

THE INDIAN CONTRACT ACT, 1872

Unit 1- Contract of Indemnity and Guarantee

A) Multiple Choice Questions

Q1) A contracts to save B against the consequences of any proceedings, which C may take against B in respect of a certain sum of ₹500. This is a:

- (a) Contract of guarantee
- (b) Quasi contract
- (c) Contract of indemnity
- (d) Void contract

Q2) S and P go into a shop. S says to the shopkeeper, C, "Let P have the goods, and if he does not pay you, I will." This is a

- (a) Contract of Guarantee
- (b) Contract of Indemnity
- (c) Wagering agreement
- (d) Quasi-contract

Q3) A contract by which one party promises to save the other from loss caused to him by the conduct of the promisor himself or by the conduct of any other person is called as:

- (a) Surety Contract
- (b) Simple contract
- (c) Contract of Indemnity
- (d) None of the above

Q4) Any guarantee obtained by means of misrepresentation made by the creditor or with his knowledge and assent concerning a material part of the transaction is

- (a) Valid
- (b) Invalid
- (c) Both (a) and (b)
- (d) None of the above

Q5) A continuing guarantee may at any time be revoked by the surety as to future transaction by giving notice to

- (a) The Creditor
- (b) Principal Debtor
- (c) Without giving any notice to any person
- (d) None of the above

Q6) Atul contracts to indemnify Neha against the consequences of any proceedings which Chirag may take against Neha in respect of a sum of ₹15,000/- advanced by Chirag to Neha. Now, Neha who is called upon to pay the sum of money due to Chirag but she fails to do so. Now, as per the provisions of the Indian Contract Act, 1872, advise the future course of action to be taken by Chirag.

- (a) Chirag can recover the amount only from Neha
- (b) Chirag can recover the full amount from Atul
- (c) Chirag cannot recover the amount from Atul
- (d) Chirag can recover at least 10% of the total amount from Neha

B) Case Based Questions

Question 1

What are the rights of the indemnity-holder when sued?

Answer

Rights of Indemnity- holder when sued (Section 125):

The promisee in a contract of indemnity, acting within the scope of his authority, is entitled to recover from the promisor—

- (1) all damages which he may be compelled to pay in any suit in respect of any matter to which the promise to indemnify applies;
- (2) all costs which he may be compelled to pay in any such suit if, in bringing or defending it, he did not contravene the orders of the promisor, and acted as it would have been prudent for him to act in the absence of any contract of indemnity, or if the promisor authorised him to bring or defend the suit;
- (3) all sums which he may have paid under the terms of any compromise of any such suit, if the compromise was not contrary to the orders of the promisor, and was one which it would have been prudent for the promisee to make in the absence of any contract of indemnity, or if the promisor authorised him to compromise the suit.

It may be understood that the rights contemplated under section 125 are not exhaustive. The indemnity holder/indemnified has other rights besides those mentioned above. If he has incurred a liability and that liability is absolute, he is entitled to call upon his indemnifier to save him from the liability and to pay it off.

Question 2

Define contract of indemnity and contract of guarantee and state the conditions when guarantee is considered invalid?

Answer

Section 124 of the Indian Contract Act, 1872 states that “A contract by which one party promises to save the other from loss caused to him by the conduct of the promisor himself, or the conduct of any person”, is called a “contract of indemnity”.

Section 126 of the Indian Contract Act, 1872 states that “A contract to perform the promise made or discharge liability incurred by a third person in case of his default” is called a “contract of guarantee”.

The conditions under which the guarantee is invalid or void is provided in *Section 142, 143 and 144* of the Indian Contract Act.

These include:

- (i) Guarantee obtained by means of misrepresentation.
- (ii) Guarantee obtained by means of keeping silence as to material circumstances.
- (iii) When contract of guarantee is entered into on the condition that the creditor shall not act upon it until another person has joined in it as co-surety and that other party fails to join as such.

Question 3

A contracts with B for a fixed price to construct a house for B within a stipulated time. B would supply the necessary material to be used in the construction. C guarantees A's performance of the contract. B does not supply the material as per the agreement. Is C discharged from his liability. (RTP, Nov 2018) (MTP, Nov 2019) (MTP, May 2020)

Answer

According to **Section 134** of the Indian Contract Act, 1872, the surety is discharged by any contract between the creditor and the principal debtor by which the principal debtor is discharged or by any act or omission for the creditor the legal consequence of which is the discharge of the principal debtor. In the given case the B omits to supply the necessary construction material. Hence, C is discharged from his liability.

Question 4

Mr. D was in urgent need of money amounting to ₹ 5,00,000. He asked Mr. K for the money. Mr. K lent the money on the sureties of A, B and N without any contract between them in case of default in repayment of money by D to K. D makes default in payment. B refused to contribute, examine whether B can escape liability?

(CA Inter, May 2018); (MTP, Nov 2020) ; (MTP, Dec 2021); (CA Inter, Dec 2021)

Answer

Co-sureties liable to contribute equally (Section 146 of the Indian Contract act, 1872):

Equality of burden is the basis of Co-suretyship. This is contained in section 146 which states that “when two or more persons are co-sureties for the same debt, or duty, either jointly, or severally and whether under the same or different contracts and whether with or without the knowledge of each other, the co-sureties in the absence of any contract to the contrary, are liable, as between themselves, to pay each an equal share of the whole debt, or of that part of it which remains unpaid by the principal debtor”.

Accordingly, on the default of D in payment, B cannot escape from his liability. All the three sureties A, B and N are liable to pay equally, in absence of any contract between them.

Question 5

Rahul is the owner of electronics shop. Priyanka reached the shop to purchase an air conditioner whose compressor should be of copper. As Priyanka wanted to purchase the air conditioner on credit, Rahul demand a guarantor for such transaction. Mr. Arvind (a friend of Priyanka) came forward and gave the guarantee for payment of air conditioner. Rahul sold the air conditioner of a particular brand, misrepresenting that it is made of copper while it is made of aluminium. Neither Priyanka nor Mr. Arvind had the knowledge of fact that it is made of aluminium. On being aware of the facts, Priyanka denied for payment of price. Rahul filed the suit against Mr. Arvind. Explain with reference to the Indian Contract Act 1872, whether Mr. Arvind is liable to pay the price of air conditioner?
(RTP, Dec 2021)

Answer

As per the provisions of **Section 142** of the Indian Contract Act 1872, where the guarantee has been obtained by means of misrepresentation made by the creditor concerning a material part of the transaction, the surety will be discharged. Further according to provisions of **section 134**, the surety is discharged by any contract between the creditor and the principal debtor, by which the principal debtor is released, or by any act or omission of the creditor, the legal consequence of which is the discharge of the principal debtor.

In the given question, Priyanka wants to purchase air conditioner whose compressor should be of copper, on credit from Rahul. Mr. Arvind has given the guarantee for payment of price. Rahul sold the air conditioner of a particular brand on misrepresenting that it is made of copper while it is made of aluminium of which both Priyanka & Mr. Arvind were unaware. After being aware of the facts, Priyanka denied for payment of price. Rahul filed the suit against Mr. Arvind for payment of price.

On the basis of above provisions and facts of the case, as guarantee was obtained by Rahul by misrepresentation of the facts, Mr. Arvind will not be liable. He will be discharged from liability.

Unit 2-Bailment & Pledge

A) Multiple Choice Questions

Q1) With respect to Contract of Bailment, which of the following statement is incorrect

- (a) No consideration is necessary to create a valid contract of bailment.
- (b) It involves the delivery of goods from one person to another for some purposes.
- (c) Bailment is only for immovable goods and never for moveable goods
- (d) The change of possession does not lead to change of ownership.

Q2) Mr. Vishal parks his car at a parking lot, locks it, and keeps the keys with himself. Which of the following statement is correct in this regard?

- (a) This is a case of bailment
- (b) The parking people has possession of the car of Mr. Vishal
- (c) The parking people has custody of car of Mr. Vishal
- (d) This is the case of mortgage

Q3) The Pawnee doesn't have the right to retain the goods pledged for

- (a) Performance of the promise
- (b) Extraordinary expenses incurred by him for preservation of goods pledged
- (c) Payment of debt
- (d) Necessary expenses incurred by him in respect of possession of goods pledged

B) Case based Questions

Question 1

Mrs. A delivered her old silver jewellery to Mr. Y a Goldsmith, for the purpose of making new a silver bowl out of it. Every evening she used to receive the unfinished good (silver bowl) to put it into box kept at Mr. Y's Shop. She kept the key of that box with herself. One night, the silver bowl was stolen from that box. Was there a contract of bailment? Whether the possession of the goods (actual or constructive) delivered, constitute contract of bailment or not?
(MTP, May 2020; Dec 2021)

Answer

Section 148 of Indian Contract Act 1872 defines 'Bailment' as the delivery of goods by one person to another for some purpose, upon a contract that they shall, when the purpose is accomplished, be returned or otherwise disposed of according to the direction of the person delivering them.

According to **Section 149** of the Indian Contract Act, 1872, the delivery to the bailee may be made by doing anything which has the effect of putting the goods in the possession of the intended bailee or of any person authorised to hold them on his behalf. Thus, delivery is necessary to constitute bailment.

Thus, the mere keeping of the box at Y's shop, when A herself took away the key cannot amount to delivery as per the meaning of delivery given in the provision in section 149. Therefore, in this case there is no contract of bailment as Mrs. A did not deliver the complete possession of the good by keeping the keys with herself.

Question 2

Amar bailed 50 kg of high quality sugar to Srijith, who owned a kirana shop, promising to give ₹ 200 at the time of taking back the bailed goods. Srijith's employee, unaware of this, mixed the 50 kg of sugar belonging to Amar with the sugar in the shop and packaged it for sale when Srijith was away. This came to light only when Amar came asking for the sugar he had bailed with Srijith, as the price of the specific quality of sugar had trebled. What is the remedy available to Amar?
(CA Inter, Nov 2018) (MTP, Nov 2020)

Answer

According to **section 157** of the Contract Act, 1872, if the bailee, without the consent of the bailor, mixes the goods of the bailor with his own goods, in such a manner that it is impossible to separate the goods bailed from the other goods and deliver them back, the bailor is entitled to be compensated by the bailee for the loss of the goods. In the given question, Srijith's employee mixed high quality sugar bailed by Amar and then packaged it for sale. The sugars when mixed cannot be separated. As Srijith's employee has mixed the two kinds of sugar, he (Srijith) must compensate Amar for the loss of his sugar.

Question 3

Srushti acquired valuable diamond at a very low price by a voidable contract under the provisions of the Indian Contract Act, 1872. The voidable contract was not rescinded. Srushti pledged the diamond with Mr. VK. Is this a valid pledge under the Indian Contract Act, 1872?

Answer

Pledge by person in possession under voidable contract [Section 178A of the Indian Contract Act, 1872]:

When the pawnor has obtained possession of the goods pledged by him under a contract voidable under section 19 or section 19A, but the contract has not been rescinded at the time of the pledge, the pawnee acquires a good title to the goods, provided he acts in good faith and without notice of the pawnor's defect of title. Therefore, the pledge of diamond by Srushti with Mr. VK is valid.

Unit 3-Agency

A) Multiple Choice Questions

Q1) _____ is one who represents to be an agent of another when in reality he has no such authority from the other agent at all.

- (a) Substituted agent
- (b) Subordinate agent
- (c) Pretended agent
- (d) Both (a) & (b)

Q2) Mr. Jane has appointed Ms. Vinita as his agent to sell the garments manufactured by Jane. Vinita due to her personal issues could not work effectively. Hence, she appointed Mr. Kanth to sell on her behalf. Can Mr. Jane be bound by the acts of Mr. Kanth?

- (a) No, an agent without authority cannot lawfully appoint a subagent.
- (b) Yes, Vinita is liable for the acts of Kanth and in turn Jane is liable for the transaction.
- (c) No, Kanth will be liable on his own account for any sales made.
- (d) Yes, Kanth now becomes direct agent of Jane as Kanth has sold garments manufactured by Jane.

Q3) A is residing in Delhi and has a house in Mumbai. A appoints B by a power of attorney to take care of his house. State the nature of agency created between A and B:

- (a) Implied agency
- (b) Agency by ratification
- (c) Agency by necessity
- (d) Express agency

Q4) An agent is not liable to the principal if

- (a) He is a minor
- (b) He is of unsound mind
- (c) (a) and (b) both
- (d) None of these

B) Case based Questions

Question 1

A rented his house to B on lease for 3 years. The lease agreement is terminable on 3 month notice by either party. C, the son of A, being in need of a separate house to live, served a notice on B, without any authority, to vacate the house within a month and requested his father A to ratify his action. Examine whether it shall be valid for A to ratify the action of C taking into account the provisions of the Indian Contract Act, 1872?

(CA Inter, July 2021)

Answer

As per section 200 of the Indian contract Act, 1872, an act done by one person on behalf of another, without such other person's authority, which, if done with authority, would have the effect of subjecting a third person to damages, or of terminating any right or interest of a third person, cannot, by ratification, be made to have such effect.

In the given instance, A rented his house to B on lease for 3 years. The lease agreement was terminable on three months' notice. C, son of A, gives notice of termination to B, without any authority, to vacate the house within a month. Also requested A to ratify his action. Here by the act of C, the interest of B is affected, therefore the principle of ratification does not apply.

Hence, it's not valid for A to ratify the action of C, thereby causing the notice to be binding on B.

Question 2

ABC Ltd. sells its products through some agents and it is not the custom in their business to sell the products on credit. Mr. Pintu, one of the agents sold goods of ABC Ltd. to M/s. Parul Pvt. Ltd. (on credit) which was insolvent at the time of such sale. ABC Ltd. sued Mr. Pintu for compensation towards the loss caused due to sale of products to M/s. Parul Pvt. Ltd. Will ABC Ltd. succeed in its claim?

Answer

To conduct the business of agency according to the principal's directions (Section 211 of the Indian Contract Act, 1872):

An agent is bound to conduct the business of his principal according to the direction given by the principal, or, in the absence of any such directions, according to the custom which prevails in doing business of the same kind at the place where the agent conducts such business. When the agent acts otherwise, if any loss be sustained, he must make it good to his principal, and, if any profit accrues, he must account for it.

In the present case, Mr. Pintu, one of the agents, sold goods of ABC Ltd. to M/s Parul Pvt. Ltd. (on credit) which was insolvent at the time of such sale.

Also, it is not the custom in ABC Ltd. to sell the products on credit. Hence, Mr. Pintu must make good the loss to ABC Ltd.

Question 3

Comment on the statement 'Principal is not always bound by the acts of a sub-agent'.

Answer

The statement is correct.

Normally, a sub-agent is not appointed, since it is a delegation of power by an agent given to him by his principal. The governing principle is, a delegate cannot delegate'. (Latin version of this principle is, "delegates non potest delegare").

However, there are certain circumstances where an agent can appoint sub-agent. In case of proper appointment of a sub-agent, by virtue of Section 192 of the Indian Contract Act, 1872 the principal is bound by and is held responsible for the acts of the sub-agent. Their relationship is treated to be as if the sub-agent is appointed by the principal himself.

However, if a sub-agent is not properly appointed, the principal shall not be bound by the acts of the sub-agent. Under the circumstances the agent appointing the sub-agent shall be bound by these acts and he (the agent) shall be bound to the principal for the acts of the sub-agent.

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