As per Sant Gadge Baba Amravati Vidyapeeth new restructured syllabus NEP Pattern (2025-26). Also useful for other Universities.

INDIAN CONTRACT ACT 1872 (II)

B.Com. Semester II

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PREFACE

The **Indian Contract Act, 1872** is a core subject for students of **Commerce, Management, and Law**, forming the legal foundation of business transactions in India. A sound understanding of this Act is essential not only for university examinations but also for professional and practical application in business life. However, students often find the subject challenging due to complex legal terminology and inadequate linkage between theory and practice.

This book has been prepared primarily for B.Com students of Sant Gadge Baba Amravati University (SGBAU) and is written strictly in accordance with the latest syllabus prescribed under the National Education Policy (NEP) 2020. Special care has been taken to align the content with the outcome-based, competency-oriented, and multidisciplinary approach emphasized under NEP 2020. At the same time, the book has been designed to remain useful for students of other Indian universities, competitive examinations, and beginners in contract law.

The main objective of this book is to present the provisions of the Indian Contract Act, 1872 in a simple, systematic, and student-friendly manner, without compromising legal accuracy. The subject matter has been explained in easy and clear language, supported by definitions, illustrations, practical examples, important case laws, short notes, and exam-oriented questions, enabling students to develop both conceptual understanding and practical insight.

In accordance with **NEP 2020**, this book focuses on:

- Conceptual clarity and analytical thinking
- Outcome-based learning
- Application-oriented examples
- Skill development and practical relevance
- Continuous and comprehensive assessment readiness

Each chapter has been structured to help students understand, analyse, and apply legal principles, rather than merely memorize them. Important sections, definitions, and likely examination questions have been highlighted to assist students in effective preparation.

I sincerely acknowledge the guidance and encouragement received from teachers, students, and academic peers, which motivated the preparation of this book. Constructive suggestions for improvement are always welcome and will be duly considered in future editions.

It is hoped that this book will serve as a reliable guide and companion for students and teachers, and will contribute meaningfully to the study and understanding of the Indian Contract Act under the NEP 2020 framework.

Author
(Prof. Aditi S. Deokar)

ACKNOWLEDGEMENT

First and foremost, I offer my humble gratitude to Almighty God, whose blessings, grace, and guidance made this academic work possible.

I express my deep sense of gratitude to all those who have directly or indirectly contributed to the successful completion of this book on the Indian Contract Act, 1872. I am sincerely thankful to my teachers and mentors, whose valuable guidance, academic insight, and encouragement have been a constant source of inspiration throughout the preparation of this work. Their support helped me develop clarity of thought and a better understanding of the subject.

I also extend my heartfelt thanks to my students, whose questions, feedback, and academic needs motivated me to present the subject matter in a simple, practical, and student-friendly manner, in accordance with the National Education Policy (NEP) 2020. I gratefully acknowledge the support and cooperation of my colleagues and well-wishers, whose suggestions and moral support contributed significantly to shaping this book.

I owe a special debt of gratitude to my family members for their patience, encouragement, and unwavering support throughout this academic endeavour. I also acknowledge the contribution of various textbooks, research articles, journals, judicial decisions, and online academic resources, which have been consulted while preparing this book.

Despite sincere efforts to maintain accuracy and clarity, any errors or omissions that may remain are entirely my own. Constructive suggestions for improvement will be gratefully welcomed and incorporated in future editions.

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SYLLABUS

B.Com. I (NEP) Semester II
Indian Contract Act II

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Introduction: Law of Indemnity and Guarantee - Contract of Indemnity,

Definition-Essentials, Rights of indemnity holder, Rights of indemnifier.

Unit II : Contract of Guarantee

Definition, Consideration in a contract of guarantee, Essentials of contract of Guarantee, Law as to bank guarantee, Distinction between a contract of indemnity and a contract of guarantee. Contract of Insurance Guarantee and Indemnity. Distinguished – Continuing guarantee, Revocation of Continuing guarantee, when surety is not discharged? Exceptions- Invalid guarantees, Rights of surety, Law as to co-sureties, right of surety against the co-surety

Unit III: Contract of Bailment & Pledge

Bailment, Definition, Essentials, Kinds of Bailments, Rights, duties and liabilities of Bailor, Rights, duties and liabilities of a Bailee, what is lien? General Lien, Particular or Specific lien, Particular lien a& General lien. Finder of Goods.

Pledge: Definition, Essentials, Pledge and Lien distinguished, Pledge and Bailment distinguished Rights of a Pawnee, Liabilities of a Pawnee Rights of Pawn or, Pledge by persons other than the true owner.

Unit IV : Law of Agency

Appointment of Agent , who is an agent and a principal, who can appoint an agent? Who can employ agent, Test of Agency, how is agency constituted? Ratification, Rules governing ratification. Classification of Agents, sub-agent, Relationship between Principal and agent and subagent. Agent's authority, Implied authority, Effect of agents' authority. Revocation and renunciation of agent's authority, Rights, duties and liabilities of Principal and agents. Termination or determination of agency. Effect of termination.

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UNIT – I

Law of Indemnity and Guarantee

Contents

Introduction

In commercial and business transactions, parties often enter into agreements where one party promises to protect the other from loss or assures the performance of another's obligation. The Indian Contract Act, 1872 recognises such arrangements under special contracts — namely, Contract of Indemnity and Contract of Guarantee — covered in Chapter VIII (Sections 124–147). These provisions provide a legal framework to ensure security, trust, and smooth functioning in various business and financial dealings.

In simple terms, a contract of indemnity is an agreement in which one party undertakes to compensate the other for any loss suffered due to certain specified events. On the other hand, a contract of guarantee involves three parties, where the guarantor promises to discharge the liability or perform the obligation of a third person (principal debtor) in case of default. Both these contracts are essential tools used to manage and reduce risk in commercial transactions.

These concepts are widely applied in practical situations such as insurance contracts, bank guarantees, loans, and credit facilities. They help businesses and individuals safeguard their

interests, build confidence in transactions, and ensure that obligations are fulfilled. By clearly defining the rights, duties, and liabilities of the parties, these contracts minimize disputes and provide legal protection.

From a student-friendly perspective, understanding indemnity and guarantee is very important as it builds a strong base in contract law and connects theoretical knowledge with real-life applications. It also helps students develop clarity about legal relationships in business transactions, which is highly useful for careers in commerce, law, banking, and management.

1.1 Contract of Indemnity (section 124)

A contract of indemnity is a special type of contract made to protect a person from loss or damage. The main aim of this contract is to provide financial security against possible risks that may arise in the future. In many business and legal transactions, one person agrees to compensate another if a loss occurs due to certain events or the actions of a third party. According to the Indian Contract Act, a contract of indemnity creates a legal duty on one party, called the indemnifier, to compensate the other party, known as the indemnity holder, for the loss suffered. The loss may arise due to an act, omission, or an uncertain future event. This type of contract helps the indemnity holder to feel safe and confident while entering into agreements.

Contracts of indemnity are very important in modern business and commercial activities. They are commonly used in insurance contracts, guarantee agreements, agency relationships, and other commercial contracts. By deciding in advance who will bear the loss, contracts of indemnity help in

reducing financial risk and maintaining trust and fairness between the parties.

A contract of indemnity is a special type of contract made to protect a person from loss or damage. The main aim of this contract is to provide financial security against possible risks that may arise in the future. In many business and legal transactions, one person agrees to compensate another if a loss occurs due to certain events or the actions of a third party. According to the Indian Contract Act, 1872, a contract of indemnity creates a legal duty on one party, called the indemnifier, to compensate the other party, known as the indemnity holder, for the loss suffered. The loss may arise due to an act, omission, or an uncertain future event. This type of contract helps the indemnity holder to feel safe and confident while entering into agreements.

In addition, a contract of indemnity is based on the principle of protection against loss rather than the transfer of risk. The indemnifier undertakes to make good the loss only when it actually occurs, thereby ensuring fairness between the parties. Such contracts may be express or implied, depending on the nature of the agreement and the conduct of the parties. This flexibility makes indemnity contracts suitable for a wide range of legal and commercial situations.

Contracts of indemnity are very important in modern business and commercial activities. They are commonly used in insurance contracts, guarantee agreements, agency relationships, and other commercial contracts. By deciding in advance who will bear the loss, contracts of indemnity help in reducing financial risk and maintaining trust and fairness between the parties.

Furthermore, these contracts also define the rights of the indemnity holder, such as the right to recover damages, legal costs, and other expenses incurred while dealing with the loss. This ensures that the indemnity holder is fully protected and does not suffer financially due to unforeseen circumstances. From a student-friendly point of view, understanding the concept of indemnity provides clarity about how businesses manage risks and secure their transactions in practical life.

1.2 Definition (Section 124)

A Contract of Indemnity is defined under Section 124 of the Indian Contract Act, 1872 as:

"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."

This contract is entered into to protect against anticipated loss, rather than to impose new liabilities.

In addition to the statutory definition, various legal scholars have also explained the concept of indemnity in a broader and more practical sense. According to **Pollock**, a contract of indemnity is "a promise to save another harmless from the consequences of an act." Similarly, **Anson** defines it as a promise by one party to compensate another for any loss suffered. These definitions emphasize the idea of protection and compensation rather than punishment or enforcement.

From a practical and student-friendly perspective, all these definitions highlight that the core purpose of indemnity is to provide security against loss. It ensures that if a person suffers a loss due to a specified event or action, another party will make good that loss. Thus, a contract of indemnity acts as a safeguard in business transactions by reducing uncertainty and promoting confidence between the parties.

Parties to a Contract of Indemnity

There are two principal parties:

1. **Indemnifier (Promisor)** – The person who promises to make good the loss.
2. **Indemnity-holder (Promisee / Indemnified)** – The person who is protected against loss under the contract.

Essentials of a Contract of Indemnity

A contract of indemnity must meet the following essentials:

1. **Existence of a Contract:** The agreement must be valid, fulfilling all essentials of a valid contract (offer, acceptance, consideration, lawful object, capacity, free consent).
2. **Promise to Indemnify:** A clear promise by one party to protect the other from loss.
3. **Loss:** There should be a potential or actual loss to the indemnity-holder.
4. **Two Parties Only:** It typically involves only the indemnifier and the indemnified.
5. **Contingent Nature:** Liability arises only upon the happening of a specified contingency (i.e., loss).

Let's take some easy example

Contract of Indemnity – Meaning with Examples

A contract of indemnity is an agreement where one person promises to protect another person from a possible loss.

Example 1 (Between Neighbours)

There is a shared wall between the houses of Ram and Shyam. Ram wants to demolish his house and rebuild it. Shyam is worried that his house might get damaged while Ram is breaking the wall.

So, Ram promises to pay Shyam for any loss that may happen during the demolition. This promise is called a contract of indemnity between Ram and Shyam.

Example 2 (Insurance Case)

An insurance company gives car insurance to a person. Later, the car meets with an accident and the owner suffers a loss of ₹10,000.

In this situation, the insurance company must compensate the owner for the loss. Here, the insurance company is giving indemnity (compensation) to the car owner.

Types of Contracts of Indemnity

Like other contracts, a contract of indemnity can be of two kinds:

Express Contract – The promise is clearly stated in words (spoken or written).

Implied Contract – The promise is not directly stated but is understood from the situation or behaviour of the parties.

Essentials of a Valid Contract (Also Required in Indemnity Contract)

For a contract of indemnity to be legally valid, it must include all the basic elements of a valid contract:

a) Agreement – There must be an offer (proposal) by one party and acceptance by the other.

b) Capacity of Parties – Both persons must be legally capable of entering into a contract (major, sound mind, not disqualified by law).

c) Free Consent – Agreement must be made without force, fraud, pressure, or misunderstanding.

d) Lawful Consideration and Lawful Object – The purpose of the agreement and the benefit exchanged must be legal.

e) Agreement Should Not Be Declared Void by Law – It should not be one of the agreements that the law treats as invalid.

If any one of these points is missing, the indemnity contract will not be valid.

Example of an Invalid (Void) Contract

Suppose Anil tells Sunil that he will protect him from loss if Sunil threatens Sushil by showing a gun and firing in the air. Sunil does this and later faces legal trouble.

Anil cannot legally compensate Sunil because:

The object of the agreement is illegal (involves threat and violence).

So, this contract is not valid, and Sunil cannot claim compensation.

Key Idea in One Line   **A contract of indemnity means one person agrees to make good the loss suffered by another, but it is valid only when all legal conditions of a contract are satisfied.**

1.3 Rights of the Indemnity-Holder (section 125)

Under **Section 125** of the Act, the indemnity-holder has the right to recover the following from the indemnifier, *provided he acts within the scope of his authority*:

Rights of an Indemnity Holder (Section 125, Indian Contract Act)

The person who is protected under a contract of indemnity is called the Indemnity Holder. When he suffers a loss, he has the legal right to recover certain amounts from the Indemnifier (the person who promised to compensate).

These rights are:

1) Right to Recover Damages

The indemnity holder can claim all the damages that he has been forced to pay in a case connected with the indemnity agreement.

This applies when the legal case is related to the promise of indemnity.

2) Right to Recover Legal Expenses (Cost of Litigation)

The indemnity holder can also recover all the legal costs he spent while defending himself in court.

But this is allowed only when:

He followed the instructions given by the indemnifier, or

He acted in a sensible and honest way, just like a reasonable person would act even if there was no indemnity contract, or

The indemnifier gave him permission to fight or defend the case.

3) Right to Recover Amount Paid in Settlement (Compromise)

If the indemnity holder settles the matter out of court and pays some amount as a compromise, he can claim that money back from the indemnifier.

However, this is valid only when:

The settlement was not against the orders of the indemnifier and The compromise was made carefully and in good faith (like a reasonable person would do) or The indemnifier had agreed that such a compromise could be made.

In Simple Words

An indemnity holder can get back: Money paid as damages Money spent on court cases Money paid during a legal settlement

— but only when he acts honestly, sensibly, and according to the agreement.

Note: The indemnity-holder's rights are subject to reasonableness and authority — he cannot act contrary to the promisor's instructions.

1.4 Rights of the Indemnifier

Although the Act does not expressly detail the rights of the indemnifier, judicial interpretation and legal principles recognise the following after indemnifying the indemnity-holder:

1. **Right to Subrogation:** The indemnifier can step into the shoes of the indemnified to recover from third parties responsible for the loss.
2. **Right to Security:** If the indemnity contract provided for any securities, the indemnifier can enforce those.
3. **Right to Prevent Loss:** The indemnifier may utilise all lawful means to prevent or minimize the loss once the indemnity obligation arises.

In conclusion, the Contract of Indemnity plays an important role in the Law of Contracts by providing protection against loss and ensuring financial security between parties. This chapter has explained the meaning and definition of indemnity, its essential elements, and the rights of both the indemnity holder and the indemnifier in a clear and systematic manner. A proper understanding of these concepts helps students to appreciate how indemnity operates in practical business and legal situations such as insurance and commercial agreements. The knowledge gained from this chapter forms a strong foundation for studying related topics like contracts of guarantee and other special contracts under the Indian Contract Act, 1872.

Unit II

Contract of Guarantee

In this chapter, we will study the important concepts of the Contract of Guarantee and Contract of Indemnity as provided under the Indian Contract Act, 1872. These contracts play a significant role in business, banking, and commercial transactions, where one party promises to safeguard the interests of another. The chapter explains the meaning and essentials of a contract of guarantee, consideration, continuing guarantee, rights and liabilities of the surety, co-sureties, and circumstances under which a guarantee may be revoked or becomes invalid. Special emphasis is also given to bank guarantees and the distinction between indemnity, guarantee, and insurance contracts, enabling students to clearly

understand their practical application. This chapter is designed in a simple, systematic, and exam-oriented manner to help students develop a strong conceptual foundation and confidently answer university examinations.

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2.1 Contract of Guarantee – Definition (Section 126)

- A contract of guarantee is defined under Section 126 of the Indian Contract Act, 1872.
- It is a contract to perform the promise or discharge the liability of a third person in case of his default.
- There are three parties involved:
  - **Surety** – the person who gives the guarantee
  - **Principal Debtor** – the person whose default is guaranteed
  - **Creditor** – the person to whom the guarantee is given
- The contract may be oral or written.

For example,

A Contract of Guarantee is a contract where one person promises to take responsibility for the debt or default of another person.

In simple words:

"If he does not pay, I will pay."

Example:

Ram takes a loan from a bank. Shyam says, "If Ram does not repay, I will repay."

This is a contract of guarantee.

2.2 Consideration in a Contract of Guarantee (Section 127)

- Consideration is essential for a valid contract of guarantee.
- As per Section 127, anything done or any promise made for the benefit of the principal debtor is sufficient consideration for the surety.
- The consideration need not move directly to the surety.

Example:

- A gives a loan to B on the guarantee of C → the loan to B is sufficient consideration for C.

2.3 Essentials of a Contract of Guarantee

A contract of guarantee must satisfy the following essential elements to be valid under the Indian Contract Act, 1872:

1. There must be three parties

A contract of guarantee necessarily involves three parties:

- **Surety** – the person who gives the guarantee and undertakes to fulfil the obligation in case of default.
- **Principal Debtor** – the person whose liability is guaranteed.

- **Creditor** – the person to whom the guarantee is given. These three parties must enter into the contract with a common understanding regarding the guarantee.

Example:

Suppose **A** takes a loan of ₹50,000 from **B**. **C** promises **B** that if **A** fails to repay the loan, he will pay the amount on behalf of **A**.

In this case:

- **C** is the *Surety* (who gives the guarantee)
- **A** is the *Principal Debtor* (whose liability is guaranteed)
- **B** is the *Creditor* (to whom the guarantee is given)

Thus, all three parties are involved with a common understanding that if **A** defaults, **C** will be responsible to pay the amount to **B**.

2. There must be a principal debt or obligation

- A guarantee can exist only if there is a principal debt or obligation.
- If there is no primary liability, the guarantee cannot arise.
- The liability of the surety is secondary and dependent on the liability of the principal debtor.
- If the principal debt is void, the guarantee also becomes void.

Example:

A) Suppose **A** borrows ₹20,000 from **B** and **C** gives a guarantee that he will repay the amount if **A** fails to do so. Here, the loan taken by **A** is the **principal debt**, and **C's** liability as a surety depends on this debt.

B) If **A** fails to repay, then **C** becomes liable to pay **B**. However, if the loan agreement between **A** and **B** is **void** (for example, if it was made for an illegal purpose), then there is no valid principal debt. In such a case, the guarantee given by **C**

will also become **void**, and **C** will not be liable to pay anything.

3. The guarantee must be given for the default of the principal debtor

- The surety's liability arises only when the principal debtor makes a default in payment or performance.
- The surety is not liable immediately; his obligation begins only after the debtor fails to fulfil his promise.
- This condition clearly distinguishes a contract of guarantee from a contract of indemnity.

Example:

Suppose **A** takes a loan of ₹30,000 from **B**, and **C** gives a guarantee that he will pay the amount if **A** fails to repay it. As long as **A** pays the loan on time, **C** has no liability. However, if **A** defaults in repayment, only then does **C's** liability arise, and he becomes responsible to pay **B**.

This shows that the surety's liability is **secondary** and begins only after the principal debtor fails to perform his obligation, which clearly distinguishes a contract of guarantee from a contract of indemnity.

4. There must be free consent of the surety

- The consent of the surety must be free and voluntary.
- If the guarantee is obtained by coercion, undue influence, fraud, misrepresentation, or concealment of material facts, the contract becomes invalid.
- Free consent ensures that the surety is fully aware of the nature and extent of liability undertaken.

Example:

Suppose **A** asks **C** to become a surety for a loan taken from **B**. **C** agrees because **A** tells him that the loan amount is only ₹10,000, while in reality it is ₹50,000. Here, **C's** consent

is obtained by **misrepresentation**, as he was not informed of the true facts. In this situation, the guarantee becomes **invalid**, and **C** will not be liable as a surety. This example shows that free and informed consent is essential, and the surety must clearly understand the nature and extent of the liability before giving the guarantee.

5. Consideration must be lawful and sufficient

- Consideration is essential for a valid contract of guarantee.
- Any act done or promise made for the benefit of the principal debtor is sufficient consideration for the surety.
- The consideration must be lawful and not opposed to public policy.
- It is not necessary that the consideration should move directly to the surety.

Example:

Suppose **A** wants to take goods on credit from **B**, but **B** agrees to sell the goods only if someone gives a guarantee. **C** then promises **B** that if **A** fails to pay for the goods, he will pay the amount. Based on this guarantee, **B** supplies goods to **A** on credit.

In this case, the **consideration** is the benefit received by **A** (the goods supplied on credit). Even though **C** (the surety) does not receive any direct benefit, the contract of guarantee is still valid because the consideration moves to the principal debtor (**A**), and that is sufficient in law.

6. The contract must not be invalid or illegal

- The contract of guarantee must satisfy all essentials of a valid contract under the Indian Contract Act.
- It should not be illegal, immoral, or opposed to public policy.

- A guarantee relating to an illegal agreement is void and unenforceable.
- If the principal contract itself is invalid, the guarantee automatically becomes invalid.

Example:

Suppose **A** takes a loan from **B** to carry out an illegal business activity, such as smuggling, and **C** gives a guarantee that he will repay the loan if **A** fails to do so. In this case, the main agreement between **A** and **B** is **illegal**.

Since the principal contract itself is unlawful, the guarantee given by **C** is also **void and unenforceable**. Therefore, **B** cannot recover the amount from **C**. This shows that a contract of guarantee must be based on a lawful agreement; otherwise, it becomes invalid.

2.4 Law as to Bank Guarantee

A bank guarantee is a written and legally binding promise given by a bank on behalf of its customer, assuring the beneficiary that the bank will make payment if the customer fails to fulfil his contractual obligation. It is commonly used in commercial, industrial, and government contracts to provide financial security. A bank guarantee is a written and legally binding promise given by a bank on behalf of its customer, assuring the beneficiary that the bank will make payment if the customer fails to fulfil his contractual obligation. It is commonly used in commercial, industrial, and government contracts to provide financial security.

A bank guarantee involves three parties — the bank (guarantor), the customer (applicant), and the beneficiary. The bank undertakes the responsibility to pay a specified amount if the customer defaults in performing the contract. This

assurance increases trust between parties, especially when large financial transactions are involved.

There are different types of bank guarantees such as financial guarantees and performance guarantees. A financial guarantee ensures payment of money, while a performance guarantee ensures completion of a contract as per agreed terms. These guarantees are widely used in construction contracts, supply agreements, and international trade.

Bank guarantees play a vital role in reducing risk and ensuring smooth business operations. They protect the interests of the beneficiary by providing a secure remedy in case of non-performance or default by the customer. At the same time, they help businesses expand their operations by building credibility and financial reliability.

From a practical and student-friendly perspective, understanding bank guarantees is important as they are closely linked with banking and commercial law. They demonstrate how legal principles are applied in real-world financial transactions and help students grasp the functioning of modern business practices.

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Example:

Suppose a construction company **A** enters into a contract with a government department **B** to build a road. **B** requires assurance that the work will be completed on time. Therefore, **A** obtains a bank guarantee from **C Bank**, promising that if **A**

fails to complete the project as agreed, the bank will pay a specified amount to **B**. If **A** successfully completes the project, the guarantee is discharged. However, if **A** defaults, **B** can claim the guaranteed amount from the bank.

1. Nature of Bank Guarantee

- A bank guarantee is issued by a bank to secure the performance or payment obligations of its customer.
- The bank acts as a surety, while the customer is the principal debtor and the beneficiary is the creditor.
- It creates a sense of trust and reduces risk in business transactions.

Example:

Suppose **A Ltd.** enters into a contract with **B Ltd.** to supply machinery worth ₹10 lakhs. To ensure that **A Ltd.** fulfils its obligation, **B Ltd.** asks for a bank guarantee. **A Ltd.** approaches **C Bank**, which issues a guarantee stating that if **A Ltd.** fails to supply the machinery or complete the contract, the bank will pay the specified amount to **B Ltd.**

In this case, the bank (**C Bank**) acts as the **surety**, **A Ltd.** is the **principal debtor**, and **B Ltd.** is the **creditor**. This arrangement creates trust between the parties and reduces the risk for **B Ltd.**, as it is assured of compensation even if **A Ltd.** defaults.

2. Liability of the Bank

- The bank undertakes to pay a specified sum of money to the beneficiary in case the customer defaults.
- The liability of the bank is absolute and unconditional, subject to the terms mentioned in the guarantee.
- Once the conditions of default are satisfied, the bank is bound to make payment.

The bank, while issuing a guarantee, undertakes a clear obligation to pay a specified amount to the beneficiary if the customer fails to perform the contract or make payment. This liability is considered **absolute and unconditional**, meaning that once the terms of the guarantee are fulfilled and default occurs, the bank cannot refuse payment on the ground of disputes between the customer and the beneficiary. The bank's duty is to honour the guarantee strictly according to its terms.

Example:

Suppose **A Ltd.** enters into a contract with **B Ltd.** for construction work and obtains a bank guarantee from **C Bank**. If **A Ltd.** fails to complete the project as agreed, **B Ltd.** can invoke the guarantee. Once the conditions mentioned in the guarantee are satisfied, **C Bank** is bound to pay the guaranteed amount to **B Ltd.**, even if **A Ltd.** disputes the claim.

3. Independence of Bank Guarantee

- A bank guarantee is independent of the main contract between the customer and the beneficiary.
- Any dispute or disagreement in the main contract does not affect the bank's obligation under the guarantee.
- The bank is concerned only with the terms of the guarantee, not with the performance of the main contract.

A bank guarantee is **independent of the main contract** between the customer and the beneficiary. This means that the obligation of the bank is separate and distinct from the original agreement between the parties. Even if there is any dispute, delay, or disagreement regarding the performance of the main contract, it does not affect the bank's duty to honour the guarantee. The bank is concerned only with whether the terms and conditions of the guarantee have been fulfilled, and not with the actual performance or breach of the main contract.

Example:

Suppose **A Ltd.** enters into a contract with **B Ltd.** to supply goods and obtains a bank guarantee from **C Bank**. Later, a dispute arises between **A Ltd.** and **B Ltd.** regarding the quality of goods supplied. Despite this dispute, if **B Ltd.** invokes the bank guarantee as per its terms, **C Bank** is bound to make the payment. The bank cannot refuse payment on the ground that there is a dispute between **A Ltd.** and **B Ltd.**, as its obligation is independent of the main contract.

4. Honour of Guarantee on Demand

- The bank must honour the guarantee on demand made by the beneficiary.
- The bank cannot refuse payment merely because the customer objects or raises disputes.
- Exception: Payment may be refused in cases of clear fraud or where enforcement would result in irretrievable injustice.

The bank is under a legal obligation to **honour the guarantee on demand** made by the beneficiary, provided the terms of the guarantee are complied with. It cannot refuse payment simply because the customer raises objections or disputes the claim. This ensures reliability and trust in commercial transactions. However, there are limited exceptions to this rule — the bank may refuse payment in cases of **clear fraud** or where enforcing the guarantee would result in **irretrievable injustice**, such as when the beneficiary is acting dishonestly or the situation would cause irreversible harm to the customer.

Example:

Suppose **A Ltd.** obtains a bank guarantee from **C Bank** in favour of **B Ltd.** for a supply contract. If **A Ltd.** fails to

perform, **B Ltd.** can demand payment from the bank, and **C Bank** must honour the guarantee even if **A Ltd.** objects. However, if **A Ltd.** proves that **B Ltd.** is making a fraudulent claim (for example, demanding payment despite full performance), the bank may refuse to pay.

5. Common Types of Bank Guarantees

(a) Financial Guarantee

- It assures payment of money in case of financial default by the customer.
- Commonly used for loans, credit facilities, and payment obligations.

Example:

- Guarantee for repayment of a loan amount.

A financial guarantee is a type of bank guarantee that assures the **payment of money** in case the customer fails to meet financial obligations. It is commonly used in loans, credit facilities, and deferred payment arrangements, where the bank promises to pay the beneficiary if the borrower defaults. This type of guarantee provides financial security and confidence to the creditor in monetary transactions.

Example:

Suppose **A** takes a loan from **B Bank**, and **C Bank** gives a financial guarantee assuring repayment. If **A** fails to repay the loan, **C Bank** will pay the outstanding amount to **B Bank** on behalf of **A**.

(b) Performance Guarantee

- It ensures the proper performance of contractual duties.
- Used in construction, supply contracts, and government tenders.
- If the contractor fails to perform, the bank pays compensation to the beneficiary.

A performance guarantee ensures that a party performs its contractual duties as agreed. It is widely used in construction contracts, supply agreements, and government tenders. If the contractor or supplier fails to complete the work or perform as per the contract terms, the bank compensates the beneficiary for the loss.

Example:

Suppose **A Ltd.** enters into a contract with **B Ltd.** to construct a building and obtains a performance guarantee from **C Bank**. If **A Ltd.** fails to complete the project on time or does not meet the agreed standards, **B Ltd.** can claim compensation from **C Bank** under the guarantee.

6. Importance of Bank Guarantee

- It promotes confidence in commercial dealings.
- It protects the beneficiary from financial loss.
- It helps businesses obtain contracts and credit facilities easily.

A bank guarantee plays an important role in promoting **confidence in commercial dealings** by assuring the beneficiary that financial protection is available in case of default. It safeguards the beneficiary from potential financial loss and reduces the risk involved in transactions. At the same time, it helps businesses secure contracts and obtain credit facilities more easily, as the guarantee enhances their credibility and trustworthiness in the eyes of other parties.

Example:

Suppose **A Ltd.** wants to participate in a government tender but is required to provide financial security. It obtains a bank guarantee from **C Bank** in favour of the government department **B**. Due to this guarantee, **B** feels confident in awarding the contract to **A Ltd.** If **A Ltd.** fails to fulfil the

contract, **B** can recover the loss from the bank, ensuring financial protection.

Conclusion

Thus, a bank guarantee plays a vital role in modern trade and commerce by providing security and assurance of performance or payment, while remaining legally independent of the main contract.

2.5 Distinction between a contract of indemnity and a contract of guarantee.

Basis	Contract of Indemnity	Contract of Guarantee
Parties	Two parties	Three parties
Liability	Indemnifier's liability is primary	Surety's liability is secondary
Number of contracts	One contract	Three contracts
Purpose	To compensate loss	To secure debt
Example	Insurance contract	Bank guarantee

2.6 Contract of Insurance, Guarantee and Indemnity – Distinguished

Basis	Contract of Insurance	Contract of Guarantee	Contract of Indemnity
Meaning	A contract in which the insurer promises to compensate the insured for loss caused by specified risks	A contract to perform the promise or discharge the liability of a third person in case of his default	A contract in which one party promises to compensate the other for loss
Nature	Contract of indemnity, except life insurance	Contract of secondary liability	Contract of primary liability
Parties Involved	Two parties – insurer and insured	Three parties – surety, principal debtor and creditor	Two parties – indemnifier and indemnity holder

Basis	Contract of Insurance	Contract of Guarantee	Contract of Indemnity
Basis of Contract	Based on risk	Based on default of a third person	Based on loss suffered
Liability	Liability arises on occurrence of insured event	Liability arises only on default of principal debtor	Liability arises when loss occurs
Purpose	To protect against financial risk	To secure performance or payment	To compensate for loss
Consideration	Premium paid by insured	Consideration for benefit of principal debtor	Consideration for promise of indemnity
Example	Fire insurance, marine insurance	Bank guarantee	Contract of compensation

2.7 Continuing Guarantee (section 129)

Students often come across situations where a guarantee is not given for a single transaction but for a number of transactions over a period of time. Such guarantees are very common in business dealings, especially in credit sales and banking transactions. To understand this concept clearly, the Indian Contract Act introduces the idea of a continuing guarantee.

Students often come across situations where a guarantee is not given for a single transaction but for a number of transactions over a period of time. Such guarantees are very common in business dealings, especially in credit sales and banking transactions. To understand this concept clearly, the Indian Contract Act, 1872 introduces the idea of a continuing guarantee.

A continuing guarantee is a type of guarantee that extends to a series of transactions rather than a single transaction. It remains in force for all such transactions until it

is revoked by the surety or discharged by law. This makes it highly useful in business relationships where dealings occur regularly over time.

Such guarantees are commonly seen in cases where goods are supplied on credit continuously or where a bank allows an overdraft facility to a customer. Instead of giving a separate guarantee for each transaction, one continuing guarantee covers multiple dealings, making the process simple and efficient.

A continuing guarantee can be revoked by the surety at any time for future transactions by giving notice to the creditor. However, the surety remains liable for all transactions that took place before the revocation. This ensures fairness and protects the interests of the creditor.

From a practical and student-friendly perspective, understanding continuing guarantees helps in grasping how long-term business arrangements are secured. It shows how legal provisions support ongoing transactions while balancing the rights and liabilities of all parties involved.

Meaning and Explanation

A continuing guarantee is a type of guarantee which extends to a series of transactions rather than being limited to one specific deal. It remains effective for all transactions covered under it until it is legally revoked.

- It may relate to continuous supply of goods, repeated loans, or running accounts.
- The liability of the surety continues for each transaction until the guarantee is withdrawn.
- Each new transaction under the agreement is automatically covered by the same guarantee.

In addition, a continuing guarantee provides convenience and flexibility in business transactions where dealings are frequent and ongoing. Instead of executing a new guarantee for each transaction, one agreement is sufficient to cover multiple dealings, thereby saving time and effort for all parties involved. It is important to note that a continuing guarantee may be limited either by time or by the amount involved. For example, the surety may restrict the guarantee to transactions within a particular period or up to a specified monetary limit, beyond which the liability will not extend. From a practical point of view, continuing guarantees are widely used in trade and banking, especially in cases of credit sales and overdraft facilities. They help maintain smooth business relationships while ensuring that the creditor remains protected against default throughout the course of repeated transactions.

Example:

If A gives a guarantee to B for payment of all goods supplied on credit to C during a year, it is a continuing guarantee. The surety will be liable for every supply made during that period.

Features of Continuing Guarantee

- It covers more than one transaction.
- It continues to operate over a period of time.
- The surety's liability is ongoing but limited to the terms of the guarantee.
- It can be revoked for future transactions by giving proper notice.

Importance in Business

- It provides convenience in regular business dealings.
- It saves time and effort by avoiding the need for a fresh guarantee every time.

- It builds trust between parties involved in continuous transactions.

To sum up, a continuing guarantee plays an important role in commercial and banking practices where transactions occur frequently. It protects the creditor while allowing flexibility to the surety, as the guarantee can be revoked for future dealings. Understanding this concept helps students connect legal theory with real-life business situations.

2.8 Revocation of Continuing Guarantee (section 130)

A continuing guarantee does not last forever. The law gives the surety the right to withdraw from future liability when circumstances change. This process of ending a continuing guarantee is known as revocation of continuing guarantee, which students must clearly understand for both exams and practical application. Revocation of a continuing guarantee may take place by giving **notice to the creditor**. When the surety gives such notice, the guarantee comes to an end for all future transactions, but the surety remains liable for transactions that have already taken place before the notice was given.

A continuing guarantee may also be revoked by the **death of the surety**, unless there is a contract to the contrary. In such a case, the liability of the surety's legal representatives is limited to transactions that occurred before the death, and they are not liable for future transactions.

Further, a continuing guarantee can be discharged by **variation in the terms of the contract** between the creditor and the principal debtor without the consent of the surety. Any material change in the contract releases the surety from liability for subsequent transactions.

From a practical and student-friendly perspective, understanding revocation helps in knowing the limits of a surety's liability and the ways in which it can be terminated. It ensures that the surety is not bound indefinitely and can protect himself when the risk or circumstances change.

Meaning

Revocation of a continuing guarantee means cancellation of the guarantee for future transactions. It does not affect transactions that have already taken place. The surety remains liable for obligations incurred before revocation, but not for those arising afterward. Revocation of a continuing guarantee may take place by giving **notice to the creditor**. When the surety gives such notice, the guarantee comes to an end for all future transactions, but the surety remains liable for transactions that have already taken place before the notice was given.

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Modes of Revocation of Continuing Guarantee

A continuing guarantee may be revoked in the following ways:

1. By Notice of Revocation

- The surety may revoke the guarantee by giving clear notice to the creditor.
- Revocation is effective only for future transactions.
- Past transactions remain unaffected.

2. By Death of the Surety (section 131)

- The death of the surety automatically revokes the continuing guarantee for future dealings.
- The legal heirs of the surety are not liable for future transactions, unless there is a contract to the contrary.

3. By Variation in Terms of Contract

- Any material change in the terms of the contract without the consent of the surety revokes the guarantee.
- This is because such changes may increase the risk of the surety.

4. By Discharge of Principal Debtor

- If the principal debtor is discharged from liability, the continuing guarantee also comes to an end.

Here are some examples for students.

1. By Notice of Revocation

Example:

Suppose A gives a continuing guarantee to B for all goods supplied on credit to C. Later, A sends a notice to B stating that he will no longer be responsible for future transactions. After receiving the notice, if B supplies more goods to C, A will not be liable for those future supplies. However, A remains liable for goods supplied before the notice.

2. By Death of the Surety (Section 131 of the Indian Contract Act, 1872)

Example:

Suppose A gives a continuing guarantee to B for credit sales made to C. If A dies, the guarantee is automatically revoked for future transactions. If B continues to supply goods to C after A's death, A's legal heirs will not be liable for those transactions, unless there was an agreement stating otherwise.

3. By Variation in Terms of Contract

Example:

Suppose A guarantees that C will repay a loan taken from B under certain agreed terms. Later, B and C change the terms of the loan (for example, increase the loan amount or extend the repayment period) without informing A. In this case, A is discharged from liability because the contract terms were changed without his consent.

4. (Extension / Understanding – Increase of Risk due to Change)

Example:

Suppose A gives a guarantee for C's purchase of goods up to ₹50,000 from B. Later, B allows C to purchase goods worth ₹1,00,000 without informing A. This increases the risk of A without his consent, so the guarantee is revoked for such increased transactions, and A will not be liable beyond the agreed limit.

Effect of Revocation

- The surety is discharged from liability for future transactions only.
- The surety remains liable for all transactions made before revocation.

The revocation of a continuing guarantee releases the surety from liability for **future transactions only**, while maintaining responsibility for all transactions that took place before the revocation. This means the surety's obligation is divided into two parts — past and future. The law protects the creditor for earlier dealings but ensures that the surety is not bound indefinitely once the guarantee is revoked.

Example:

Suppose **A** gives a continuing guarantee to **B** for goods supplied on credit to **C**. If **A** revokes the guarantee on 1st July, then **A** will remain liable for all goods supplied to **C** before 1st July. However, for any goods supplied after that date, **A** will not be liable.

This principle ensures fairness by balancing the interests of both parties. The creditor is protected for transactions already made in reliance on the guarantee, while the surety is given the freedom to withdraw from future risks when circumstances change.

In conclusion, revocation of a continuing guarantee protects the surety from unlimited future liability while maintaining responsibility for past commitments. This balance ensures fairness and flexibility in long-term business and credit arrangements. For students, this concept is important to understand how law safeguards the interests of the surety in continuing obligations.

2.9 When Surety is Not Discharged

Many students believe that a surety is discharged as soon as the creditor delays action or shows leniency to the principal debtor. However, this understanding is not correct. The Indian Contract Act clearly mentions certain situations where, even

after delay or inaction by the creditor, the surety continues to remain liable. This concept is important because it protects the interests of the creditor and ensures stability in commercial transactions.

Meaning

A surety is not discharged when his responsibility under the contract of guarantee continues despite certain acts of the creditor or the principal debtor. In such cases, the surety cannot avoid liability and is still bound to fulfil the obligation if the principal debtor defaults. A surety is not discharged when his responsibility under the contract of guarantee continues despite certain acts of the creditor or the principal debtor. In such cases, the surety cannot avoid liability and is still bound to fulfil the obligation if the principal debtor defaults.

In some situations, the law specifically provides that the surety will continue to remain liable even if certain changes or events take place. For example, mere delay by the creditor in taking action against the principal debtor does not discharge the surety. The surety's obligation remains intact unless there is a clear legal ground for discharge.

According to Section 137 of the Indian Contract Act, 1872, mere forbearance (i.e., delay or inaction) on the part of the creditor to sue the principal debtor or to enforce any remedy against him does not discharge the surety. This means that the surety cannot claim discharge simply because the creditor has not taken immediate legal action.

Further, under Section 136, if the creditor enters into an agreement with a third person to give time to the principal debtor, it does not discharge the surety unless the surety's consent is required and not obtained. Thus, certain arrangements made by the creditor do not automatically release

the surety from liability. From a practical point of view, these provisions ensure that the surety cannot escape liability on minor or technical grounds. They help maintain the reliability of guarantees in business transactions and protect the interests of the creditor by ensuring that the surety remains responsible unless legally discharged under specific provisions.

Circumstances When Surety is Not Discharged

1. Mere Forbearance to Sue the Principal Debtor

- If the creditor does not immediately file a suit or take legal action against the principal debtor, the surety is not discharged.
- The creditor is not legally bound to take instant action after default.
- Mere patience or waiting does not affect the surety's liability.

Example:

If a creditor gives extra time to the debtor without entering into a formal agreement, the surety remains liable.

2. Mere Delay in Enforcing Rights

- Delay on the part of the creditor in recovering the debt does not discharge the surety.
- The surety cannot claim discharge simply because the creditor did not act promptly.
- The law assumes that delay alone does not increase the risk of the surety.

3. Loss Caused by Default of Principal Debtor

- If loss occurs due to the negligence or default of the principal debtor, the surety is not discharged.
- The surety's liability arises precisely because of such default.

- The surety cannot avoid responsibility by blaming the debtor's failure.

4. Non-material or Minor Variations in Contract

- Small or insignificant changes in the terms of the contract that do not increase the surety's risk do not discharge him.
- Only material changes made without the consent of the surety can lead to discharge.
- Minor procedural changes do not affect the validity of the guarantee.

5. Mere Inaction of the Creditor

- If the creditor does nothing for some time but does not release the debtor or alter the contract, the surety is not discharged.
- Inaction must be distinguished from a legal agreement giving time or altering terms.

Purpose of These Provisions

- These rules ensure that a guarantee remains effective and reliable.
- They prevent sureties from escaping liability on technical grounds.
- At the same time, they maintain fairness by discharging the surety only in genuine cases of increased risk.

In conclusion, a surety is not discharged merely because the creditor delays action, shows patience, or the principal debtor defaults. The law clearly protects the creditor by ensuring that the surety remains liable in such situations. For students, understanding these circumstances is essential to correctly answer examination questions and to appreciate the practical importance of guarantees in business and banking.

2.10 Exceptions – Invalid Guarantees

While a contract of guarantee is an important tool to protect the interests of creditors, the law also ensures that a surety is not unfairly bound by an invalid or dishonest agreement. Therefore, the Indian Contract Act, 1872 clearly provides certain exceptions where a guarantee becomes invalid or unenforceable. These provisions protect the surety from fraud, misrepresentation, and illegal agreements. For students, this topic is very important because questions on *invalid guarantees* are frequently asked in university examinations.

Meaning of Invalid Guarantee

An invalid guarantee is a guarantee which is not legally enforceable due to the absence of essential legal requirements or because it has been obtained by unfair means. In such cases, the surety is not liable, even if the principal debtor defaults. In simple terms, an invalid guarantee is one that fails to create a binding legal obligation on the surety. This may happen when the contract does not fulfil the basic essentials of a valid contract such as free consent, lawful consideration, or legality of object under the Indian Contract Act, 1872.

A guarantee may also become invalid if it is obtained by **misrepresentation, fraud, or concealment of material facts**. Since the surety agrees to take responsibility based on trust and full knowledge, any unfair practice affecting consent makes the guarantee void.

Further, if the **principal contract itself is invalid or illegal**, the guarantee automatically becomes invalid because the liability of the surety is dependent on the existence of a valid principal obligation.

From a student-friendly perspective, understanding invalid guarantees helps in identifying situations where a

surety is legally protected from liability. It also highlights the importance of fairness, transparency, and legality in forming contracts of guarantee.

Circumstances When a Guarantee Becomes Invalid

1. Guarantee Obtained by Misrepresentation

- A guarantee becomes invalid if it is obtained through misrepresentation by the creditor or with his knowledge.
- Misrepresentation means making a false statement of material facts or presenting incorrect information to the surety.
- If the surety gives consent based on wrong facts, the guarantee cannot be enforced.

Example:

If the creditor falsely tells the surety that the principal debtor is financially sound, when in reality he is insolvent, the guarantee becomes invalid.

2. Guarantee Obtained by Concealment of Material Facts

- A guarantee is invalid if the creditor intentionally conceals important facts from the surety.
- The creditor has a duty to disclose all facts that may affect the surety's risk.
- Concealment of material facts misleads the surety and destroys free consent.

Example:

If the creditor hides the fact that the principal debtor has already defaulted earlier, the surety is not bound by the guarantee.

3. Guarantee Obtained by Fraud

- If the guarantee is obtained by fraud, it is void.

- Fraud includes intentional deception, false promises, or dishonest practices to induce the surety to enter into the contract.
- Fraud directly affects the validity of consent.

Example:

Suppose **A** asks **C** to become a surety for a loan taken from **B**. **A** knowingly tells **C** that he has a strong financial position and no existing debts, even though he is already heavily indebted and unlikely to repay the loan. Relying on this false information, **C** agrees to give the guarantee. In this case, the guarantee is obtained by **fraud**, and therefore it is **invalid**. As a result, **C** (the surety) will not be liable to pay if **A** defaults.

4. Guarantee Without Free Consent

- Free consent of the surety is an essential element of a valid guarantee.
- If consent is obtained by:
    - Coercion
    - Undue influence
    - Fraud
    - Misrepresentation

  then the guarantee becomes invalid.
- A surety must clearly understand the nature and extent of liability before giving consent.

Example:

Suppose **A** forces **C** to become a surety for a loan taken from **B** by threatening him with harm. Due to this pressure (coercion), **C** agrees to give the guarantee. In this case, since **C's** consent was not free, the guarantee is **voidable**, and **C** can refuse to be liable if **A** defaults.

5. Guarantee for an Illegal or Unlawful Object

- A guarantee related to an illegal agreement is void.
- If the principal transaction itself is unlawful, the guarantee automatically becomes invalid.
- The law does not support agreements that are illegal or opposed to public policy.

Example:

A guarantee given for repayment of money borrowed for illegal gambling is invalid.

6. Guarantee Given Without Consideration

- Consideration is essential for a valid contract of guarantee.
- If there is no consideration, the guarantee becomes void.
- However, consideration need not move directly to the surety; benefit to the principal debtor is sufficient.

Example:

Suppose A asks C to give a guarantee for a loan from B, but B does not give any loan or benefit to A in return. Since there is no consideration involved in the transaction, the guarantee given by C is invalid, and C will not be liable.

7. Guarantee Given Under Mistake

- If the surety enters into the guarantee due to a mistake of fact, the contract may become invalid.
- Mistake must be material and should affect the foundation of the contract.

Example:

Suppose A asks C to give a guarantee for a loan from B, but B does not give any loan or benefit to A in return. Since there is no consideration involved in the transaction, the guarantee given by C is invalid, and C will not be liable.

8. Guarantee Contrary to Public Policy

- Any guarantee that is opposed to public policy is invalid.
- Agreements that promote corruption, illegal trade, or immoral activities are unenforceable.

Example:

Suppose A takes money from B to carry out an illegal activity such as bribery, and C gives a guarantee that he will repay the amount if A fails to do so. Since the purpose of the agreement is against public policy, the guarantee is void, and C (the surety) will not be liable**.**

Effect of Invalid Guarantee

- The surety is completely discharged from liability.
- The creditor cannot claim payment from the surety.
- The principal debtor alone remains responsible, if the principal contract is valid.

When a guarantee is invalid, it creates **no legal obligation** on the part of the surety. This means the surety is completely discharged from liability and cannot be compelled to pay the creditor, even if the principal debtor defaults. An invalid guarantee is treated as if it never existed in the eyes of law. Since the guarantee is not enforceable, the creditor cannot claim any amount from the surety. The creditor can proceed only against the principal debtor for recovery of the debt. Thus, the protection that a valid guarantee provides to the creditor is not available in such cases. Further, any rights that normally arise in a valid contract of guarantee, such as the right of subrogation or indemnity, do not come into existence because the contract itself is void. Therefore, the surety neither has obligations nor legal rights under an invalid guarantee.

From a practical and student-friendly perspective, understanding the effect of an invalid guarantee helps in identifying situations where a surety is protected from liability. It also emphasizes the importance of fulfilling all legal requirements while entering into a contract of guarantee under the Indian Contract Act, 1872.

Importance of These Exceptions

- These exceptions protect the surety from unfair exploitation.
- They ensure honesty and transparency in guarantee contracts.
- They maintain a balance between the rights of the creditor and the protection of the surety.

In conclusion, a guarantee is not always binding merely because it exists in writing. The Indian Contract Act provides several exceptions where a guarantee becomes invalid, especially when it is obtained through misrepresentation, concealment, fraud, lack of free consent, or illegal objectives. These provisions safeguard the surety against injustice and ensure fairness in commercial transactions. For students, understanding invalid guarantees is essential to correctly analyse problems and score well in examinations.

2.11 Rights of Surety

A surety undertakes a serious responsibility by guaranteeing the debt or obligation of another person. To ensure fairness, the Indian Contract Act, 1872 provides several rights to the surety. These rights protect the surety from unnecessary loss and enable him to recover the amount paid on behalf of the principal debtor. For students, understanding the rights of a surety is very important, as questions on this topic are commonly asked in university examinations.

Meaning of Rights of Surety

The rights of surety are the legal privileges given to the surety to safeguard his interests. These rights arise either before payment, at the time of payment, or after payment of the guaranteed amount. They help the surety recover losses and ensure that the burden of liability ultimately falls on the principal debtor.

A. Rights of Surety Against the Principal Debtor

1. Right of Subrogation

- After paying the debt of the principal debtor, the surety steps into the shoes of the creditor.
- This means the surety acquires all the rights which the creditor had against the principal debtor.
- The surety can sue the principal debtor to recover the amount paid.

Example:

If the creditor had the right to recover the debt by filing a suit, the surety can exercise the same right after payment.

2. Right to Indemnity

- There is an implied promise by the principal debtor to indemnify the surety.
- The surety can recover:
    - The amount paid to the creditor
    - Any lawful costs or expenses incurred
- This right arises only after the surety has made payment.

3. Right to Benefit of Securities

- The surety has a right to the benefit of all securities held by the creditor against the principal debtor.
- This right exists whether or not the surety was aware of such securities.

- If the creditor loses or parts with the securities, the surety is discharged to that extent.

B. Rights of Surety Against the Creditor

1. Right to Securities

- The surety is entitled to all securities that the creditor holds at the time the guarantee is given.
- This ensures that the surety's risk is reduced.

2. Right to Claim Discharge

- The surety can claim discharge if the creditor:
  - Makes a material alteration in the contract without consent
  - Releases the principal debtor
  - Acts in a way that impairs the surety's remedies

3. Right to Set-Off

- The surety can claim the benefit of any set-off which the principal debtor could have claimed against the creditor.

C. Rights of Surety Against Co-Sureties

1. Right to Contribution

- When two or more persons act as co-sureties for the same debt, they are liable to contribute equally.
- If one surety pays more than his share, he has the right to recover the excess from other co-sureties.
- Contribution depends on the maximum liability undertaken by each co-surety.

Example:

If three co-sureties guarantee ₹90,000 equally, each must bear ₹30,000.

2. Right in Case of Unequal Guarantees

- When co-sureties agree to bear different proportions, contribution is made according to the agreed shares.

- However, no co-surety can be made to pay more than the amount guaranteed by him.

Importance of Rights of Surety

- These rights protect the surety from financial hardship.
- They ensure that the ultimate burden lies on the principal debtor.
- They encourage people to act as sureties, which supports business and credit systems.

In conclusion, the Indian Contract Act provides comprehensive rights to the surety against the principal debtor, the creditor, and co-sureties. These rights ensure fairness, reduce risk, and prevent exploitation of the surety. For students, a clear understanding of the rights of surety is essential to answer problem-based and theoretical questions effectively in examinations.

2.12 Law as to Co-Sureties

In many practical business situations, a single surety may not be sufficient to guarantee a large debt or obligation. In such cases, two or more persons jointly give a guarantee for the same debt. These persons are known as co-sureties. The Indian Contract Act, 1872 lays down clear principles governing the rights, liabilities, and contribution among co-sureties. Understanding the law relating to co-sureties is important for students because it explains how responsibility is shared fairly and how the burden of payment is distributed when more than one surety is involved.

Meaning of Co-Sureties

Co-sureties are two or more persons who guarantee the same debt or obligation of the same principal debtor, either by the same contract or by separate contracts. The essential

feature is that all co-sureties are bound for the same liability, though the amount guaranteed by each may be equal or different.

Even if co-sureties sign separate guarantee agreements at different times, they are still treated as co-sureties if their guarantee relates to the same debt.

Nature of Liability of Co-Sureties

The liability of co-sureties is generally joint and several, unless otherwise agreed. This means the creditor has the right to recover the entire amount of debt from any one of the co-sureties. The creditor is not bound to divide the claim among all the co-sureties.

However, once payment is made, the paying surety gets the right to recover proportionate contributions from the other co-sureties. Thus, while the creditor enjoys full protection, fairness among co-sureties is ensured through the principle of contribution.

Principle of Equal Contribution

As a general rule, co-sureties are liable to contribute equally towards the debt, irrespective of whether they knew about the existence of other co-sureties or not. Equality is the foundation of contribution unless the contract provides otherwise.

For example, if three co-sureties guarantee a debt of ₹90,000 and one surety pays the full amount, each co-surety must ultimately bear ₹30,000. The paying surety can recover ₹60,000 from the remaining two co-sureties.

Contribution When Guarantees Are Unequal

Sometimes, co-sureties may agree to guarantee different maximum amounts. In such cases, contribution is not based on

equality but on the extent of liability undertaken by each co-surety.

However, an important legal rule applies here:

No co-surety can be made liable to pay more than the amount guaranteed by him.

For instance, if A guarantees ₹50,000, B guarantees ₹30,000, and C guarantees ₹20,000 for the same debt, their contribution will be adjusted according to these limits. If the total debt is ₹60,000, the burden will be shared proportionately but within their maximum guarantees.

Effect of Insolvency of a Co-Surety

If one of the co-sureties becomes insolvent and is unable to pay his share, the remaining solvent co-sureties must bear the loss equally among themselves.

The creditor does not suffer due to insolvency of a co-surety, as he can still recover the full amount from any solvent surety. The loss due to insolvency is ultimately shared by the remaining co-sureties.

Co-Sureties Bound by Different Contracts

Co-sureties may enter into separate contracts of guarantee at different times and on different terms. Even in such cases, they are considered co-sureties if they guarantee the same debt.

The law does not require that co-sureties must know each other or sign the same document. What matters is the common liability towards the same principal debt.

Release of One Co-Surety

If the creditor releases one co-surety from liability, the other co-sureties are not discharged. However, the released co-surety remains liable to contribute to the others, unless the

release was intended to discharge him completely from all liabilities.

This rule protects the interests of the remaining co-sureties and prevents unfair advantage to the released surety.

Rights of Co-Sureties Inter Se

Among themselves, co-sureties enjoy the right to mutual contribution. This ensures that no one surety bears more than his fair share of the burden.

This right arises only after payment has been made by one co-surety. Before payment, there is no question of contribution.

Importance of Law Relating to Co-Sureties

The law relating to co-sureties plays a vital role in:

- Ensuring fairness and equality among sureties
- Encouraging people to act as sureties without fear of excessive liability
- Providing strong security to creditors
- Maintaining balance between commercial convenience and individual protection

To conclude, the law as to co-sureties under the Indian Contract Act is based on the principles of equity, fairness, and justice. While the creditor is fully protected and can recover the entire debt from any one co-surety, the law ensures that the burden is ultimately shared fairly among all co-sureties. Understanding these provisions helps students clearly grasp how guarantees operate in real business situations and enables them to answer both theoretical and problem-based questions effectively in examinations.

2.13 Right of Surety Against Co-Surety

When more than one person stands as surety for the same debt, the law does not expect one person to bear the entire

burden alone. Fairness and equality form the foundation of the law relating to co-sureties. Therefore, the Indian Contract Act, 1872 provides the right of contribution, which allows a surety who has paid more than his share of the debt to recover the excess from other co-sureties. This right is known as the right of surety against co-surety and is extremely important for students to understand the practical working of guarantees.

Meaning of Right of Contribution

The right of surety against co-surety refers to the legal right of a surety to claim a proportionate share of payment from other co-sureties when he has paid more than his share of the guaranteed debt. This right is based on the principle that equality is equity.

This right arises only after payment has been made by one surety. Until payment, no surety can demand contribution from another.

Basis of the Right

The right of contribution is not based on contract alone but arises by operation of law. Even if there is no express agreement between co-sureties, the law assumes that they have undertaken a common burden and must share it fairly.

The creditor is free to recover the entire amount from any one surety, but the law ensures that this does not result in injustice among the co-sureties.

Extent of Contribution

As a general rule, co-sureties are liable to contribute equally towards the debt, irrespective of:

- Whether they knew each other or not
- Whether they signed the guarantee at the same time or separately

If three co-sureties guarantee a debt of ₹90,000 and one surety pays the entire amount, he is entitled to recover ₹30,000 each from the remaining two co-sureties.

Contribution When Maximum Liability Is Fixed

In many cases, co-sureties agree to guarantee different maximum amounts. In such situations, contribution is determined according to the maximum limit of liability undertaken by each surety.

However, an important rule applies here:

No co-surety can be compelled to pay more than the amount guaranteed by him, even if the total debt exceeds his share.

This rule protects co-sureties from excessive liability and ensures fairness.

Effect of Insolvency of a Co-Surety

If one co-surety becomes insolvent and is unable to pay his share, the loss caused by such insolvency is borne equally by the remaining solvent co-sureties.

The creditor does not suffer due to insolvency because he can recover the entire amount from any solvent surety. The burden of insolvency is adjusted only among the co-sureties themselves.

Right of Contribution in Case of Unequal Guarantees

Where co-sureties guarantee the same debt but for different amounts, contribution is adjusted proportionately, keeping in mind the maximum amount guaranteed by each co-surety.

This ensures that:

- No surety pays more than agreed
- The burden is distributed fairly

Release of One Co-Surety

If the creditor releases one co-surety from liability, the remaining co-sureties are not discharged. However, the released co-surety remains liable to contribute to the others, unless the release expressly frees him from all responsibility.

This provision prevents misuse of release by the creditor and protects the interests of the remaining sureties.

Right Arises Only After Payment

The right of contribution arises only when a surety has actually paid the debt or more than his share of it. A mere promise to pay or liability to pay does not give rise to this right.

This rule ensures that contribution claims are based on actual loss suffered.

Importance of Right of Contribution

The right of surety against co-surety plays an important role in:

- Preventing unfair financial burden on one surety
- Encouraging people to act as sureties without fear
- Promoting justice and equality
- Supporting smooth functioning of commercial transactions

To conclude, the right of surety against co-surety is based on the principles of fairness, equality, and justice. While the creditor is fully protected and may recover the entire debt from any one surety, the law ensures that the burden is ultimately shared proportionately among all co-sureties. For students, understanding this right is essential to grasp the real-life working of contracts of guarantee and to answer examination questions with confidence and clarity.

To understand this concept clearly, let us take some examples with amounts.

Numerical Illustrations: Right of Surety Against Co-Surety (for understanding purpose)

Illustration 1: Equal Contribution by Co-Sureties

A, B, and C become co-sureties for a loan of ₹90,000 taken by D. There is no agreement specifying separate limits of liability. On default by D, the creditor recovers the entire amount from A. Since there are three co-sureties and the guarantee is equal, each surety must ultimately bear one-third of the liability. Therefore, the share of each surety is ₹30,000. A has paid ₹90,000 but is liable only for ₹30,000. Hence, A has the right to recover ₹30,000 each from B and C. Thus, A can recover a total amount of ₹60,000 from his co-sureties.

Illustration 2: Contribution Where Maximum Liability Is Unequal

A, B, and C act as co-sureties for a loan of ₹60,000. A guarantees payment up to ₹30,000, B up to ₹20,000, and C up to ₹10,000. On default by the principal debtor, the creditor recovers the entire amount from A. Each co-surety is liable only up to the maximum amount guaranteed by him. Therefore, B must contribute ₹20,000 and C must contribute ₹10,000. A, having paid the full amount, can recover ₹30,000 from B and C together. A cannot claim more than the guaranteed limits of the co-sureties.

Illustration 3: Insolvency of One Co-Surety

A, B, and C are co-sureties for a debt of ₹90,000. Later, C becomes insolvent and is unable to contribute his share. The creditor recovers the entire amount from A. Normally, each co-surety would bear ₹30,000. Since C is insolvent, his share of ₹30,000 must be borne equally by the remaining solvent co-

sureties, A and B. Therefore, an additional burden of ₹15,000 each falls on A and B. As a result, A's total liability is ₹45,000. Since A has paid ₹90,000, he can recover ₹45,000 from B. The loss due to insolvency is thus shared equally between the solvent co-sureties.

Illustration 4: Co-Sureties Under Separate Contracts

A and B give separate guarantees at different times for the same loan of ₹40,000 taken by C. Even though the guarantees were given separately, both A and B are co-sureties for the same debt. On default by C, the creditor recovers the full amount from A. Since the liability is common, each surety must ultimately bear ₹20,000. Therefore, A can recover ₹20,000 from B by exercising his right of contribution.

Illustration 5: Right of Contribution Arises Only After Payment

A and B are co-sureties for a debt of ₹50,000. The creditor demands payment from A, but A has not yet paid the amount. Before making payment, A asks B to contribute his share. In this case, A has no right to claim contribution because the right of surety against co-surety arises only after actual payment has been made to the creditor. Until payment is made, no contribution can be claimed.

UNIT III

Contract of Bailment & Pledge

3.1 Bailment – Meaning and Definition

Bailment means giving goods to another person for a specific purpose, with the understanding that the goods will be returned after the purpose is completed or will be dealt with as instructed by the owner.

In simple words, when a person temporarily gives his goods to someone he trusts, and that person agrees to take care of them and return them later, it is called bailment.

According to the Indian Contract Act, 1872, a bailment arises when goods are delivered by one person to another on the basis of an agreement. The person who gives the goods is called the bailor, and the person who receives the goods is called the bailee. Only possession of goods is transferred, not ownership.

Example:

If A gives his laptop to B for repair and B agrees to return it after repairing, this is a bailment. A is the bailor and B is the bailee.

Thus, bailment is a common arrangement seen in daily life, such as giving clothes for dry cleaning, depositing goods in a warehouse, or lending a book to a friend for some time.

3.2 Essential Elements of Bailment

For a bailment to be valid, the following essential elements must be present:

1. Delivery of Goods

There must be a delivery of goods by the bailor to the bailee. Bailment is possible only for goods and not for money unless it is given in a specific form. The delivery may be actual or constructive.

2. Delivery for Some Purpose

The goods must be delivered for a specific purpose such as safe custody, repair, use, or security. Bailment does not exist if goods are delivered without any definite purpose.

3. Agreement Between the Parties

Bailment is based on an agreement between the bailor and the bailee. The agreement may be express or implied, but it must be made with the consent of both parties.

4. Return or Disposal of Goods

After the purpose of bailment is completed, the goods must be returned to the bailor or disposed of according to his directions.

5. Ownership is Not Transferred

In bailment, only possession of goods is transferred to the bailee. The ownership of goods always remains with the bailor.

3.3 Kinds of Bailment

Bailment can be of different types depending on the purpose and nature of the agreement between the parties. The main kinds of bailment are explained below:

1. Gratuitous Bailment

A gratuitous bailment is a bailment made without any reward or consideration. Either the bailor or the bailee does not receive any benefit. This type of bailment ends on the death of either party or when the agreed purpose is completed.

2. Non-Gratuitous Bailment

A non-gratuitous bailment is made for consideration, that is, both parties get some benefit. Examples include giving a car for repair or goods for transport on payment.

3. Bailment for Safe Custody (Deposit)

When goods are delivered to another person for safe keeping, it is called bailment for safe custody. For example, depositing jewellery in a bank locker.

4. Bailment for Use (Commodatum)

When goods are given to someone for use for a certain time and purpose and are to be returned after use, it is bailment for use. Example: lending a book to a friend.

5. Bailment for Finding Goods

A person who finds goods belonging to another and takes them into his possession becomes a bailee and has the rights and responsibilities of a bailee.

6. Bailment by Pledge

When goods are delivered as security for a loan or performance of a promise, it is called a pledge. It is a special kind of bailment.

3.4 Rights, Duties and Liabilities of Bailor

The bailor is the person who delivers the goods for bailment. The Indian Contract Act, 1872, lays down certain **duties, rights and liabilities** of the bailor to ensure fair dealing between the parties.

3.4.1. Rights of bailor

1. Right to Claim Compensation (Section 152)

The bailor has the right to claim compensation if the bailee does not take proper care of the goods. The bailee is expected to take the same care of the goods as a reasonable person would take of his own goods. If the bailee is careless or negligent and the goods are damaged or lost, the bailor can demand compensation for the loss suffered.

2. Right to Terminate the Contract (Section 153)

If the bailee uses the goods in a manner that is not agreed upon in the contract of bailment, the bailor has the right to terminate the bailment. Unauthorized use of goods gives the bailor the legal right to end the contract immediately.

3. Right to Compensation for Unauthorized Use (Section 154)

When the bailee uses the goods against the conditions of bailment or beyond the agreed purpose, the bailor can claim compensation for any loss or damage caused due to such misuse, even if the goods are otherwise returned safely.

4. Right When Goods Are Mixed (Sections 155–157)

Sometimes the bailee may mix the bailor's goods with his own goods.

- **With the consent of the bailor:** Both parties will share the mixed goods according to the agreement.
- **Without consent but goods are separable:** The bailee must bear the cost of separation and compensate the bailor for any damage caused.
- **Without consent and goods are not separable:** The bailee must compensate the bailor for the total loss of goods.

5. Right to Demand Return of Goods (Section 160)

After the purpose of bailment is completed or the agreed time period is over, the bailor has the right to demand the return of the goods from the bailee. If the bailee fails to return the goods, he becomes liable for any loss or damage.

6. Right to Any Increase or Profit from Goods (Section 163)

If the goods given in bailment produce any increase or profit during the period of bailment, such increase belongs to the bailor. For example, if a cow given in bailment gives birth to a calf, the calf also belongs to the bailor.

3.4.2. Duties of Bailor

The bailor is the person who gives goods to another person for bailment. The Indian Contract Act, 1872, imposes certain duties on the bailor to protect the interests of the bailee.

1. Duty to Disclose Defects (Section 150)

It is the duty of the bailor to inform the bailee about all known defects in the goods at the time of bailment. These defects may cause danger, loss, or injury to the bailee. If the

bailor fails to disclose such defects and the bailee suffers loss, the bailor must compensate the bailee.

In the case of bailment for hire, the bailor is responsible even if he did not know about the defect, because he is expected to ensure that the goods are safe for use.

Example:

If Suresh gives a horse for riding without informing that the horse is dangerous and the rider gets injured, Suresh will be liable for the injury caused.

2. Duty to Repay Necessary Expenses (Section 158)

In a gratuitous bailment, the bailee may incur necessary expenses to preserve or maintain the goods. In such cases, the bailor must repay all necessary and reasonable expenses incurred by the bailee.

This duty exists even though the bailment is made without any reward.

Example:

If Shyam agrees to take care of Mohan's dog free of cost and spends money on its food and shelter, Mohan must repay the expenses incurred by Shyam.

3. Duty to Pay Extraordinary Expenses

If the bailee incurs extraordinary expenses for the protection or preservation of the goods, the bailor must bear such expenses. Extraordinary expenses are those expenses which go beyond ordinary care.

Example:

If goods require special repair or medical treatment, the bailor must reimburse the bailee for such expenses.

4. Responsibility in Case of Early Return of Goods (Section 159)

When goods are given for a specific time or purpose, and the bailor takes them back before the agreed time or before the purpose is completed, the bailor must compensate the bailee for any loss caused due to such early return.

This rule applies mainly in gratuitous bailment, where sudden termination may cause inconvenience or financial loss to the bailee.

5. Duty to Indemnify the Bailee (Section 164)

If the bailor had no right to bail the goods and the bailee suffers any loss as a result, the bailor must indemnify the bailee. This protects the bailee from losses caused due to the bailor's defective title.

Example:

If a person bails goods which do not belong to him and the true owner claims them, the bailor must compensate the bailee for the loss suffered.

Conclusion

Thus, the bailor must act honestly and responsibly. Failure to perform these duties makes the bailor liable for compensation under the Indian Contract Act, 1872.

3.4.3. Liabilities of Bailor

Liabilities of Bailor

The bailor is legally responsible for certain losses suffered by the bailee. When the bailor fails to perform his duties properly, he becomes liable to compensate the bailee under the Indian Contract Act, 1872.

1. Liability for Non-Disclosure of Defects (Section 150)

The bailor is liable if he does not inform the bailee about known defects in the goods. If such defects cause loss, injury, or damage to the bailee, the bailor must compensate for it.

In the case of bailment for hire, the bailor is responsible even if he was unaware of the defect.

2. Liability to Bear Necessary Expenses (Section 158)

In a gratuitous bailment, if the bailee incurs necessary expenses for the preservation or maintenance of goods, the bailor is liable to repay those expenses. Failure to repay makes the bailor responsible for the loss suffered by the bailee.

3. Liability to Bear Extraordinary Expenses

If the bailee spends money on extraordinary expenses for the safety or protection of goods, the bailor is liable to reimburse such expenses. These expenses are beyond normal care and are necessary due to special circumstances.

4. Liability for Early Termination of Bailment (Section 159)

If goods are bailed for a fixed time or purpose and the bailor takes them back before completion, causing loss to the bailee, the bailor is liable to compensate the bailee for such loss.

5. Liability to Indemnify the Bailee (Section 164)

If the bailor does not have a valid right to bail the goods and the bailee suffers loss as a result, the bailor must indemnify the bailee. This includes losses caused due to defective title of the bailor.

6. Liability to Receive Back the Goods (Section 164 read with Section 160)

After the purpose of bailment is completed or the agreed time is over, the bailor must accept the goods back. If he refuses to do so and the bailee suffers loss, the bailor becomes liable for such loss.

Conclusion

Thus, the bailor is liable for losses caused due to his negligence, dishonesty, or failure to perform legal duties.

These liabilities ensure fairness and protect the interests of the bailee under the Indian Contract Act, 1872.

Confusion is very common among students, so let's clear it once and for all in a simple way.

Are Duties and Liabilities of Bailor the Same?

Short answer:

No, they are NOT the same, but they are **closely connected**.

Difference Explained in Easy Language

Duties of Bailor

- Duties are what the bailor is expected to do under the law.
- They are legal obligations that must be followed during bailment.

Example:

- Duty to disclose defects (Sec.150)
- Duty to repay expenses (Sec.158)

Think of duties as rules to follow.

Liabilities of Bailor

- Liabilities arise when the bailor fails to perform his duties.
- Liability means legal responsibility to pay compensation for loss or damage.

Example:

- If bailor hides defects → liability to compensate
- If bailor takes goods back early → liability under Sec.159

Think of liability as punishment or consequence of not following duties.

Simple Formula to Remember (Exam Tip)
Duty broken = Liability arises

Why Do Books Look Similar?

- In bailment, the same section creates both duty and liability.
- That's why:
    - Sections 150, 158, 159, 164 appear under both headings.
- But presentation changes:
    - *Duties* → what must be done
    - *Liabilities* → what happens if not done

How to Write in Exams

If the question is:

- **"Duties of Bailor"** → write obligations
- **"Liabilities of Bailor"** → write consequences + compensation
- **"Rights, Duties and Liabilities"** → you can merge them logically

3.5 Rights, Duties and Liabilities of Bailee

The bailee is the person who receives goods from the bailor for a specific purpose. The law lays down certain duties for the bailee, gives him certain rights, and makes him liable if he fails to perform his duties properly.

3.5.1.Duties of Bailee

1. Duty to Take Reasonable Care of Goods (Section 151)

The bailee must take the same care of the goods as a reasonable person would take of his own goods. If he fails to take proper care, he is responsible for any loss or damage.

2. Duty Not to Make Unauthorized Use of Goods (Section 154)

The bailee must use the goods only for the agreed purpose. If he uses them in a manner not agreed upon, he becomes liable for any loss caused.

3. Duty Not to Mix Bailor's Goods (Sections 155–157)

The bailee should not mix the bailor's goods with his own goods without consent. If he mixes them, he must bear the cost of separation or compensate the bailor if separation is not possible.

4. Duty to Return Goods on Completion of Purpose (Section 160)

After the purpose of bailment is completed or the agreed time is over, the bailee must return the goods to the bailor.

5. Duty to Return Accretions to Goods (Section 163)

If any increase or profit arises from the goods during bailment, the bailee must return such increase along with the goods.

3.5.2.Rights of Bailee

1. Right to Deliver Goods as per Bailor's Directions (Section 160)

The bailee has the right to deliver the goods according to the instructions given by the bailor. Once the purpose of bailment is completed or the agreed time period expires, the bailee must return the goods as directed by the bailor. If the bailor has given clear instructions regarding the manner, place, or person to whom the goods are to be delivered, the bailee is legally protected when he follows those instructions in good faith.

2. Right to Claim Necessary Expenses (Section 158)

The bailee has the right to claim reimbursement of all necessary expenses incurred by him for the preservation or maintenance of the goods. This right is especially important in the case of gratuitous bailment, where the bailee does not receive any reward. Necessary expenses include costs such as

storage, feeding of animals, or basic repairs required to keep the goods safe.

3. Right to Indemnity (Section 164)

The bailee has the right to be indemnified by the bailor for any loss suffered due to the bailor's defective title or wrong instructions. If the bailor had no authority to bail the goods or if the bailee suffers loss by acting according to the bailor's directions, the bailor must compensate the bailee. This right protects the bailee from losses that occur due to no fault of his own.

4. Right to Deliver Goods to Any One of Joint Bailors (Section 165)

When goods are delivered by two or more joint bailors, the bailee has the right to deliver the goods to any one of them, unless there is an agreement to the contrary. Delivery made in good faith to one joint bailor is considered valid, and the bailee is discharged from his responsibility.

5. Right to Deliver Goods on Bailor's Death (Section 166)

In the event of the death of the bailor, the bailee has the right to deliver the goods to the legal representatives of the bailor. Once delivery is made to the rightful legal heirs, the bailee is freed from further responsibility regarding the goods.

3.5.3.Liabilities of Bailee

The bailee is legally responsible for the safety and proper use of the goods entrusted to him. If the bailee fails to perform his duties or acts negligently, he becomes liable to compensate the bailor for any loss or damage caused.

1. Liability for Negligence (Section 151)

The bailee must take reasonable care of the goods as an ordinary person would take of his own goods. If the bailee fails

to take such care and the goods are damaged, destroyed, or lost, he is liable to compensate the bailor for the loss suffered.

2. Liability for Unauthorized Use of Goods (Section 154)

If the bailee uses the goods in a manner not agreed upon in the contract of bailment, he becomes responsible for any loss caused due to such misuse. Even if the loss occurs accidentally during unauthorized use, the bailee is liable.

3. Liability for Mixing Bailor's Goods (Sections 155–157)

If the bailee mixes the bailor's goods with his own goods without consent, his liability depends on the nature of mixing:

- If the goods can be separated, the bailee must bear the cost of separation and compensate for any damage.
- If the goods cannot be separated, the bailee must compensate the bailor for the total loss.

4. Liability for Failure to Return Goods (Section 160)

After the purpose of bailment is completed or the agreed time has expired, the bailee must return the goods to the bailor. If he fails to do so, he becomes liable for any loss or damage caused due to delay or non-return of goods.

5. Liability for Not Returning Accretions (Section 163)

If any increase or profit arises from the goods during bailment, the bailee must return such accretions to the bailor. Failure to return them makes the bailee liable.

6. Liability for Acting Against the Terms of Bailment

If the bailee acts contrary to the terms of the bailment contract, such as transferring goods to an unauthorized person, he becomes liable for any loss or damage suffered by the bailor.

Thus, the bailee is legally bound to act carefully and honestly. Any negligence, misuse, or failure to return goods results in legal liability, and the bailee must compensate the

bailor under the Indian Contract Act, 1872.

3.6 Lien – Meaning

A lien is the right of a person to keep possession of goods belonging to another person until a lawful claim is paid. It means the goods are not returned until the dues related to those goods are cleared.

In simple words, when someone has done some work on goods or has a legal claim against the owner, he can retain the goods as security until payment is made.

Under the Indian Contract Act, 1872, lien mainly arises in bailment and is recognized under Sections 170 and 171.

A lien does not give the right to sell the goods; it only gives the right to retain possession until the payment is made, unless there is a special contract.

Example:
If a tailor stitches clothes and the customer does not pay the charges; the tailor can keep the clothes until payment is received. This right is called lien.

3.7 General Lien

A general lien is the right of a person to retain goods belonging to another person for the payment of a general balance of account, and not just for charges related to those specific goods.

Under Section 171 of the Indian Contract Act, 1872, certain persons are given the right of general lien unless there is a contract to the contrary.

Persons who enjoy general lien include:

- Bankers
- Factors
- Wharfingers

- Attorneys of High Court
- Policy brokers

These persons can keep the goods of their customers until all dues owed by the customer are cleared, even if those dues are not directly related to the particular goods.

Example:
If a customer owes money to a bank, the bank can retain the customer's securities or goods in its possession until the entire outstanding balance is paid. This right of the bank is called general lien.
Thus, general lien is wider in scope than particular lien, as it covers the overall balance due and not only a specific charge.

3.8 Particular or Specific Lien

A particular lien, also called specific lien, is the right of a person to retain specific goods for the payment of charges related only to those goods. This right exists only when some skill or labour has been used on the goods.

This right is recognized under Section 170 of the Indian Contract Act, 1872. It applies when:

- The bailee has done some work on the goods, and
- Payment for that work is still due.

A particular lien is available to all bailees, unless there is a contract to the contrary. Unlike general lien, it is limited in nature and cannot be used for recovering a general balance of account.

Example:
If a mechanic repairs a bicycle and the owner does not pay the repair charges; the mechanic can keep that bicycle until the payment is made. This right is called a

particular or specific lien.
Thus, a particular lien is a narrow right, limited only to the goods on which work has been done and only for the charges related to that work.

3.9 Difference between Particular Lien and General Lien

The main points of difference between **Particular (Specific) Lien** and **General Lien** are explained below:

Basis	Particular (Specific) Lien	General Lien
Meaning	Right to retain specific goods for charges related to those goods only	Right to retain goods for a general balance of account
Legal Section	Section 170 of Indian Contract Act, 1872	Section 171 of Indian Contract Act, 1872
Scope	Limited in nature	Wider in nature
Availability	Available to all bailees	Available only to certain persons like bankers, factors, attorneys, etc.
Purpose	For payment of charges due on particular goods	For recovery of total dues
Relation to Goods	Charges must be connected with the same goods	Charges may not be related to the same goods
Example	A tailor keeping stitched clothes till stitching charges are paid	A bank retaining securities until all loans are cleared

3.10 Finder of Goods

A finder of goods is a person who finds goods belonging to another person and takes them into his possession. Although there is no contract between the owner and the finder, the law treats the finder as a bailee of the goods.

According to the Indian Contract Act, 1872, a finder of goods has the same rights and responsibilities as a bailee. This means the finder must take reasonable care of the goods and should not misuse them.

The finder has the right to keep the goods safely and can claim a reward if the owner has promised one. However, the finder cannot sue the owner for reward unless it was promised. The finder also has the right of lien, which means he can keep the goods until the reward is paid, if a reward was announced.

At the same time, the finder has certain duties. He must take proper care of the goods, should not mix them with his own goods, and must return them to the true owner when found. If the finder acts negligently or uses the goods for personal benefit, he will be responsible for any loss or damage.

Example:
If Ravi finds a lost wallet on the road and keeps it safely until the owner is found, Ravi is a finder of goods and is treated as a bailee under law.

3.11 Pledge – Meaning and Definition

A pledge is a special kind of bailment where goods are delivered as security for the repayment of a debt or for the performance of a promise.

According to Section 172 of the Indian Contract Act, 1872:

A pledge is the bailment of goods as security for the payment of a debt or performance of a promise.

The person who gives the goods as security is called the Pawnor, and the person who receives the goods is called the Pawnee.

In a pledge, only possession of goods is transferred, not ownership. The pawnee keeps the goods only as security and must return them once the debt is paid or the promise is fulfilled.

Pledge is very common in business and daily life, such as taking a loan by keeping gold, jewellery, or other valuables as security.

Example:
If Ramesh gives his gold chain to a bank as security for a loan, the transaction is called a pledge. Ramesh is the pawnor and the bank is the pawnee.

3.12 Essentials of Pledge (with Sections)

For a pledge to be valid, the following essential elements must be present as laid down in the Indian Contract Act, 1872:

1. Bailment of Goods (Section 172)

A pledge is a special type of bailment. Therefore, there must be a bailment of goods by the pawnor to the pawnee. Only goods can be pledged, not money.

2. Delivery of Goods (Sections 149 & 172)

There must be a delivery of goods from the pawnor to the pawnee. Delivery may be actual, constructive, or symbolic. Without delivery of possession, a pledge cannot be created.

3. Goods Delivered as Security (Section 172)

The goods must be delivered **as security**. The purpose of pledge is not transfer of ownership but to provide security for repayment of debt or performance of a promise.

4. Pledge for Payment of Debt or Performance of Promise (Section 172)

The pledge must be made to secure:

- payment of a debt, or
- performance of a promise.

5. Ownership Not Transferred (Section 176)

In a pledge, ownership of goods always remains with the pawnor. The pawnee has only the right to retain the goods until the debt is paid or promise is performed.

6. Parties to a Pledge (Section 172)

There must be two parties:

- **Pawnor** – person who gives the goods
- **Pawnee** – person who receives the goods as security

Thus, when goods are delivered as security for a debt or promise, with transfer of possession but not ownership, a valid pledge is created under Section 172 of the Indian Contract Act, 1872.

3.13 Pledge and Lien Distinguished

Both **pledge** and **lien** are rights related to goods, but they are different in nature and purpose. The main differences are explained below:

Basis	Pledge	Lien
Meaning	Bailment of goods as security for a debt or promise	Right to retain goods until payment of lawful charges
Legal Section	Section 172 of Indian Contract Act, 1872	Sections 170 & 171 of Indian Contract Act, 1872
Purpose	To provide security for repayment of debt or performance of promise	To recover charges due for services rendered

Basis	Pledge	Lien
Transfer of Possession	Possession of goods is transferred to pawnee	Possession is already with the person claiming lien
Right to Sell Goods	Pawnee can sell goods on default after giving notice (Section 176)	Person having lien has no right to sell, only right to retain goods
Nature of Right	A special kind of bailment	A legal right attached to possession
Example	Gold pledged to bank for loan	Tailor keeping clothes till stitching charges are paid

Conclusion
Thus, a pledge creates a security interest in goods with a right to sell on default, while a lien only allows retention of goods until payment is made, without any right of sale.

3.14 Pledge and Bailment Distinguished

A pledge is a special type of bailment, but both are different in purpose and scope. The main points of difference are explained below:

Basis	Bailment	Pledge
Meaning	Delivery of goods for some purpose upon a contract	Bailment of goods as security for a debt or promise
Legal Section	Section 148 of Indian Contract Act, 1872	Section 172 of Indian Contract Act, 1872
Purpose	Goods may be delivered for any purpose such as safe	Goods are delivered only as security

Basis	Bailment	Pledge
	custody, use, or repair	
Parties	Bailor and Bailee	Pawnor and Pawnee
Scope	Wide in nature	Limited and specific
Right to Sell Goods	Bailee generally has no right to sell goods	Pawnee has the right to sell goods on default (Section 176)
Nature	General concept	Special form of bailment
Example	Giving a watch for repair	Pledging gold for a loan

Conclusion
Thus, bailment is a broad concept covering various types of delivery of goods, while pledge is a specific form of bailment created only for security of debt or promise.

3.15 Rights of Pawnee

The pawnee is the person who receives goods as security in a contract of pledge. Since the pawnee gives a loan or accepts goods as security, the Indian Contract Act, 1872, grants him certain rights to protect his interest.

1. Right to Retain the Pledged Goods (Section 173)

The pawnee has the right to retain the pledged goods until the pawnor pays the full amount of the debt. This right also includes retention for:

- interest on the debt, and
- ordinary and necessary expenses incurred for the preservation of the goods.

This means the pawnee is not required to return the goods until all dues are completely cleared.

2. Right to Extraordinary Expenses (Section 175)

If the pawnee incurs extraordinary expenses to protect or preserve the pledged goods, such as special repairs or storage, he has the right to recover these expenses from the pawnor. These expenses are over and above ordinary care.

3. Right to Receive Necessary Expenses (Section 173)

Apart from the loan amount, the pawnee can retain the goods for payment of necessary expenses incurred in connection with the pledged goods. This ensures that the pawnee does not suffer any financial loss while safeguarding the goods.

4. Right to Sue the Pawnor and Retain the Goods (Section 176)

If the pawnor fails to repay the debt or perform the promise at the agreed time, the pawnee has the right to file a suit against the pawnor for recovery of the debt. Even after filing the suit, the pawnee can continue to keep the pledged goods as security until the matter is settled.

5. Right to Sell the Pledged Goods on Default (Section 176)

In case of default by the pawnor, the pawnee may sell the pledged goods after giving reasonable notice to the pawnor. If the sale proceeds are less than the debt, the pawnor must pay the remaining balance. If there is any excess amount after sale, it must be returned to the pawnor.

Conclusion

Thus, the rights of the pawnee ensure proper protection of his financial interest. These rights make the pledge a safe and reliable form of security under the Indian Contract Act, 1872.

3.16 Liabilities of Pawnee

The pawnee is the person who receives goods as security in a pledge. Along with rights, the law also imposes certain

liabilities on the pawnee. If the pawnee fails to follow these duties, he becomes responsible for loss or damage to the pledged goods.

1. Liability to Take Reasonable Care of Goods (Section 151)

The pawnee must take reasonable care of the pledged goods. He is expected to take the same care as an ordinary person would take of his own goods under similar circumstances.

If the goods are damaged or lost due to negligence of the pawnee, he will be liable to compensate the pawnor.

2. Liability Not to Make Unauthorized Use of Goods (Section 154)

The pawnee must use the pledged goods only for the purpose agreed upon. If he uses the goods in an unauthorized manner or for personal benefit, he becomes liable for any loss or damage caused, even if the loss occurs accidentally.

3. Liability Not to Mix Pawnor's Goods (Sections 155–157)

The pawnee should not mix the pawnor's goods with his own goods without consent.

- If goods are mixed with consent, both parties share the mixture as agreed.
- If goods are mixed without consent and can be separated, the pawnee must bear the cost of separation and compensate for damage.
- If goods are mixed without consent and cannot be separated, the pawnee must compensate the pawnor for total loss.

4. Liability to Return Goods After Payment (Section 177)

Once the pawnor pays the debt or performs the promise, the pawnee must return the pledged goods to the pawnor. If the

pawnee fails to return the goods, he will be liable for loss or damage caused due to such failure.

5. Liability to Return Accretions to Goods (Section 163)

If any increase or profit arises from the pledged goods during the period of pledge, the pawnee must return such accretions along with the goods. Failure to do so makes the pawnee liable.

Conclusion

Thus, the pawnee must act honestly, carefully, and according to the terms of pledge. Any negligence, misuse, or failure to return goods makes the pawnee legally liable under the Indian Contract Act, 1872.

3.17 Rights of Pawnor

The pawnor is the person who gives goods as security for a debt in a contract of pledge. Even though the goods are in the possession of the pawnee, the law protects the pawnor by giving him certain important rights under the Indian Contract Act, 1872.

1. Right to Redeem the Goods (Section 177)

The most important right of the pawnor is the right of redemption.The pawnor can redeem (take back) the pledged goods at any time before the actual sale of goods, even if the time fixed for repayment has expired.

To redeem the goods, the pawnor must pay:

- the principal debt,
- interest (if any), and
- necessary expenses incurred by the pawnee.

Example:

If Ramesh pledges gold to a bank and fails to pay on time, he can still redeem the gold before it is sold by paying the dues.

2. Right to Extraordinary Accretions (Section 163)

If any increase or profit arises from the pledged goods during the period of pledge, the pawnor has the right to receive such accretions.

Example:

If a cow is pledged and it gives birth to a calf, the calf also belongs to the pawnor and must be returned along with the cow.

3. Right to Receive Goods Back on Discharge of Debt (Section 176 & 177)

Once the pawnor pays the debt or performs the promise, the pawnee must return the pledged goods. If the pawnee fails to return the goods even after payment, he becomes liable for loss or damage.

4. Right to Receive Notice Before Sale (Section 176)

If the pawnor makes a default in payment, the pawnee has the right to sell the goods, but only after giving reasonable notice to the pawnor. This notice gives the pawnor a final chance to repay the debt and save his goods from sale.

5. Right to Excess Sale Proceeds (Section 176)

If the pledged goods are sold and the sale proceeds are more than the amount due, the excess amount must be returned to the pawnor. The pawnee cannot keep the extra money.

Conclusion

The rights of the pawnor ensure fairness and protect him from misuse of power by the pawnee. Even after default, the pawnor is given reasonable opportunities to recover his goods under the Indian Contract Act, 1872.

Unit IV

Law of Agency

4.1 Law of Agency

The Law of Agency is an important part of the Indian Contract Act, 1872 (Sections 182 to 238). It explains how one person can legally act on behalf of another person in business or other dealings.

In daily life and business, it is not always possible for a person to do everything personally. Therefore, the law allows a person to appoint someone else to represent him. This relationship is called agency.

In simple terms, agency means a relationship where one person (agent) works for another person (principal) and creates legal relations between the principal and third parties.

For example, if a shop owner sends his manager to purchase goods from a supplier, the manager acts as an agent and the shop owner is the principal. Any contract made by the manager within his authority will legally bind the shop owner.

The Law of Agency is important because:

- It makes business activities easier.
- It allows people to act through representatives.
- It clearly defines the rights, duties, and responsibilities of both parties.
- It protects third parties who deal with agents in good faith.

Thus, agency is a legal relationship that connects three parties — the principal, the agent, and the third party — and ensures smooth functioning of commercial transactions.

4.2 Appointment of Agent

Appointment of an agent means giving authority to a person to act on behalf of another person. Under the Indian Contract Act, 1872, an agency relationship is created when one person authorizes another person to represent him in dealings with third parties.

An agent can be appointed in different ways. The most common method is by agreement, which may be written or oral. A written appointment is often called a *Power of Attorney*. However, even a simple verbal instruction can create a valid agency relationship.

Agency may also arise through conduct of the parties. If a person behaves in a way that shows he has given authority to another, the law may treat it as a valid agency.

In some special situations, agency can arise:

- By **necessity**, when a person acts on behalf of another in an emergency to protect his interests.
- By **estoppel**, when a person's words or actions make others believe that someone is his agent.
- By **ratification**, when a person later approves an act done on his behalf without prior authority.

No special form is required to appoint an agent. The important point is that the principal must give authority and the agent must agree to act on his behalf.

Thus, appointment of an agent makes business transactions smooth and allows one person to legally represent another.

4.3 Who is an Agent and a Principal

Under the Indian Contract Act, 1872, an agent is a person who is employed to do any act for another person or to represent another person in dealings with third parties. The person who gives such authority is called the principal.

In simple words, the agent acts on behalf of the principal. The agent does not act for himself but represents the principal in business transactions or contracts.

For example, if A asks B to sell his house and B agrees to do so, B becomes the agent and A becomes the principal. If B sells the house within his authority, A will be legally bound by that sale.

The important feature of this relationship is that the acts of the agent, done within the scope of authority, are treated as the acts of the principal. This means the principal is responsible for the agent's actions when they are properly authorized.

Thus, in an agency relationship:

- The principal gives authority.
- The agent uses that authority to act.
- The contract is created between the principal and the third party.

This relationship helps in carrying out business smoothly when the principal cannot personally handle all transactions.

4.4 Who Can Appoint an Agent

Under the Indian Contract Act, 1872, any person who is competent to contract can appoint an agent. This means the person must:

- Be of the age of majority
- Be of sound mind
- Not be disqualified by any law

Since agency creates legal obligations, only a person who has the legal capacity to enter into a contract can appoint someone else to act on his behalf.

For example, a major person who is mentally sound can appoint an agent to sell property or purchase goods. However, a minor cannot appoint an agent because he himself is not legally capable of entering into a binding contract.

The principal must also have the legal right to do the act which he wants the agent to perform. A person cannot appoint an agent to do something that is illegal.

Therefore, only a legally competent person can appoint an agent, and the appointment must be for lawful purposes.

4.5 Who Can Be an Agent

According to the Indian Contract Act, 1872, any person can become an agent. Even a minor or a person of unsound mind can act as an agent.

The reason is that an agent only creates a contract between the principal and the third party. The agent himself is generally not personally responsible for the contract made on behalf of the principal. Therefore, even a person who is not competent to contract can be appointed as an agent.

For example, a minor can be appointed as an agent to deliver goods or collect payments on behalf of the principal.

However, although a minor can act as an agent, he cannot be held personally liable to the principal for his actions. The responsibility mainly lies with the principal.

Thus, while only a competent person can appoint an agent, any person can become an agent, because the agent mainly represents the principal in dealings with third parties.

Under Section 184, any person can become an agent, but only a person competent to contract can appoint an agent (as per Section 183).

4.6 Test of Agency

The test of agency helps to determine whether the relationship between two persons is that of principal and agent. In simple words, it checks whether one person is legally acting on behalf of another.

The main test of agency is the existence of authority. If one person has the power to create legal relations between another person and a third party, then an agency relationship exists.

This principle is supported by the following provisions of the Indian Contract Act, 1872:

Section 182 defines an agent as a person employed to do any act for another or to represent another in dealings with third persons. This shows that representation is the core element of agency.

Section 186 states that the authority of an agent may be express or implied.

Section 187 explains that express authority is given by spoken or written words, while implied authority is inferred from the conduct of the parties or the circumstances of the case.

Section 188 provides that an agent having authority to do an act has authority to do every lawful thing necessary to complete that act.

From these sections, it is clear that the real test of agency is:

- Whether the person has authority to act on behalf of another, and
- Whether he can legally bind the principal by his acts.

It is not necessary that the parties use the words "agent" or "principal." Even if these terms are not used, if a person has authority to represent and bind another, the law will treat the relationship as one of agency.

For example, if a shop manager regularly purchases goods on behalf of the owner and the owner is legally bound by those purchases, the manager is considered an agent.

Thus, the true test of agency is the authority to represent another person and create legal obligations on his behalf, as recognized under Sections 182, 186, 187, and 188 of the Indian Contract Act, 1872.

4.7 How Agency is Constituted

The Law of Agency is governed by Sections 182 to 238 of the Indian Contract Act, 1872. Agency is created when one person gives authority to another to act on his behalf.

Agency may be constituted in the following ways:

1. By Agreement (Sections 186 & 187)

According to Section 186, the authority of an agent may be expressed or implied.

Section 187 explains that authority is said to be express when it is given by words spoken or written, and implied when it is inferred from the conduct of the parties or circumstances of the case.

2. By Ratification (Sections 196 to 200)

Under Section 196, when a person does an act on behalf of another without authority, and the other person later approves it, the act is said to be ratified. After ratification, the act becomes binding as if authority was originally given.

3. By Necessity (Section 189)

Section 189 states that an agent has authority in an emergency to do all such acts as a person of ordinary prudence would do to protect the principal from loss.

4. By Estoppel (Section 237)

If a principal, by his words or conduct, makes a third party believe that a person is his agent, he cannot later deny the agency. This is known as agency by estoppel.

Thus, agency can be created either by agreement between parties or by operation of law under specific sections of the Indian Contract Act.

4.8 Ratification

Ratification means approval of an act that has already been done. In the law of agency, ratification happens when a person does something on behalf of another person without having proper authority, and later the other person accepts or approves that act.

The rules relating to ratification are given under Sections 196 to 200 of the Indian Contract Act, 1872.

According to Section 196, when a person does an act for another without authority, the person on whose behalf the act was done can either reject it or approve it. If he approves it, the act becomes valid from the beginning. This means it is treated as if the authority was given earlier.

For ratification to be valid, certain conditions must be satisfied:

- The act must have been done on behalf of the principal.
- The principal must be in existence at the time of the act.
- The principal must have full knowledge of all material facts before approving the act (Section 198).
- The act must be lawful and capable of being ratified.
- The whole transaction must be ratified, not just a part of it (Section 199).

If these conditions are fulfilled, ratification makes the act binding on the principal as if he had originally authorized it.

For example, if A purchases goods in the name of B without B's permission, B can later approve the purchase. Once B approves it, he becomes legally bound to pay for the goods.

Thus, ratification allows a principal to accept and validate an unauthorized act done on his behalf, provided the legal requirements are satisfied.

Example:
A purchases 50 chairs from a supplier in the name of B without B's permission. When B comes to know about the purchase, he approves the transaction and agrees to pay the price.
In this case, B's approval is called ratification. After ratification, the purchase becomes legally binding on B as if he had originally given authority to A to buy the chairs.

4.9 Rules Governing Ratification

The rules relating to ratification are given under Sections 196 to 200 of the Indian Contract Act, 1872. Ratification is valid only when certain legal conditions are fulfilled.

The important rules are as follows:

Ratification must be done by a person who was in existence at the time when the act was done. A person cannot ratify an act done before he came into existence.

The act must have been done on behalf of the principal. If a person acts in his own name and not on behalf of someone else, the act cannot be ratified later.

The principal must have full knowledge of all important facts before ratifying the act. According to Section 198, ratification is not valid if it is made without knowledge of material facts.

Ratification must be of the whole transaction. As stated in Section 199, a principal cannot approve one part of the act and reject the rest.

The act ratified must be lawful. An illegal or void act cannot be made valid by ratification.

Ratification should not cause injury to a third party. According to Section 200, ratification cannot be used to harm the rights of a third person.

When all these rules are satisfied, ratification makes the act binding on the principal as if authority had been given from the beginning.

4.10 Classification of Agents

Agents can be classified into different types based on the nature of their authority and the work they perform. The classification helps in understanding the scope of their powers and responsibilities.

A Special Agent is appointed for a specific task or a particular transaction. His authority is limited to that work only. Once the work is completed, his authority ends.

A General Agent is appointed to carry out a series of transactions or to conduct business on behalf of the principal. His authority is broader than that of a special agent.

A Universal Agent has wide authority to act on behalf of the principal in all matters, except those that are personal in nature or restricted by law.

There are also some commercial or mercantile agents, such as brokers, factors, auctioneers, and del credere agents, who are commonly appointed in business transactions.

Thus, agents are classified based on the extent of their authority and the type of work they perform for the principal.

Special Agent – Example:
A appoints B to sell his car only. B's authority is limited to selling that car. Once the car is sold, B's authority ends.

General Agent – Example:
A shop owner appoints a manager to handle daily purchases and sales of the shop. The manager can enter into regular business transactions on behalf of the owner.

Universal Agent – Example:
A person going abroad gives full authority to his trusted friend to manage all his property, bank accounts, and business matters. This is an example of a universal agent.

These examples show how agents differ based on the extent of authority given by the principal.

4.11 Sub-Agent

1. Introduction

In the law of agency, an agent is appointed by the principal to perform certain acts on his behalf. However, in

practical situations, the agent may not always be able to do all the work alone. In such cases, the agent may appoint another person to assist him — this person is called a sub-agent.

The concept of sub-agent helps in carrying out work efficiently, especially when the task is large, complex, or requires multiple people.

2. Meaning of Sub-Agent

A sub-agent is a person who is appointed by the original agent and works under his control to help in performing the duties of agency.

In simple words:

A sub-agent is the "agent of an agent," not directly of the principal.

3. Legal Definition (Simplified)

According to the Indian Contract Act, 1872, a sub-agent is a person employed by and acting under the control of the original agent in the business of the agency.

4. Appointment of Sub-Agent

A sub-agent can be appointed in the following situations:

a) When Expressly Allowed

If the principal clearly permits the agent to appoint a sub-agent.

b) When Impliedly Allowed

When the nature of work requires assistance (e.g., large-scale business operations).

c) In Emergency Situations

When immediate action is required to protect the principal's interest.

5. Types of Sub-Agent

1) Properly Appointed Sub-Agent

This is when the sub-agent is appointed with authority (express or implied) of the principal.

Effects:

- The principal is bound by the acts of the sub-agent
- The sub-agent is indirectly responsible to the principal
- The agent is responsible to the principal for sub-agent's conduct

2) Improperly Appointed Sub-Agent

This happens when the agent appoints a sub-agent without authority.

Effects:

- The principal is not bound by sub-agent's acts
- The agent becomes personally responsible
- No direct relationship between principal and sub-agent

6. Relationship Between Parties

a) Principal and Sub-Agent

- No direct relationship (in improper appointment)
- Indirect relationship (in proper appointment)

b) Agent and Sub-Agent

- Sub-agent works under the control of agent
- Agent is responsible for sub-agent's acts

7. Duties of a Sub-Agent

A sub-agent must:

- Act honestly and in good faith
- Follow instructions of the agent
- Avoid negligence
- Protect the interest of the principal

8. Rights of a Sub-Agent

- Right to remuneration from the agent
- Right to protection for lawful acts
- Right to claim compensation for work done

9. Illustrative Examples

Example 1: Proper Appointment

A appoints B to manage a construction project. B hires C (an engineer) to assist.

Since the work requires expertise, C is a properly appointed sub-agent.

A (principal) is bound by C's work.

Example 2: Improper Appointment

A appoints B to sell his car. B appoints C without permission.

If C makes a mistake, A is not responsible.

B will be personally liable.

Example 3: Business Scenario

A company appoints a manager (agent). The manager appoints supervisors (sub-agents).

This is valid because large businesses require delegation.

10. Difference Between Agent and Sub-Agent

Basis	Agent	Sub-Agent
Appointment	Appointed by principal	Appointed by agent
Control	Works under principal	Works under agent
Relationship	Direct with principal	Usually, indirect
Responsibility	Directly liable to principal	Liable through agent

11. Importance of Sub-Agent

- Helps in handling large work
- Saves time and effort

- Brings specialization and expertise
- Makes business operations smooth

The concept of sub-agent is very important in modern business where work is complex and cannot be handled by a single person. However, the appointment of a sub-agent must be done carefully and with proper authority.

In simple terms, a sub-agent is useful, but if appointed wrongly, it can create legal problems for the agent.

4.12 Relationship between Principal and Agent

1. Introduction

In the law of agency, the relationship between the principal and the agent is very important because it forms the base of all business transactions done through representatives.

This relationship is based on trust, confidence, and mutual understanding. The agent acts on behalf of the principal, and whatever the agent does within his authority is treated as if the principal himself has done it.

In simple words:

"Agent ka act = Principal ka act" (Agent's act is considered the principal's act)

2. Meaning of Principal and Agent

- **Principal**: The person who appoints another person to act on his behalf
- **Agent**: The person who acts for the principal and represents him in dealings with third parties

A principal is a person who appoints another person to act on his behalf, while an agent is the person who performs such acts and represents the principal in dealings with third parties. The most important thing to understand here is that the agent does not act for himself. He acts on behalf of the principal and therefore his actions directly affect the principal.

For example, if a shop owner in Pune sends his employee to purchase goods from a wholesaler, the employee acts as an agent. The contract is actually between the shop owner and the wholesaler, even though the employee carried out the transaction.

3. Nature of Relationship (Fiduciary Relationship)

The relationship between principal and agent is known as a fiduciary relationship, which simply means a relationship based on trust and confidence.

The principal trusts the agent to act honestly and carefully, while the agent is expected to work in the best interest of the principal. Because of this trust, the agent must not misuse his position or take any personal advantage.

For instance, if an agent is asked to sell goods at the best possible price, he should not secretly sell them at a lower price just to benefit a friend. Doing so would be a breach of trust.

Key Features:

- High level of trust
- Honesty is compulsory
- No misuse of authority
- Agent must act in the best interest of principal

4. Creation of Relationship

This relationship can arise in different ways, not always through a formal written contract.

In many cases, it is created simply by agreement between the parties. For example, a person may appoint a property broker to sell his house. Sometimes, even without a clear agreement, the conduct of the parties may show that such a relationship exists. In certain situations, the law itself creates agency out of necessity. For example, if perishable goods are

likely to spoil, a person in charge may sell them to prevent loss, even without express permission.

There are also cases where an act is done without authority but is later approved by the principal. This approval is called ratification, and it creates a valid agency relationship. The relationship between principal and agent can be created in the following ways:

1) By Agreement

When both parties mutually agree (express or implied)

Example

A shop owner in Pune appoints a salesperson to sell goods → agency created by agreement

2) By Conduct

When actions of parties show existence of agency

Example:

A allows B to regularly buy goods on his behalf → agency created by conduct

3) By Necessity

In emergency situations to protect interests

Example:

A transport company delays goods due to rain, and the driver sells perishable goods to avoid loss

4) By Ratification

When principal later approves agent's act

Example:

B buys goods without authority, A later approves → valid agency

5. Legal Position of Agent

An agent acts as a representative or bridge between the principal and third parties. He does not become personally involved in the contract if he acts within his authority.

This means that the rights and obligations created through the agent's actions belong to the principal. For example, if an agent purchases goods for the principal, the payment responsibility lies with the principal, not the agent.

- Agent represents the principal
- Agent does not act in personal capacity
- Contract is between principal and third party

So, the agent becomes a link or bridge between principal and third party

6. Rights of Agent Against Principal

The agent has certain rights to protect his interests:

1) Right to Remuneration

Agent has right to receive agreed commission or payment

Example:

A property broker in Mumbai gets commission after sale

2) Right of Lien

Agent can retain goods until payment is made

Example:

A transporter holds goods until transport charges are paid

3) Right of Indemnity

Agent can claim compensation for lawful acts

Example:

If agent suffers loss while following instructions, principal must compensate

7. Duties of Agent Towards Principal

In a contract of agency, the agent is trusted by the principal to act on his behalf. Because of this trust, the law imposes certain duties on the agent. These duties ensure that the agent works honestly, carefully, and in the best interest of the principal.

If the agent fails to perform these duties, he can be held legally responsible for any loss caused to the principal.

1) Duty to Follow Instructions

One of the most important duties of an agent is to strictly follow the instructions given by the principal. The agent must act according to the directions provided and should not deviate from them without permission.

If the agent ignores or disobeys instructions and causes loss, he will be personally liable for that loss.

Explanation:

The principal appoints the agent with a specific purpose in mind. Therefore, it is necessary that the agent respects those instructions and carries out the work accordingly.

Example

A cloth merchant in Surat instructs his agent to sell fabric at not less than ₹500 per meter. If the agent sells it at ₹400 without permission, he must bear the loss of ₹100 per meter.

2) Duty of Care and Skill

The agent must perform his work with reasonable care, skill, and diligence. This means that the agent should act as a careful and sensible person would act in similar circumstances. He is not expected to be perfect, but he must not be careless or negligent.

Explanation:

If the agent lacks skill or acts carelessly, it may result in financial loss to the principal. In such cases, the agent will be responsible.

Example

A transport agent is entrusted with delivering goods safely from Pune to Mumbai. If he handles the goods carelessly and they get damaged, he will be liable for the loss.

3) Duty of Good Faith (Honesty and Loyalty)

The agent must act in good faith, which means he must be honest, loyal, and act only in the interest of the principal. He should not make any secret profit or misuse his position for personal benefit.

Explanation:

Since the relationship is based on trust, any dishonest act by the agent is considered a serious breach of duty.

Example

A property agent is asked to sell land for ₹10 lakh. If he secretly sells it for ₹12 lakh and keeps ₹2 lakh for himself, he is violating his duty of good faith and must return the extra profit to the principal.

4) Duty to Render Accounts

The agent must maintain proper accounts of all transactions carried out on behalf of the principal. He should keep clear and accurate records and present them whenever required.

Explanation:

This duty ensures transparency and allows the principal to check how the agent has handled the business.

Example

A shop owner sends his employee (agent) to purchase goods from the wholesale market. The employee must keep bills, receipts, and records of expenses. If he fails to provide proper accounts, he may be held responsible.

The duties of an agent towards the principal are essential for maintaining trust and smooth functioning of the agency relationship. These duties ensure that the agent acts responsibly, honestly, and carefully.

In simple terms, the agent must always remember that he is working on behalf of someone else, and therefore, he must protect the interests of the principal at all times.

8. Duties of Principal Towards Agent

Just like the agent has duties towards the principal, the principal also has certain important duties towards the agent. The relationship of agency is based on mutual trust and fairness, so both parties must act responsibly.

If the principal fails to perform his duties, the agent has the right to claim compensation or take legal action.

1) Duty to Pay Remuneration

The principal is bound to pay the agreed remuneration or commission to the agent for the work done. This payment may be fixed, commission-based, or a combination of both.

The agent becomes entitled to remuneration once he has completed the work or fulfilled his part of the contract.

Explanation:

The agent works on behalf of the principal, so it is only fair that he is properly compensated for his efforts.

Example:

A property broker in Pune successfully finds a buyer for a flat. Once the deal is completed, the owner must pay the agreed brokerage. If he refuses, the broker can claim it legally.

2) Duty to Indemnify the Agent

The principal must compensate (indemnify) the agent for all lawful acts done by the agent in the course of agency.

This means if the agent suffers any loss while following lawful instructions, the principal must bear that loss.

Explanation:

Since the agent acts on behalf of the principal, any lawful consequences of those actions should be the responsibility of the principal.

Example:

A sends his agent to purchase goods. Due to market conditions, the price increases suddenly, and the agent has to pay more. The principal must reimburse the extra amount.

3) Duty to Compensate for Agent's Injury

If the agent suffers any injury or loss due to the principal's neglect or lack of care, the principal is responsible for compensating the agent.

Explanation:

The principal must ensure that the working conditions or instructions given to the agent do not cause harm.

Example:

A warehouse owner asks his agent to handle goods in an unsafe storage area. If the agent gets injured due to poor conditions, the principal must compensate him.

4) Duty to Act in Good Faith

The principal must deal with the agent honestly and fairly. He should not mislead, cheat, or hide important information from the agent.

Explanation:

Since the agent depends on the principal's instructions and information, any dishonesty from the principal can harm the agent.

Example :

If a principal hides important details about a defective product and asks the agent to sell it, the agent may suffer loss

or legal trouble. The principal will be responsible for such consequences.

5) Duty Not to Prevent the Agent from Earning Remuneration

The principal should not interfere in a way that prevents the agent from earning his commission or completing his work.

Explanation:

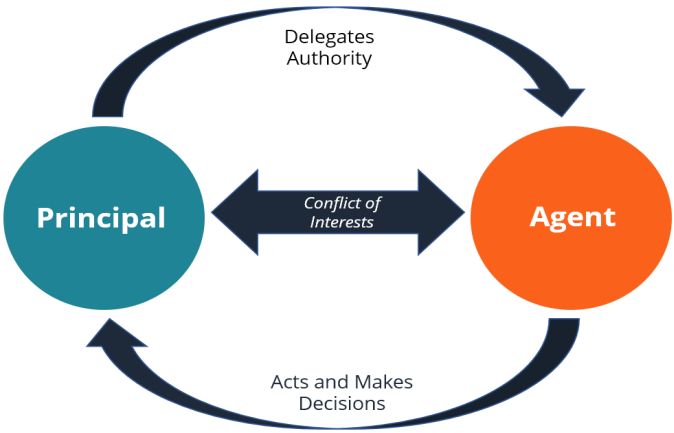
If the agent has already started working and the principal unfairly stops him, the agent may still be entitled to remuneration.

Example :

A appoints a broker to sell his shop but later cancels the deal after the broker has already found a buyer. In such a case, the broker may still claim his commission.

The duties of the principal towards the agent are essential to maintain fairness and balance in the agency relationship. Just as the agent must act honestly and carefully, the principal must also act responsibly and support the agent.

In simple terms, the principal should treat the agent fairly, pay him properly, and protect him from loss when he acts on the principal's behalf.



9. Liability in Agency Relationship

In a contract of agency, the concept of liability is very important because it determines who is legally responsible for the acts done by the agent. Since the agent acts on behalf of the principal, the law generally treats the acts of the agent as the acts of the principal.

However, this is not always the case. Liability depends on whether the agent has acted within his authority, outside his authority, or in a wrongful manner.

General Rule of Liability

The basic rule in agency is simple:

"Acts of the agent = Acts of the principal (if done within authority)"

This means that when an agent acts within the limits of his authority, the principal becomes liable to third parties for those acts.

1) Liability of Principal

The principal is mainly liable in the following situations:

When Agent Acts Within Authority

If the agent performs an act within the scope of his authority, the principal is bound by that act.

Explanation:

The agent represents the principal, so any lawful act done within authority creates rights and obligations for the principal.

Example: :

A appoints B to purchase goods worth ₹50,000. B purchases the goods as instructed. A (principal) is liable to pay the seller.

When Agent Acts in Emergency

In certain emergency situations, even if there is no prior authority, the principal may still be liable.

Example:

A transport agent sells perishable goods to prevent loss during delay.

The principal is bound by such action.

When Principal Ratifies the Act

If the agent acts without authority but the principal later approves (ratifies) the act, the principal becomes liable**.**

Example:

B buys goods without permission, but A later approves the purchase.

A becomes liable.

2) Liability of Agent

Although the agent usually does not become personally liable, there are certain situations where he is responsible:

When Agent Exceeds Authority

If the agent goes beyond the authority given, he becomes personally liable for that part.

Example :

A allows B to buy goods worth ₹50,000. B buys goods worth ₹1,00,000.

A is liable only up to ₹50,000, and B is liable for the excess.

When Agent Acts Without Authority

If the agent acts without any authority and the principal does not approve, the agent is personally liable.

When Agent Acts Fraudulently or Negligently

If the agent commits fraud or acts carelessly, he is responsible for the loss caused.

Example:

An agent sells defective goods by hiding facts → agent is liable.

When Agent Acts in His Own Name

If the agent does not disclose that he is acting for a principal, he may become personally liable.

3) Liability of Both Principal and Agent

In some situations, both the principal and agent can be held liable.

Case of Undisclosed Principal

When the third party does not know about the principal, both agent and principal may be liable.

Example :

Agent purchases goods without revealing the principal's identity.

The seller can sue either the agent or the principal.

4) Liability Towards Third Parties

The relationship between principal, agent, and third party is very important:

- The contract is mainly between principal and third party
- The agent acts only as a connecting link
- The third party can hold the principal responsible if the agent acted properly

5) Important Points to Remember

- Authority of agent determines liability
- Principal is liable for lawful acts within authority
- Agent is liable for wrongful or unauthorized acts
- Ratification can shift liability to principal

Liability in an agency relationship ensures that responsibility is clearly defined between the principal and the

agent. The general rule is that the principal is liable for the acts of the agent, but only when those acts are within authority and done properly. In simple terms, the law tries to balance fairness by protecting both the principal and the third party, while also holding the agent accountable for any misuse of authority.

10. Examples (Easy to Understand)

Example 1: Real Estate

A appoints B as a broker to sell his flat in Pune

If B sells it, agreement is between A and buyer

Example 2: Online Business

A seller on Flipkart appoints delivery partner

Delivery partner acts as agent

Example 3: Banking

Customer authorizes bank employee to process transaction

Employee acts as agent

Example 4: Shop Scenario

Shop owner sends employee to purchase goods from wholesaler

Employee is agent

11. Importance of Relationship

- Helps in smooth business operations
- Saves time and effort
- Enables large-scale transactions
- Builds trust in commercial dealings

The relationship between principal and agent is the foundation of the law of agency. It is built on trust and legal responsibility. The agent acts as a representative, and his actions bind the principal.

In simple terms, this relationship ensures that business can be carried out even when the principal is not personally present.

4.13 Agent's Authority

In a contract of agency, the idea of authority is the most important factor that decides the rights and responsibilities of both the principal and the agent. Authority simply means the legal power given to the agent to act on behalf of the principal. Under the Indian Contract Act, 1872, this authority determines whether the principal will be legally bound by the acts of the agent. If the agent acts within the limits of his authority, the principal is responsible. But if the agent goes beyond it, the agent himself may have to face the consequences.

Meaning of Agent's Authority

Agent's authority refers to the power of the agent to create legal relations between the principal and third parties. It defines what the agent can do, how far he can go, and under what conditions his acts will bind the principal.

This authority is not always written or clearly stated. Sometimes it is understood from the situation, the nature of the work, or the conduct of the parties.

Express and Implied Authority (Sections 186 and 187)

According to Section 186, the authority of an agent may be either express or implied.

Express authority is directly given by the principal, either orally or in writing. In such cases, the agent clearly knows what he is allowed to do.

On the other hand, Section 187 explains implied authority. This type of authority is not clearly stated but is understood from the circumstances of the case. It includes all those powers which are necessary to carry out the assigned work properly.

Example:

If a shop owner in Pune appoints a person as a shop manager, even if he does not specifically mention every task, the manager has the authority to purchase goods, deal with customers, and manage daily operations. This is implied authority.

Extent of Authority (Section 188)

As per Section 188, an agent has the authority to do all lawful things which are necessary to perform the assigned work. It also includes acts that are usually done in the course of such business.

This means the agent is not restricted only to specific instructions but can also do what is normally required to complete the task.

Example:

If an agent is appointed to sell goods, he can advertise the goods, negotiate prices, and finalise the deal. These actions are naturally connected to the work and are therefore included in his authority.

Authority in Emergency (Section 189)

According to Section 189, an agent has the authority to act in emergency situations to protect the principal from loss. In such cases, the agent can even go beyond normal instructions if it is necessary.

Example:

A transport agent carrying fruits from Nashik to Mumbai faces a delay due to heavy rains. To prevent the goods from spoiling, he sells them at the nearest market. This act is valid because it was done in an emergency to protect the principal's interest.

Effect of Agent Acting Within Authority

When the agent acts within his authority, his actions are legally considered as the actions of the principal. The principal becomes bound by such acts and is responsible towards third parties.

Example:

If an agent purchases goods within the given limit, the principal must pay for those goods.

Effect of Agent Exceeding Authority

If the agent goes beyond the authority given to him, the situation changes. The principal is not bound by the excess act, and the agent may become personally liable.

In some cases, the act may be partly valid and partly invalid.

Example:

If an agent is authorised to buy goods worth ₹50,000 but buys goods worth ₹80,000, the principal is liable only up to ₹50,000. The agent must bear the remaining ₹30,000.

Importance of Agent's Authority

The concept of authority is important because it clearly defines the limits within which the agent can act. It protects the principal from unauthorised acts and also provides clarity to third parties dealing with the agent.

It also ensures smooth functioning of business activities, especially when the principal cannot be personally present.

Agent's authority is the foundation of the agency relationship. It determines the power of the agent and the liability of the principal. The Indian Contract Act, 1872 clearly explains different types and limits of authority to ensure fairness and clarity in business transactions.

In simple terms, authority acts like a boundary — within it, the agent is protected and the principal is bound; beyond it, the agent may have to take responsibility himself.

4.14 Implied Authority

Introduction

In practical business situations, it is not always possible for the principal to clearly mention every power given to the agent. Many times, the agent is expected to act based on the nature of work and surrounding circumstances. This gives rise to the concept of implied authority.

Under the Indian Contract Act, 1872, implied authority plays a very important role because it allows the agent to perform his duties effectively, even when specific instructions are not given.

Meaning of Implied Authority

Implied authority refers to the authority which is not expressly given by the principal but is understood from:

- The nature of the work
- The conduct of the parties
- The circumstances of the case

In simple terms, it includes all those powers which are necessary and usual for carrying out the assigned work.

Legal Provision (Section 187)

According to Section 187 of the Indian Contract Act, 1872, an agent has implied authority to do every lawful thing which is necessary for carrying out the agency.

This means that even if the principal does not specifically mention certain actions, the agent is allowed to perform them if they are required to complete the task.

Nature of Implied Authority

Implied authority is flexible and depends on the situation. It is not fixed or written but is understood logically. It generally includes:

- Acts necessary to complete the work
- Acts commonly done in similar businesses
- Acts arising from past dealings

The agent is expected to act like a reasonable and sensible person in such situations.

Implied Authority in Business Situations

In business, implied authority is very common. When a person is appointed to a position, certain powers automatically come with that role.

Example:

If a person is appointed as a manager of a retail shop in Pune, he automatically gets the authority to:

- Purchase stock
- Deal with customers
- Hire workers

Even if these powers are not clearly written, they are understood as part of his role.

Implied Authority Through Conduct

Sometimes, authority is inferred from the behaviour of the principal and agent over time.

If the principal allows the agent to perform certain acts repeatedly without objection, it creates implied authority.

Example :

A regularly allows his employee to purchase goods on his behalf. Even without formal permission, the employee gains implied authority to continue such purchases.

Implied Authority in Usual Course of Business (Section 188)

As per Section 188, an agent has authority to do all acts which are:

- Necessary to perform the assigned task
- Usually done in such type of business

This section supports the concept of implied authority by recognising normal business practices.

Example:

An agent appointed to sell goods can:

- Advertise products
- Negotiate prices
- Arrange delivery

All these are considered part of implied authority.

Limitations of Implied Authority

Implied authority is not unlimited. The agent must not:

- Go against express instructions
- Do illegal acts
- Act for personal benefit

If the agent crosses these limits, he may become personally liable.

Consequences of Exceeding Implied Authority

If the agent performs acts beyond what is reasonably implied:

- The principal may refuse to accept such acts
- The agent becomes personally responsible
- The third party may take action against the agent

Example:

If a shop manager is allowed to purchase goods but buys unnecessary luxury items for personal use, the principal is not bound by such acts.

Importance of Implied Authority

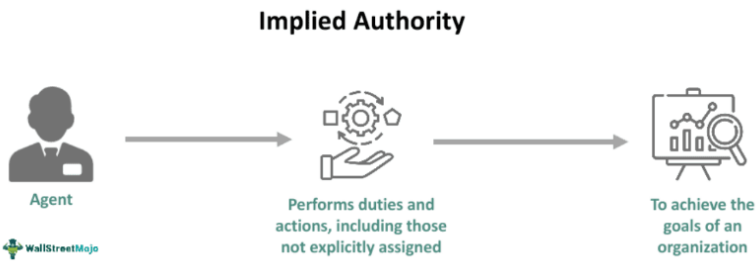
Implied authority is important because:

- It makes business operations smooth
- It avoids the need for constant instructions
- It gives flexibility to the agent
- It reflects real business practices

Without implied authority, it would be difficult for agents to perform even simple tasks.

Implied authority is an essential part of the agency relationship. It allows the agent to act efficiently based on practical needs and business customs. The Indian Contract Act, 1872 recognises this concept to ensure that agency relationships function smoothly in real-life situations.

In simple words, implied authority fills the gaps where express instructions are not given, allowing the agent to act sensibly and effectively on behalf of the principal.



4.15 Effects of Agents' Authority

In the law of agency, giving authority to an agent is not just about allowing him to act—it also creates legal effects. These effects decide who will be responsible for the acts done by the agent.

Under the Indian Contract Act, 1872, when an agent acts within his authority, his actions are treated as if the principal himself has acted. This is what makes agency so powerful and useful in business.

Basic Principle of Effect of Authority

The fundamental rule is simple:

"Acts done by the agent within authority bind the principal."

This means any contract entered into by the agent, within his authority, creates legal rights and obligations for the principal and the third party.

Effect When Agent Acts Within Authority (Section 226)

According to Section 226, contracts entered into through an agent, and obligations arising from such acts, are enforceable in the same manner as if the principal had entered into them himself.

Explanation:

The agent acts only as a representative. The real party to the contract is the principal.

Example:

A appoints B to purchase goods. B buys goods from C within his authority.

The contract is between A and C, not B and C.

A must pay C.

Effect on Agreements Made by Agent (Section 227)

As per Section 227, if an agent exceeds his authority but the authorised and unauthorised parts can be separated, then:

- The principal is bound by the authorised part
- The agent is responsible for the unauthorised part

Explanation:

The law tries to protect valid transactions while limiting liability for unauthorised acts.

Example:

A authorises B to buy 100 units of goods. B buys 150 units.

A is liable for 100 units

B is liable for extra 50 units

When Authority is Not Separable (Section 228)

According to Section 228, if the authorised and unauthorised parts cannot be separated, then the principal is not bound at all.

Explanation:

If the entire transaction is mixed and cannot be divided, the principal can reject it completely.

Example:

A allows B to purchase goods of a specific type. B purchases a completely different type along with authorised goods in a single contract.

A may reject the whole transaction.

Effect of Notice Given to Agent (Section 229)

As per Section 229, any information or notice given to the agent in the course of business is considered as given to the principal.

Explanation:

The agent is treated as an extension of the principal.

Example:

If a supplier informs the agent about defective goods, it is treated as if the principal has received that information.

Effect of Agent's Fraud or Misrepresentation (Section 238)

According to Section 238, if an agent commits fraud or makes misrepresentation while acting within his authority, the principal is bound by it.

However, if the agent acts outside his authority, the principal is not liable.

Explanation:

The law protects third parties who rely on the agent's actions.

Example:

If an agent falsely claims that goods are of high quality while selling them, the principal will be responsible if the agent acted within authority.

Relationship Between Principal, Agent and Third Party

The effect of authority creates a clear relationship:

- The principal is the main party responsible
- The agent acts as a connecting link
- The third-party deals with the agent but enters into a contract with the principal

This system makes business transactions smooth and efficient.

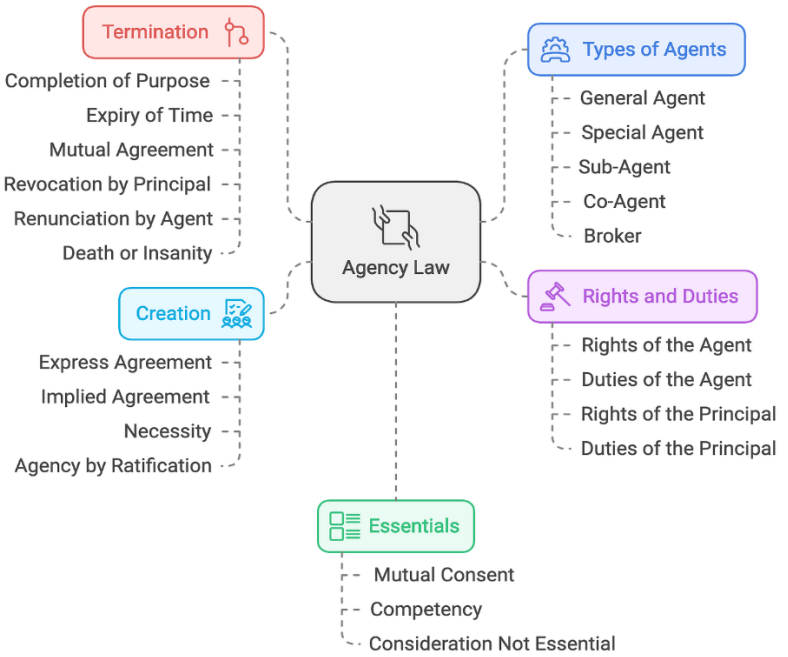
Importance of Effect of Authority

Understanding the effect of agent's authority is important because:

- It clarifies legal responsibility
- It protects third parties
- It ensures smooth business operations
- It reduces confusion in transactions

The effect of agent's authority determines how the actions of the agent influence the legal position of the principal. The Indian Contract Act, 1872 clearly provides rules to ensure fairness and clarity in such situations.

In simple terms, if the agent acts properly within his authority, the principal must accept the results. But if the agent goes beyond his limits, the law carefully decides how responsibility should be shared.



4.16 Revocation and Renunciation

In a contract of agency, the relationship between the principal and the agent does not continue forever. It may come to an end either by the act of the principal or by the act of the agent.

When the principal ends the authority, it is called revocation, and when the agent gives up his authority, it is called renunciation.

The Indian Contract Act, 1872 provides clear rules regarding how and when such termination can take place.

Meaning of Revocation and Renunciation

Revocation means cancellation of the agent's authority by the principal before the work is completed.

Renunciation means the agent voluntarily gives up his authority and refuses to continue the agency work.

In simple words:

- Principal ends agency → Revocation
- Agent leaves agency → Renunciation

When Can Agency Be Revoked? (Section 203)

According to Section 203, the principal may revoke the authority of the agent at any time before the authority has been exercised.

Explanation:

The principal has the right to cancel the agency relationship, but this must be done before the agent has already acted.

Example:

A appoints B to purchase goods, but before B makes the purchase, A cancels the authority.

This is valid revocation.

Revocation After Partial Exercise (Section 204)

As per Section 204, if the agent has already partly exercised his authority, the principal cannot revoke it for acts already done.

Explanation:

The principal cannot cancel responsibility for actions already completed.

Example:

B has already purchased part of the goods. A cannot refuse liability for those goods.

Compensation for Revocation (Section 205)

According to Section 205, if there is an agreement for a fixed period and the principal revokes the agency without sufficient cause, he must compensate the agent.

Explanation:

The law protects the agent from unfair termination.

Example:

A appoints B as agent for 1 year but removes him after 3 months without reason.

A must compensate B.

Notice of Revocation or Renunciation (Section 206)

As per Section 206, reasonable notice must be given before revocation or renunciation. If proper notice is not given, the party causing loss must compensate the other.

Explanation:

This ensures fairness and avoids sudden loss.

Example:

If an agent suddenly quits without informing the principal, and the principal suffers loss, the agent must compensate.

When Revocation and Renunciation Take Effect (Section 207)

According to Section 207, revocation or renunciation may be expressed or implied through conduct.

Explanation:

It does not always need to be in writing. Actions may also indicate termination.

Effect on Third Parties (Section 208)

As per Section 208, termination of authority takes effect:

- For the agent → when he comes to know
- For third parties → when they come to know

Explanation:

Until notice is received, third parties can still assume the agent has authority.

Example:

If a customer is not informed about termination, the principal may still be bound by the agent's acts.

When Authority Cannot Be Revoked (Section 202)

According to Section 202, when the agent has an interest in the subject matter, the agency cannot be revoked.

Explanation:

This protects the agent's personal interest.

Example:

If B is given authority to sell goods and recover his own money from the sale, A cannot revoke the authority until B recovers his amount.

Renunciation by Agent

Just like the principal, the agent also has the right to renounce the agency. However:

- He must give reasonable notice
- He must not cause unnecessary loss

- Otherwise, he must compensate the principal

Importance of Revocation and Renunciation

This concept is important because:

- It provides flexibility to both parties
- It ensures fairness in ending the relationship
- It protects both principal and agent from sudden losses

Revocation and renunciation are essential aspects of the agency relationship that allow either party to end the contract when necessary. The Indian Contract Act, 1872 provides clear rules to ensure that such termination is done fairly and without causing unnecessary harm.

In simple terms, both the principal and the agent have the right to end the relationship, but they must do so responsibly and with proper notice.

4.17 Rights, Duties and Liabilities of Principal and Agent

4.17.1 Introduction

In an agency relationship, both the principal and the agent have certain rights, duties, and liabilities towards each other and towards third parties. The Indian Contract Act, 1872 clearly defines these responsibilities to ensure fairness and trust in business transactions.

Understanding this topic is very important for students because it explains who is responsible for what in an agency relationship.

4.17.2 Duties of Agent Towards Principal

The agent occupies a position of trust. Therefore, the law expects him to act honestly, carefully, and in the best interest of the principal.

(1) Duty to Follow Instructions (Section 211)

According to Section 211, an agent must act according to the directions given by the principal. If no instructions are given, he must follow the customs of the business.

If the agent does not follow instructions, he will be responsible for any loss.

Example*:*

If a principal asks the agent to sell goods at ₹5000 but the agent sells at ₹4000 without permission, he must compensate for the loss.

(2) Duty of Care, Skill and Diligence (Section 212)

An agent must act with reasonable care, skill, and diligence while performing his work.

If he acts negligently, he is liable for damages.

Example*:*

If an agent carelessly stores goods and they get damaged; he must bear the loss.

(3) Duty to Render Proper Accounts (Section 213)

The agent must maintain correct and clear accounts of all transactions and produce them when demanded.

Example*:*

A sales agent must keep records of all sales and expenses and show them to the principal.

(4) Duty to Communicate (Section 214)

The agent must communicate with the principal in case of difficulty and seek instructions.

Example*:*

If market conditions suddenly change, the agent should inform the principal before taking action.

(5) Duty Not to Deal on Own Account (Section 215 & 216)

The agent should not make any secret profit or deal on his own account without the principal's consent.

If he does, the principal can:

- Cancel the transaction
- Claim any secret profit

Example*:*

If an agent buys goods cheaply and sells to the principal at a higher price secretly, the principal can recover the profit.

(6) Duty of Good Faith and Loyalty

The agent must act honestly and faithfully for the benefit of the principal.

He should not misuse his position.

4.17.3 Rights of Agent Against Principal

The law also protects the agent by giving him certain rights.

(1) Right to Remuneration (Section 219)

The agent has the right to receive agreed commission or payment after completing the work.

Example*:*

A broker earns commission after successfully completing a deal.

(2) Right of Retainer (Section 217)

The agent can retain money received on behalf of the principal to recover his dues.

(3) Right of Lien (Section 221)

The agent can keep goods or property of the principal until his lawful charges are paid.

(4) Right to Indemnity (Sections 222 & 223)

The principal must compensate the agent for:

- Lawful acts done in good faith (Section 222)
- Acts done under principal's instructions (Section 223)

Example*:*

If an agent suffers loss while following lawful instructions, the principal must compensate him.

(5) Right to Compensation (Section 225)

If the agent suffers injury due to the principal's negligence, he can claim compensation.

4.17.4 Duties of Principal Towards Agent

The principal also has certain responsibilities.

He must act fairly and support the agent in lawful work. The principal must pay agreed remuneration and indemnify the agent against losses suffered during lawful performance of duties.

He should not create situations that cause unnecessary loss or harm to the agent.

4.17.5 Liabilities of Principal

The principal is liable for acts done by the agent within the scope of authority.

(1) Liability for Authorized Acts (Section 226)

Contracts entered into by the agent are binding on the principal.

Example*:*

If an agent purchases goods on behalf of the principal, the principal must pay.

(2) Liability for Acts Beyond Authority (Section 227 & 228)

- If authorized and unauthorized parts can be separated → principal is liable only for authorized part
- If they cannot be separated → principal may not be liable

(3) Liability for Misrepresentation or Fraud (Section 238)

The principal is liable for fraud or misrepresentation committed by the agent within his authority.

4.17.6 Liabilities of Agent

Generally, an agent is not personally liable, but there are exceptions.

(1) Personal Liability in Certain Cases (Section 230)

An agent is personally liable when:

- He expressly agrees
- He acts for a foreign principal
- The principal is undisclosed

(2) Liability for Breach of Duty

If the agent violates his duties (like negligence or disobedience), he must compensate the principal.

The relationship between principal and agent is based on trust, honesty, and responsibility. The Indian Contract Act, 1872 provides detailed rules regarding their rights, duties, and liabilities to ensure smooth business functioning.

For students, remember:

Agent must act honestly and carefully, and principal must support and compensate fairly.

Aspect	Party	Key Point (Short & Easy)	Section (ICA, 1872)
Duty to follow instructions	Agent	Must follow principal's directions	Sec. 211
Duty of care & skill	Agent	Act carefully and professionally	Sec. 212
Duty to maintain accounts	Agent	Keep proper records	Sec. 213
Duty to communicate	Agent	Inform principal in	Sec.

Aspect	Party	Key Point (Short & Easy)	Section (ICA, 1872)
		difficulty	214
No secret profit	Agent	Cannot earn hidden profit	Sec. 215–216
Right to remuneration	Agent	Get commission/payment	Sec. 219
Right of retainer	Agent	Adjust dues from money received	Sec. 217
Right of lien	Agent	Hold goods till payment	Sec. 221
Right to indemnity	Agent	Compensation for lawful acts	Sec. 222–223
Right to compensation	Agent	For principal's negligence	Sec. 225
Duty to pay agent	Principal	Must pay remuneration	—
Duty to indemnify	Principal	Compensate agent for losses	Sec. 222
Liability for agent's acts	Principal	Bound by agent's contracts	Sec. 226
Liability beyond authority	Principal	Depends on separability	Sec. 227–228
Fraud/misrepresentation	Principal	Liable for agent's fraud	Sec. 238
Personal liability	Agent	Liable in special cases	Sec. 230

4.18 Termination (Determination) of Agency

4.18.1 Introduction

An agency relationship is created for a specific purpose and duration, and it does not continue forever. At some point, the authority given by the principal to the agent comes to an end. This ending of the agency relationship is known as termination or determination of agency.

Termination is important because once the agency ends, the agent loses the authority to act on behalf of the principal. Any act done after termination may not bind the principal. Therefore, the law provides clear rules regarding how and when an agency comes to an end.

4.18.2 Legal Framework under the Indian Contract Act, 1872

The provisions relating to termination of agency are covered under Sections 201 to 208:

- Section 201 – Modes of termination
- Section 202 – Agency coupled with interest
- Section 203 – Revocation of authority by principal
- Section 204 – Revocation where authority partly exercised
- Section 205 – Compensation for revocation without sufficient cause
- Section 206 – Notice of revocation or renunciation
- Section 207 – Express and implied termination
- Section 208 – When termination takes effect

These sections together explain the complete legal position of termination of agency.

4.18.3 Modes of Termination (Section 201)

According to Section 201, an agency may be terminated either by the act of parties or by operation of law.

(A) Termination by Act of Parties

In many cases, the agency ends because of the actions or decisions taken by the principal or the agent.

When both the principal and the agent mutually agree to end their relationship, the agency is terminated by agreement. This is the most simple and peaceful method.

The principal also has the right to revoke the authority of the agent under Section 203. This means the principal can cancel the agent's authority at any time before it is exercised. However, this right must be used carefully and reasonably.

On the other hand, the agent also has the right to renounce the agency, meaning he can refuse to continue acting as an agent. This may happen due to personal reasons or dissatisfaction.

(B) Termination by Operation of Law

In certain situations, the agency ends automatically due to legal reasons.

When the purpose of the agency is completed, the relationship naturally comes to an end. For example, if an agent is appointed to sell a house, the agency ends once the house is sold.

Similarly, if the agency is created for a fixed time, it will terminate when that time expires.

Under Section 201, the death or insanity of either the principal or the agent automatically terminates the agency. This is because the relationship is based on personal trust and confidence.

If the principal becomes insolvent, the agency also comes to an end, as he loses the capacity to contract.

In addition, if the subject matter of the agency is destroyed (for example, goods are destroyed in fire), the agency cannot continue and is therefore terminated.

4.18.4 Agency Coupled with Interest (Section 202)

An important exception to termination is given under Section 202. When the agent has a personal interest in the subject matter of the agency, the agency cannot be terminated without his consent.

This type of agency is known as agency coupled with interest.

For example, if an agent has lent money to the principal and is authorized to recover it from the sale of goods, the principal cannot terminate the agency until the agent recovers his money.

This rule protects the agent's financial interest**.**

4.18.5 Revocation of Authority (Sections 203–204)

Under Section 203, the principal can revoke the authority of the agent at any time before it is exercised. However, this right is not absolute.

According to Section 204, once the agent has partly exercised his authority, the principal cannot revoke it for the part already completed. This ensures fairness and prevents injustice to third parties.

For example, if the agent has already entered into a contract, the principal cannot cancel that contract.

4.18.6 Compensation Under Section 203,

The principal can revoke the authority of the agent at any time before it is exercised. However, this right is not absolute.

According to Section 204, once the agent has partly exercised his authority, the principal cannot revoke it for the

part already completed. This ensures fairness and prevents injustice to third parties.

For example, if the agent has already entered into a contract, the principal cannot cancel that contract.

For Wrongful Termination (Section 205)

If the agency is terminated without sufficient cause, the party terminating the agency must compensate the other party for any loss caused.

For instance, if a principal removes an agent suddenly without any valid reason, the agent can claim compensation.

This provision ensures that termination is done fairly and not arbitrarily.

4.18.7 Notice of Termination (Section 206)

The law requires that reasonable notice must be given before terminating the agency.

If proper notice is not given and it results in loss to the other party, compensation must be paid.

This rule promotes fairness and prevents sudden and unfair termination.

4.18.8 Express and Implied Termination (Section 207)

Termination of agency can be made either:

- Expressly – by clearly communicating the intention to terminate
- Impliedly – through conduct or behavior

For example, if a principal appoints another agent for the same work, it may imply termination of the previous agency.

4.18.9 When Termination Takes Effect (Section 208)

According to Section 208, termination does not become effective immediately in all cases.

- As regards the agent, termination takes effect when he comes to know about it.
- As regards third parties, it takes effect when they become aware of it.

This rule protects third parties who may otherwise act in good faith without knowing that the agency has ended.

4.18.10 Conclusion

Termination of agency is an essential concept that determines the end of the agent's authority. The provisions under Sections 201 to 208 of the Indian Contract Act, 1872 ensure that termination takes place in a fair, reasonable, and legally valid manner.

For students, the key idea to remember is:
Agency ends either by mutual decision, legal circumstances, or completion of purpose.

4.19 Effect of Termination of Agency

4.19.1 Introduction

After understanding how an agency comes to an end, it is equally important to know what happens after termination. The termination of agency affects not only the principal and agent but also third parties who deal with them.

The Indian Contract Act, 1872 clearly explains the effects of termination to ensure that no party suffers unfairly. Even after termination, certain rights and liabilities may continue.

4.19.2 Relevant Legal Provisions

The effects of termination are mainly covered under:

- Section 208 – When termination takes effect
- Section 209 – Agent's duty on termination
- Section 210 – Termination of sub-agent

- Section 211–221 (Indirect relevance) – Duties and rights which may continue

4.19.3 Effect on Agent (Section 208)

According to Section 208, termination becomes effective for the agent only when he comes to know about it.

This means that if the agent, without knowledge of termination, enters into a contract, the principal may still be bound.

Example*:*

A principal revokes authority but the agent is unaware and makes a contract. The contract is still valid.

This rule protects the agent acting in good faith.

4.19.4 Effect on Third Parties (Section 208)

Termination becomes effective for third parties only when they come to know about it.

If a third-party deals with the agent without knowing that the agency has ended, the principal will still be liable.

Example*:*

If a customer buys goods from an agent unaware of termination, the principal must honor the contract.

This protects innocent third parties in business transactions.

4.19.5 Duty of Agent After Termination (Section 209)

Even after termination, the agent has certain responsibilities.

According to Section 209, the agent must take reasonable steps to protect the interests of the principal.

Example:

If goods are in the agent's custody, he must safely store or protect them even after termination.

This duty ensures that the principal does not suffer unnecessary loss.

4.19.6 Effect on Sub-Agent (Section 210)

When the main agency is terminated, the sub-agent's authority also comes to an end.

However, the sub-agent becomes directly responsible to the principal in certain cases.

Example*:*

If an agent appoints a sub-agent and the agency ends, the sub-agent's role also ends.

4.19.7 Continuing Rights and Liabilities

Termination of agency does not always end all rights and duties immediately. Some rights and liabilities continue even after termination.

For example, the agent can still:

- Claim remuneration for work already done
- Exercise lien for unpaid dues
- Claim indemnity for lawful acts

Similarly, the principal remains liable for acts done by the agent before termination.

4.19.8 Practical Example (Easy Understanding)

Suppose a company terminates its sales agent but does not inform customers. The agent continues selling goods to customers who are unaware of termination.

In this case:

- The company (principal) is still bound by the agent's actions (Section 208)
- The agent must protect company goods (Section 209)

The effect of termination of agency is not limited to ending authority. It also determines the continuing rights, duties, and liabilities of the principal, agent, and third parties.

The provisions under Sections 208 to 210 of the Indian Contract Act, 1872 ensure fairness and protect all parties involved.

For students, remember:
Termination ends authority, but responsibilities may still continue.

📊 Quick Revision Table

Effect	Explanation	Section
Effect on agent	Valid till agent knows	Sec. 208
Effect on third party	Valid till they know	Sec. 208
Duty after termination	Protect principal's interest	Sec. 209
Sub-agent	Authority ends with agent	Sec. 210
Continuing rights	Remuneration, lien, indemnity	Sec. 211–221

MCQ's

1)UNIT I

Q1. A contract of indemnity is a contract where:
A) One party promises to perform an act
B) One party promises to compensate for loss
C) One party gives a loan
D) One party transfers ownership
✅ **Correct Answer**: B

Q2. In a contract of indemnity, the parties are called:
A) Creditor and debtor
B) Bailor and bailee
C) Indemnifier and indemnity holder
D) Lessor and lessee
✅ **Correct Answer**: C

Q3. A contract of indemnity mainly protects against:
A) Profit
B) Loss
C) Ownership
D) Gift
✅ **Correct Answer**: B

Q4. According to the Indian Contract Act, a contract of indemnity is defined under:
A) Section 10
B) Section 124
C) Section 126
D) Section 148
✅ **Correct Answer**: B

Q5. Which of the following is an essential element of indemnity?
A) Transfer of goods

B) Promise to compensate loss
C) Delivery of goods
D) Loan agreement
✅ **Correct Answer**: B

Q6. The loss in indemnity may arise due to:
A) Natural disaster only
B) Human conduct only
C) Conduct of promisor or third party
D) Government order only
✅ **Correct Answer**: C

Q7. The person who gives indemnity is called:
A) Indemnity holder
B) Indemnifier
C) Surety
D) Bailee
✅ **Correct Answer**: B

Q8. Rights of indemnity holder are given under:
A) Section 124
B) Section 125
C) Section 126
D) Section 73
✅ **Correct Answer**: B

Q9. The indemnity holder can recover damages which he:
A) Refuses to pay
B) Is compelled to pay
C) Wants to avoid
D) Ignores
✅ **Correct Answer**: B

Q10. The indemnity holder can recover costs if they are:
A) Illegal
B) Unnecessary
C) Reasonable and prudent
D) Avoidable
✅ **Correct Answer**: C

Q11. The indemnity holder can recover sums paid under:
A) Void agreement
B) Compromise made in good faith
C) Illegal contract
D) Gift
✅ **Correct Answer**: B

Q12. The rights of indemnifier are:
A) Clearly defined in the Act
B) Not defined but implied
C) Fully prohibited
D) Not allowed
✅ **Correct Answer**: B

Q13. The indemnifier has the right to:
A) Refuse all payments
B) Recover damages from indemnity holder
C) Be subrogated to rights of indemnity holder
D) Cancel contract anytime
✅ **Correct Answer**: C

Q14. Subrogation means:
A) Transfer of ownership
B) Stepping into the shoes of another
C) Ending a contract
D) Giving a loan
✅ **Correct Answer**: B

Q15. The indemnifier can recover from third party:
A) Always
B) Never
C) After indemnifying the indemnity holder
D) Before contract
✅ **Correct Answer**: C

Q16. Which of the following is NOT related to indemnity?
A) Compensation for loss
B) Risk coverage
C) Guarantee of loan
D) Protection against damage
✅ **Correct Answer**: C

Q17. A contract of indemnity can be:
A) Oral only
B) Written only
C) Both oral and written
D) Not valid
✅ **Correct Answer**: C

Q18. The main objective of indemnity is:
A) Profit earning
B) Loss recovery
C) Ownership transfer
D) Business expansion
✅ **Correct Answer**: B

Q19. Indemnity is different from guarantee because:
A) It has three parties
B) It has two parties
C) It involves loan
D) It is illegal
✅ **Correct Answer**: B

Q20. Which section deals with rights of indemnity holder?
A) 124
B) 125
C) 126
D) 127
✅ **Correct Answer**: B

UNIT II

Contract of Guarantee

Q1. A contract of guarantee is defined under:
A) Section 124
B) Section 126
C) Section 148
D) Section 73
✅ **Correct Answer: B**

Q2. A contract of guarantee involves how many parties?
A) Two
B) Three
C) Four
D) One
✅ **Correct Answer: B**

Q3. The three parties in a contract of guarantee are:
A) Buyer, seller, agent
B) Indemnifier, holder, third party
C) Creditor, principal debtor, surety
D) Lessor, lessee, agent
✅ **Correct Answer: C**

Q4. Consideration for a guarantee may be:
A) Benefit to creditor only
B) Benefit to surety only
C) Any act done for benefit of principal debtor

D) Cash payment only

✅ **Correct Answer: C**

Q5. Consideration in a contract of guarantee is given under:
A) Section 127
B) Section 128
C) Section 130
D) Section 124

✅ **Correct Answer: A**

Q6. Which of the following is NOT an essential element?
A) Existence of debt
B) Free consent
C) Ownership transfer
D) Three parties

✅ **Correct Answer: C**

Q7. The liability of surety is:
A) Secondary
B) Primary
C) Optional
D) Illegal

✅ **Correct Answer: A**

Q8. A bank guarantee is a promise by:
A) Customer
B) Bank
C) Government
D) Seller

✅ **Correct Answer: B**

Q9. Bank guarantee ensures:
A) Profit
B) Payment on default
C) Ownership transfer

D) Loan waiver

✅ **Correct Answer: B**

Q10. Contract of indemnity has:
A) 3 parties
B) 2 parties
C) 4 parties
D) No parties

✅ **Correct Answer: B**

Q11. In guarantee, liability of surety arises:
A) Immediately
B) After default of debtor
C) Before contract
D) Never

✅ **Correct Answer: B**

Q12. A contract of insurance is mainly a:
A) Guarantee
B) Indemnity
C) Bailment
D) Agency

✅ **Correct Answer: B**

Q13. Insurance protects against:
A) Profit
B) Loss
C) Ownership
D) Debt

✅ **Correct Answer: B**

Q14. A continuing guarantee applies to:
A) Single transaction
B) Series of transactions
C) Illegal acts

D) Gifts

✅ **Correct Answer: B**

Q15. Continuing guarantee is defined under:
A) Section 129
B) Section 126
C) Section 124
D) Section 148

✅ **Correct Answer: A**

Q16. A continuing guarantee can be revoked by:
A) Death of surety
B) Notice by surety
C) Both A and B
D) Court order only

✅ **Correct Answer: C**

Q17. Surety is not discharged when:
A) Contract is varied without consent
B) Creditor releases debtor
C) Mere forbearance to sue
D) Securities are lost

✅ **Correct Answer: C**

Q18. A guarantee obtained by misrepresentation is:
A) Valid
B) Illegal
C) Invalid
D) Enforceable

✅ **Correct Answer: C**

Q19. Right of subrogation means:
A) Right to cancel contract
B) Right to step into creditor's shoes
C) Right to avoid liability

D) Right to transfer goods

✅ **Correct Answer: B**

Q20. Co-sureties are liable:

A) Separately only

B) Equally unless agreed otherwise

C) Not liable

D) Only one pays

✅ **Correct Answer: B**

UNIT III

Bailment & Pledge

Q1. Bailment is defined under:

A) Section 126

B) Section 148

C) Section 124

D) Section 73

✅ **Correct Answer: B**

Q2. Bailment means:

A) Sale of goods

B) Delivery of goods for some purpose

C) Loan agreement

D) Transfer of ownership

✅ **Correct Answer: B**

Q3. The parties in bailment are:

A) Creditor & debtor

B) Bailor & bailee

C) Lessor & lessee

D) Principal & agent

✅ **Correct Answer: B**

Q4. Which of the following is essential for bailment?
A) Ownership transfer
B) Delivery of goods
C) Written agreement only
D) Profit making
✅ **Correct Answer: B**

Q5. After completion of purpose, goods must be:
A) Sold
B) Destroyed
C) Returned
D) Gifted
✅ **Correct Answer: C**

Q6. Gratuitous bailment means:
A) Bailment for reward
B) Bailment without reward
C) Illegal bailment
D) Business contract
✅ **Correct Answer: B**

Q7. Non-gratuitous bailment involves:
A) No benefit
B) Mutual benefit
C) Loss only
D) Gift
✅ **Correct Answer: B**

Q8. Bailor must disclose:
A) Profits
B) Known defects in goods
C) Ownership documents
D) Taxes
✅ **Correct Answer: B**

Q9. Bailor has right to:
A) Use goods anytime
B) Demand return of goods
C) Sell goods always
D) Ignore contract
✅ **Correct Answer: B**

Q10. Bailee must take:
A) No care
B) Reasonable care
C) Excess care
D) Personal use
✅ **Correct Answer: B**

Q11. Bailee is liable for:
A) Normal wear and tear
B) Negligence
C) Natural loss
D) Act of God
✅ **Correct Answer: B**

Q12. Lien means:
A) Right to sell goods
B) Right to retain goods
C) Right to destroy goods
D) Right to gift goods
✅ **Correct Answer: B**

Q13. Particular lien is:
A) General right
B) Right for specific charges
C) Illegal right
D) Unlimited right
✅ **Correct Answer: B**

Q14. General lien is available for:
A) Specific goods only
B) All goods for general balance
C) Illegal claims
D) Gifts
✅ **Correct Answer: B**

Q15. Finder of lost goods has rights of:
A) Owner
B) Bailee
C) Creditor
D) Agent
✅ **Correct Answer: B**

Q16. Pledge is defined under:
A) Section 172
B) Section 148
C) Section 126
D) Section 124
✅ **Correct Answer: A**

Q17. In pledge, goods are delivered as:
A) Gift
B) Security for debt
C) Sale
D) Rent
✅ **Correct Answer: B**

Q18. Pledge is a:
A) Type of sale
B) Special type of bailment
C) Lease
D) Agency
✅ **Correct Answer: B**

Q19. Pawnee has right to:
A) Destroy goods
B) Retain goods for payment
C) Gift goods
D) Ignore contract
✅ **Correct Answer: B**

Q20. Pledge by non-owner is valid when:
A) Always invalid
B) With consent of owner
C) Finder of goods pledges
D) Both B and C
✅ **Correct Answer: D**

UNIT IV

LAW OF AGENCY

Q1. An agent is a person who:
A) Works independently
B) Represents another person
C) Buys goods for himself
D) Lends money
✅ **Correct Answer**: B

Q2. The person who appoints an agent is called:
A) Bailee
B) Principal
C) Creditor
D) Surety
✅ **Correct Answer**: B

Q3. Who can appoint an agent?
A) Minor
B) Person of sound mind
C) Insolvent

D) Stranger

✅ **Correct Answer**: B

Q4. Who can be an agent?
A) Only major
B) Only minor
C) Any person (including minor)
D) Only businessman

✅ **Correct Answer**: C

Q5. The test of agency is based on:
A) Ownership
B) Authority
C) Profit
D) Payment

✅ **Correct Answer**: B

Q6. Agency can be created by:
A) Agreement
B) Ratification
C) Operation of law
D) All of the above

✅ **Correct Answer**: D

Q7. Ratification means:
A) Cancelling act
B) Approving unauthorized act
C) Selling goods
D) Lending money

✅ **Correct Answer**: B

Q8. Ratification must be made by:
A) Agent
B) Third party
C) Principal

D) Court
✅ **Correct Answer**: C

Q9. Ratification relates back to:
A) Date of contract
B) Date of act
C) Future date
D) Court order
✅ **Correct Answer**: B

🔷 Classification of Agents
Q10. A factor is an agent who:
A) Has possession of goods
B) Only negotiates
C) Acts without authority
D) Gives loan
✅ **Correct Answer**: A

Q11. A sub-agent works under:
A) Principal directly
B) Agent
C) Creditor
D) Court
✅ **Correct Answer**: B

Q12. Properly appointed sub-agent is responsible to:
A) Third party
B) Principal
C) Agent only
D) No one
✅ **Correct Answer**: B

Q13. Implied authority means:
A) Written authority
B) Oral authority

C) Authority inferred from circumstances
D) Illegal authority
✅ **Correct Answer**: C

Q14. Agent's authority includes acts:
A) Express only
B) Implied only
C) Necessary to carry out express authority
D) Illegal acts
✅ **Correct Answer**: C

Q15. Acts done within authority bind:
A) Agent
B) Principal
C) Third party only
D) Court
✅ **Correct Answer**: B

Q16. Revocation means:
A) Agent leaving job
B) Principal cancelling authority
C) Court order
D) Agreement creation
✅ **Correct Answer**: B

Q17. Renunciation means:
A) Principal cancels
B) Agent withdraws
C) Court cancels
D) Third party cancels
✅ **Correct Answer**: B

Q18. Agent must:
A) Make secret profit
B) Act in good faith

C) Ignore principal
D) Act for himself
✅ **Correct Answer**: B

Q19. Agency terminates by:
A) Death of principal
B) Insanity
C) Completion of work
D) All of the above
✅ **Correct Answer**: D

Q20. After termination, agent must:
A) Continue work
B) Inform third parties
C) Ignore principal
D) Sell goods
✅ **Correct Answer**: B

PRACTICE SET

📘 UNIT I: Law of Indemnity

🔷 Long Questions

Q1. Explain the Contract of Indemnity with definition and essentials.
Q2. Discuss the rights of indemnity holder under the Indian Contract Act.
Q3. Explain the rights of indemnifier and their legal position.
Q4. Describe the nature and scope of contract of indemnity with examples.
Q5. Distinguish between indemnity and other related contracts.

🔷 Short Questions

Q1. Define Contract of Indemnity.
Q2. State any two essentials of indemnity.
Q3. Who is an indemnifier?
Q4. What is meant by indemnity holder?
Q5. Mention any two rights of indemnity holder.

UNIT II: Contract of Guarantee

Long Questions

Q1. Define Contract of Guarantee and explain its essentials.
Q2. Explain consideration in a contract of guarantee.
Q3. Distinguish between contract of indemnity and contract of guarantee.
Q4. Discuss the rights of surety and law relating to co-sureties.
Q5. Explain continuing guarantee, its revocation, and cases where surety is not discharged.

Short Questions

Q1. Who is a surety?
Q2. What is a bank guarantee?
Q3. Define continuing guarantee.
Q4. What is an invalid guarantee?
Q5. State any two rights of surety.

UNIT III: Bailment & Pledge

Long Questions

Q1. Define Bailment and explain its essentials and kinds.
Q2. Discuss the rights, duties, and liabilities of bailor and bailee.
Q3. Explain the concept of lien and distinguish between general lien and particular lien.
Q4. Define Pledge and distinguish it from bailment and lien.
Q5. Explain the rights and liabilities of pawnee and pawnor, including pledge by non-owner.

Short Questions

Q1. Who is a bailor?
Q2. What is gratuitous bailment?
Q3. Define lien.
Q4. Who is a finder of goods?
Q5. What is pledge?

📘 UNIT IV: Law of Agency

🔷 Long Questions

Q1. Define agent and principal and explain who can appoint an agent.
Q2. Explain the modes of creation of agency and rules of ratification.
Q3. Discuss the classification of agents and concept of sub-agent.
Q4. Explain authority of agent (express and implied) and its effects.
Q5. Discuss termination of agency, its modes, and effects.

🔷 Short Questions

Q1. Who is an agent?
Q2. What is implied authority?
Q3. Define ratification.
Q4. What is revocation of agency?
Q5. State any two duties of an agent.

SECTIONS LIST FOR STUDENTS

UNIT I - I : Law of Indemnity and Unit Guarantee

🔷 1. Contract of Indemnity – Definition

- Section 124
- Defines contract of indemnity
- Two parties:
    - Indemnifier
    - Indemnity Holder

🔷 2. Essentials of Contract of Indemnity
(derived from Section 124 + general contract principles)

- Section 124 → Basic definition
- Section 10 → Essentials of valid contract
    - Free consent
    - Lawful consideration
    - Competent parties

🔷 3. Rights of Indemnity Holder

- Section 125

Indemnity holder can recover:

1. Damages he is compelled to pay
2. Legal costs (if reasonable)
3. Amount paid under compromise

◆ 4. Rights of Indemnifier

- Not expressly mentioned in one section
- Derived from general principles + case laws

Implied rights include:

- Right of subrogation
- Right to recover from third party

Unit II - Contract of Guarantee

◆ 1. Definition of Contract of Guarantee

- Section 126
- Defines guarantee and parties:
  - Creditor
  - Principal Debtor
  - Surety

◆ 2. Consideration in Contract of Guarantee

- Section 127
- Consideration = anything done for benefit of principal debtor is sufficient

◆ 3. Essentials of Contract of Guarantee

- Section 126 → Definition
- Section 127 → Consideration
- Section 128 → Liability of surety (co-extensive with debtor)

◆ 4. Law as to Bank Guarantee

- No specific section
- Based on:
  - Section 126
  - Section 128
- Governed mainly by judicial decisions

◆ 5. Distinction: Indemnity vs Guarantee

- Indemnity → Section 124

- Guarantee → Section 126

🔷 6. Insurance, Guarantee & Indemnity (Distinction)
- Insurance based on indemnity
- Relevant section:
  - Section 124 (Indemnity)
- No single direct section (conceptual topic)

🔷 7. Continuing Guarantee
- Section 129
- Applies to a series of transactions

🔷 8. Revocation of Continuing Guarantee
- Section 130 → By notice
- Section 131 → By death of surety

🔷 9. When Surety is NOT Discharged
- Section 137 → Mere delay/forbearance does not discharge surety
- Section 138 → Release of one co-surety does not discharge others

🔷 10. Exceptions – Invalid Guarantees
- Section 142 → Misrepresentation → Invalid
- Section 143 → Concealment → Invalid

🔷 11. Rights of Surety
- Section 140 → Right of subrogation
- Section 141 → Right to securities
- Section 145 → Right of indemnity

🔷 12. Law as to Co-Sureties
- Section 146 → Equal contribution
- Section 147 → Different liabilities

🔷 13. Right of Surety against Co-Surety
- Section 146 & 147
- Right of contribution

UNIT – III Bailment & Pledge

- 1. Bailment – Definition
  - Section 148
  - Bailment = delivery of goods for some purpose upon contract
- 2. Essentials of Bailment
  - Section 148 → Delivery of goods
  - Section 149 → Delivery how made
  - Section 150–152 → Duties and care
- 3. Kinds of Bailment
  - No specific section
  - Based on concept:
    - Gratuitous bailment
    - Non-gratuitous bailment
- 4. Duties & Liabilities of Bailor
  - Section 150 → Disclosure of defects
  - Section 158 → Bailor to bear expenses
  - Section 159 → Gratuitous bailment termination
  - Section 164 → Bailor's responsibility
- 5. Rights of Bailor
  - Derived from:
    - Section 153 → Termination for misuse
    - Section 154 → Liability of bailee
    - Section 161 → Bailee's default
- 6. Duties of Bailee
  - Section 151 → Reasonable care
  - Section 152 → Not liable if care taken
  - Section 153–154 → Proper use
  - Section 160–161 → Return of goods
- 7. Rights of Bailee
  - Section 165 → Delivery as per bailor directions
  - Section 166 → Deliver goods accordingly
  - Section 170–171 → Right of lien

🔷 8. Lien (General & Particular)

🔶 Particular Lien

- Section 170
- Right to retain goods for specific charges

🔶 General Lien

- Section 171
- Right to retain goods for general balance

🔷 9. Finder of Goods

- Section 168 → Right to reward
- Section 169 → Right to sue for reward

Finder has rights of a bailee

📘 PLEDGE

🔷 10. Definition of Pledge

- Section 172
- Bailment of goods as security for debt

🔷 11. Essentials of Pledge

- Section 172
- Based on bailment principles

🔷 12. Pledge vs Bailment

- Pledge = special type of bailment
- Based on:
    - Section 148 & 172

🔷 13. Pledge vs Lien

- Lien → Right to retain
- Pledge → Right to retain + sell
- Sections:
    - 170–171 (Lien)
    - 172 (Pledge)

🔷 14. Rights of Pawnee

- Section 173 → Right to retain goods
- Section 174 → Extraordinary expenses
- Section 175 → Right to sue
- Section 176 → Right to sell

🔷 15. Liabilities of Pawnee

- Based on bailee duties:
    - Section 151–152

◆ 16. Rights of Pawnor
- Section 177 → Right to redeem goods

◆ 17. Pledge by Non-Owner
- Section 178 → By mercantile agent
- Section 178A → By person with voidable contract
- Section 179 → Limited interest

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D. Case Laws

- Gajanan Moreshwar v Moreshwar Madan Gajanan Moreshwar v. Moreshwar Madan, AIR 1942 Bom 302.
- Birkmyr v Darnell Birkmyr v. Darnell (1704) 1 Salk 27.
- Coggs v Bernard Coggs v. Bernard (1703) 2 Ld Raym 909.
- Kaliaperumal Pillai v Visalakshmi Kaliaperumal Pillai v. Visalakshmi (1938).
- Freeman & Lockyer v. Buckhurst Park Properties (1964) 2 QB 480.
- Keighley Maxsted & Co v Durant Keighley, Maxsted & Co v. Durant (1901) AC 240.

E. Journals & Articles

- Indian Law Institute. (Various issues).
- All India Reporter. (Various issues).
- Supreme Court Cases. (Various issues).
- Journal of Indian Law Institute. (Various issues).
- Harvard Law Review. (Various issues).
- Modern Law Review. (Various issues).

F. Online Legal Resources

- Ministry of Law and Justice (India)
- Indian Kanoon
- SCC Online

- Manupatra

G. Additional Academic Sources

- University textbooks (Mumbai, Pune, Delhi University syllabi)
- UGC NET Law study material
- IGNOU Law Notes
- ICAI Business Law Modules

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