.

Example 1: X has two cars one Maruti car and one Honda city car. Y does not know that X has two cars Y offers to buy the car at Rs. 50,000. Hence, there is no identity of mind in respect of the subject matter. Hence there is no consent at all and the agreement is void – ab-inito.

Example 2: An Illiterate woman signed a gift deed thinking that it was a power of attorney- no consent at all and the agreement was void-ab-into (Bala Devi v/s Manumdats)

Free Consent

- Consent is said to be free when it is not caused by (Section 14)
- Coercion (Section15)
- Undue influence(Section16)
- Fraud(Section17)
- Misrepresentation(Section18)
- Mistake(Section 20, 21, 21)

Effect of absence of Free Consent:

If consent coercion, undue influence, fraud, Misrepresentation the contract is voidable at the option of the party whose consent was not free (19,19A)

Coercion (Section 15)

- Committing any act which is forbidden by the IPC
- Threatening to commit any act which is forbidden by the IPC
- Unlawful detaining of any property

- Threatening to detain any property

Coercion(section 15)

CASE LAW- A Madrasi Gentleman died leaving a young widow. The relatives of the deceased threatened the widow to adopt a boy otherwise they would not allow her to remove the dead body of her husband for cremation. The widow adopted the boy and subsequently applied for cancellation of the adoption. It was held that her consent was not free but induced by coercion, as any person who obstructed a dead – body from being removed for cremation would be guilty of an offense under section 297 of the I.P.C. The adoption was set aside (Ranganayakamma v/s Alwar Seti).

Essential elements of coercion

Above four (a-d)

- (e)Coercion need not necessarily to proceed from party to contract.
- (f) Coercion need not necessarily be directed against the other contracting party.
- (g) It is immaterial whether the IPC is or is not force at the time or at the place where the coercion is employed.

Effect of the threat to file a suit:

A threat to file a suit does not amount to coercion unless the suit is on a false charge. The threat to file a suit on the false charge is an act forbidden by the IPC and thus will amount to an act of coercion.

Effect of Threat to commit suicide:

The threat to commit suicide does not amount to coercion because the attempt to suicide is punishable in IPC not threat to commit suicide. Therefore voidable. (Chikham Ammiraju v/s Seshama).

Effect of a threat to strike:

A threat to strike by employees in support of their demands is not regarded as coercion. This is because the threat to strike is not an offense under the IPC it is a right given under the Industrial Disputes Act.

Effect:

When coercion is employed to obtain the consent of a party the contract is voidable at the option of the party where consent was obtained by coercion.

Detaining property under mortgage:

Detention of property by a mortgage until the payment of loan does not amount to coercion.

Undue Influence (Section 16)

Meaning of undue influence: dominating the will of the other person to obtain an unfair advantage over the other.

- Where the relation subsisting between the parties must be such that one party is in a position to dominate the will of the other.
- The dominant party uses his position.
- Obtain an unfair advantage over the other.

Example:

X was suffering from a number of sickness and Y was his family doctor. Y induced X to agree to pay Y, an unreasonable sum for his professional services. Here, Y has employed undue influence over

1. In the case, Y uses his superior position to obtain an unfair advantage over X.

No presumption of domination of will:

- Landlord and Tenant
- Creditor and Debtor
- Husband and wife (other than Pardanashin)
- Principal and Agent

Effect of undue influence: (Section 19A)

When consent to an agreement is caused by undue influence, the contract is voidable at the option of the party whose consent was so caused.

The burden of Proof:

A contract is presumed to be induced by undue influence if the following two conditions:

- A party has the position to dominate the will of the others.
- The transaction is unconscionable (unreasonable).

In such a case dominate party is under the burden to prove the undue influence was not employed.

Fraud (Section 17)

- The term fraud means a take representation of facts made wilfully with a view to deceive the other party.

- 17- fraud means any act committed by a party to a contractor with his connivance or by his agent with intent to deceive another party thereto or his agent or to induce to enter into a contract.

Essentials of fraud:

- By a party to the contract
- There must be representation- [an opinion a statement of expression – does not fraud].
- The representation must be false.
- Before the conclusion of the contract.
- The misrepresentation must be made willfully.
- The misrepresentation must be made with a view to deceive the other party.
- The other party must have actually been deceived.
- The other party has suffered a loss.

Fraud- definition include

- The suggestion, as to fact, of that which is not true by one who does not believe it to be true.
- The active concealment of a fact by one having knowledge or belief of the fact.

ILLUSTRATION:

1. Varun purchases a ring from Prateek on credit without any intention of paying for it is a clear case of fraud from the varun side: hence contract is voidable at the option of Prateek.
- Any other act fitted to deceive.
2. Sonata presents herself as an agent to an insurance company and convinces Mala, who deposit some amount to her, This car of fraud and contract is voidable at the option Mala.

Any such act or omission as the law specially declared to be fraudulent.

Silence be Fraudulent

The Explanation to Section 17 deals with cases as to "when silence is fraudulent". It, therefore, follows that:

- As a rule, mere silence is not fraud because there is no duty cast by law on a party to a contract to make a disclosure to the other party, of material facts within his knowledge.

ILLUSTRATION:

- Suraj and Prakash, being traders, enter upon a contract. Suraj has private information about a change in prices that would affect Prakesh's willingness to proceed with the contract. Suraj is not bound to inform Prakesh.
- Silence is fraudulent if the circumstance of the case is such that it is the duty of tn<<pttton keeping silence to speak

In the words, silence is fraudulent in contracts of 'untmost good faith' contracts. These are contracts in while the law imposes a duty of abundant disclosure on one of the parties thereto, due to the peculiar relationship of the parties or due to the fact that one of the parties has peculiar means of knowledge which are not accessible to the other. The following contracts come within this class:

- Fiduciary relationship.

When the parties stand in a fiduciary relationship to each other, the person in whom confidence is reposed is under a duty to act with utmost good faith and to make full disclosure of all material facts concerning the transaction known to him. Example of a fiduciary relationship includes those of principal and agent, solicitor and client, guardian and ward, and trustee and beneficiary, master and servant, father and son, guru and disciple, doctor and patient, police and accused, etc.

ILLUSTRATION:

1. Where a broker who was employed to buy shares for the client, sold his own shares to the client, without disclosing this fact to him and without obtaining his consent, therefore, it was held that the client could avoid the sale.
2. Where solicitor purchased a certain property from his client nominally for his brother, but really for himself, it was held that the sale can be avoided by the client, if the transaction was a perfectly proper one.

- Contracts of insurance.

In contracts of marine, fire and life insurance, the insurer on the basis that all material facts have been communicated to him; and that if there has been non-disclosure he shall be entitled to avoid the contract.

The assured, therefore, must disclose to the insurer all material facts concerning the risk to be undertaken e.g., disease, etc., in case of life insurance. Concealment or misstatement of a material fact will render the contract void.

- Contracts of a marriage engagement

Both parties to a contract of marriage must disclose every material fact otherwise the other party is justified in breaking off the engagement.

- Contracts of family settlements.

Contracts of family settlements and arrangements also require full disclosure of all material facts within the knowledge of the parties to such contracts.

- Share allotment contracts.

Promoters and directors, who issue prospectus of a company to invite the public to subscribe shares should disclose all the information regarding the company to the general public.

3. Silence is fraudulent where the circumstance is such that "alliance in itself, equivalent to speech"

ILLUSTRATION:

1. A says to Z- "if you do not deny. I shall presume that the horse is sound." A says nothing hence A's silence is equivalent to speech. If the horse is unsound A's silence is fraudulent.

Effect of fraud:

Sec.19: A contract induced by fraud is voidable at the option of the party defrauded. Till the exercise of such option, the contract is valid.

Effect of fraud:

1. Rescinds of contracts
2. Right to insist upon performance
3. Right to claim damages-if he suffered loss.

MISREPRESENTATION (SECTION 18)

When a false statement is made with the knowledge that it is false and also with the intention to deceive the other party and makes him enter into a contract on that basis, it is known as fraud. But when the person making a false statement believes the statement to be true and does not intend the other party to the contract it is known as "misrepresentation". A finding of misrepresentation allows for a remedy of rescission and sometimes damages depending on the type of misrepresentation.

Section18 define misrepresentation as under: "MISREPRESENTATION" means and includes-

1. The positive assertion, in a manner not warranted by the information of the person making it of that which is not the truth, though he believes it to true;

ILLUSTRATION:

1. A says to B who intends to purchase his land, "my land produces 10 quintals of wheat per acre." A belief the statement to be true, although he did not have sufficient ground for the belief. Later on, it transpires that the land produces only 7 quintals of wheat per acre. This is a misrepresentation.
2. Any breach of duty which, without an intent to deceive, gains an advantage to the person committing it, or anyone claiming under him, by misleading another to his prejudice or to the prejudice of anyone claiming under him;

ILLUSTRATION:

1. A, before signing a contract with Z for sale of a business , rightly states that his monthly sale Rs.20000. this negotiation lasts for five months when the contract for sale was signed.
2. During this period the production reduced to Rs.15000 per month. A unintentionally keeps quite. This is the case of misrepresentation and is voidable at the option of Z.
3. Causing mistake innocently, about the subject-matter.

Mistake (Sec. 20,21,22)

Mistake Erroneous Belief about some facts

- Mistake of fact

Unilateral(Sec. 22)

- One party under Mistake of fact the contract is valid (Not voidable is void)

Bilateral(Sec. 20)

- Both parties under Mistake of facts the contract is void

The mistake of law(Sec. 21)

- The mistake of Indian law the contract is valid

Mistake of foreign law

- Same as mistake fact
- Both parties under the mistake

When the consent of the parties to the contract is caused by mistake it is not free consent, which is needed for the validity of a contract. One, or both, of the parties, may be working under some misunderstanding or misapprehension of some fact relating to the agreement.

If such a misunderstanding or misapprehension had not been there, probably they would not have entered into the agreement. Such a contract is said to have been caused by mistake.

Section 20 provides that "where both the parties to an agreement are under a mistake as to a matter of fact essential to the agreement, the agreement is void".

The three conditions which must be fulfilled are:

- Both the parties must be under a mistake i.e, the mistake must be mutual. Both the parties should misunderstand each other so as to mollify consent.

ILLUSTRATION:

- Menu, having two houses A and B, offers to sell house A, and neal not knowing that M has two houses, thinks of house B and agrees to buy it. Here there is no real consent the agreement is void.
- The mistake must relate to some fact and not to judgment or opinion etc. An erroneous opinion as to the value of the thing that forms the subject matter of the agreement is not to deemed a mistake as to a matter of fact.

ILLUSTRATION:

- If a buys a motorcar thinking that it is worth Rs.70000 and pays Rs.70000 for it when it is only worth Rs.50000, the contract remains valid. A has to blame himself for his ignorance of the true value of the motorcar and he cannot avoid the contract on the ground of mistake.
- The fact must be essential to the agreement: this mean fact is such which goes to the very root of agreement.

On the basis of judicial decision, common law has identified four different types of mistake in the contract that may broadly be put into the following heads:

- Mistake as to the existence of the subject matter of the agreement. If at the time of the agreement and unknown to parties, the subject matter of the agreement has ceased to exist, or if it has never been in existence, then the agreement is void.

ILLUSTRATION:

- A agrees to sell to B a specific cargo good supposed to be on its way from England to Bombay. It turns out that, before the way of the bargain, the ship conveying the cargo had been cast away, and the goods lost, neither party was aware of these facts. The agreement is void.

- A agrees to buys from B a certain horse. It turns out that the horse was dead at the time the bargain, though neither party was aware of the fact. The agreement is void.
- Mistake as to the identity of the subject matter. Where parties are working under a mistake as to the identity of the subject matter i.e., one party had one thing in mind and the other party had another, the agreement is void for want of consensus-ad-idem.

ILLUSTRATION:

- Where there was a contract for the sale of a certain quantity of cotton arriving per ex ships at the time of entering into the contract, held there was no contract.
- Mistakes as to the quantity of the subject matter. If both the parties are working under a mistake as to the quantity of the subject matter, the agreement is void.

ILLUSTRATION:

- Punit enquired about the price of rifles from Hitesh stating that he may buy as many as 50. Hitesh quoted the price. Punit telegraphed "send thirty rifles". The telegraph clerk transcribed the message as " send the rifles. Hitesh sends 50 rifles. Punit accepted only thirty and returned twenty. Hitesh filed a suit for damages for non-acceptance of 20 rifles. It was held that there was no contract as there was no consent and it made no difference even if the mistake was caused by the negligence of a third party.
- Mistake as to the quality of the subject matter. If there is a mutual mistake of both the parties as to the quality of the subject matter i.e. if the subject matter is something essentially different, from what the parties of the matter i.e., if the subject matter is something essentially, from what the parties believed it to be, the agreement is void.

ILLUSTRATION:

A sold certain seeds to B. Both parties honestly believed that the seeds were two years old. Actually, the seeds proved to be only one year eleven months old. The contract cannot be avoided, as the mistake does not affect the substance of the transaction.

TOPIC NO 4

DISCHARGE OF CONTRACTS

1. Discharge of Contracts

A contract becomes discharged by any one of the following methods :

a) By proper performance :

This means the obligations are performed according to the terms of the agreement by the parties to the contract.

b) Impossibility or Frustration:

When performance becomes impossible or unlawful the contract becomes discharged. This means subsequent to the making of the contract it becomes void due to frustration (Section 56). Hence it was held in Fibrosa case, that the contract was void.

c) By death of the contracting party :

The contract becomes discharged. This applies when there is a personal service to be done according to contract. In such a case on the death of the party, the contract gets discharged. Ex : Artist, Musician etc. The contract becomes void.

d) By rescission of contract:

A party to the contract may rescind by exercising his right in respect of a voidable contract. The contract becomes discharged.

e) By Novation : [New]

By entering into a new contract the original contract is superseded and hence becomes discharged. Novation means a new contract made by the parties. As the House of Lords have pointed out, "in the case of Novation the parties to the contract agree to put an end to the original

contract'. This is provided for in Section 62 of the contract Act. According to it, the Original Contract need not be performed if there is a Novation which substitutes a new contract for the original contract.

Eg: 1. In an Insurance of A, A has mentioned his mother as his Nominee. Later with the consent of the insurer this is changed to the name of the wife of A. This is Novation.

2. A enters into agreement with W to buy goods on instalment basis. Subsequently by mutual agreement the number of instalments is reduced.

This is Novation.

Novation" is a catch-word. There are two elements : The discharge of one contract; the substitution of another. Reconstitution of a partnership firm with the incoming or outgoing partners is a novation.

A owes money to B. A, B and C agree that C should pay this money to B. This is novotion.

A owes B Rs.10000/- under a P/N. A executed a mortgage in favour of B for the same amount. The P/N is discharged. There is a novotion with the mortgage-deed.

f. Discharge by operation of law

1) By Merger

2) By making alteration in the instrument of contract

3)By Bankruptcy

2. **Anticipatory breach :**

There may be a breach of contract even before the actual time fixed for the performance has arrived. Thus, if a promisor has refused to perform or disables himself from performing his promise, the promises is entitled to treat:

a) the contract as at an end, and to sue for damages without waiting for the time to come or

b) he may wait until the time comes, and then sue for the breach.

This applies only to an executory contract. The rule is that one party may keep the transaction alive without rescinding it ; and sue only after actual time has arrived.

Eg : a) If 'A' a singer contracts to sing at B's theatre for two nights every week for 2 months, and wilfully absents himself on the second week, B is at liberty to put an end to the contract.

b) In the above example, if B allows A to sing after the breach, he has agreed to the continuance and hence cannot put an end to the contract.

c) A agrees to supply on 1-6-92,100 metric tons of coal to B. On 1-3-92, A writes to B, stating that he would not deliver. B may sue immediately or wait until 1-6-92 and then sue.

d) In Frost Vs. Knight

D promised to marry P on the death of D's father. Even when D's father is alive, D refuses to marry. P may sue without waiting for D's father to die.

e) **Rochester Vs. Dela Tour**:

D agreed to employ H ascourier on a continental tour from 1st June for 3 months. In May, Dwrote to H stating that he did not want him. H without waiting, sued D for breach of contract. Held, the contract had been expressly breached and H need not wait until June 2. Held : D liable.

f) **Avery** Vs. **Bowdon** :

Here D agreed to load P's ship with cargo, within 45 days at Odessa, the ship arrived and waited for D to load, but D told the captain that there was no cargo. But, captain waited hoping D may bring cargo, In the meanwhile war broke out.

Held, contract frustrated. There was no anticipatory breach in the circumstances of the case.

3. Doctrine of Impossibility :

Two aspects are dealt with in section 56 of the contract act.

1) The impossibility of performance. Sn. 56 (1)

2) The contract becoming frustrated Sn. 56 (2)

1) An agreement to do an impossible act is void. Sn 56 (1).

Eg : 1) A agrees with B to discover treasure by magic. This is void.

2) A and B contract to marry. Before the time fixed for marriage, A becomes mad. This is void.

"Implied condition theory" : The general rule is that every contract is legally binding on the parties to the contract. When there is a breach, the other party may sue for damages. There is one exception to this. Due to vital change of circumstances, the contractual obligation may become impossible of performance. In such a case, the court reads a clause into the contract an implied condition, that the contract would be void when there were vital change of circumstances.

In the following cases such an implied condition is presumed :

i) Extinction or destruction of the subject matter

ii) Death or personal disablement of party

iii) State's declaration of war

iv) Subsequent illegality of the subject of the contract

v) Frustration

4. **Doctrine of frustration :**

Sn. 56(2) provides that (i) A contract to do an act, which after the contract is made, becomes impossible, is void, (ii) A contract to do an act, which by reason of some event which the promisor could not prevent, becomes unlawful, the contract is void.

Eg : 1) A contracts to supply a Cargo to B at a foreign port. Both countries of A and B declare war against each other. Contract becomes void when war is declared.

2) A contracts to act in a film for 6 months. A becomes ill on several occasions, the contract becomes void on such occasions.

This is called the doctrine of frustration.

The origin of this can be traced to Parlin's case where the rule of absolute liability was enunciated.

In the 19th century a new doctrine was enunciated in **Tayler Vs. Caldwell,** where a music hall was let out on certain dates, but before those dates, the hall was destroyed by fire.

Held : Owner not liable. The court held that there is in every contract an implied condition that the parties shall be excused, when the performance becomes impossible from the perishing of the subject matter, without any default of the parties.

Frustration was defined in this case. It means that the intention of the parties is frustrated, when the object which they had in view is no longer attainable because of change of circumstances. (Rebus sic stantibus) These are so fundamental as to strike at the root of the agreement. Hence contract becomes void.

Circumstances :

1) **Event not happening:**

The leading case **is Krell** Vs. **Henry** also called Coronation case. In this case D agreed to hire from P a flat on June 26th and 27th, to make arrangements to view coronation procession. Part of rent was paid as advance. However, the procession was cancelled. P sued D for balance of rent. Held contract frustrated as the event never took place. - Not recoverable.

2. **Incapacity to do service** : The contract becomes void if the promisor dies or becomes incapable of doing personal service as per the agreement.

In Robinson Vs. Davison, A piano player had agreed to perform the contract on a particular day but due to illness he could not perform. Held : There was frustration of contract.

3. **Government Intervention** :

   The contract may become in capable of performance if the govt. make laws prohibiting trade activities. A number of cases have been reported during the time of the First and the Second World Wars.

Leading cases : Metropolitan Water Board Vs. Dick Tamplin

Vs. Anglo Mexican Co.

4. **Subsequent illegality** : If a particular trade which is valid at the time of making a contract is subsequently declared illegal by the Govt. the contract becomes frustrated due to illegality.
5. **Contract may become frustrated by delay :**

Limitation : Certain limitations or qualifications are provided for.

i) The frustration must not be due to the fault of either of the parties to the contract.

ii) Lease : Doctrine of frustration does not apply to the case of lease or tenancy.

iii) Express contract: If the parties expressly make the contract with reference to the supervening event then frustration is not applicable.

6. **Effect of Frustration** : In Fibosa case it was held that money paid in advance must be returned back.

In Fibosa Vs. **Fairburn,** A contract to manufacture and deliver to B certain machinery, part of the price i.e., 1000 pounds was paid as advance. Then war broke out. Performance became impossible and the contract became frustrated. Lord Simon held that as there was a total failure of consideration, the money paid could be recovered. The Law Reforms Act 1943, has provided that in case of frustration, the money paid was recoverable.

In Satyabrata Ghosh V. Mugneeram the Indian position was explained when any person has received an advantage over another in a void or frustrated agreement or contract, such a party should restore the same to the other party..

The facts were as follows :

D company had agreed to develop a big plot of land under a development scheme. It made a sale deed with Satyabrata Ghosh, (plaintiff), for sale of a portion of the plot of land, during the second world war ; the deed was to be executed within a month after the completion of the scheme. P had made earnest deposits. However, before the scheme started, the Govt. requisitioned a major portion of the land, and entry was made illegal. The company offered to return the earnest deposit, or to convey the land in the existing circumstances. If P did not agree the company stated that it would declare the contract as frustrated and the deposit would be forfeited. P sued.

Held : There was no frustration as the taking by the Govt. was temporary ; and that there was no time limit for the scheme. Held that D was liable.

TOPIC NO. 5

REMEDIES FOR BREACH OF CONTRACT

Remedy means a course of action available to an aggrieved party when other party breaches the contract.

Remedies for breach of contract:

1. Rescission of contract
2. Suit for damage
3. Suit for specific performance
4. Suit for injunction
5. Quantum merit

Recission Of Contract **– Section 39**

- It means right to party to cannot contract.
- In case of breach of contract, other parties may rescind the contract.
- Effect of rescission of the contract
- The aggrieved party is not required to perform his party of an obligation under the contract.
- The aggrieved party claims compensation for any loss.
- Party is liable to restore benefit if any.
- When can court grant rescind the contract?
- The court can rescind the contract in the following situation:
    - The contract is voidable.
    - The contract is unlawful.

Suit For Damages Under Remedies For Breach Of Contract

- It means monetary compensation allowed for loss.
- The purpose is to compensate the aggrieved party and not to punish the party as a fault.

- In India, rules relating to damages are based on English judgment of Hadley vs Baxendale.

The facts of the case were – H's mill was stopped due to the breakdown of the shaft. He delivered the shaft to the common carrier to repair it and agree to pay a certain sum of repair it and agree to pay a certain sum of money for doing this work. H has informed B that delay would result in a loss of profit. It was held that B is not liable for loss of profit. The court laid down the rule that damage can be recovered if the party has been a breach of contract.

Kind Of Damages Under Remedies For Breach Of Contract

The following are the different kinds of damages:

- **Ordinary damages:** These are the damages which are payable for the loss arising naturally and directly as a result of a breach of contract. It is also known as proximate damage or natural damage.
- **Special damages:** These are damages which are payable for loss arising due to some special circumstances. It can be recovered only if special circumstances which result in a special loss in case of breach of contract and party have notice of such damage. Example: A sends samples of his products for exhibition to an agent of a railway company for carriage to "NEW DELHI" for an exhibition. The consignment note stated: "much be at new Delhi, Monday certain." Due to the negligence of the company, the goods reached only after the exhibition was over. Held, the company was liable for the loss caused by the late arrival of the products because the company's agent was aware of the special circumstances.
- **Exemplary or punitive or vindictive damages:** These damages are allowed not to compensate party but as mean of punishment to the defaulting party. The court may award these damage in the case of:
  Breach of contract to marry – loss based on mental injury.
  Wrongful dishonour of cheque – smaller amount, larger the damage.
- **Nominal damages:** Where the party suffers no loss, the court may allow nominal damages simply to establish that party has proved his case and won. Nominal damage is very small in amount.

- **Damages for the inconvenience:** If the party has suffered physical inconvenience, discomfort for mental agony as a result of a breach of contract, the party can recover the damage for such inconvenience.

Example: A photographer agreed to take photographs at a wedding ceremony but failed to do so. The bride brought an action for the breach of contract. Held, she was entitled to damages for her injured feeling.

- **Liquidated damages and penalty:** Party may specify amount at the time of entering into the contract. The amount so specified may be (a) liquidated damage, or (b) penalty. But if the specified sum is disproportionate to the damages, it is called a penalty. As regard, the payment of liquidated damages and penalty court can't increase the number of damages beyond the amount specified in the contract.

Example: A given B, a bond for the repayment of Rs,1000 with interest at 12 per cent, at the end of six months, with a stipulation that, in case of default, the interest shall be payable at the rate of 75 per cent, from the date of default. This is a stipulation by way of penalty, and B is only entitled to recover from A such compensation as the court considers reasonable.

Forfeiture of the security deposit: Any clause in contract entitling the aggrieved party to forfeit security deposit like penalty and court may award reasonable compensation.

Payment of interest: It is permissible. If interest in nature of the penalty, the court may grant relief. If no rate of interest is specified in contract party shall be liable to pay as per the law in force or as per custom or usage of trade.

Cost of suit or decree: The court has also the discretion to award cost of suit for damages in addition to the damages for breach of contract.

Suit for specific performance under Remedies For Breach Of Contract: It means, demanding an order from the court that promise agreed in contract shall be carried out.

- When is specific performance allowed?
- Where actual damages arising from a breach is not measurable.

- Where monetary compensation is not an adequate remedy.
- When specific performance is not allowed?
- When damages are an adequate remedy.
- When the performance of the contract requires the number of minute details and therefore not possible for the court to supervise.
- When the contract is of personal.
- When a contract made by the company beyond its power. (ultra – virus)
- Where one party to contract is minor.
- Where a contract is inequitable to either party.

Example: A agrees to sell B an artist painting for Rs.30000. later on, he refused to sell it. Here B can file suit against A for specific performance of the contract.

Suit for an injunction:

- It means stay order granted by the court. This order prohibits a person to do a particular activity.
- Where there is a breach of contract by one party and order, of specific performance, is not granted by the court, an injunction may be granted.

Example: film actress agreed to act exclusively for W for a year and no one else. During the year she contracted to act for Z.

Suit Upon Quantum Meruit: Quantum merits means, "As much as is earned" or " in proportion to the work done." Ordinarily, if a person has agreed to do some work or render some services, has done only a part of what he was required to do, he cannot claim anything for what he had done.

When a person agrees to complete some work for a lump sum non-completion of the work does not entitle him to any remuneration even for the part of the work done. But the law recognizes an important exception to this rule by way of an act of 'Quantum Meruit'.

ILLUSTRATION:

1. If A and B have entered into a contract, is prevented by B from performing the rest of his obligation under the contract, A can recover from B reasonable for whatever he has already done. By this action, the injured party (who himself has not made the breach of contract) is entitled to be compensated for whatever work he may have already done, or whatever expense he may have incurred.
2. If A agrees to deliver B,500 bags of cement &when A has already delivered 100 bags, B refuses to accept any further supply, A can recover from B the value of wheat which he has already delivered.

DIFFERENCE BETWEEN QUASI CONTRACT AND CONTRACT MATTER QUASI-CONTRACT CONTRACT

- Intentionally from It is not formed but the law imposes upon the parties. It is intentionally formed by parties.
- Essential of contract A quasi-contract does not possess all the essential of a valid contract. A contract possesses all the essentials of a valid contract.
- Obligations Obligation are implied by the law. It is mutually created by the parties.
- Foundation: It is founded upon the principle of equity. It is founded upon the general principle of the law of contracts.

TOPIC NO 6
SALE OF GOODS ACT 1930

Scope of the Act

The sale of Goods Act deals with 'Sale of Goods Act,1930,'contract of sale of goods is a contract whereby the seller transfers or agrees to transfer the property in goods to the buyer for a price." 'Contract of sale' is a generic term which includes both a sale as well as an agreement to sell.

Essential elements of Contract of sale

1. Seller and buyer

There must be a seller as well as a buyer.'Buyer' means a person who buys or agrees to buy goods[Section 2(1)].'Seller' means a person who sells or agrees to sell goods [Section 2(13)].

2. Goods

There must be some goods.'Goods' means every kind of movable property other than actionable claims and money includes stock and shares,growing crops,grass and things attached to or forming part of the land which are agreed to be severed before sale or under the contract of sale[Section 2(7)].

3. Transfer of property

Property means the general property in goods,and not merely a special property [Section 2(11)].General property in goods means ownership of the goods. Special property in goods means possession of goods.Thus,there must be either a transfer of ownership of goods or an agreement to transfer the ownership of goods.The ownership may transfer either immediately on completion of sale or sometime in future in agreement to sell.

4. Price

There must be a price.Price here means the money consideration for a slae of goods[Section 2(10)].When the consideration is only goods,it amounts to a 'barter' and not sale.When there is no consideration ,it amounts to gift and not sale.

5. Essential elements of a valid contract

In addition to the aforesaid specific essential elements,all the essential elements of a valid contract as specified under Section 10 of Indian Contract Act,1872 must also be present since a contract of sale is a special type of a contract.

Meaning and types of goods

Meaning of goods[Section 2(7)]

Goods means every kind of movable property other than actionable claims and money,and includes the following:

- Stock and share
- Growing crops,grass and thing attached to or forming part of the land which are agreed to be served before sale or under the Contract of sale.

Types of Goods[Section 6]

1.Existing Goods

Existing goods mean the goods which are either owned or possessed by the seller at the time of contract of sale.The existing goods may be specific or ascertained or unascertained as follows:

a) Specific Goods[Section 2(14)]:

These are the goods which are identified and agreed upon at the time when a contract of sale is made-For example,specified TV,VCR,Car,Ring.

b) Ascertained Goods:

Goods are said to be ascertained when out of a mass of unascertained goods,the quantity extracted for is identified and set aside for a given contract.Thus,when part of the goods lying in bulk are identified and earmarked for sale,such goods are termed as ascertained goods.

c) Unsanctioned Goods:

These are the goods which are not identified and agreed upon at the time when a contract of sale is made e.g. goods in stock or lying in lots.

2. Future Goods[Section 2(6)]

Future goods mean goods to be manufactured or produced or acquired by the seller after the making of the contract of sale.There can be an agreement to sell only.There can be no sale in respect of future goods because one cannot sell what he does not possess.

3. Contingent Goods [Section 6(2)]

These are the goods the acquisition of which by the seller depends upon a contingency which may or may not happen.

Price Of Goods

Meaning[Section 2(10)]

Price means the money consideration for a sale of goods.

Modes of determining Price [Section 9(1)]

There are three modes of determining the price as under:

- It may be fixed by the contract or
- It may be left to be fixed in an agreed manner
- It may be determined by the course of dealing between the parties.
- Thus,the price need not necessarily be fixed at the time of sale.

Consequences of not determining the Price in any of the Mode [Section 9(2)]

Where the price is not determined in accordance with Section 9(1),the buyer must pay seller a reasonable price.What is a reasonable price is a question of fact dependent on the circumstances of each particular case.It may be noted that a reasonable price need not be market price.

Consequence of not Fixing Price by third party[Section 10(1)]

The agreement to sell goods becomes void if the following two conditions are fulfilled.

- If such agreement provided that the price is to be fixed by the valuation of a third party,
- If such third party cannot or does not make such valuation.

Duty of buyer

A buyer who has received and appropriated the goods,must pay a reasonable price therefor.

Right of party not at fault to sue

Where such a third party is prevented from making the valuation by fault of the seller or buyer,the party not at fault may maintain a suit for damages against the party in fault.

Conditions and Warranties

It is usual for both seller and buyer to make representations to each other at the time of entering into a contract of sale. Some of these representations are mere opinions which do not form a part of contract of sale.Whereas some of them may become a part of contract of sale.Representations which become a part of contract of sale are termed as stipulatuins which may rank as condition and warranty e.g. a mere commendation of his goods by the seller doesn't become a stipulatuin and gives no right of action to the buyer against the seller as such representations are mere opinion on the part of the seller.But where the seller assumes to assert a fact of which the buyer is ignorant,it will amount to a stipulation forming an essential part of the contract of sale.

Meaning of Conditions [Section 12(2)]

A condition is a stipulation
Which is essential to the main purpose of the contract
The breach of which gives the aggrieved party a right to terminate the contract.

Meaning of Warranty[Section 12(3)]

A warranty is a stipulation
Which is collateral to the main purpose of the contract
The breach of which gives the aggrieved party a right to claim damages but not a right to reject goods and to terminate the contract.

Conditions to be treated as Warranty[Section 13]

In the following three cases a breach of a condition is treated as a breach of a warranty: Where the buyer waives a conditions; once the buyer waives a conditions,he cannot insist on its fulfillment e.g. accepting defective goods or beyond the stipulated time amount to waiving a conditions.

Where the buyer elects to treat breach of the condition as a breach of warranty;e.g. where he claims damages instead of repudiating the contract.

Where the contract is not severable and the buyer has accepted the goods or part thereof,the breach of any condition by the seller can only be treated as breach of warranty.It can not be treated as a gorund for rejecting the goods unless otherwise specified in the contract.Thus,where the buyer after purchasing the goods finds that some condition is not fulfilled,he cannot reject the goods.He has to retain the goods entitling him to claim damages.

Express and Implied Conditions and Warranties

In a contract of sale of goods,conditions and warranties may be express or implied.

1.Express Conditions and Warranties.

These are expressly provided in the contract.For example,a buyer desires to buy a Sony TV Model No. 2020.Here,model no. is an express condition.In an advertisement for Khaitan fans,guatantee for 5 years is an express warranty.

2. Implied Conditions and Warranties

These are implied by law in every contract of sale of goods unless a contrary intention appears from the terms of the contract.The various implied conditions and warranties have been shown below:

Implied Conditions

1. Conditions as to title [Section 14 (a)]

There is an implied condition on the part of the seller that

In the case of a sale,he has a right to sell the goods,and
In the case of an agreement to sell,he will have a right to sell the goods at the time when the property is to pass.

2. Condition in case of sale by description [Section 15]

Where there is a contract of sale of goods by description,there is an implied condition that the goods shall correspond with description.The main idea is that the goods supplied must be same as were described by the seller.Sale of goods by description include many situations as under:
i. Where the buyer has never seen the goods and buys them only onm the basis of description given by the seller.
ii. Where the buyer has seen the goods but he buys them only on the basis of description given by the seller.
iii. Where the method pf packing has been described.

3. Condition in case of sale by sample [Section 17]

A contract of sale is a contract for sale by sample when there is a term in the contract, express or implied,to that effect.Such sale by sample is subject to the following three conditions:

The goods must correspond with the sample in quality.
The buyer must have a reasonable opportunity of comparing the bulk with the sample.
The goods must be free from any defect which renders them unmerchantable and which would not be apparent on reasonable examination of the sample.Such defects are called latent defects and are discovered when the goods are put to use.

4. Condition in case of sale by description and sample [Section 15]

If the sale is by sample as well as by description, the goods must correspond with the sample as well as the description.

5. Condition as to quality or fitness [Section 16(1)]

There is no implied condition as to the quality or fitness for any particular purpose of goods supplied under a contract of sale.In other words,the buyer must satisfy himself about the quality as well as the suitability of the goods.

Exception to this rule:

There is an implied condition that the goods shall be reasonably fit for a particular purpose described if the following three conditions are satisfied:

1. The particular for which goods are required must have been disclosed(expressly or impliedly) by the buyer to the seller.
2. The buyer must have relied upon the seller's skill or judgement.
3. The seller's business must be to sell such goods.

6. Condition as to merchantable quality[Section 16(2)]

Where the goods are bought by description from a seller who deals in goods of that description,there is an implied condition that the goods shall be of merchantable quality.The expression ' merchantable quality' means that the quality and condition of the goods must be such that a man of ordinary prudence would accept them as the goods of that description.Goods must be free from any latent or hidden defects.

7. Condition as to wholesomeness

In case of eatables or provisions or foodstuffs,there is an implied condition as to wholesomeness.Condition as to wholesomeness means that the goods shall be fit for human consumption.

8. Coditions implied by custom [Section 16(3)]

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

Implied warranties

a)Warranty as to quiet possession [Section14(b)]

There is an implied warranty that the buyer shall have and enjoy quiet possession of the goods.The reach of this warranty gives buyer a right to claim damages from the seller.

b)Warranty of freedom from encumbrances [Section 14(c)]

There is an implied warranty that the goods are free from any charge or encumbrance in favour of any third person if the buyer is not aware of such charge or encumbrance.The breach of this warranty gives buyer a right to claim damages from the seller.

-
- Warranty as to quality or fitness for a particular purpose annexed by usage of trade[Section 16(3)]
- Warranty to disclose dangerous nature of goods

In case of goods of dangerous nature the seller fails to do so, the buyer may make him liable for breach of implied warranty.

Transfer of property in goods

Meaning of Passing of Property/Transfer of Property

Passing of property implies transfer of ownership and not the physical possession of goods.For example,where a principal sends goods to his agent,he merely transfers the physical possession and not the ownership of goods.Here,the principal is the owner of the goods but is not having possession of goods and the agent is having possession of goods but us not the owner.

Significance of Transfer of Property

The time of transfer of ownership of goods decides various rights and liabilities of the seller and the buyer.Thus,it becomes very important to know the exact time of transfer of ownership of goods from seller to buyer to answer the following questions:

1. Who shall bear the risk?

It is the owner who has to bear the risk and not the person who merely has the possession.

2. Who can take action against third party?

It is the owner who can take action and not the person who merely has the possession.

3. Whether a seller can sue for price?

The seller can sue for the price only if the ownership of goods has been transferred to the buyer.

4. In case of insolvency of a buyer whether the official receiver or assignee can take the possession of goods from seller?

The Official Receiver or Assignee can take the possession of of goods from seller only if the ownership of goods has been transferred to the buyer.

5. In case of insolvency of a seller whether the official receiver or assignee can take the possession of goods from buyer?

The official receiver or assignee can take the possession of goods from buyer onlu if the ownership of goods has not been transferred to the buyer.

Rules relating to Passing of Property/Transfer of Ownership from seller to buyer

For the purposes of ascertaining the time at which the ownership is transferred from seller to the buyer,the goods have been classified into the following three categories:

a) Specific or ascertained goods

Specific goods mean goods identified and agreed upon at the time when a contract of sale is made.[Section 2(14)]

b) Unascertained goods

c) Goods sent ‘on approval’ or ‘on sale on return’ basis.

Performance of the Contract

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

Unless otherwise agreed, payment of the price and the delivery of the goods and concurrent conditions, i.e., they both take place at the same time as in a cash sale over a shop counter.

Delivery (Sections 33-39)

Delivery is the voluntary transfer of possession from one person to another. Delivery may be actual, constructive or symbolic. Actual or physical delivery takes place where the goods are handed over by the seller to the buyer or his agent authorized to take possession of the goods.

1.Constructive delivery takes place when the person in possession of the goods acknowledges that he holds the goods on behalf of and at the disposal of the buyer. For example, where the seller, after having sold the goods, may hold them as bailee for the buyer, there is constructive delivery.

2.Symbolic delivery is made by indicating or giving a symbol. Here the goods themselves are not delivered, but the "means of obtaining possession" of goods is delivered, e.g, by delivering the key of the warehouse where the goods are stored, bill of lading which will entitle the holder to receive the goods on the arrival of the ship.

Rules as to delivery

The following rules apply regarding delivery of goods:

(a) Delivery should have the effect of putting the buyer in possession.
(b) The seller must deliver the goods according to the contract.
(c) The seller is to deliver the goods when the buyer applies for delivery; it is the duty of the buyer to claim delivery.
(d) Where the goods at the time of the sale are in the possession of a third person, there will be delivery only when that person acknowledges to the buyer that he holds the goods on his behalf.

(e) The seller should tender delivery so that the buyer can take the goods. It is no duty of the seller to send or carry the goods to the buyer unless the contract so provides. But the goods must be in a deliverable state at the time of delivery or tender of delivery. If by the contract the seller is bound to send the goods to the buyer, but no time is fixed, the seller is bound to send them within a reasonable time.

(f) The place of delivery is usually stated in the contract. Where it is so stated, the goods must be delivered at the specified place during working hours on a working day. Where no place is mentioned, the goods are to be delivered at a place at which they happen to be at the time of the contract of sale and if not then in existence they are to be delivered at the place at which they are manufactured or produced.

(g) The seller has to bear the cost of delivery unless the contract otherwise provides. While the cost of obtaining delivery is said to be of the buyer, the cost of the putting the goods into deliverable state must be borne by the seller. In other words, in the absence of an agreement to the contrary, the expenses of and incidental to making delivery of the goods must be borne by the seller, the expenses of and incidental to receiving delivery must be borne by the buyer.

(h) If the goods are to be delivered at a place other than where they are, the risk of deterioration in transit will, unless otherwise agreed, be borne by the buyer.

(i) Unless otherwise agreed, the buyer is not bound to accept delivery in instalments.

Acceptance of Goods by the Buyer

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

(a) intimates to the seller that he has accepted the goods; or

(b) retains the goods, after the lapse of a reasonable time without intimating to the seller that he has rejected them; or

(c) does any act on the goods which is inconsistent with the ownership of the seller, e.g., pledges or resells.

If the seller sends the buyer a larger or smaller quantity of goods than ordered, the buyer may:

(a) reject the whole; or

(b) accept the whole; or

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

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

Instalment Deliveries

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

Suits for Breach of Contract

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

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

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

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

Where there is a breach of warranty or where the buyer elects or is compelled to treat the breach of condition as a breach of warranty, the buyer cannot reject the goods. He can set breach of

warranty in extinction or dimunition of the price payable by him and if loss suffered by him is more than the price he may sue for the damages.

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

Anticipatory Breach

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

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

(a) his right of performance on the due date in spite of his prior repudiation; or

(b) his rights to set up any defence for non-performance which might have actually arisen after the date of the prior repudiation.

Measure of Damages

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

Unpaid seller and his rights

Meaning of an Unpaid Seller [Sec 45(1)(2)]

The seller of goods is deemed to be an 'unpaid seller'-

When the whole of the price has not been paid or tendered
When a bill of exchange or other negotiable instrument(such as cheque) has been received as conditional payment,and it has been dishonoured[Section 45(1)].
The term 'seller'includes any person who is in the position of a seller(for instance,an agent of the seller to whom the bill of lading has been endorsed,or a consignor or agent who has himself paid,or is directly responsible for the price) [Section 4592)].

Rights of an Unpaid Seller [Section 46-52,54-56,60-61]

The rights of an unpaid seller can broadly be classified under the following two categories:

Rights against the goods
Rights against the buyer personally

I **Rights against the goods where the property in the goods has passed to the buyer**

a) Right of Lien [Section 47,48 and 49]

Meaning of Right of Lein:
The right of lien means the right to retain the possession of the goods until the full price is received.

Three circumstance under which right of lien can be exercised[Section 47(1)]
1.Where the goods have been sold without any stipulation to credit;
2.Where the goods have been sold on credit,but the term of credit has expired;
3.Where the buyer becomes insolvent.

Other provisions regarding right of lien[Sections 47(2),48,49(2)]

1.The seller may exercise his right of lien,even if he possesses the goods as agent or bailee for buyer[Section 47(2)]
2.Where an unpaid seller has made part delivery of the goods,he may exercise his right of lien on the remainder,unless such part delivery has been made under such circumstances as to show agreement to waive the lien[Section 48].

3.The seller may exercise his right of lien even though he has obtained a decree for the price of the goods[Section 49(2)].

Circumstances under which right of lien in the following cases:

1.When he delivers the goods to a carrier or other bailee for the purpose of transmission to the buyer without reserving the right of disposal of the goods[Section 49(1)(a)].
2.When the buyer or his agent lawfully obtains possession of the goods [Section 49(1)(b)]
3.When the seller waives his right of lien[Section 49(1)(c)].
4.When the buyer disposes of the goods by sale or in any other manner with the consent of the seller[Section 53(1)].
5.Where document of title to goods has been issued or lawfully transferres to any person as buyer or owner of the goods and that person transfers the document by way of sale,to a person who takes the document in good faith and for consideration.[Proviso to Section 53(1)].

b) Right of Stoppage of Goods in Transit

The right of stoppage of goods means the right of stopping the goods while they are in transit,to regain possession and to retain them till the full price is paid.

Conditions under which right of stoppage in transit can be exercised[Section 50]

The unpaid seller can exercise the right of stoppage in transit only if the following conditions are fulfilled:
1.The seller must have parted with the possession of goods,i.e. the goods must not be in the possession of seller.
2.The goods must be in the course of transit.
3.The buyer must have become insolvent.

c)Right of Resale[Section 46(1) and 54]

An unpaid seller can resell the goods under the following three circumstance:
1.Where the goods are of a perishable nature.
2.Where the seller expressly reserves a right of resale if the buyer commits a default in making

payment.

3.Where the unpaid seller who has exercised his right of lien or stoppage in transit gives a notice to the buyer about his intention to resell an dbuyer does not pay or tender within a reasonable time.

II Rights against the goods where the property in the goods has not passed to the buyer

Right of withholding delivery[Section 46(2)]

Where the property in the goods has not been passed to the buyer, the unpaid seller, cannot exercise right of lien, but get a right of withholding the delivery of goods, similar to and co-extensive with lien and stoppage in transit where the property has passed to the buyer.

Rights of Unpaid Seller against the Buyer Personally

The unpaid seller, in addition to his rights against the goods as discussed above, has the following three rights of action against the buyer personally:

1. Suit for price (Sec. 55). Where property in goods has passed to the buyer; or where the sale price is payable 'on a day certain', although the property in goods has not passed; and the buyer wrongfully neglects or refuses to pay the price according to the terms of the contract, the seller is entitled to sue the buyer for price, irrespective of the delivery of goods. Where the goods have not been delivered, the seller would file a suit for price normally when the goods have been manufactured to some special order and thus are unsaleable otherwise.

2. Suit for damages for non-acceptance (Sec. 56). Where the buyer wrongfully neglects or refuses to accept and pay for the goods, the seller may sue him for damages for non-acceptance. The seller's remedy in this case is a suit for damages rather than an action for the full price of the goods.

3. Suit for Interest[Section 61(2)]

In case of breach of the contract on the part of seller, the buyer may sue the seller for interest from the date on which the payment was made.

TOPIC NO.7

INDIAN PARTNERSHIP ACT, 1932

For a layman, a partnership is an association of people who have common objectives and goals. Even a business owned or managed by two or more people is termed as partnership. The idea of a partnership or such collaboration is that every member or partner contributes something which helps achieve an aim and is beneficial to all the members. A member may contribute money, skill or labour which in turn makes it easier to achieve the common objective. Thus, partnership is an arrangement where people consent to work together and advance their mutual interests. For example, two doctors may decide to work together on the same case as partners and share the fees.

Initially, partnership was governed by provisions contained in *Sections 239 to 266* of chapter XI of the Indian Contract Act, 1872. These sections were repealed in 1930 and a new act – the Indian Partnership Act, 1932 was passed. The Act came in to force on the 1st of October 1932, except *Section 69* which came into force on the 1st of October, 1933. It aims to define and amend the law relating to partnership. The Act is not exhaustive. Partnership is a special kind of contract and thus, the provisions of Indian Contract Act, 1872 also apply to a partnership firm unless the Indian Partnership Act provides otherwise.

PARTNERS

The term 'partner' is linked to various other words. It is said to be derived from the Latin term '*partitionem*' which means 'portion or division'. The word 'partner' is also associated with the French term '*parçener*' which means 'joint heir' or 'one that shares or has a part with another'. The term can also be broken down to '*to part*' which means 'to divide' or 'to share'.

Section 4 of the Indian Partnership Act 1932 defines 'partnership' as the "relation between persons who have agreed to share the profit of a business carried on by all or any of them acting for all". Persons who have entered into partnership with one another are called individually '*partners*' and collectively a '*firm*' and the name under which their business is carried on is called the '*firm name*'.

Example: A is a goldsmith. He agrees with B to buy and provide gold to B for making ornaments. They plan to sell the ornaments and share the profit. Here, A and B are partners.

Example: Both, A and B are carpenters. They decide to work together. But they have an agreement under which A will keep all the profits and pay B a pre-determined salary. Here, A and B are not partners.

Sir Fredrick Pollock defines partnership as 'the relationship between persons who have agreed to share the profits of a business that is carried on by one of them or all of them'.

Under the English Partnership Act, 1890 partnership is defined as 'the relation subsisting between persons carrying on business in common with a view to profits'. In simple words, if two people agree to combine money, skill or labour in a business and to share profits thereof, their relationship is called partnership.

ESSENTIAL FEATURES

The essential features of partnership as per the definition of partnership are listed below:

1) Two or more people

2) Valid Agreement

3) Created for the purpose of carrying on business

4) Sharing of Profits

5) Mutual Agency

1) ***Two or more people:*** Minimum two people are needed to create a partnership. The Indian Partnership Act, 1932 does not prescribe any upper limit on the number of people who can be partners. However, *Section 11* of the Companies Act, 1956 provides that number of partners cannot exceed 10 persons in case of banking business and 20 in other businesses. If the number of partners exceeds the limit, the partnership becomes an illegal association. Similarly, if the number falls below two, the partnership is deemed dissolved.

The people who are partners in a firm must be competent to contract. If all partners are minors or if there is only one adult partner, it is not a partnership at all.

2) ***Valid Agreement:*** The foundation of partnership is an agreement. *Section 5* clearly states that partnership is not created by status – the relationship of partnership can arise only out of a contract. Thus, if a Hindu Undivided Family is carrying on a family business, it is not a partnership. Similarly, a Burmese Buddhist husband and wife carrying business are not partners in such business.

The partnership agreement must fulfil all the requirements of a valid contract. There should be free consent, competency of the parties, lawful consideration and object. The agreement to create

partnership may be express or implied. The agreement can also be inferred from the conduct of the parties. The agreement need not be in writing except where required under the Income Tax Act or if the partners wish to get the firm registered.

Partnership does not arise by mere joint acquisition of property like in the case of co-ownership. If a wife entrusts her *stridhan* to her husband, it is not an agreement of partnership even if the husband uses the property for business.

3) ***Created for the purpose of carrying on business:*** The partnership must have been created to carry on business. It is not necessary that all the partners actively participate in the conduct of the business. For example, one partner may contribute skill or experience while another may contribute capital for the firm. The business may be permanent or temporary, trading or non trading.

Section 2(b) of the Indian Partnership Act, 1932 says that 'Business' includes every trade, occupation and business. Thus, a partnership does not exist between members of a religious association and the like.

Services rendered jointly also constitute a partnership. For example, if two advocates may agree to jointly plead a case and divide the fees, they are partners in respect to that case. But an agreement to carry on business in the future is not a partnership.

4) ***Sharing of Profits:*** The purpose of a partnership is to carry on business. Thus, it is obvious that the partners have an interest in sharing the profits so earned from the business of the firm. Here, profits include losses as well. Division of profits is an important element in a partnership. There was a time when sharing of profits was used as a test to determine whether a partnership existed or not. If a person shared the profits and incurred liabilities too, he was deemed a partner as held in *Grace vs. Smith* [1775 2 WM Blacks 998]

However, in the present day, a person does not become a partner merely because he shares the profits of the business. Similarly, sharing of losses is not a must for a partnership. Sharing profits and contributing to losses are indications or *prima facie* evidence of a partnership but not the conclusive test of partnership. It is possible that a partner may be paid salary or a fixed sum periodically in lieu of profits. In *Cox vs. Hickman* [1860 8 HL Cas 268], it was held that the conclusive test for partnership is mutual agency because it is possible that every man who gets a share in the profits might not be liable for the losses of the firm or might not be a partner.

For example, a servant or agent may receive a share of profits instead of his salary or as a bonus. Similarly, a person who sells his business and goodwill may be given a share of profits as consideration for sale. An employee of the firm may loan some money to the firm. But these persons do not *ipso facto* become partners in the firm due to such participation.

In the case of *Mollow vs. Court of Wards* [1872 LR 4 PC 419], a Hindu Raja loaned some money to a company. In return, he was given a certain percentage of profit and also allowed to exercise control on some aspects of the business. But the Raja was not empowered to direct the transactions of the company. It was held that although sharing of profits is a very strong test, the relationship of partnership depends on the real intention and conduct of the parties.

The partners can decide the ratio or proportion of share in profits and losses through an agreement between them. A partner may get more percentage of the profits than the other(s) based on factors like contribution of capital, special skills or taking a more active part in the daily functioning of the firm.

5) ***Mutual Agency:*** *Section 4* of the Act states that the business of the partnership must be carried on by all or any of them acting for all. Thus, there must be a relationship of mutual agency amongst all the partners.

Mutual agency means that every partner has a dual role – that of a principal and of an agent. Every partner is an agent of the other partners and can bind other partners by his acts done on behalf of the firm in all matters that are within the scope and object of the partnership. Similarly, every agent is also the principal for the other partners in the firm and in turn, is bound by their acts. *Section 18*stresses the necessity of mutual agency again and states that a partner is an agent of the firm. The act of the partner is binding on the firm just like an act of an agent is binding upon the principal.

The foundation or basis of the law of partnership is agency. The law of partnership is undoubtedly, a branch of the law of the principal and agent. Every partner is both – an agent and principal for the other partners. For example, a notice to partner serves as a notice to the firm. The acts of a partner during the ordinary course of business bind the other partners and they are liable for the same.

Subject to limitations under *Section 20* of the Act, one partner can always bind the other partner(s) in any matter that falls within the scope of partnership. Partners are not agents for each other outside of the firm or for other purposes.

COX vs. HICKMAN [1860 8 HL Cas 268]

Facts: The business of Smith & Son into some financial problems. They entered into an agreement with their creditors that five representatives of the creditors would be appointed as trustees to manage the business. A was one of the trustees. While the trustees were managing the business, the firm was supplied some goods on credit. The invoice was marked accepted by agents for the trustees. This converted the invoice into a negotiable instrument. The accepted invoice was then endorsed in favour of B who paid a sum of money for the endorsement in his favour. After all the debts of the creditors were repaid, the business was returned to the owners. But the invoice remained unpaid and B an action against the trustees including B for the price.

Held: A was not a partner in the firm of Smith & Son and thus, he was not liable. Though the creditors had a share in the profits of the firm and were managing the affairs of the firm through their trustees, the nature of relationship between them never changed. The trustees were managing the business to recover money of the creditors and not as partners of the firm helping it survive. The intention of being partners was absent.

In the above case, House of Lords clarified that the sharing of profits only created a rebuttable presumption of partnership. Lord Cranworth elaborated further "*Where two or more persons are engaged as partners in any ordinary trade, each of them has an implied authority from the other to bind all by contracts entered into according to the usual course of business in that trade. ..The public have a right to assume that every partner has authority from his co-partner to bind the whole firm in contracts made according to the ordinary usages of trade.*"

Whether there was a partnership or not is a mixed question of fact and law, depending upon the varying circumstances in different cases.

FIRM & FIRM NAME

In the case of *Ex parte Corbett: In re Shand* [1880 LR 14 Ch.D 122 126], James, LJ said "*…there is no such thing as firm known to law. A firm is nothing more than a compendious name of the partners forming it…Unlike a joint stock company which is a legal entity, a firm has no separate existence apart from it members. A firm is not a body corporate. The rights and obligations of the firm are, in fact, those of the individuals composing a firm."*

Thus, a firm is only a convenient phrase used to describe the two or more persons constituting the partnership. It has no legal existence apart from such persons. If some partners draw a salary from the firm, they are still not the employees of the firm. A firm cannot be a member of a partnership nor enter into partnership with another firm. The property or assets of the firm are jointly owned property of the partners.

A firm has limited identity for purpose of tax laws. Though a partnership firm is not a juristic person, the Civil Procedure Code, 1908 enables the partners of a partnership firm to sue or to be sued in the name of the firm depending upon whether the firm is registered or not.

The name in which the partners carry on their business is the firm name. A firm name can be anything as long as it does not go against the rules relating to trade name or goodwill. *Section 58 (3)*of the Indian Partnership Act. 1932 says that "A firm name shall not contain any of the following words, namely – 'crown', 'Emperor', 'Empress', 'Implied', 'King', 'Queen', 'Royal', or words expressing or implying the sanction, approach or patronage of government except when the State government signified its consent to the use of such words as part of the firm name by order in writing".

It can be said that a firm is the concrete description of the people who constitute it while partnership is an abstract notion that is the relationship between the people constituting the firm.

PARTNERSHIP AND CO-OWNERSHIP

Co-ownership means two or more people have joint ownership of a property. The two or more people who own the property jointly are called co-owners.

Basis of distinction	*Partnership*	*Co-ownership*
Contract	It arises by contract. The interests of partners are determined by contract of partnership.	It may arise out of status or contract – for example birth, marriage or adoption.
Business and Profit – Sharing	It always implies a business. It involves the sharing of profits and losses.	It may exist without any business. It may not involve sharing of profits and losses.

Agent	Every partner in a partnership is an agent of the other partners.	A co-owner is not the agent of the others co-owners.
Transfer of Interest	A partner cannot transfer his interest without the consent of all other partners.	A co-owner may transfer his interest to a third party without the consent of other co-owners,
Partition	A partner may sue the other partners for dissolution of firm and accounts but he cannot claim partition of the firm property.	A co-owner has the right to claim partition of the jointly owned property.
Change in membership	It is dissolved by death or insanity of a partner.	It is not dissolved by death or insanity of one of the co-owners.
	A partner's liability is not limited to the extent of his interests in the assets of the firm.	A co-owner's liability is limited to the extent of his share.
Number of members	There is a restriction on the number of partners in a firm.	There is no restriction on number of co-owners.
Mutual Agency	Mutual agency between partners is a must.	There is no mutual agency between co-owners.
Lien	A partner has a right of lien on the partnership property for the expenses he may incur on behalf of the firm.	A co-owner has no lien on the jointly owned property for expenses or for a common debt.

PARTNERSHIP AND COMPANY

A company is an artificial person – a body corporate created by the operation of law and registration under the Companies Act 1956. It is a separate legal entity from its members. It has perpetual succession and a common seal.

Basis of distinction	*Partnership*	*Company*
Legal Personality	A firm is not a legal entity. It is the collective name of the individuals who constitute it.	A company is a legal person.
Relationship to members	A partnership firm has no existence apart from its members.	A company is a separate legal entity distinct from all its members.
Mutual Agent	Mutual agency is the essence of partnership.	A member of a company is not an agent of other members.
Liability	The liability of a partner is unlimited and includes his personal assets.	The liability of a shareholder is limited to the extent of value of shares held by him.
Transfer of Interest	A partner cannot his share or interest in the partnership without the consent of all the other partners of the firm.	A shareholder can freely transfer his share subject to restrictions contained in the Articles of association.
Change in membership	The death, retirement or insolvency of a partner can result in the dissolution of the firm unless there is a contract to the contrary.	A company enjoys a perpetual succession. The death or insolvency of a member of the company does not dissolve the company.

Number of members	There must be minimum two people to constitute a partnership. *Section 11* of the Companies Act, 1956 provides that number of partners cannot exceed 10 persons in case of banking business and 20 in other businesses.	The minimum membership is 2 in case of private companies and 7 in case of public companies. There is no limit for maximum membership in case of a public company but a private company cannot have more 50 members.
Property	Property of the firm is the joint property of all the partners.	The company property belongs to the company and not to individual members – separately or jointly.
Audit	Audit is not compulsory	For companies, there is an obligatory audit of the accounts.

PARNTERSHIP AND HINDU UNDIVIDED FAMILY

A Hindu Undivided Family is a family which consists of all people lineally descended from a common ancestor and includes their wives and unmarried daughters. A HUF carries on its traditional business under the management of the *Karta* – the senior most male member of the family. A HUF is governed by Hindu Law and the members of the family are called co-parcerners

Basis of distinction	*Partnership*	*Joint Hindu Family*
Contract	*Section 5* of the Indian Partnership Act, 1932 states that a partnership arises out of a contract A	It exists because of the status. One becomes a member by birth. *Section 5*specifically provides

	partnership comes into existence through an express or implied agreement between the partners.	that the members of a Hindu undivided family carrying on a family business as such or a Burmese Buddhist husband and wife carrying business as such are not partners in such business.
Membership	New members can be admitted into the partnership with the consent of all the members.	No such consent is needed for the addition of a member into the joint Hindu family.
Number of members	There is a minimum and maximum limit on the number of partners.	There is no limit on the number of members.
Restriction on membership	There is no bar on females becoming partners.	Females cannot be members unless they are the wives of the co-parcerners or unmarried daughters.
Minor	A minor cannot become a partner but he can be admitted to the benefits of an already existing partnership	Minors are members from the date of their birth.
Change in membership	Death of a partner dissolves the firm unless agreed otherwise.	Death leaves the business of the HUF unaffected.
Mutual Agency	Mutual agency is important. Here, every partner is an agent of the rest of the partners and his acts bind the firm.	The family members are not mutual agents. The *Karta* has the authority to contract and bind the family; the other coparceners cannot do so.

Liability	Every partner is unlimitedly liable.	Only the *Karta* is liable unlimitedly. Other members are liable only to the extent of share in profits of the family business unless they took part in the act or transaction done by the *Karta*.
Partition.	A partner can file a suit for dissolution and accounts.	A co-parcener has the tight to file a suit for partition.

TEST OF PARTNERSHIP

Whether or not the relationship between two or more people is partnership or not depends on what the true relationship is and not on any mere label attached to that relationship.

Section 6 makes it clear that 'in determining whether a group of persons is or is not a firm, or whether a person is or is not a partner in a firm, regard shall be had to the real relation between the parties, as shown by all relevant facts taken together'.

The existence of a partnership cannot be determined on the basis of expressed intentions. In*Raghunathan vs. Hormusjee* [51 Bom 342], it was held that mere use of the word 'partner' does give rise to a partnership where there is none. The existence of a partnership is determined by the actual or real relationship between the so called partners of the firm as inferred from all relevant facts. It depends upon the intention of the parties as shown by their agreement or conduct which gives rise to an implied agreement or both. Mere common interest does not make a person a partner. In the same manner, sharing finances does not mean two people are partners. In *Cox vs. Hickman* [1860 8 HL Cas 268], it was decided that of all the essentials of a partnership, sharing profits is an important criterion but is not conclusive. The true test of determining the existence of partnership is *mutual agency*. If one partner can bind the other partners and the firm by his actions and is also, in turn, bound by the actions of the other partners, only then it can be said that a partnership exists.

The *Explanations* to *Section 6* provide a list of people who may be interested in the profits of a business but do not become partners just because of their interest in the partnership or business.

Explanation 1 to the Section makes it clear that two or more people who jointly own a property or have common interest in a particular property do not become partners merely by sharing the profits or gross returns that arise from such property.

Example: In a case, two people become co-owners of a house. They rented out the house and shared the rent received every month. This does not constitute a partnership.

Similarly, *Explanation 2* of the Section provides a list of person who they receive a share of the profits of a business or payments contingent upon the profits earned by a business but are not partners in a business.

1. i) A person who has lent money to a partner or firm engaged in business may be offered a share of the profits instead of or in addition of the money lent by him. However, he will not become a partner due to such a share in profits.
1. ii) A servant or agent of a business may be given a portion of the profits of the business either in addition to or in lieu of his regular remuneration. But that does not make him a partner in the business.

Example: A is an assistant in a firm of brokers and he receives a share in the profits over and above his salary. At times, A also signs some letters and documents on behalf of the firm. Nevertheless, A is only an agent of the firm and does not become a partner merely because he received a share in profits. This illustration is similar to the case of *Mc Laren Morrison vs. Verschoyle* [1901 6 CWN 429].

iii) Often, the widow or descendents of a deceased partner receive a share in the profits of the firm as annuity. This does not make the widow or the descendents partners in the firm.

1. iv) A share in the profits may be offered as consideration to a part owner or the previous owner of a business who sold his share or his business along with the goodwill. But such a person thereby does not of itself become a partner in the business.

Example: A is a doctor who sold his medical practice and its goodwill to B. They enter into an agreement under which A will help B by introducing him to his patients. In turn, A will get a share of profits. Here, A and B are not partners. This illustration is similar to the case of *Pratt vs. Strick* [1932 7 Tax Cas. 459]

Thus, *Explanations 1* and *2* set out cases where the element of mutual agency is missing. In partnership, the burden of proving that two or more people are not partners lies on the person who affirms it.

Section 11 lays down that partners in a firm may write an agreement that prescribes the rights and duties of the partners. The partners cannot go beyond the terms and conditions or the boundaries laid down in such an agreement. The agreement may be varied by consent of all the partners, and such consent may be express or may be implied by a course of dealing. The agreement may be in writing or it may be implied by their actions.

RIGHTS OF A PARTNER

Subject to the specific contract between the partners, every partner has the following rights:

a) Every partner has a right to take part in the conduct of the business as per *Section 12 (a)*. The principle is well illustrated by the case of *CRAG vs. FORD (1842) 1 Y C 280*. Even if authority of a partner is restricted by contract, outside party is not likely to be aware of such restriction. In such case, if such partner acts within the apparent authority, the firm will be liable for his acts.

CRAG vs. FORD [1842] 1 Y C 280.

FACTS: Crag and Ford were partners in a firm dealing with cotton. They purchased a certain quantity of cotton. After a month's time, Crag told Ford to sell the same. But Ford did not do so as the prevailing market rates were low and he hoped that they would rise in the coming months. After three months, the rates were still low and Ford finally sold the cotton. Crag sued Ford alleging the delay of two three months caused much greater losses to the firm than those the firm would have suffered if Ford had followed Crag's directions. Crag claimed damages from Ford for these extra losses suffered by the firm.

HELD: The plaintiff's case failed as the judges held that both partners had equal rights and duties in the partnership firm. Crag could have sold the cotton himself; after all, he was also responsible for running the business of the firm. He did not perform hid duties diligently or in time to be able to succeed in the action for damages.

b) Any difference arising as to ordinary matters connected with the business may be decided by a majority of the partners and every partner shall have the right to express his opinion, before the matter is decided, but no changes may be made in the nature of the business without the consent of all the partners. This is provided in *Section 12 (c)*.

But it must be noted that the majority powers cannot be used for flimsy reasons or to injure or harm a co-partner.

BLISSET vs. DANIEL [1853] 90 RR 454

FACTS: Blisset was a partner in a firm where a proposal was mooted to appoint one of the partner's son as a co-manager of the firm. Blisset objected to such an appointment. The partner whose son was nominated complained to the other partners behind Blisset's back and persuaded them to sign and serve a notice of expulsion to him. This was in keeping with a partnership clause that empowered a majority of the partners to expel any partner without citing any reason. Blissett contested the validity of the expulsion.

HELD: The plaintiff's expulsion was set aside. The court held that it was up to the partners and the majority to decide what was good for the firm but the partners are required to act in good faith when making use of such powers.

c) Every partner has a right to have access to and to inspect and copy any of the books of the firm as per *Section 12*

*(d)***.** Even the legal representatives of a partner have this right to access to books, whether the firm has been dissolved or not. However, secret information should not be taken and the documents should not be taken to any other place except for the registered office of the firm. A minor, however, can access only the account books. He is not allowed to access documents dealing with trade secrets or other papers.

e) Every partner is entitled to share equally in profits earned as per *Section 13 (b).* Even a sleeping partner has all the rights and liabilities. Thus, he has a right to profit of the firm.

A partner is not entitled to receive remuneration for participating in the business of the firm as per*Section 13 (a)* of the IPA, 1932. But, if the partnership agreement allows for such remuneration, a partner will be allowed remuneration provided all the partners consent to it.

f) A partner is a joint owner of the property of the firm.

g) A partner has a right to do, in an emergency, all such acts as are reasonably necessary to protect the firm from losses.

h) A partner who made, for the purpose of the business, any payment or advances by and the amount of capital he agreed to subscribe, is entitled to claim interest at the rate of 6 percent per annum as provided under *Section 13(d).* A partner is entitled to interest on the capital subscribed by him, such interest shall be payable only out of profits.

i) A partner has a right to be indemnified for payments he makes or liabilities he incurs in certain scenarios whether in ordinary course of business or in emergency situation. The firm shall indemnify a partner in respect of payments made and liabilities incurred by him in the ordinary course and proper conduct of the business as per *Section13 (e) of the IPA, 1932*. A partner will also be indemnified in doing any act, in an emergency, for the purpose of protecting the firm from losses, as would be done by a person of ordinary prudence, in his own case, under similar circumstance.

j) A partner has a right not to be expelled. But *Section 33(1)* says a partner may be expelled if a power is conferred upon the partners to expel and the power is exercised bona fide by a majority of partners.

k) A partner has a right to resist the introduction of a new partner. *Section 31(1)* says that no new partner can be introduced unless all partners consent thereto.

l) A partner has a right to retire. As per *Section 32(1),* a partner may retire with consent of all other partners; in accordance with an express agreement by the partners or where the partnership is partnership-at-will, a partner may retire by giving notice to all the partners of his intention to retire.

m) A partner has a right to carry on competing business. Though *Section 36(1)* says the business should not use firm's names or clients. Unless restrained by a reasonable agreement, not to carry on business within local limits specified, a partner might set up his business as per *Section 36(1).* A reasonable restriction on an ex-partner doing the same business in the same locality or in same trade as the firm is not in contravention of *Section 27* of the Indian Contract Act, 1872 that talks about 'Restraint of Trade'.

n) A partner has a right as an outgoing partner in certain cases to share subsequent profit. Certain situations are listed in *Section 36.*

DUTIES OF A PARTNER

The general duties of a partner start from the moment of negotiation and continue even after cessation.

a) *Section 9* enlists the general duties of a partner:

i) to carry on the business of the firm to the greatest common advantage.

ii) to be just and faithful to each other.

iii) to render true accounts and full information of all things affecting the firm to any partner or his legal representatives.

These are all based on the principle of good faith or uberrimae fidei.

BENTLEY vs CRAVEN is a classic example of how a partner may not benefit his personal self by the business transaction of a firm.

b) *Section 10* deals with the duty to indemnify the firm for the loss caused to it by his fraud in the conduct of the business of the firm. It tries to impose on the partners a duty to conduct themselves fairly and honesty towards their partners and the persons dealing with the firm.

c) *Section 11 (2)* says that a partner is restricted by an agreement with the other partners; he has a duty not to carry on any business other than that of the firm, where he is a partner.

d) *Sections 12 (b)* and *13(f)* impose a duty on the agent of due diligence and if this rule is violated, liability will be incurred.

e) *Section 12 (b)* says that a partner has to attend diligently to his duties in the conduct of the firm's business without any remuneration.

f) *Section 13 (f)* of the IPA says that a partner has to indemnify the firm for any loss caused to it by his wilful neglect in the conduct of the business of the firm.

g) *Section 15* imposes a duty on the agent to use the property of the firm properly. The property has to be used only for the purposes of the firm. If a partner does not submit an account of his dealings with respect to the firm property, he will be liable for it.

h) *Section 16 (a)* asks a partner to account for any profit, including secret profit derived by the partner from any transaction of the firm, or from the property, or the business connections of the firm or the firm name. *Section 16(b)* says that if a partner carries on any business competing with that of the firm, he shall account for and pay to the firm all the profits made by him in that business.

i) A partner also has the duty not to carry on any business similar to or in competition with the business of the firm as per *Section 16(b)*. A partner should not exploit any information received by him on the course of conducting the firm business or due to his connection with the firm.

j) A partner has the duty not to assign his share or else the partnership will stand dissolved.

k) A partner also has the duty to contribute equally and make good for the losses of the firm unless otherwise agreed.

BENTLEY vs. CRAVEN [1853] 18 BEAV 75

FACTS: Craven was a partner in a firm in the business of sugar. When prices in the market were particularly low, he bought a huge stock of sugar with his own personal money and stored the same in his own godowns. Soon, the firm needed to purchase sugar for its business and entrusted the job to purchase the sugar to Craven. Craven immediately supplied the required quantity of sugar from his own stock at the prevailing market rates. Craven made a good amount of profit and later, the partners of the firm came to know about this. They demanded the difference amount of Craven's cost price and selling price to the firm be paid to the firm. Craven contended that there was no deception and he had used only his personal resources and if he wanted he could have sold the sugar to other people at the same market rate.

HELD: The firm was entitled to an account for the profit made by Craven as well as to be paid the profit Craven earned in the said transaction. This is so because all partners must work for the greatest common good and no partner is entitled to personal profits from the transactions of the firm. Further more, a partner is duty bound to give account of all the things that concern and affect the business of the firm.

TYPES OF PARTNERSHIP

Section 5 states that partnership is not created by status. It makes it clear that relation of partnership can arise out of a contract only.

There must be a minimum two or more people in a partnership. There is no upper limit on the number of members in a partnership under the Act. However, *Section 11* of the Companies Act, 1956 provides that number of partners cannot exceed 10 persons in case of banking business and 20 in others. If the number of members exceeds the limit, the partnership becomes an illegal association. It gets dissolved if the number goes below one. Thus, it follows that if there is a partnership to carry on an illegal business or if the number of partners exceeds the maximum given, then it is an illegal partnership.

The Indian Partnership Act, 1932 gives two specific types of partnerships on the basis of duration:

1) Partnership at will

2) Particular Partnership

1) ***Partnership at will:*** *Section 7* says "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".

The survival of such partnership depends on the willingness of the partners. It can be dissolved at any time by any of the partners by giving a notice to the other partners. The partnership at will dissolves from the date of notice of termination. If a partnership constituted for a particular time period is still carried on after the expiry of the time, it will be presumed that the limitation is no longer applicable.

For example, if two people decide to sell coconut water at two ends on a particular street without having any contract or without specifying when will the partnership come to an end, it is a partnership at will. It will exist only as long as both the parties want the partnership to last.

But if the partnership deed provides of termination only by mutual agreement, a mere notice to the other partners will not dissolve the partnership firm. Also, a partnership at will dissolves immediately upon the death or insanity of a partner.

2) ***Particular Partnership:*** *Section 8* states that "a person may become a partner with another person in particular adventures or undertakings." Such a partnership ends on the completion of the task. A partner cannot retire from such a partnership – half way through the project for which partnership was entered into – without the other partners.

When two people enter into a partnership for a particular construction project, this is particular partnership. A person can still carry on his usual business or work while he in a particular partnership; he is not required to give up his other professional pursuits. For example, partnership between two advocates or doctors for a particular case does not take away their freedom to attend to their other cases. Two auditors engaged in a particular audit might be regarded as partners in that audit.

It does not matter whether the business is of temporary or permanent nature. A single venture can amount to carrying on of business. In the case of *K Jaggaiah vs. Kokumanu* [AIR 1984 AP 149], three people got together and managed a contract for road maintenance. It was a partnership for building roads. The activity of the partnership arose from a single contract but was spread over a particular period and various aspects. The employment of workers,

supervision, getting sanctions and approvals was just a part 'carrying on of business' under *Section 4*.

English Law: There is a concept of a limited partnership. In the case of *Miles vs. Clarke* [1953 1 AER 779], a photographer cum photo studio owner entered into an agreement with a freelance photographer. The agreement was that the freelance photographer would go to marriages and other functions and get the prints from the particular photo studio. The profits earned were shared equally. After a few years, a dispute arose whereby the freelance photographer claimed a partnership with the photo studio and thus, entitlement to the property. It was held to a particular partnership and not a partnership with the photo studio. Thus, the freelance photographer was not entitled to a share in the photo studio.

Section 17 of the act contemplates situations where the partnership has to be continued despite no provisions for it. The Section says that subject to the contract to the contrary:

1. i) The rights and duties of partners after a change in the firm will remain the same as before.
2. ii) The mutual rights and duties of the partners will the same after the expiry of the term of the firm as far as they are consistent with a partnership at will.

iii) The rights and duties of partners are the same as in the original undertakings if the partnership has taken up additional undertakings.

TYPES OF PARTNERS

i) Partner by holding out or Partner by Estoppel.

The rule of agency by Estoppel has been extended to the case of partnership too. Holding out is merely application of the principle of Estoppel which is a rule of evidence wherein a person is prevented or 'estopped' from denying a statement he made or existence of facts that he makes another person believe. Holding out refers to course of action or omission that leads others to believe that one possesses an authority which in fact one does not.

Simply put, if a person represents that he is a partner of a particular firm, he is estopped from denying this representation later on.

Section 28 says that a person is held liable as a partner by holding out if:

a) he represented himself or knowingly allowed himself to be represented as a partner.

b) such representation may be by spoken or written words, by conduct or by knowingly permitting others to make such representation by words or conduct.

c) the other party on the faith of such representation gave credit to the firm.

For example, A and B are partners in a firm. Another person C manages the firm on their behalf; places all the orders, makes the payments due etc. If C places an order, A and B will have to pay for the same as they have allowed C to function as a partner and did not to inform the suppliers or the customers that C was only a manager.

But a person who is aware that C is not a partner can not sue A and B to make good losses incurred by dealing with C.

A partner by holding out is liable to the person giving credit, to make good the loss which any third party may suffer. But he does not acquire any claim over the firm. A person does not become a 'real' partner but he does become liable for compensation to the third party whom he induced as a partner by holding out and caused such man loss or injury. The real partners of the firm are safe unless the partner by holding out has acted on their orders or with their consent.

SCARF vs. JARDINE is an important case for the principle of holding out wherein the importance of notice of retirement was highlighted. A partner must give notice of his retirement from a firm the same way the notice of a new member to the firm is made to the public so that people know about his status or rather the absence of participation of such retiring person in the firm. Otherwise, he might be treated as partner by holding out no matter how long back he retired from the firm without notice.

Thus, the liability of a retired partner to old creditors or customers continues till a notice of his retirement is given. Similarly, the firm will also be liable for the retired partner, should just a situation arise, if the notice has not been give. It is immaterial whether the retiring partner gives the notice or the other partners.

SCARF v. JARDINE 1882 7 APP CAS 345 – 198, 371, 431 435

FACTS: A firm consisted of two partners, Scarf and Rodgers. Scarf retired and Beach joined in his place. The business was carried on as before and no public notice about the change of partners was given to the customers of the firm. Jardine was an old supplier to the firm. He supplied the goods ordered without any idea about the change. He came to know about the change when the firm failed to pay the dues and he was considering a legal action against the firm. He preferred to sue the new firm which subsequently went bankrupt. Then he sued the earlier partner, Scarf.

HELD: He had a right against Scarf provided he had proceeded against the old firm and

partners in the first instance itself. Now he had acknowledged the new firm, he could not reject its identity and sue Scarf. It was held that novation might involve either a change of parties with the contract remaining the same or a change in the contract between the same parties. An implied agreement is presumed from the fact that the creditor, after the knowledge of the change, has brought a suit against the new firm. Jardine knew of the change of the constitution of the firm when he sued and he chose to sue the new firm. Now he could not sue the older firm for the same cause of action as it is against principles of natural justice as well as Partnership Act.

There are exceptions to the rule established in the *SCARF vs. JARDINE* case as given below:

a) Death of a partner constitutes sufficient notice by itself.

b) Insolvency of a partner is also sufficient notice and attracts Section 42 of the Indian Partnership Act.

c) If one has been a dormant or sleeping from beginning to end, notice can be dispensed with as neither the customers nor the clients know of his participation in the firm.

In English law, Partnership by holding out is referred to as apparent partnership instead and the legal provisions in both countries are very similar.

In *SMITH vs. BAILEY 2 QB 432*, it was decided that the liability on the principle of Estoppel extends only on account of credit given to the firm and not to torts or civil wrongs committed on behalf of the firm.

ii) Dormant or Sleeping Partner

A dormant partner does not take active part in the business, but he is liable like any other partner. Likened to an undisclosed principal, the moment he is discovered to be a partner, he can be made liable. He is not required to give notice in order to absolve himself from the liability for the acts of other partners after he ceases to be a partner.

iii) Nominal Partner

A nominal partner is a partner only in name. He is not entitled to share the profits of the firm but is liable for all the acts of the firm as if he was a real partner.

iv) Sub Partner.

He comes into existence when one of the partners agrees to share the profits derived by him from the firm with a stranger. He is not a partner in law and has no rights against the firm and is not liable for the debts of the firm.

v) Working Partner

A partner, due to his special qualifications, may be assigned the management and control of the business. He normally receives a fixed amount of salary, besides his share in the profits. For all his acts, the other partners will be liable to third parties.

vi) Incoming Partner

He is a person who is admitted as a partner in an already existing firm with the consent of all the existing partners as under Section 31. He is not liable for any act done by the firm before his admission. Where he specifically agrees to bear the past liabilities, he will be liable to the other partners for the same. But third parties cannot hold him liable as there is no privity of contract between the new partner and the creditors.

vii) Outgoing or retiring Partner

A partner who leaves a firm in which the rest of the partners continue to carry on the business is an outgoing partner. A partner can retire by the consent of all the partners *(Section 31)***,** by agreement between the partners *(Section 3)* and by notice as per *Section 32*, by death *(Section 35)*, insolvency*(Section 34)* or by expulsion under *Section 33.*

He has to retire as per *Section 36(1).* He is liable to the third parties for all the acts of the firm until public notice is given about the retirement. Such notice can be given by the outgoing partner himself or by any member of the new firm. He does not cease to be liable for debts and obligations of the firm incurred before his retirement. He is also liable to a third party for transactions of the firm begun but unfinished at the time of his retirement. However, *Section 36* also acknowledges a retiring partner's right to compete as long as he:

a) does not use the name of the firm for the firm from which he has retired.
b) does not represent that he is working for the firm from which he has retired.
c) does not solicit the clients of the firm from which he has retired.

He may be discharged from any liability to any third party for the acts of the firm done before his retirement if it is so agreed with the third party and the partners of the reconstituted firm. Such

agreement may be implied from the course of dealing between the firm and the third party after he had knowledge of the retirement.

Section 33 further provides that though a partner may retire, he cannot be expelled unless such a power is conferred by the contract between partners and exercised in good faith. Grounds of expulsion in the contract can include, committing a criminal act, becoming insolvent, not investing the required share in the firm or causing loss to the firm die to grossly negligent act. A retiring partner is also entitled to a share in the subsequent profits if his account has not been finally settled as per *Section 30* of the IPA. In case of death, his legal representatives have a right to the same.

Section 38 says that the continuing guarantee by the outgoing partner given to the firm or a third party can be revoked with respect to future transactions in the absence of a contract to the contrary.

viii) Minor as a partner

Partnership arises of a contract and minors are deemed incompetent to contract as per *Section 11* of the Indian contract Act, 1872. Thus, a person domiciled in India under the age of 18 years or 21 years if covered under Guardianship Act, can not enter into a partnership. In *Mohribibee vs. Dharmodas Ghose [1903] ILR 30 CAL 539*, it was held that a minor cannot enter into a contract and minor's contract is void.

However, if all the partners agree, a minor may be admitted to the benefits of an already existing firm. There can be no partnership firm with just one adult and all other partners being minor.

A minor does not become a full fledged partner. He is not personally liable; only his share in the partnership is. As per *Section 30*, he

a) has a right to such share of the property and of the profits of the firm as may be agreed upon by the partners.

b) may have access to and inspect and copy any of the accounts of the firm. Since the word used is 'may', it seems that right of minor to inspect accounts can be restricted by agreement among partners. Trade secrets of the firm are, however, not accessible to a minor.

c) has a share in the property and profits of the firm and therefore, these are liable to the acts of the firm but the minor is not personally liable and neither is his private property liable.

d) has no right to file a suit against the other partners for accounts or for payments of his share in the profits or property of the firm while he continues to be a member. He can do so only when he has or is the process of severing the connection with the firm.

e) may file a suit for severing his connections with firm and his share will be determined by the valuation according to the principles laid down in *Section 48* for making accounts of a dissolved firm. This severance can be effected by a guardian on behalf of the minor. If the firm dissolves, the share of the minor will determined along with the share of the other partners.

f) can at any time within 6 months of attaining majority or of him obtaining the knowledge that he has been admitted (whichever is later) give a public notice that he has or he has not elected to become a member of the partnership. This proceeds on the presumption that a minor may not actually know that he has been admitted to the benefits of a partnership and gives him the right to elect whether he wants to be a partner or not. Failure to give notice within 6 months will give rise to the presumption that he is a partner in the firm.

During the six months, the position of the minor remains the same i.e., a minor admitted to the benefits of the partnership but without any personal liability.

g) may have his share in the firm attached for the acts of the firm.

h) may be liable for holding himself out as a partner despite the fact he elected not to be a partner after attaining majority.

i) During minority, the privilege of minority or infancy can be used only as a shield and therefore, a minor is liable under tort.

j) If a minor does decide to become a partner after attaining majority, he will become personally liable to third parties for all acts of the firm done from since he was first admitted to the benefits of partnership. The share in property and profits he was entitled to as a minor will continue when he has elected to be a partner.

k) If a minor decides not to be a partner, his rights and liabilities (as those of a minor in benefits of partnership) will continue till the date of his public notice of his decision. His share will not be liable for any act of the firm after the date of the notice and he can sue for his share in the property and profits.

If he elects to be a partner or if he fails to give a public notice that he does not elect to be a partner, he will be liable for the debts of the firm contracted since the time he was admitted to the benefits of the partnership.

The Indian Partnership Act

Elements of a Partnership

A partnership as we know is an agreement between two or more persons to run a business together and share the profits they earn from this business. Now according to the Indian Partnership Act 1932, there is five important and necessary elements of a partnership. Let us learn about them.

Elements of a Partnership

The Indian Partnership Act 1932 defines a partnership as a relation between two or more persons who agree to share the profits of a business run by them all or by one or more persons acting for them all. As we go through the Act we will come across five essential elements that every partnership must contain. Let us take a look at them.

1] Contract for Partnership

A partnership is contractual in nature. As the definition states a partnership is an association of two or more persons. So a partnership results from a contract or an agreement between two or more persons. A partnership does not arise from the operation of law. Neither can it be inherited. It has to be a voluntary agreement between partners.

A partnership agreement can be written or oral. Sometimes such an agreement is even implied by the continued actions and mutual understanding of the partners.

2] Association of Two or More Persons

A partnership is an association between two or more persons. And persons by law only includes individuals, not other firms. The law also prohibits minors from being partners. But minors can be admitted to the benefits of a partnership.

The Act is actually silent on the maximum number of partners. But this has been covered under the Companies Act 2013. So a partnership can only have a maximum of 10 partners in a banking firm and 20 partners in all other kinds of firms.

3] Carrying on of Business

There are two aspects of this element. Firstly the firm must be carrying on some business. Here the business will include any trade, profession or occupation. Only that some business must exist and the partners must participate in the running of such business.

Also, the business must be run on a profit motive. The ultimate aim of the business should be to make gains, which are then distributed among the partners. So a firm carrying on charitable work will not be a partnership. If there is no intention to earn profits, there is no partnership.

4] Profit Sharing

The sharing of profits is one of the essential elements of a partnership. The profit sharing ratio or the manner of sharing profits is not important. But one partner cannot be entitled to the entire profits of the firm.

However, the sharing of losses is not of any essence. It is up to the partners whether the losses will be shared by all the partners. If nothing is said then the losses are also split in the profit sharing ratio.

Say for example two individuals are operating out of the same warehouse. So they agree to divide the rent amongst themselves. This is not a partnership since there is no profit sharing between the two.

5] Mutual Agency

The definition states that the business must be carried out by the partners, or any partner/s acting for all of them. This is a contract of mutual agency another one of the five elements of a partnership. This means that every partner is both a principle as well as an agent for all the other partners of the firm. An act done by any of the partners is binding on all the other partners and the firm as well. And so every partner is bound by the acts of all the other partners. This is one of the most important aspects of a partnership. It is, in fact, the truest test of a partnership.

Kinds of Partnership

A partnership between two people is when they run a business together with the intention of sharing the profits amongst themselves. However, there can be various types of partnerships according to their duration or the intent of their creation. Let us take a look at the kinds of partnerships like a general partnership, partnership at will etc.

Kinds of Partnership

The distinction between partnerships can be done on the basis of two criteria. They are as follows

1. With Regard to the Duration of the partnership – either Partnership at Will or Partnership for Fixed Duration
2. With regards to the extent of the business carried by the partnership – either General Partnership or Particular Partnership

So let us take a look at these kinds of partnership in some detail.

1] Partnership at Will

When forming a partnership if there is no clause about the expiration of such a partnership, we call it a partnership at will. According to Section 7 of the Indian Partnership Act 1932, there are two conditions to be fulfilled for a partnership to be a partnership at will. These are

- There is no agreement about a fixed period for the existence of a partnership.
- No provision with regards to the determination of a partnership

So if there is an agreement between the partners about the duration or the determination of the firm, this will not be a partnership at will. But if a partnership was entered into a fixed term and continues to operate beyond this term it will become a partnership at will from the expiration of this term.

2] Partnership for a Fixed Term

Now during the creation of a partnership, the partners may agree on the duration of this arrangement. This would mean the partnership was created for a fixed duration of time.

Hence such a partnership will not be a partnership at will, it will be a partnership for a fixed term. After the expiration of such a duration, the partnership shall also end.

However, there may be cases when the partners continue their business even after the expiration of the duration. They continue to share profits and there is an element of mutual agency. Then in such a case, the partnership will now be a partnership at will.

3] Particular Partnership

A partnership can be formed for carrying on continuous business, or it can be formed for one particular venture or undertaking. If the partnership is formed only to carry out one business venture or to complete one undertaking such a partnership is known as a particular partnership.

After the completion of the said venture or activity, the partnership will be dissolved. However, the partners can come to an agreement to continue the said partnership. But in the absence of this, the partnership ends when the task is complete.

4] General Partnership

When the purpose for the formation of the partnership is to carry out the business, in general, it is said to be a general partnership.

Unlike a particular partnership in a general partnership the scope of the business to be carried out is not defined. So all the partners will be liable for all the actions of the partnership.

Types of Partners

A partnership is when two or more people work together and share the profits from the business or profession. However, one must not always assume that all partners participate in the work or profits or even liabilities of the firm equally. In fact, there are various types of partners based on the extent of their liability, or their participation in the firm – like an active partner or dormant partner etc. Let us take a look.

Types of Partners

Here we will look at six types of partners we come across on a regular basis. This list is not exhaustive, the Partnership Act does not restrict any unique kind of partnership that the partners want to define for themselves. Let us take a look at some of the important types of partners.

1] Active Partner/Managing Partner

An active partner is also known as Ostensible Partner. As the name suggests he takes active participation in the firm and the running of the business. He carries on the daily business on behalf of all the partners. This means he acts as an agent of all the other partners on a day to day basis and with regards to all ordinary business of thefirm.

Hence when an active partner wishes to retire from the firm he must give a public notice about the same. This will absolve him of the acts done by other partners after his retirement. Unless he gives a public notice he will be liable for all acts even after his retirement.

2] Dormant/Sleeping Partner

This is a partner that does not participate in the daily functioning of the partnership firm, i.e. he does not take an active part in the daily activities of the firm. He is however bound by the action of all the other partners.

He will continue to share the profits and losses of the firm and even bring in his share of capital like any other partner. If such a dormant partner retires he need not give a public notice of the same.

3] Nominal Partner

This is a partner that does not have any real or significant interest in the partnership. So, in essence, he is only lending his name to the partnership. He will not make any capital contributions to the

firm, and so he will not have a share in the profits either. But the nominal partner will be liable to outsiders and third parties for acts done by any other partners.

4] Partner by Estoppel

If a person holds out to another that he is a partner of the firm, either by his words, actions or conduct then such a partner cannot deny that he is not a partner. This basically means that even though such a person is not a partner he has represented himself as such, and so he becomes partner by estoppel or partner by holding out.

5] Partner in Profits Only

This partner will only share the profits of the firm, he will not be liable for any liabilities. Even when dealing with third parties he will be liable for all acts of profit only, he will share none of the liabilities.

6] Minor Partner

A minor cannot be a partner of a firm according to the Contract Act. However, a partner can be admitted to the benefits of a partnership if all partner gives their consent for the same. He will share profits of the firm but his liability for the losses will be limited to his share in the firm.

Such a minor partner on attaining majority (becoming 18 years of age) has six months to decide if he wishes to become a partner of the firm. He must then declare his decision via a public notice. So whether he continues as a partner or decides to retire, in both cases he will have to issue a public notice.

Relation of Partners with One Another

All partners are free to form their own terms and conditions with respect to functioning in their partnership deed. The Indian Partnership Act, 1932 has also prescribed provisions to govern their relationship *inter se* (amongst them), and these provisions are applicable if no such deed exists. Let us take a look at the duties and the rights of partners.

Right to Determine Relationship

Partners can determine their mutual rights and duties by a contract called partnership deed, which determines aspects of general administration, such as which partner will do what work, what will be their share in profits, etc. It may be varied by express or implied consent of all the partners.

Such deed can be expressly made or implied by a course of dealing. For example, if one partner checks accounts of the firm daily and others do not object, his conduct will be presumed to be a

right of all partners in the absence of a written partnership deed between them. So they can themselves determine the rights of partners.

Agreement in Restraint of Trade is Valid

Section 27 of the Indian Contracts Act, 1872 declares contracts in restraint of trade as void. All agreements restraining exercise of a lawful profession, trade or business are invalid.

Section 11 of Partnership Act, however, states that partners can validly levy such a restraint on each other, but such restraint must be provided for under the partnership deed. Partners can use this agreement to prohibit each other from carrying on any business other than that of the firm.

Rights of Partners *Inter Se*

Partners can exercise the following rights under the Act unless the partnership deed states otherwise:

1. **Right to participate in business:** Each partner has an equal right to take part in the conduct of their business. Partners can curtail this right to allow only some of them to contribute to the functioning of the business if the partnership deed states so.
2. **Right to express opinions:** Another one of the rights of partners is their right to freely express their opinion. Partners, by a majority, can determine differences with respect to ordinary matters connected with the business. Each partner can express his opinion to decide such matters.
3. **Right to access books and accounts:** Each partner can inspect and copy books of accounts of the business. This right is applicable equally to active and dormant partners.
4. **Right to share profits:** Partners generally describe in their deed the proportion in which they will share profits of the firm. However, they have to share all the profits of the firm equally if they have not agreed on a fixed profit sharing ratio.
5. **Right to be indemnified:** Partners can make some payments and incur liabilities through their decisions in the course of their business. They can claim indemnity from each other for these decisions. Such decisions must be taken in situations of emergency and should be of such nature that an ordinarily prudent person would resort to under similar conditions.
6. **Right to interest on capital and advances:** Partners generally do not get an interest on the capital they contribute. In case they decide to take an interest, such payment must be made only out of profits. They can, however, receive interest of 6% p.a. for other advances made subsequently towards the business.

Duties of Partners *inter se*

Now that we have seen the rights of partners let us see the duties the Act has prescribed,

1. **General duties:** Every partner has the following general duties like carrying on the business to the greatest common good, duty to be just and faithful towards each other, rendering true accounts, and providing full information of all things affecting the firm. etc
2. **Duty to indemnify for fraud:** Every partner has to indemnify the firm for losses caused to it by his fraud in the conduct of business. The Act has adopted this principle because the firm is liable for wrongful acts of partners. Any partner who commits fraud must indemnify other partners for his actions.
3. **Duty to act diligently:** Every partner must attend to his duties towards the firm as diligently as possible because his not functioning diligently affects other partners as well. He is liable to indemnify others if his willful neglect causes losses to the firm.
4. **Duty to use the firm's property properly:** Partners can use the firm's property exclusively for its business, and not for any personal purpose, because they all own it collectively. Hence, they must be careful while using these properties.
5. **Duty to not earn personal profits or to compete:** Each partner must function according to commonly shared goals. They should not make any personal profit and must not engage in any competing business venture. They should hand over personal profits made to their firm.

Effect on Rights and Duties after a change in Firm

The nature of the existing relationship between partners will be affected whenever there is a change in the firm's constitution. Such changes occur in the following situations:

1. Change in constitution of the firm due to incoming or outgoing or partner(s);
2. Expiry of the pre-determined term of the firm; and
3. Carrying out of additional business undertakings than originally agreed upon.

Mutual rights and duties of the partners will continue to be the same as they existed prior to such changes, but partners can change this by making a fresh partnership deed.

Relation of Partners to Third Parties

In this article, we will look at the various rules that govern the relation of partners in a firm to a third party. Sections 18 to 22 of the Indian Partnership Act, 1932, offer details of different scenarios under which partners can have different relations with a third party.

A Partner is an Agent of the Firm (Section 18)

A partnership is a relationship between partners who agree to share the profits of the business. The business can be carried on by all of them or any of them acting for all. This definition suggests that a partner can be an agent of the others.

Section 18 specifies that a partner is an agent of the firm for the purpose of businessof the firm. This is actually one of the essential elements of a partnership.

Hence, a partner embraces the character of both, the principal and the agent. Therefore, if he acts for himself and in his own interest in the common concern of the partnership, then he is acting as a principal. On the other hand, if he acts for and in the interest of his partners, then he is acting as an agent.

It is important to note that a partner is an agent only or the purpose of business of the firm. He is not an agent for all transactions and dealings between the partners themselves.

Implied Authority of a Partner (Section 19)

If a partner does an act in the usual course of business of the firm, then his act binds the firm.

This authority of a partner to bind the firm is Implied Authority. Unless a contrary agreement exists, implied authority does not empower a partner to (Section 19 – subsection 2 of the Indian Partnership Act, 1932):

- Submit a dispute, relating to the business of the firm, to arbitration
- Open a bank account in his name, on behalf of the firm
- Compromise or relinquish, full or part of a claim by the firm
- Withdraw a suit or proceedings filed on behalf of the firm
- Admit any liability in a suit or proceedings against the firm
- Acquire an immovable property on behalf of the firm
- Transfer an immovable property belonging to the firm
- Enter into a partnership on behalf of the firm

Section 22 of the Indian Partnership Act, 1932, adds that the act which was done by the partner to bind the firm must be done in the name of the firm or in any other manner which implies an intention to bind the firm.

While the implied authority depends on the nature of the business of the firm, a partnership of a general commercial nature may allow the partner to:

- Pledge or sell the partnership property

- Purchase goods on behalf of the partnership
- Borrow money, contract and pay debts on account of the partnership
- Draw, make, sign, endorse, transfer, negotiate and procure negotiable papers in the name and on account of the partnership.

According to Section 20 of the Indian Partnership Act, 1932, the partners of a firm can make a contract to extend or restrict the implied authority of a partner.

These restrictions or extensions apply to a third party only when the third party is aware of the restrictions or does not know that he is dealing with a partner of the firm.

Partner's Authority in an Emergency (Section 21)

As per Section 21 of the Indian Partnership Act, 1932, if there is an emergency, then every partner has the authority to do all such acts that a person of ordinary prudence would do to protect the firm from a loss. Such acts bind the firm.

Minors Admitted to Benefits of Partnership

As we have seen in the Contract Act, minors cannot be a party to a contract. A contract involving a minor is void-ab-initio. However, the Partnership Act has its own sets of legal rules regarding minors. So let us study about minor partner and the benefits they gain from a partnership.

Minors Admitted to Benefits of Partnership

Section 30 of the Indian Partnership Act 1932 contains legal provisions about a minor in a partnership. Now we know the Indian Contract Act 1857 clearly states that no person less than the age of 18, i.e. a minor can be a party to a contract. And a partnership is a contract between the partners. Hence a minor cannot be a partner in a partnership firm.

However, according to the Partnership Act, a minor may be admitted to the benefits of a partnership. So while the minor will not be a partner he will enjoy all the benefits of a partnership. To admit all the minor to the benefits of the partnership all of the partners of the firm must be in agreement.

Rights of a Minor Partner

Once the minor is given the benefits in a partnership there are certain rights that he enjoys. Let us take a look at the rights of a minor partner.

i. A minor partner will obviously have the right to his share of the profits of the firm. But the minor partner is not liable for any losses beyond his interests in the firm. So a minor partner's personal assets cannot be liquidated to pay the firms liabilities.
ii. He can also like any other partner inspect the books of accounts of the firm. He can demand a copy of the books as well.
iii. If necessary he can sue any or all of the other partners for his share of the profits or benefits.
iv. A minor partner on attaining majority has the right to become a partner of the firm. He has six months from attaining majority to decide if he will execute this right. Whether he decides to become a partner or not he must give public notice about the same.

Liabilities of a Minor Partner

i. A minor cannot be held personally liable for the losses of the firm. And if the firm declares insolvency the minor's share is kept with the Official Receiver
ii. After turning 18 the minor partner can choose to become a partner of the firm. But he may choose to not become a partner. In this case, the minor partner has to give a public notice about this decision. And the notice has to be given within 6 months of gaining a majority. If such a notice is not given even after 6 months then the minor partner will become liable for all acts done by the other partners till the date of such notice.
iii. Should the minor partner choose to become a partner he will be liable to all the third parties for the acts done by any and all partners since he was admitted to the benefits of the partnership.
iv. If he becomes a full-time partner he will be treated as a normal partner and have all the liabilities of one. His share in the profits and property of the firm will remain the same as it was when he was a minor partner.

Partnership Property

Section 14 of the Indian Partnership Act, 1932, details the law surrounding the property of the firm or partnership property. Further, section 15 explains the various applications of such property. In this article, we will endeavor to understand partnership property and its applications.

Partnership Property (Section 14)

The property of a firm is also known as partnership property, partnership assets,joint stock, common stock, or joint estate. A partnership property includes all property and rights, and interest in property that the partnership firm purchases.

These purchases can also be made for the purpose and in course of the business of the firm, including the goodwill of the firm. All partners collectively own such properties.

Hence, a partnership property comprises of the following items if there is no agreement between the partners showing any contrary intention:

- All property and rights and interest in property that the partners purchase in the common stock as their contribution to the common business.
- All property and rights and interest in property that the firm purchases either for the firm or for the purpose and in course of the business of the firm.
- Goodwill of the business.

Determining whether a particular property is partnership property depends on the true intention or agreement between the partners.

Hence, if a firm uses the property of a partner for its purposes, it does not make it a partnership property unless that was the real intention. At any time, the partners may agree to convert the property of a partner or partners into partnership property.

If such a conversion is made in good faith, then it would be effectual between the partners and against the creditors of the firm. The partners may also agree to convert the separate property of any partners into the property of the firm.

Goodwill

Section 14 specifies that the goodwill of a business is the property of the firm and is subject to a contract between the partners. However, it does not define the termgoodwill.

Goodwill is the value of the reputation of a business in respect of the expected futureprofits OVER AND ABOVE the profits that a firm earns in the same class of business. It is a part of partnership property. The firm can sell the goodwill separately or along with other properties.

When a partnership firm dissolves, all partners have a right to have the goodwill sold for the benefit of all the partners unless there is an agreement contrary to the same. After the firm sells the goodwill, any partner may make an agreement with the buyer to not carry on any business similar to that of the firm within a certain time-period or local limits. Such an agreement is notwithstanding anything contained in Section 27 of the Indian Contract Act, 1872 and is valid if the restrictions are reasonable.

Application of Partnership Property (Section 15)

According to section 15, the partnership property should be held and used exclusively for the purpose of the firm. While all partners have a community of interest in the property, during the subsistence of the partnership no partner has a proprietary interest in the assets of the firm.
Each partner has a right to his share in the profits of the firm until the firm subsists. He also has a right to see that the application and use of the assets of the firm are for the purpose of the business of the partnership.

Rights of Outgoing Partner

A partner who leaves the partnership firm in which the remaining partners continue the business is an outgoing partner. Such a partner has certain liabilities and rights as prescribed by the Partnership Law. In this article, we will focus on the rights of an outgoing partner.

Right of an Outgoing Partner to Carry on a Competing Business

Section 36 (1) of the Indian Partnership Act, 1932 (Partnership law), imposes certain restrictions but allows an outgoing partner to carry on a business andadvertise it, which competes with the partnership firm. However, it restricts him from:

- Using the name of the partnership firm
- Representing himself as a partner of the firm
- Soliciting the custom of persons who were dealing with the firm before he ceased to be a partner.

Section 36 (2) talks about an agreement in restraint of trade. According to this subsection, an outgoing partner may make an agreement with his partners that when he ceases to be a partner of the firm, he will not carry on any business similar to that of the firm within a specified period or local limits. This is notwithstanding anything contained in Section 27 of the Indian Contract Act, 1872.

Right of an Outgoing Partner to Share Subsequent Profits

According to Section 37, of the Partnership Law, if a member of the firm dies or otherwise ceases to be a partner of the firm, and the remaining partners carry on the business without any final settlement of accounts between them and the outgoing partner, then the outgoing partner or his estate is entitled to share of the profits made by the firm since he ceased to be a partner.

The share may be attributable to the use of his share of the property of the firm or the interest at six percent per annum on the amount of his share in the property.

The surviving partners also have an option of purchasing the interest of the deceased or outgoing partner. If the surviving partners choose to purchase the interest, then the outgoing partner is not entitled to any further share in profits of the firm.

Legal Consequences of Admission or Retirement of a Partner

Whenever there is an admission of a new partner or retirement of a partner, or expulsion or insolvency of a partner, etc., the partnership firm undergoesreconstitution. Sections 31 to 35 of the Indian Partnership Act, 1932 help us understand the legal consequences of a partner coming in or going out. Let us take a look.

Admission or Introduction of a Partner (Section 31)

According to this section, the consent of all the existing partners is necessary before introducing a new partner into a partnership firm. This is subject to the provisions of Section 30 regarding minors in the firm. Further, the new partner has no liability for any actions of the firm done before his admission.

Rights and Liabilities of a New Partner

All liabilities of a new partner commence from the date of his admission as a partner in the firm. This is unless he accepts liability for the obligations incurred by the firm before his admission.

So, after the admission of a new partner, the new firm may agree to assume liability for the debts of the old firm and the creditors may accept the new firm as their debtor, discharging the old firm. It is important to note that the creditor's consent is important to make the transaction operative.

In a contract, the technical term for substituted liability is Novation. Hence, a mere agreement amongst the partners cannot operate as Novation unless the creditors provide their consent.

The retirement of a Partner (Section 32)

A partner retires when he ceases to be a member of the firm without ending the subsisting relations between the other members of the firm or between the firm and other parties. If a partner withdraws from a firm by dissolving it, then it is a dissolution and not retirement of a partner. The retirement of a partner from a firm does not dissolve it.

In a partnership, a partner may retire:

- With the consent of all the partners,
- In accordance with an express agreement by the partners, or

- The partnership is at will, by giving notice in writing to all the other partners of his intention to retire

Liabilities of an Outgoing Partner

A retired partner continues to be liable to the third party for acts of the firm till such time that he or other members of the firm give a public notice of his retirement. However, if the third party deals with the firm without knowing that he was a partner in the firm, then he will not be liable to the third party.

The retired partner, however, continues to be liable for acts of the firm done before such retirement of a partner. This liability holds good unless there is an agreement between him, the concerned third party, and partners of the reconstituted firm. Such an agreement can also be implied by the course of dealings between the third party and the reconstituted firm post announcement of the retirement of a partner.

If the partnership is at will, then it can relieve a partner without giving a public notice. To do so, the partnership needs to give a written notice to all the partners of his intention to retire.

Expulsion of a Partner (Section 33)

A partnership firm can expel a partner provided:

- The power of expulsion exists in the contract between the partners
- Majority of the partners exercise the power
- The power is used in good faith

If these conditions are not met, then the expulsion is not bona fide in the interest of the business.

The test of good faith includes three aspects:

1. The expulsion should be in the interest of the partnership.
2. Before expelling a partner the firm serves a notice to him.
3. The partner being expelled is given an opportunity to state his version of events leading up to the expulsion.

If these aspects are not met, then the expulsion is not considered to be made in good faith and is null and void. It is important to note that the expulsion of partners does not necessarily result in the dissolution of the firm.

Insolvency of a Partner (Section 34)

When a partner of a firm is adjudicated as insolvent –

- He ceases to be a partner of the firm from the date of the adjudication

- Whether or not the firm subsequently dissolves
- His estate, which vests in the official assignee, ceases to be liable for any act of the firm from the said date
- The firm ceases to be liable for any act of such a partner.

Liability of Estate of a Deceased Partner (Section 35)

Usually, the death of a partner results in the dissolution of the partnership. However, if the partner's contract to not dissolve the partnership post the death of any partner, then the surviving partner continue the business of the firm after absolving the deceased partner's estate from any liability of the future obligations of the firm.

Further, it is not necessary for the firm to give a public notice or inform the persons dealing with the firm about the death of the partner.

An exception is a partnership consisting of only two partners. In such cases, the death of a partner results in the dissolution of the partnership.

Consequences of Non-Registration of Firm

While the English Law makes registration of firms compulsory and levies a fine for non-registration, the Indian Partnership Act, 1932 has no such compulsions for firm registration and no fines for non-registration either. However, under Section 69 of the Act, certain disabilities are imposed on non-registered firms. These disabilities have a persuasive pressure on firms for registration. In this article, we will discuss these aspects in detail.

Consequences of Non Registration of Firm

Section 69 of the Indian Partnership Act, 1932 offers a detailed explanation of the consequences of not opting for firm registration. These are:

1] No suit in a civil court by the firm or other co-partners against any third party

If the firm registration is not done, then the firm or any other person on its behalf cannot file a suit against a third party for breach of contract which the firm has entered into. Further, the person filing the suit on behalf of the firm should be in the register of the firm as a partner.

2] No relief to partners for set-off of claim

Without firm registration, any action brought against the firm by a third party having a value of more than Rs. 100 cannot be set-off by the firm or any of its partners. Pursuance of other proceedings to enforce rights arising from the contract cannot be done either.

3] An aggrieved partner cannot bring legal action against other partner or the firm

A partner of the firm or any person on his behalf cannot bring legal action against the firm or against any partner (or alleged to be a partner) if firm registration is not done. However, if the firm is dissolved, then such a person can sue the firm for dissolution it accounts and realization of his share in the firm's property.

4] A third party can sue the firm

Even if the firm registration is not done a third party can bring legal action against the firm.

It is also, important to note that despite these disabilities, the non-registration of a firm does not affect the following rights:

1. The right of a third party to sue the firm or any partner
2. Partners' right to sue the firm for dissolution or settlement of accounts (in case of dissolution)
3. The power of the Official Assignees, Receiver of Court to release the property of the insolvent partner and bring an action
4. The right of the firm and partners to sue or claim set-off of the value of the suit does not exceed Rs. 100.

Dissolution of a Firm

When the partnership between all the partners of a firm is dissolved, then it is called dissolution of a firm. It is important to note that the relationship between all partners should be dissolved for the firm to be dissolved. Let us look at the legal provisions for the dissolution of a firm.

Modes of Dissolution of a Firm

A firm can be dissolved either voluntarily or by an order from the Court.

Voluntary Dissolution of a Firm (without the order of the Court)

Voluntary dissolution can be of four types. Let us take a look.

1] By Agreement (Section 40)

According to Section 40 of the Indian Partnership Act, 1932, partners can dissolve the partnership by agreement and with the consent of all partners. Partners can also dissolve the partnership based on a contract that has already been made.

2] Compulsory Dissolution (Section 41)

An event can make it unlawful for the firm to carry on its business. In such cases, it is compulsory for the firm to dissolve. However, if a firm carries on more than one undertakings and one of them

becomes illegal, then it is not compulsory for the firm to dissolve. It can continue carrying out the legal undertakings. Section 41 of the Indian Partnership Act, 1932, specifies this type of voluntary dissolution.

3] On the happening of certain contingencies (Section 42)

According to Section 42 of the Indian Partnership Act, 1932, the happening of any of the following contingencies can lead to the dissolution of the firm:

- Some firms are constituted for a fixed term. Such firms will dissolve on the expiry of that term.
- Some firms are constituted to carry out one or more undertaking. Such firms are dissolved when the undertaking is completed.
- Death of a partner.
- Insolvent partner.

4] By notice of partnership at will (Section 43)

According to Section 43 of the Indian Partnership Act, 1932, if the partnership is at will, then any partner can give notice in writing to all other partners informing them about his intention to dissolve the firm.

In such cases, the firm is dissolved on the date mentioned in the notice. If no date is mentioned, then the date of dissolution of the firm is the date of communication of the notice.

Dissolution of a Firm by the Court

According to Section 44 of the Indian Partnership Act, 1932, the Court may dissolve a firm on the suit of a partner on any of the following grounds:

1] Insanity/Unsound mind

If an active partner becomes insane or of an unsound mind, and other partners or the next friend files a suit in the court, then the court may dissolve the firm. Two things to remember here:

- The partner is not a sleeping partner
- The sickness is not temporary

2] Permanent Incapacity

If a partner becomes permanently incapable of performing his duties as a partner, and other partners file a suit in the court, then the court may dissolve the firm. Also, the incapacity may arise from a physical disability, illness, etc.

3] Misconduct

When a partner is guilty of conduct which is likely to affect prejudicially the carrying on of the business, and the other partners file a suit in the court, then the court may dissolve the firm. Further, it is not important that the misconduct is related to the conduct of the business. The court looks at the effect of the misconduct on the business along with the nature of the business.

4] Persistent Breach of the Agreement

A partner may willfully or persistently commit a breach of the agreement relating to

- the management of the affairs of the firm, or
- a reasonable conduct of its business, or
- conduct himself in matters relating to business that is not reasonably practicable for other partners to carry on the business in partnership with him.

In such cases, the other partners may file a suit against him in the court and the court may order to dissolve the firm. The following acts fall in the category of breach of agreement:

1. Embezzlement
2. Keeping erroneous accounts
3. Holding more cash than allowed
4. Refusal to show accounts despite repeated requests, etc.

5] Transfer of Interest

A partner may transfer all his interest in the firm to a third party or allow the court to charge or sell his share in the recovery of arrears of land revenue. Now, if the other partners file a suit against him in the court, then the court may dissolve the firm.

6] Continuous/Perpetual losses

If a firm is running under losses and the court believes that the business of the firm cannot be carried on without a loss in the future too, then it may dissolve the firm.

7] Just and equitable grounds

The court may find other just and equitable grounds for the dissolution of the firm. Some such grounds are:

- Deadlock in management
- Partners not being in talking terms with each other
- Loss of substratum (the foundation of the business)
- Gambling by a partner on the stock exchange.

Difference between Dissolution of a firm and Dissolution of a Partnership

Parameters	Dissolution of a Firm	Dissolution of a Partnership
Continuation of business	The business discontinues.	The business continues. However, the partnership is reconstituted.
Winding up	The firm is wound up. Assets are realized and liabilities are settled.	Assets and liabilities of the firm are only revalued.
Court order	A Court Order can dissolve a firm.	A Court Order cannot dissolve a partnership.
Scope	It involves the dissolution ofpartnership between all partners.	It does not involve the dissolution of the firm.
Final closure of books	Yes	No

Consequences of Dissolution of a Firm

After the dissolution of firm, the partners have certain rights and liabilities. Sections 45 to 55 of the Indian Partnership Act, 1932, provides details on the consequences of the dissolution of a firm. In this article, we will look at these sections in detail.

Liability for Acts done by Partners after the Dissolution of Firm (Section 45)

According to this section, the partners of a firm are liable to a third party for any act done by any of them unless they give a public notice of the dissolution. This notice can be given by any partner. It also specifies that the estate of a partner who dies, retires from the firm, becomes insolvent, or that

of a person who the third party is not aware of being a partner of the firm, is not liable under this section (from the date he ceases to be a partner).

In simple words, Section 45 endeavors to protect third parties who have no clue about the dissolution of firm and also the partners of a dissolved firm from liabilities towards third parties post-dissolution.

Wind up the Business Post-Dissolution (Section 46)

Once a firm is dissolved, every partner or his representative has a right to apply the property of the firm in payments of debts and liabilities of the firm. The surplus, if any, can be distributed among the partners according to their rights.

Also according to section 47 post-dissolution, the authority of each partner to bind the firm, along with other mutual rights and obligations, continue till such time that they can wind up the affairs of the firm.

This gives them a chance to complete the unfinished transactions at the time of dissolution. This does not include the acts of a partner who has been adjudicated insolvent.

Settlement of Partnership Accounts (Section 48)

Section 48 lays down certain rules for settlement of partnership accounts after the dissolution of firm under the usual course of business. However, the partners can mutually agree for a different settlement mode. The rules are as follows:

1. Any losses or deficiencies of capital will be paid out of profits. If the profits are not sufficient, then they are paid out of the capital and finally, if necessary, by the partners. The partners contribute in the proportion in which they receive their share in profits.
2. The assets of the firm, which includes the sums contributed by the partners to make up for the deficiency in the capital, is applied in the following order:
    1. Repaying the debts of the firm to third parties
    2. Paying each partner rateably what is due to him from the capital
    3. Paying each partner rateably what is due to him on account of capital
    4. If any amount is left, then dividing it among the partners in proportions in which they receive their share in profits.

Paying Firm Debts and Separate Debts (Section 49)

If there are joint debts due from the firm and separate debts due from any partner, then:

- The payment of firm debts is given priority. If there is any surplus, then the share of each partner is applied to his separate debts. It can also be paid to him.
- The separate property of the partner is applied first in the payment of his separate debts. IF there is any surplus, then it is applied to the payment of firm debts.

Personal Profits Earned after Dissolution of Firm (Section 50 and 53)

A firm is dissolved by the death of a partner. If the surviving partners, either themselves or with the representative of the deceased partner carry on the business of the firm, then they have to account for any personal profits by them, before winding up the firm.

So, if a lease expires on the death of a partner and the surviving partners renew it before the firm winds up, then the profits belong to the firm.

Section 53 clearly states that in the absence of an agreement to the contrary, a partner can restrain other partners from carrying on a similar business in the name of the firm or from using the property of the firm for their own benefit, unless the winding up process is complete.

Return of Premium on the Premature Dissolution of Firm (Section 51)

If a firm dissolves earlier than the time fixed for it, then the partner paying the premium can receive a return of a reasonable part of the premium. This holds true except when the partnership is dissolved:

- Due to the death of a partner
- Due to the misconduct of the partner paying the premium
- Post an agreement which has no provisions for the return of premium

Also, the partner paying the premium gets a return of a proportionate part of the premium. This holds true when the partnership is dissolved:

- Without either partner being at fault
- Owing to the fault of both the partners
- Due to the fault of the partner receiving the premium
- Due to unawareness about the insolvency of the partner receiving the premium

Contract Rescinded for Fraud or Misrepresentation (Section 52)

If the contract creating a partnership is rescinded due to fraud or misrepresentation, then the party who can rescind the contract is entitled to:

- Lien on the assets of the firm remaining after the debts of the firm is paid. This lien is for any sum paid by him for the purchase of a share in the firm and capital contributed by him.
- Rank as a creditor of the firm for any payment made by him towards the debts of the firm
- An indemnity from the partners guilty of the fraud or misrepresentation against all debts of the firm.

Sale of Goodwill after the Dissolution of Firm (Section 55)

The goodwill is included in the assets during the settling of the accounts of a firm after dissolution. The goodwill can be sold separately or along with the other assets of the firm. This is subject to the contract between the partners.

Once the goodwill of the firm is sold after dissolution, a partner can carry on and advertise a business competing with that of the buyer of goodwill. However, subject to the agreement between him and the buyer, he may not:

- Use the name of the firm
- Represent himself as carrying on the business of the firm
- Solicit the customs of persons dealing with the firm before the dissolution

It is also important to note that a partner can make an agreement with the buyer of goodwill that he will not carry on any business similar to that of the firm or with certain local limits. Such an agreement, notwithstanding Section 27 of the Indian Contract Act is valid if the restrictions are reasonable.