

## COMMERCIAL LAW – UNIT – I

### THE INDIAN CONTRACT ACT 1872

Definition of contract, essential elements and types of a contract, Formation of a contract, performance of contracts, breach of contract and its remedies, Quasi contracts – Contract of Agency: Nature of agency, Creation and types of agents, Authority and liability of Agent and principal: Rights and duties of principal and agents, termination of agency.

### THE SALE OF GOODS ACT 1930

Nature of Sales contract, Documents of title, risk of loss, Guarantees and Warranties, performance of sales contracts, conditional sales and rights of an unpaid seller – Negotiable Instruments Act 1881: Nature and requisites of negotiable instruments. Types of negotiable instruments, liability of parties, holder in due course, special rules for Cheque and drafts, discharge of negotiable instruments, GST.

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## 1.1 THE INDIAN CONTRACT ACT 1872

### Law:

Law is those principles applied by the state in the administration of justice.

### Business Law:

It refers to those rules and regulation which govern the formation and execution of business deals made by various people in the society.

### Mercantile Law:

It refers to the branch of civil law dealing with right and obligations of mercantile person.

### Commercial Law:

It refers to the rights and obligations of commercial persons who deal with commercial transactions in respect of commercial property.

### Agreement Meaning/Definition:

Section 2 (e) of the Indian contract act states that every promise and every set of promises, forming the consideration for each other is an agreement.

Agreement=Offer + Acceptance

### Characteristics of an Agreement:

1. Plurality of person
2. Consensus ad – idem

Agreement is the meeting of the minds of the parties in full.

E.g. A owns 2 horses named X and Y, is selling horse X to B. B thinks he is purchasing horse Y. (There is no consensus ad idem and no contract)

3. Mental condition
4. Promise or Reciprocal promises

### Kinds of Agreement:

- A. Social Agreements
  - i. Not enforceable by law
  - ii. Cannot be called contracts

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E.g. Agreement to attend a dinner at a friend's house.

B. Legal (valid) Agreement

- i. It is an agreement
- ii. An intention to create legal obligation

C. Void Agreement

- i. An agreement not enforceable by law is said to be void (sec. (g)).

D. Voidable Agreement

- i. Until it is avoided it is a good contract
- ii. A voidable agreement is one which is enforceable by law at the option of one or more of the parties thereto, but at the option of others (sec 2(i))

E.g. The sale of Y's house to X. This contract can be avoided by Y. X cannot enforce the contract. But Y can if he so desires.

E. Unenforceable Agreement

- i. An agreement is valid in the eyes of law
- ii. Cannot be enforced in the courts because of some technical defects in procedural matters of formation & enforcement.

E.g. Want of registration, Non-payment of the requisite stamp duty.

F. Illegal Agreement

- i. It is against the provisions of the law.

E.g. An agreement to commit murder.

G. Agreement to Agree in future

- i. An agreement to agree in future is a contradiction.
- ii. It is absurd to state that a man enters into an agreement till the terms of the contracts are settled.
- iii. Until the terms are settled, he is free to retire from the bargain.
- iv. There can be no binding contract unless all the material conditions of contract have been agreed upon.
- v. Thus agreement to agree in future is not a contract.

**1.1.1 Essentials of a Valid Contract: }  
1.1.2 Essentials of a Valid Contract: }**

1. Plurality of persons

- i. There must be two persons or groups of person to form a contract.
- ii. Knowledge of a contract.

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2. Offer and acceptance

- i. There must be a lawful proposal or lawful acceptance
- ii. The terms of the offer and acceptance must be definite.
- iii. Proposal when accepted becomes a promise or agreement.
- iv. Offer & acceptance must be consensus ad-idem (it means both the parties must agree on the same thing in the same sense)

3. Legal Relationship, Legal Consequences, Promises & obligations recognized by law.

- i. Two parties enter into an agreement; their intention must be to create a legal relationship between them. If not there is no contract.

E.g. A husband promised to pay his wife a household allowance of \$30 every month. Later the parties separated and the husband failed to pay the amount.

4. Lawful Consideration

- The agreement to be enforceable by law.
- Something returned by both the parties.
- Consideration may be past, present or future.
- But it must be real definite lawful.

5. Contractual capacity of parties (Competency)

- The parties to be agreement must be capable of entering into a valid contract

**Capability to valid contract**

- Age of Majority
- Is of sound mind and
- Is not disqualified from contracting by any law.

**Incapacity**

- Minority
- Lunacy
- Idiocy
- Drunkenness
- Professional status etc....

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If a party belong to any of the above, the contract becomes an invalid contract except in some special cases.

### 6. Free and Genuine consent

- There is absence of free & genuine consent if the agreement is induced by coercion, undue influence, fraud, misrepresentation, mistake etc....

### 7. Lawful object

- Object of the agreement must not be:
  - Illegal
  - Immoral
    1. Opposed to public policy

### 8. Agreement not Declared void

- Even though if contract fulfils above things but if any law declared as void.
- Section 24 to 30 of the Indian Contract Act specify certain types of agreement expressly declared to be void
  - An agreement on restraint of marriage.
  - A wagering agreement etc....

### 9. Certainty & possibility of performance

- The terms of agreement must be certain and not vague or ambiguous.
- The terms of agreement must be such as are capable of performance.

E.g. A agrees to sale B 100 tons of oil. Here agreement is vague or uncertain

If it is coconut oil dealer it is natural to say that the item is coconut oil.

#### **a. Pre-Contractual impossibility**

A contract which at the time it was entered into was impossible to perform is void ab initio.

E.g. A promise to bring honey from moon.

#### **b. Post-Contractual Impossibility**

A contract which at the time it was entered into was capable of being performed may subsequently become impossible to perform or unlawful. In such cases contract become void. It is known as supervening Impossible or Doctrine of Frustration.

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**c. Legal Formalities**

- Agreement may be oral or writing.
- Writing it must comply with the necessary legal formalities.
  - Stamping
  - Registration &
  - Attestation.
- Agreement is to be made in the presence of requisite witness.
- Above things want to fulfil if not it cannot be enforced by law.

**Some of the contracts which must be in writing if not invalid are:**

- A promise to pay a time barred debt
- An arbitration agreement.
- Lease agreement for a period of more than three years.
- Contracts of Insurance.
- Negotiable instruments.  
E.g. Bill of Exchange, Promissory notes etc....
- Memorandum & Articles of Association of a company.
- Contracts relating to transfer of immovable property & so on.

**Some of the contracts which must be registered are:**

- A promise made without consideration on account of natural love and affection between the parties standing in near relation.
- Documents of certain transactions which are compulsorily to be registered under sec.17 of the Registration Act.
- Contracts relating to transfer of immovable property under the transfer of under the Transfer of Property Act 1882.
- Memorandum & Articles of association mortgages & charges under The Companies Act 1956 & so on
- Indian Stamp Act 1894 certain instruments are chargeable with duty of stamp of the amount indicated in schedule I of the Act E.g. Bills of Exchange promissory note partition deed share/debenture certificate pledge, Mortgage deed etc....

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- If not stamped not shall not admitted on evidence in a court of law.
- A contract or legal or valid agreement must exist above all elements if not voidable, void, illegal or unenforceable.

### 1.1.3 Contract Meaning/Definition:

According to sec 2 (h) of Indian Contract Act 1872 an agreement enforceable by law is a contract.

#### Classification /Types of contracts:

##### **I. Classification according to validity**

###### 1. Void Agreement:

An agreement not enforceable by law is said to be void

###### 2. Void Contract:

A contract enforceable by law becomes void.

###### 3. Voidable Contract:

An agreement which is enforceable by law at the option of one or more of the parties thereto, but not at the option of the other or others, is a voidable contract (sec2 (i))

###### 4. Illegal Contract:

Criminal nature & where it is based on immoral.

##### **II. Classification according to formation**

###### 1. Express Contract:

Contracts entered into between the parties by works spoken or written.

###### 2. Implied Contract:

It inferred from the circumstances of the case and conduct of the parties.

E.g. Public bus – Automatic teller machine for ticket. A enters a hotel drinks coffee & pays the bills.

###### 3. Quasi – Contract: It is an obligation imposed by law, regardless of agreement.

E.g. ‘A’ a trade man leaves goods at ‘B’ house by mistake. B treats the goods as his own. He is bound to pay A for them. Both parties are not in contract.

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**III. Classification on the basis of obligation to perform**

1. Bilateral Contract:

Both parties make a promise

2. Unilateral Contract:

One party makes a promise that the other party can accept only by doing something.  
(Only one party to perform the obligation)

**IV. Classification on the basis of execution**

1. Executory:

It is a contract in which promises of both of parties have yet to be performed (one or more parties has not performed its obligation)

E.g. A has paid Rs.5 to B in consideration of which B promised to deliver a book to A. B's part to deliver the book is outstanding while A has performed his part.

2. Executed Contract:

It is when all parties have fulfilled their obligations.

**1.1.4 Formation of a Contract**

I. Offer and Acceptance

II. Consideration and capacity

III. Free Consent

IV. Lawful Object

**I. Offer and Acceptance**

Offer Meaning:

- When one person signifies to another his willingness to do.
- The person making offer is known as offeror or proposer or promisor.
- The person to whom the offer is made is called offeree or promisee.

Characteristic of Offer:

- It must be an expression of willingness to do.
- It must be made to another person.
- It must be made with a view to obtain the assent of the second party.

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- Expression of willingness to create legal obligation.

### Types of Offer:

#### **1. Express and Implied Offer**

- If an offer is made by words, spoken or written.
- If an offer is made other than in words is implied offer.

#### **2. Specific and General Offers**

- When offer is made to a definite class of persons it can be accepted by that particular person.
- When offer is made to the world at large which could be accepted by anyone. E.g. reward to a person supplying information.

#### **3. Positive and Negative Offers**

- An offer to do something is a positive offer.
- An Offer not to do something is a negative offer.

### Legal Rules & Essentials Regarding Offer

- The offer may be Express or implied
- The offer may be positive or negative
- Offer must intend to create legal relationship
- Terms of offer must be certain
- The offer must not be ambiguous, uncertain and vague.
- An Offer may be made to specific person or class of persons or to any one in the world at large.
- The offer must express the final willingness of the offeror.
- Every offer must be communicated to the offeree.
- Mode of Communication of offer
  - Word of mouth
  - By writing
  - By conduct
  - Offer by post or telephone

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- An offer must be distinguished from
  - Invitation to make/offers, quotations, circular etc.....
  - Declaration or statement of intention, tender etc....
  - An answer to a question.
- Offer must be made with a view to obtaining the assent.
- Offer should not contain a term, the non-compliance of which would amount to acceptance.
- An offer may be conditional.
  - Offer with special conditions
  - Standing Offers or open offers
  - Cross Offers.

Termination of Offer (sec 6)

- By notice of revocation or lapse
- By lapse of time
- By failure of the acceptor to fulfil a condition precedent to acceptance.
- By failure to accept according to the mode prescribed
- By the death or insanity of the offeror
- By rejection
- By subsequent illegality or destruction of subject matter.

Acceptance Meaning/Definition

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

Essentials and Legal rules of a valid acceptance

- Acceptance must be absolute and unconditional.
- Acceptance by usual mode as desired by the offeror.
- Acceptance cannot be made before communication of an offer
  - Acceptance may be express or implied.

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- Acceptance must be given within a reasonable time.
- Acceptance must show to fulfil a promise.
- Acceptance must be by an ascertained person i.e., the person to whom the offer is made (offeree)
- Offer once rejected cannot be accepted until it is renewed.
- Acceptance of offer means acceptance of all terms attached to the offer.
- Acceptance must be made before the lapse or revocation of an offer.
- The acceptor must be aware of the proposal at the time of an offer.
- Silence does not imply acceptance.
- Rules for communication of Acceptance (s.4).

## II. Consideration and Capacity

### Consideration Meaning/Definition

Bargaining that leads to an exchange of value between the parties. Consideration can be anything that someone might want to bargain for. It is the inducement to make the deal, or the thing that is bargained for.

E.g. *McInerny v. Charter Golf*

### Elements of Consideration:

- An act or abstinence
- Should be done at the desire of promisor
- Act may be done by the promisor or any other person.
- Act is either already executed or in process or in future.

### Legal Rules Regarding Consideration

- Consideration is required both for formation and discharge of an agreement or contract. – Sec.25
  - The Indian Contract Act, 1872 – Agreement without consideration is void
- Consideration may be past, present or future.
- Consideration may be either positive or negative. Sec 2(d)
- Consideration may be forbearance to sue.

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- Forbearance applicant has right of action.
- Consideration must move (i.e., must be done or promised to be done at the desire of the promisor.
- Consideration may be furnished by the promisee or any other person. Sec.10
- Consideration must be lawful.
- Consideration must be real and not illusory.
- Consideration must be of some value in the eyes of law.
- Consideration need not be adequate.
- Consideration must not be the performance of existing duties.
- Exceptions to the Rule No consideration No contract.

### **Nature of Love and Affection – Sec.25**

- Compensation for past voluntary service – sec 25(2)
- Promise to pay time-barred debt – sec 25(3)
- Completed gift
- Agency-no consideration is necessary to create agency
- Remission – receive less than what is due
- Bailment – giving article to a person.
- Guarantee.

### **Contractual Capacity Meaning**

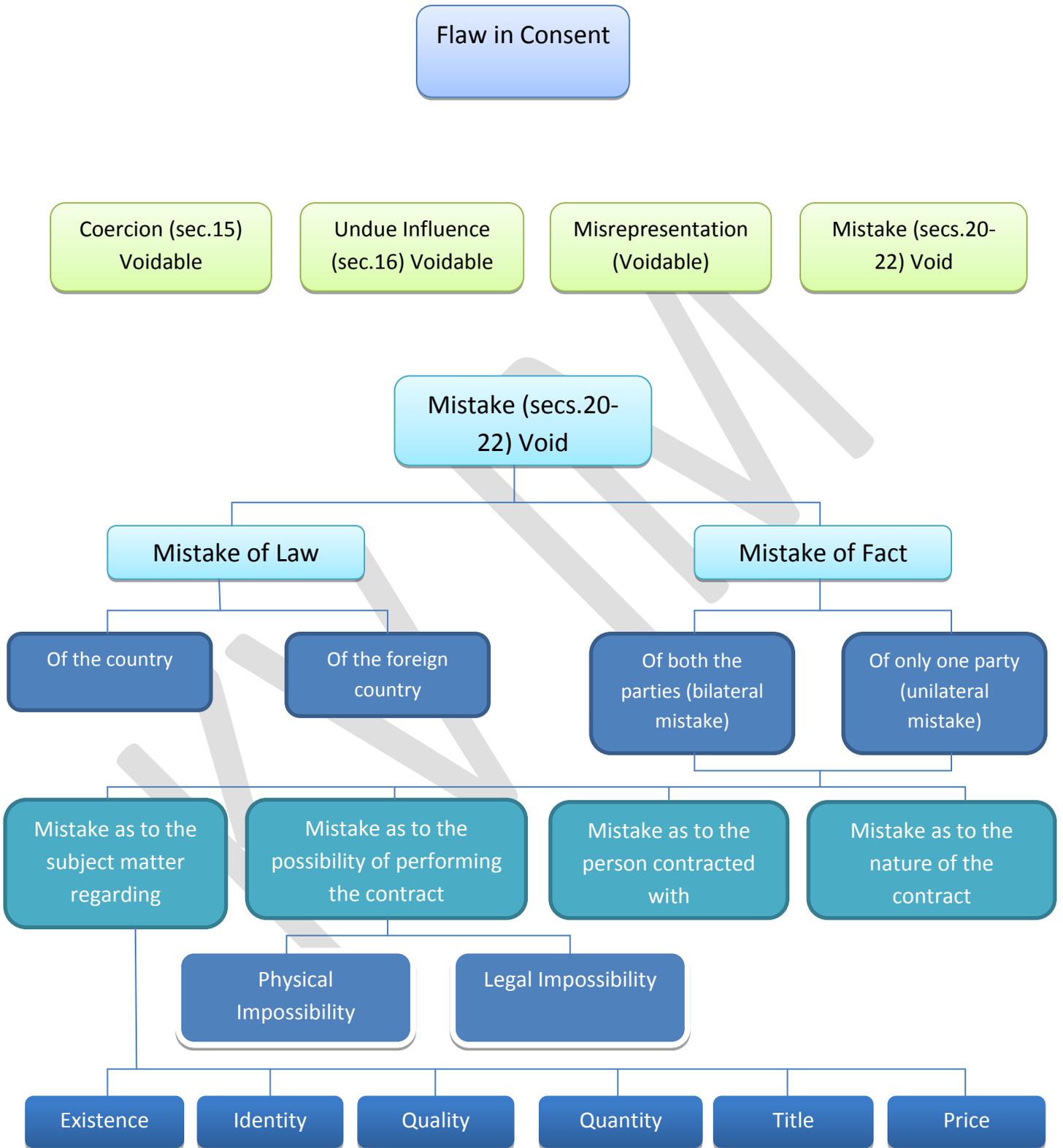
Capability of the parties. Sec 11 of the Indian Contract Act.

Capability of contract:

- Persons of Sound Mind
- Age of Majority etc.....

### **III. Free Consent:**

Meaning: Two or more persons are said to be in consent when they agree upon the same thing in the same sense.



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**1. Coercion Meaning:**

Coercion refers to an act where a person is compelled to enter into a contract by use of force by the other party.

E.g., P threatens to shoot Q if he does not let out his house to P, and Q agrees to do so.

**2. Undue Influence Meaning:**

A Person is deemed to be in a position to dominate the will of another.

E.g., Father and son

**3. Misrepresentation Meaning:**

Misrepresentation is any untrue statement made by a party about the contract to another.

**IV. Lawful Object:**

- Forbidden by law
- The object and consideration must not defeat the provisions of any law
- The object and consideration must not be Fraudulent.
- If it involves or implies injury to the person or property of another.
- The object and consideration must not be immoral
- The Object and consideration must not be opposed to public policy.

**1.1.5 Performance/Discharge of Contracts:**

Performance may be:

- Actual Performance
- Attempted Performance

Offer to perform is called Tender of Performance or Attempted performance

**Essentials of a valid Tender:**

- Tender must be unconditional
- Proper time and place
- Reasonable opportunity to promise
- Whole and not only of the part

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- Tender must be in proper form
- A tender may be either tender of goods or money
- Tender must be made to the promisee etc.....

**Person entitled to demand performance:**

- Promisee
- Legal Representative
- Joint Promisees
- Third Party

**Persons bound to perform the promise in a contract:**

- By the parties
- Promisor (sec.40)
- Representatives (Sec.37)
- Agent (sec.40)
- Third Person (sec.41)

**Time for performance:**

- When no time is specified (sec.46)
- When time is specified (sec.47)
- On Application for performance by promise (sec.48)

**Time fixed for performance as essence of the contract:**

- Effect of failure to perform at fixed time contract in which time is essential
- Effect of such failure when time is not essential
- Effect of acceptance of performance at time other than that agreed upon.

**Place for performance of a contract:**

- Without application for performance by promisee (sec.49)
- Manner of performance (sec.50)

**Performance of Reciprocal Promises:**

- Mutual and Dependent

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- Mutual and Independent
- Mutual and Concurrent
- Reciprocal promise to do things legal and also other things illegal (sec.57)
- Alternative Promises (sec.58)
- Order of Performance (sec.52)
- Consequences of Preventing performance (sec.53)
- Effect of default (sec.54)

### **Contracts which need not be performed:**

- According to Sec.62 to 67 of the Indian Contract Act
- If the parties to a contract agree to substitute a new contract for it. (sec.62)
- Promisee may dispense with or remit, wholly or part the performance or extend the time. (sec.63)
- When a person at whose option a contract is voidable rescinds it. (sec.64)
- If any promise neglects or refuses to afford the promisor for reasonable facilities. (sec.67)
- When a contract becomes void because of impossibility or illegality. (sec.56)

### **1.1.6 Breach of Contract and its Remedies**

#### **Breach of contract Meaning:**

Parties to a contract are expected to perform their respective promises. If a party breaks his obligation which the contract imposes, there take place breach of contract. Breach of contract may be:

- Unilateral
- Bilateral

Breach may be:

#### A. Actual Breach of Contract

- At the time when the performance is due
- During the performance of the contract
  - Express Repudiation (by word or act)

- Implied Repudiation or Impossibility created by the act of party to the contract.

B. Anticipatory Breach of contract

- By Renunciation (Express repudiation)
- By creating some Impossibility (Implied Repudiation)

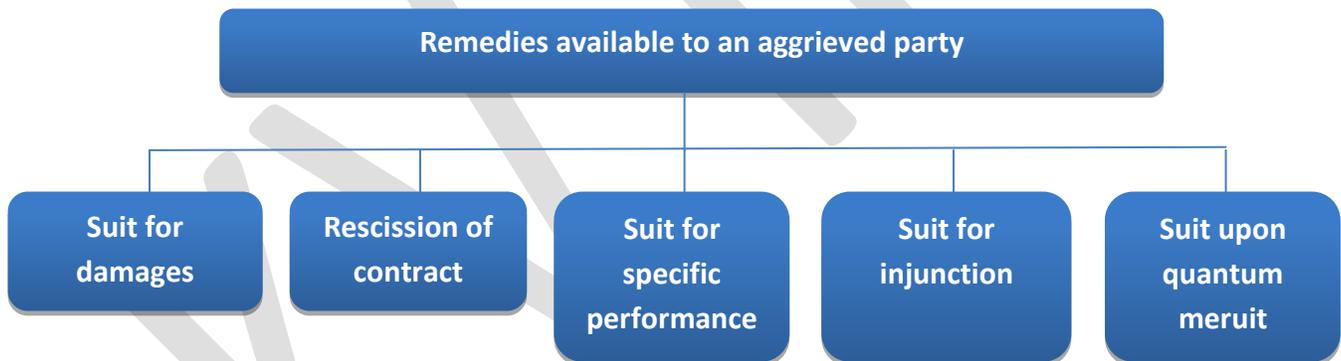
Measure of Damages in Anticipatory Breach of contract:

- If the contract is ended at once
  - If the contract is kept alive till the date of performance of the contract.
- Remedies in Case of Breach of Contract

**Remedies in Case of Breach of Contract**

I. **Suit for damages (sec.39)**

Compensation for Loss or Damage caused by Breach of contract (sec.73):



According to sec.73 of the Indian Contract Act which deals with the compensation for loss or damage, the aggrieved party may claim the damages as follows:

- Ordinary damages
- Special damages
- Aforesaid Compensation is not for remote or indirect loss or damages.

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**Kinds of Damages:**

**1. Ordinary or General Damages:**

E.g., X agreed to sell B 100 glass bottle at Rs. 20,000, the delivery to be given on 15th January. X failed to give delivery. The remedy for B would be to claim the difference between the market price and contract price.

**2. Special Damages:**

E.g., P bought some cake from L. P sold the cake to B, who sold it to various dealers who in turn sold to farmers, who used it for feeding cattle. The copra cake was poisonous and the cattle fed on it died.

**3. Exemplary Damages:**

Damages which are intended to show the court's strong disapproval of the conduct of the defendant in committing the wrong.

E.g., Promise to marry, where a banker refuses to honour the cheque in spite of having enough funds with him belonging to the person issuing cheque.

It is also known as Vindictive or Punitive damages.

**4. Nominal Damages:**

If Joe and Ann have a contract, Ann breaches and Joe suffers a \$1,000 loss as a result of Ann's breach, then Joe may be awarded \$1,000 in damages because that was the amount of loss he suffered.

**5. Remote Damage:**

E.g., Mr. X's and family travelled from Chennai to Ooty. But the train went in wrong direction and the family had to get down at a place, where there was no conveyance and no place to stay. The result is they had to walk home several miles at midnight on drizzling night. Mr. X got ill and filed a suit.

- a. for damages due to inconvenience
- b. also damages for wife's illness.

The court awarded damages in respect of the first claim but not the second.

**6. Restitution and compensation:**

If a contract is broken, law will endeavour, so far as money can do it, to place the injured party in the same position as if the contract had been performed.

E.g., in a contract of sale of goods, the damages are measured equal to the profit, i.e., the difference between the contract price and market price such goods on the date of breach.

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**7. Mental pain and suffering:**

In ordinary cases damages for mental pain and suffering caused by the breach are not allowed. But they may be allowed in special cases.

E.g., a photographer who had agreed to take photographs at a wedding, failed in breach of his contract to appear there. As a result the bride had no photographs of her wedding. She was allowed damages for resulting injury to her feelings.

**8. Mitigation of Loss:**

The injured party has to take all reasonable steps to minimize the loss caused by the breach.

E.g., X took a shop on lease and paid an advance, the person could not give him possession and the X chose to do no business for 8 months though there were other shops available in the vicinity. Held, he was entitled only to a refund of his advance, and nothing more, as he had failed in his duty to minimize the loss by not taking another shop.

**9. Liquidated and Unliquidated damages:**

Pre-estimate of the damage is known as liquidated.

**II. Suit for Rescission of contract (sec.39)**

Rescission means a right not to perform obligation.

E.g., X agrees to supply 10 tons of wheat to Y on 20th Oct. Y promises to pay for the goods on its receipt. X does not supply the goods on the due date. Here, Y is discharged from the liability of paying the price. Y is entitled to rescind the contract and to claim compensation for the damage which he has sustained because of non-supply of goods on the due date.

**III. Suit for Specific Performance:**

- Where monetary compensation is an adequate remedy.
- Where the court cannot supervise the execution of the contract e.g., building contract.
- Where the contract is for personal services e.g., contract to paint a picture.
- Where one of the parties is incompetent to contract e.g., minor.
- Where the contract is ultra-virus e.g., where the contract is made by a company in excess of its power as laid down in its memorandum of association or against the Companies Act.
- Where the contract is made by trustees in breach of trust.
- Where a material part of the subject-matter of the contract has ceased to exist, e.g., where a contract is for the purchase and sale of a ship which is sunk after the contract had been entered into.

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- Where the contract is inequitable to either party.

The contracts which may be specifically enforced are as follows:

- Agreement to sell or transfer immovable property.
- Sale with a condition to repurchase.
- Agreement for exchange of immovable property.
- Agreement to lease.
- Contract by limited owner to sell or lease.

**IV. Suit for injunction:**

An injunction is preventive relief.

**V. Suit upon quantum meruit:**

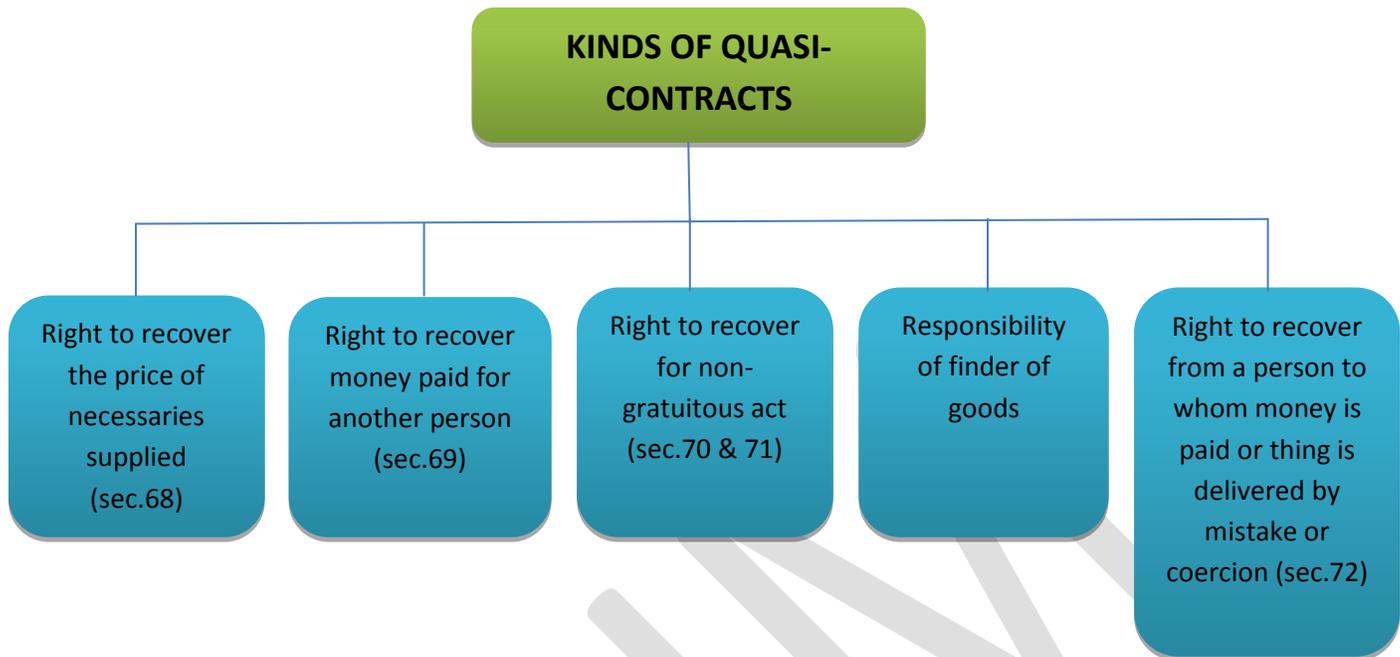
It means a right to claim the compensation for the work already done.

E.g., C an owner of a magazine engaged P to write a book to be published by instalments in his magazine. After a few instalments were published, the publication of the magazine was stopped. It was held that P could claim payment for the part already published.

**1.1.7 Quasi-Contract Meaning**

- A quasi contract is a fictitious contract created under legal obligations, similar to a valid contract.
- These contracts are also known as implied-in-law contracts. What makes this different is that the parties involved do not intend to create a contract.
- A quasi contract is created by the Court.
- For the same reason, there is no actual offer or acceptance or an agreement between the parties.
- Also, a quasi-contract is based on the principle of unjust enrichment.
- According to this principle, a person is not allowed to draw benefit at the cost of someone else.

E.g., Plumber who accidentally installs a sprinkler system in the lawn of the wrong house. The owner of the house had learnt the previous day that his neighbour was getting new sprinklers. That morning, he sees the plumber installing them in his own lawn. Pleased at the mistake, he says nothing, and then refuses to pay when the plumber hands him the bill. Will the man be held liable for payment? Yes, if it could be proven that the man knew that the sprinklers were being installed mistakenly, the court would make him pay because of a quasi-contract. If that knowledge could not be proven, he would not be liable.



Certain relations resembling those created by contract (sec.68 to 72)

- Claim for necessaries supplied to a person incapable of contracting on his account (sec.68)
- Reimbursement of a person paying money due by another in payment of which he is interested (sec.69)
- Obligation of person enjoying benefit of a non-gratuitous act (sec.70)
- Rights and liabilities of the finder of lost goods (sec.71)
- Liability of person to whom money is paid or things delivered, by mistake or under coercion (sec.72)

**1. Right to recover the price of necessaries supplied (sec.68)**

If a person is incapable of entering into contract or anyone whom such incapable person is legally bound to support, is supplied by another person with necessaries suited to his conditions in life, the person who has furnished such supplies is entitled to be reimbursed from the property of such incapable person.

Examples: A supplies B, a lunatic, with necessaries suitable to his condition in life. A is entitled to be paid out of B's property.

**2. Right to recover money paid for another person (sec.69)**

If a person who is interested in the payment of money which another is legally bound to pay, pays it, he is entitled to be reimbursed by that other.

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Example: B holds land in Bengal, on a lease granted by A, the Zamindar. The revenue payable by A to the Government being in arrears, his land is advertised for sale by the Government under the revenue law. The consequences of such sale will be the termination of B's lease. B, to prevent the sale and the consequent termination of his own lease, pays to the Government the sum due from A. A is bound to return to B the amount paid by B.

**3. Right to recover for non-gratuitous act (sec.70&71)**

Where a person lawfully does anything for another person, or delivers anything to him not intending to do so gratuitously and such other person enjoys the benefit thereof, the latter is bound to make compensation to the former in respect thereof, or to restore the thing so done or delivered.

Examples: A, a trader, leaves goods at B's house by mistake. B treats the goods as his own. He is bound to pay A for them.

**Essential rules to claim payment under Sec.70 are as follows:**

**a. The thing delivered or act done must be lawful:**

In case of an unlawful act, no payment can be recovered.

**b. The act must have been done with an intention to claim the award:**

Where the act was done without any intention of reward, no payment can be claimed.

Examples:

- i. In the case of Upendra v. Naba, a tank was owned jointly by the two owners. The Corporation ordered the filling up of the tank. One of the co-owners filled up the tank and sued the other for contribution. The Court held that the other co-owner was liable to pay the contribution as the other party filled up the tank with the intention to recover the contribution.
  - ii. A saved B's son from drowning. A cannot claim the reward as the act was done gratuitously, i.e., without any intention of reward.
- c. The other party for whom the act was done or thing delivered must have enjoyed the benefit:**

The act must not have been done against the will of the other party.

Example: Certain villages were irrigated by a tank repaired by the Government. The Government repaired the tank with the intention of recovering the cost of its repairs. The Court held that since the zamindars enjoyed the benefit of an act done lawfully and non-gratuitously, the beneficiaries, i.e., the zamindars were liable to pay. [Damodar Mudaliar v. Secretary of State for India].

#### 4. Responsibility of finder of goods

A person, who finds goods belonging to another and takes them into his possession, is liable as a bailee. As a bailee, he is under an obligation to take reasonable care of the goods found, as a man of ordinary prudence would, under similar circumstances, take of his own goods. He must make reasonable efforts to trace the real owner. For example, if the amount is substantial, he may give a public notice in a newspaper or if the address card is there in a purse found, he must contact the owner at the address.

In case he does not make reasonable efforts to trace the real owner, he will be liable for wrongful conversion of the property. However, until and unless the real owner is found, he remains the owner of the goods against the whole world.

Example: A finds a purse in B's shop. Until the true owner of the purse is found, A is the owner of the purse even though the purse was found in B's shop. However, A must take reasonable care of the purse until the true owner is found. He must also take reasonable steps to trace the real owner. However, A need not go, say, on fast into death until the real owner is found.

#### 5. Rights to recover from a person to whom money is paid or thing is delivered by mistake or under coercion (sec.72)

A person to whom money has been paid, or anything delivered by mistake or under coercion must repay or return it.

Examples: A and B jointly borrow 100 rupees from C. A returns 100 rupees to C. B, who does not know that A had already paid the whole amount and again pays 100 rupees to C. C is bound to return the amount paid by B.

##### **Essentials of a claim on the basis of quantum merit:**

- a. The party doing the work must have been prevented to perform the contract either by the other party by impossibility or illegality and not on his own volition (desire).

Example:

A engaged B to write a book to be published by instalments in a weekly magazine. The magazine had to be abandoned after a few issues. Held, B could ask for remuneration for the work done on the basis of quantum merit. [Planche v. Colburn]

- b. The contract must be divisible: If the contract is not divisible the claim on the basis of quantum merit will not arise.

Examples:

- i. A mate was engaged for a complete voyage against a lump sum payment of 30. The mate died before the voyage was completed. Hence, his wife could not claim on the

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basis of quantum merit as the voyage was not completed and the contract was not divisible. [Cutter v. Powell].

- ii. A agreed to construct four houses for B. After completing two houses, B asks A to stop construction. B must pay for the work already done, i.e., for the two houses.

#### **The cases in which a claim on the basis of quantum merit arises:**

- a. Where an agreement is discovered to be void or becomes void, the party who has taken any benefit under the agreement/contract must restore it or repay it (Sec.65).

Example: A agreed to purchase B's cow and paid an advance of Rs. 100 to B later on. It was discovered that the cow was dead at the time of the contract. B must return the sum of Rs 100 to A.

- b. When something is done or delivered without an intention to do so gratuitously (Sec 70)
- c. Where one party to the contract is prevented from performing the contract by the other party or by impossibility or illegality.

Example: Printing of a book had to be abandoned as it contained libellous matter. The plaintiff was held responsible to recover on the basis of quantum merit. [Clay v. Yates]

S. No	Agreement	Contract
1.	<p><b>Enforceability:</b></p> <p>Offer and acceptance together constitute an agreement.</p>	<p><b>Enforceability:</b></p> <p>Agreement and enforceability together constitute a contract.</p>
2.	<p><b>Legal Obligation:</b></p> <p>Certain agreement may not create any legal obligation.</p>	<p><b>Legal Obligation:</b></p> <p>Contract necessarily creates a legal obligation.</p>
3.	<p><b>Binding on parties:</b></p> <p>An agreement is not always a binding contract.</p>	<p><b>Binding on parties:</b></p> <p>_____</p>
4.	<p><b>Speciality:</b></p> <p>Agreement is a genus.</p>	<p><b>Speciality:</b></p> <p>Contract is specie of an agreement.</p>

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S. No.	Void Agreement	Voidable contract
1.	<b>Legality:</b> A void agreement cannot be enforced by either party.	<b>Legality:</b> A voidable contract can be enforced by the party at whose option it is voidable.
2.	<b>Time of Enforceability:</b> Void agreement is enforceable from the very beginning.	<b>Time of Enforceability:</b> Voidable contract becomes unenforceable only when the party at whose option the contract is voidable, rescinds it.
3.	<b>Compensation:</b> Question of compensation does not arise.	<b>Compensation:</b> Benefitted party must compensate.
4.	<b>Collateral Transaction:</b> Collateral agreement becomes void.	<b>Collateral Transaction:</b> Voidable contract does not affect collateral agreement.

S. No.	Void Agreement	Illegal Agreement
1.	<b>All Inclusive:</b> All void agreements are not necessarily illegal.	<b>All Inclusive:</b> All illegal agreements are void.
2.	<b>Proofs:</b> Void agreements are not illegal until they are proved to be illegal.	<b>Proofs:</b> Illegal agreement remains so from the very beginning.
3.	<b>Collateral Transaction:</b> Void agreements do not involve collateral transaction.	<b>Collateral Transaction:</b> Illegal agreements vitiate not only primary transaction but also collateral transaction. (vitiates – damage or impair)
4.	<b>Punishability:</b> Void agreements are non-punishable.	<b>Punishability:</b> Illegal agreements are always punishable.

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S. No.	Illegal Agreement	Unenforceable Agreement
1.	<p><b>Defect in Subject/Procedure:</b></p> <p>Illegal Agreements are against public policy and law.</p>	<p><b>Defect in Subject/Procedure:</b></p> <p>Unenforceable agreements are not enforceable because of some technical or procedural defects.</p>
2.	<p><b>Timing of Unenforceability:</b></p> <p>Illegal agreements are void from the very beginning and are not enforceable by the court of law.</p>	<p><b>Timing of Unenforceability:</b></p> <p>Unenforceable Agreements are valid in themselves but not enforceable by law.</p>
3.	<p><b>Collateral Transactions:</b></p> <p>Not only primary transaction but collateral transactions are also affected.</p>	<p><b>Collateral Transactions:</b></p> <p>Collateral transactions are possible if the technical defect is removed.</p>
4.	<p><b>Punishment:</b></p> <p>Penalty is imposed.</p>	<p><b>Punishment:</b></p> <p>No penalty is imposed.</p>

## 1.2 AGENCY

### AGENCY:

#### Meaning & Definition of Agency:

Section 182, “An agent is a person employed to do any act for another or to represent another in dealing with third persons. The person for whom such act is done or who is so represented is called the principal”.

#### Principal:

A person for whom the above act is done or who is so represented is called the “PRINCIPAL”.

#### 1.2.1 The Nature of Agency

- Agency relationships are formed by the mutual consent of a principal and an agent.
- Agency is the fiduciary relationship “which results from the manifestation of consent by one person to another that the other shall act in his behalf and subject to his control, and consent by the other so to act”.
- **Agency Law** – The large body of common law that governs agency.
- A mixture of contract law and tort law.

- **Principal** – The party who employs another person to act on his or her behalf.
- **Agent** – The party who agrees to act on behalf of another.

### 1.2.2 Creation/Formation of Agency



#### 1. Express Agency:

- An agency that occurs when a principal and an agent expressly agree to enter into an agency agreement with each other.
- Exclusive agency contract
- Power of attorney
- Express agency contracts can be either oral or written unless the Statute of Frauds stipulates that they must be written.

#### 2. Implied Agency:

- An agency that occurs when a principal and an agent do not expressly create an agency.
- The agency is implied from the conduct of the parties.
- The extent of the agent's authority is determined from the particular facts and circumstances of the particular situation.
  - Incidental authority

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**3. Apparent Agency:**

- Agency that arises when a principal creates the appearance of an agency that in actuality does not exist.
- When an apparent agency is established, the principal is estopped from denying the agency relationship.
- It is the principal's actions that create an apparent agency.

**4. Agency by Ratification:**

- An agency that occurs when:
  - A person misrepresents himself or herself as another's agent when in fact he or she is not, and
  - The purported principal ratifies (accepts) the unauthorized act.

**1.2.3 Types/Classification of agents**

1. **Special Agents** – are people employed to do some particular act or represent his principal in some particular transaction. As soon as the act is performed the authority of agent comes to an end. E.g. an agent engaged to sell a house.
2. **General Agents** – are people employed to do all such acts which are connected with the business of trade of his principal (employer). If principal limits authority secretly, he himself will be bound.
3. **Universal Agents** – are people employed to do all such acts which a principal can lawfully do & can delegate. Agent has unlimited authority.
4. **FROM THE POINT OF VIEW OF NATURE OF WORK TO BE PERFORMED:**
  - a. **Factors** – is a mercantile agent to whom the possessions of goods are given for the purpose of selling them. He usually sells the goods in own name. He can exercise a general right of lien on the goods delivered to him for balance of payment if any.
  - b. **Auctioneer** – is an agent who is appointed by the principal to sell the goods on his behalf at a public auction for a reward in form of commission. E.g. reserve price
  - c. **Broker** – is an agent appointed by the principal for the purpose of selling or buying goods on his behalf. He does not have possession of goods nor can he contract in his own name. He brings seller & buyer together to bargain. He gets commission (brokerage).
  - d. **Commission Agent** – is a mercantile agent who is employed to buy & sell goods for his principal on best possible terms. He transact in his own name. He is entitled to commission. He may or may not have possession.

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- e. **Del credere Agent** – is one who guarantees to his principal, the performance of the financial obligation by party with whom he enters into a contract on principal behalf, in consideration of an extra commission. He becomes surety & become liable on the default of third party.
- f. **Banker** – act as a mercantile agent on behalf of his customer when he collects cheques, drafts, bills, pay insurance premium and buy or sell securities.

### 1.2.4 Duties and Rights of Agent and Principal

#### **Duties of Agent:**

- To carry out the work undertaken according to the directions given by the principal.
- To carry out the work with reasonable care, skill and diligence.
- To communicate with the principal in the case of difficulty.
- To pay sums received for the principal.
- To protect and preserve the interests of the principal in the case of his death or insolvency.
- Not to make secret profit from agency.
- Not to set up an adverse title.
- Not to use information obtained in the course of the agency against the principal.

#### **Rights of Agent:**

- Right of retainer.
- Right to receive remuneration.
- Right of lien.
- Right of indemnification.
- Right of compensation.

#### **Liability of Agent:**

- An agent's liability for a contract depends on the nature of the principle.
- An agent who represents a disclosed principal is not liable on contracts made for the principal.
- Agents are liable on contracts made for a partially disclosed principal unless parties agree otherwise.
- An agent is liable to third parties on contracts made for an undisclosed principal.

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**Duties & Rights of the Principal:**

- To pay remuneration to agent.
- To recover compensation for breach of duty by the agent.
- To forfeit agent's remuneration where he is guilty of misconduct.
- To receive any extra profit made by agent.
- To enforce the various duties of the agent.
- To receive all sums.

**Principal's Liabilities:**

- To indemnify the agent
  - Against consequences of lawful act, and
  - Against consequences of the acts done in good faith.
- Compensate for injury caused.
- To pay remuneration and dues.
- Misrepresentation or fraud by Agent: Is not liable if act falls beyond Agent's authority.
- Liable for contracts entered into by Agent with third persons.
- Agent is imputed notice to Principal.

**Liability of Agent Torts:**

- Agents are liable for their torts except when:
  - Agent exercises a privilege of the principal (e.g., uses an easement).
  - Agent takes privileged action to defend his person or principal's property.
  - Agent makes a false statement in conduct of principal's business but doesn't know the falsity of the statement.
  - Third parties are injured by defective tools or instrumentalities furnished by the principal.

**1.2.5 Termination of Agency:**

**1. By act of parties:**

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- a. By agreement – mutual consent
- b. By revocation of authority by the principal – The principal can revoke the authority of an agent at any time before the authority has been exercised as to bind the principal.
- c. By renunciation by the agent – by giving reasonable notice.

**2. Termination by operation of law:**

- a. By performance of contract of agency.
- b. By death of principal or agent.
- c. By expiry of time – where agency is for fixed time period.
- d. By insolvency of the principal.
- e. By destruction of subject matter – agency was created to sell a house & house gets destroyed due to some reason.
- f. By becoming alien enemy – where principal & agent are from different countries.

**Irrevocable Agency:**

The agency which a principal cannot revoke is known as irrevocable agency.

- a. Where the agency is coupled with interest – A gives authority to B to sell A's land & to pay himself out of the proceeds, the debt due to him from A. A cannot revoke this authority.
- b. Where the agent has incurred personal liability – When the agent has bought goods in his own name, the principal cannot refuse to pay.
- c. Where the authority has been exercised partly – X authorizes Y to buy 10 bags of wheat on Y's account. Y buys 10 bags of wheat in the name of X. X cannot revoke the authority.

## **1.3 THE SALE OF GOODS ACT 1930**

### **1.3.1 Contract of sale of goods**

Section 4 (1) of the Sale of Goods Act, 1930:

“A contract of sale of goods is contract whereby the seller transfers or agrees to transfer the property in goods to the buyer for a price”.

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**Essential Characteristics of a Contract of Sale of Goods:**

- There must be two parties
- Ownership – Property
- Contract of sale must be Goods
- Consideration for sale of goods must be money not goods.
- Contract may be writing or in oral or both or implied.
- Contract of sale includes both an actual sale and agreement to sell.

**Agreement to Sell (Section4 (3) :**

The transfer of property in goods is to take place at a future date or subject to some conditions thereafter to be fulfilled, the contract is called an Agreement to sell.

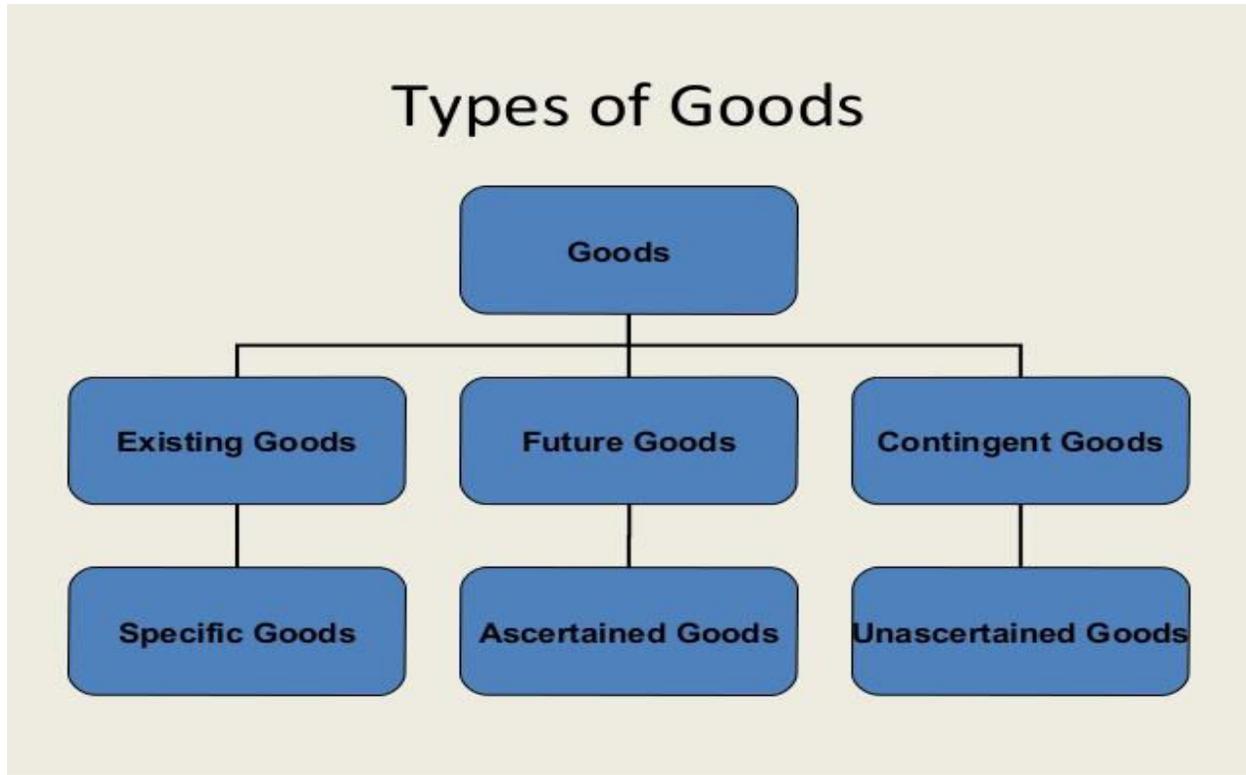
E.g., A agrees to buy B's car and pay for it, if his wife approves. It is an agreement to sell for B and an agreement to buy for A.

S. No.	Delivery	Payment
1.	Immediate	Immediate
2.	Immediate	By Instalments
3.	Immediate	At some future date
4.	By Instalments	By Instalments
5.	By Instalments	Immediate
6.	By Instalments	At some future date
7.	At some future date	At some future date
8.	At some future date	Immediate
9.	At some future date	By Instalments

**Goods-the Subject-matter of contract of Sale:**

Subject matter meaning: The things for which a contract of sale can be made. Only goods can be subject matter of sale.

**Types of goods:**



Factors	Future Goods	Contingent Goods
Possession or Acquisition	Goods not with the buyer	May or may not happen
Certainty	More certain	Less certain
Control over factors of production	Within human control	Not within human control

**Documents of Title of goods E.g.:**

- Bill of lading-given by ship owner
- Dock warrant – issued by dock owner
- Warehouse keeper’s certificate
- Railway receipt

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- Delivery Order- issued by owner of goods
- Charter party – it is not a document of title of goods. Agreement between the ship-owner and merchant for carriage of goods.

### 1.3.2 Transfer of Title by Non-owners

#### **B. Exceptions Under the Sale of Goods Act,1930**

- a. Estoppel. (sec.27)
- b. Sale by a mercantile agent (sec.27)
- c. Sale by one of several joint owner (sec.28)
- d. Sale by a person in possession of goods under a voidable contract (sec.29)
- e. Sale by seller in possession after sale [sec.30(1)]
- f. Sale by an unpaid seller [sec.54(3)]

#### **C. Exceptions as provided in other laws:**

- Sale by a finder of lost goods (sec.71)
- Sale by a Pawnee
- Sale by Official Assignee or Official Receiver in case of insolvency of individual
- Execution Sales: Under Order 21 of Civil Procedure Code, Officers of court can sell goods
- Sale by Executors and Administrators.
- Purchase in Market Overt – It means Open public and legally constituted market.

#### **D. Rights of the Buyer:**

- Rights to have delivery of the goods(sec.37)
- Right to reject the goods.[sec.37(1)(2)]
- The buyer of goods is not bound to accept delivery of the goods in instalments.[sec.38(1)]
- Right to notice of Insurance.[sec.39(3)]
- Right to Examine the goods delivered(sec.41)
- Right to sue for breach of contract.
  - Suit for Damages.(sec.57)

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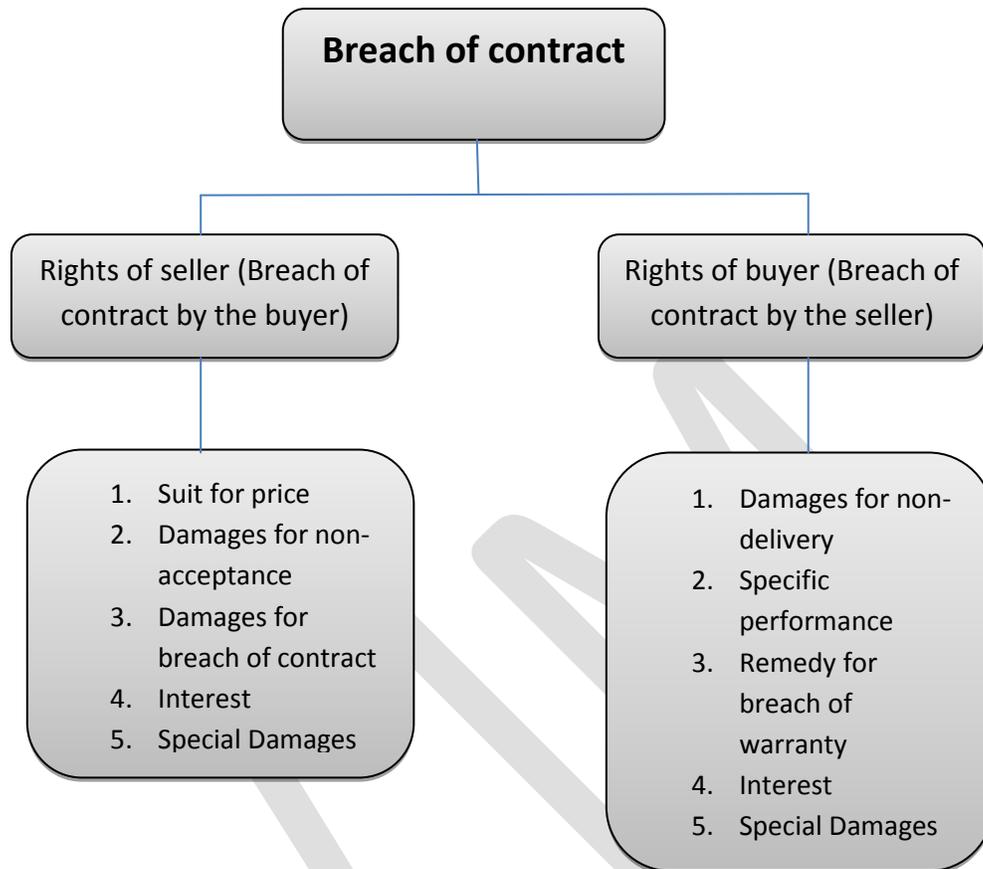
- Suit for Price.
- Right to suit for specific performance.(sec.58)
- Right to repudiate of contract before due date.(sec.60)
- Suit for Interest.[sec.61(2)]
- Suit for breach of warranty. (sec.59).

**E. Duties of the Buyer:**

- To accept the goods and pay for them.
- To apply for delivery
- To demand delivery at a reasonable hour
- To accept delivery in instalments if stipulated in the contract
- To assume risk of fall in course of transit
- To inform the seller about rejection of goods
- To accept delivery within reasonable time of its tender.
- To pay goods bought.
- To pay damages for non-acceptance of goods.

**F. Consequences of breach of contract:**

- Damages of non-acceptance.(sec.56)
- Damages for non-delivery.(sec.57)
- Specific performance.(sec.58)
- Remedy for breach of warranty.(sec.59)
- Repudiation of contract.(sec.60)
- Interest and special damages
- The rights of buyer against seller for breach of contract.



### 1.3.3 Conditions and Warranties

#### **Condition:**

It is a stipulation essential to the main purpose of the contract, the breach of which gives right to repudiate the contract and to claim damages.

E.g., A says to B, a horse dealer, I want a horse which runs at a speed of 60 kilometres per hour. B points out a particular horse and says that it runs at 60 kilometres per hour. A buys the horse. Later, A finds that the horse runs only at a speed of 45 kilometres per hour. Here there is a breach of condition.

#### **Warranty:**

It is a stipulation collateral to main purpose of the contract, the breach of which gives rise to claim for damages but not the right to reject the goods and treat contract as repudiated.

E.g., A says to B, a horse dealer, I want a good horse. B points out a particular horse and says that it runs at 60 kilometres per hour. A buys the horse. Later, A finds that the horse runs only at a speed of 45 kilometres per hour. Here there is only breach of warranty.

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Factors	Condition	Warranty
Relating to main purpose	Essential to the main purpose of the contract	Subsidiary to the main purpose of the contract
Rights of aggrieved party	Breach of condition gives the aggrieved party a right to reject the contract and get damages	Breach of warranty entitles the aggrieved party to claim damages only
Treating condition as warranty	Breach of condition may be treated as breach of warranty	Warranty cannot become a condition
Legal effect of breach	It affects the legality of the contract	It will not affect the legality of the contract
Discharge on breach	Aggrieved party is free to discharge his promise	Aggrieved party is not free to discharge his promise

**Implied Condition:**

- Conditions as to title [sec.14(a)]
- Condition in case of sale by description (sec.15)
- Condition in case of sale by sample (sec.17)
- Condition in case of sale by description and sample. (sec.15)
- Condition as to quality or fitness [sec.16(2)]
- Condition as to merchantable quality [sec.16(2)]
- Condition as to wholesomeness
- Condition implied by custom or usage of trade [sec.16 (3)].

**Implied Warranty:**

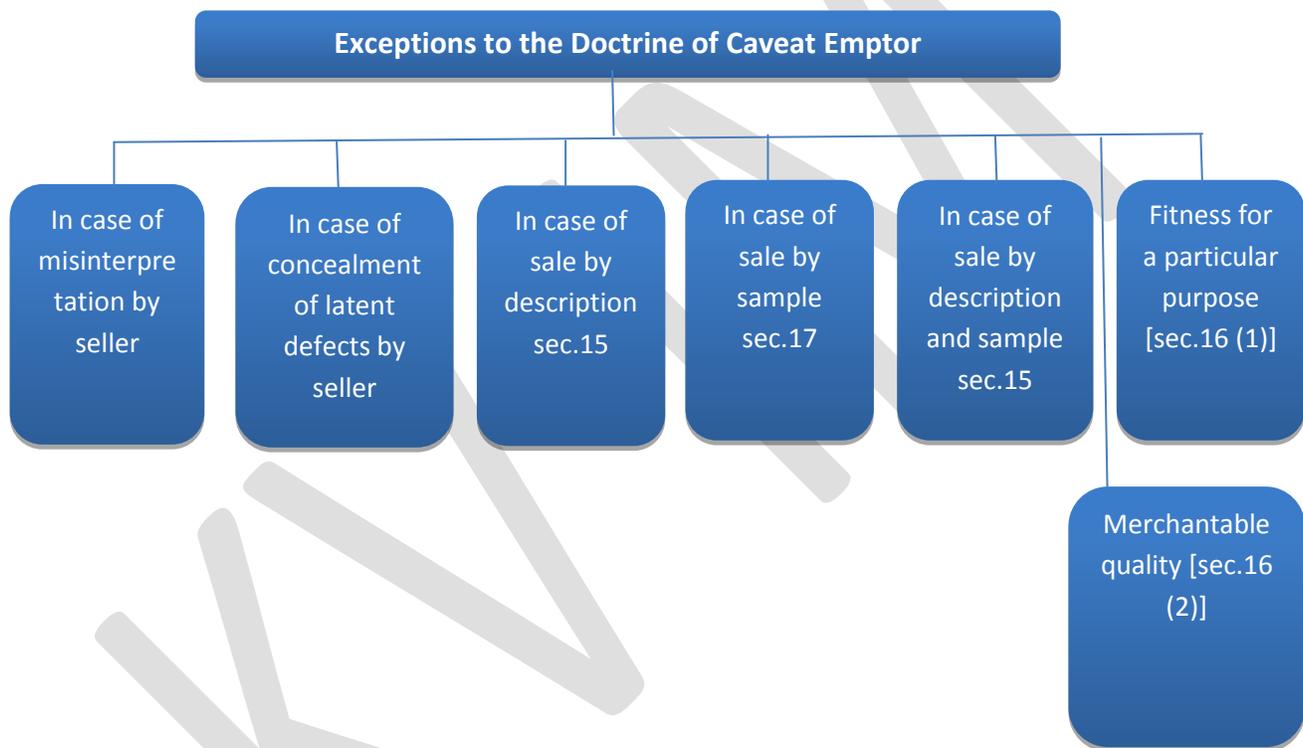
- Warranty as to quiet possession [sec.14(b)]
- Warranty of freedom from burden [sec.14(c)]
- Warranty as to quality or fitness for a particular purpose annexed by the usage of trade [sec.16(3)]
- Disclosure of dangerous nature of goods

**Exclusion of implied conditions & warranties. (sec.62)**

- Express agreement between the parties.
- The course of dealing between the parties.
- The custom or usage of trade.

**Doctrine of Caveat Emptor:**

Caveat Emptor means buyer beware. It means buyer purchase the goods at his own risk provided the seller is acting within the law.



**1.3.4 Performance of Contract of Sale**

It may be defined as the performance of the respective duties of the seller and the buyer as per the terms of the contract.

It comprises of two parties;

- Seller’s duty to deliver the goods
- Buyer’s duty to accept the goods and pay the price.

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**Delivery of goods**

**Delivery Meaning:**

Delivery means voluntary transfer of possession from one person to another. [sec.2 (2)]

**Delivery of Goods Meaning:**

Delivery of goods sold may be carried out by doing anything which the parties agree. Such an act of transfer shall be treated as delivery (sec.33).

**Rules as to Delivery of Goods:**

- Payment and delivery to be concurrent. (sec.32)
- Mode of delivery. (sec.33)
- Effect of part delivery. (sec.34)
- Buyer to apply for delivery. (sec.35)
- Place of Delivery. [sec.36(1)]
- Time of delivery.[sec.36(2)]
- Delivery when the goods are in possession of a third party. [sec.36(3)]
- Demand of delivery to be treated as ineffectual. [sec.36(4)]
- Expenses of delivery. [sec.36(5)]
- Delivery of wrong quality. (sec.37)
  - Delivery of goods less than contracted for
  - Delivery of goods in excess of the quantity contracted for
  - Delivery of goods contracted for mixed with other goods.
- Delivery by instalment. (sec.38)
- Delivery to carrier or wharfinger. (sec.39)

**Transfer of property, Possession and Risk:**

There are 3 stages in Performance:

- The transfer property in the goods
- The transfer of possession of the goods
- The passing of the risk.

**Significance of transfer of ownership:**

- Risk follows ownership
- Owner to take action against third parties
- Insolvency of the seller or the buyer
- Seller's right to suit for price.

**Passing of Property:**

- Goods must be ascertained
- Intention of the parties

**Specific Goods: (sec.20-22) – rules relating to transfer of specific goods:**

- Passing of property at the time of contract
- Passing of property delayed beyond the date of contract
  - Goods not in a deliverable state
  - When the price of goods is to be ascertained by weighing, etc.,
  - Unascertained goods (sec.23)

**Delivery to carrier:**

- Absolutely for the buyer
- Absolutely for the seller
- Goods sent on Approval or on sale or return (sec.24)

**1.3.5 Rights of Unpaid-Seller**

**Two kinds of Unpaid-Seller:**

1. Against the goods:
  - When the property in the goods has passed
    - i. Right of lien
    - ii. Right of stoppages in transit
    - iii. Right of resale
  - When the property in the goods has not passed

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- i. Right of withholding delivery
- ii. Right of lien
- iii. Right of stoppage in transit
- iv. Right of resale

2. Against the Buyer Personally:

- Right to sue for price
- Right to sue for damages
- Right to sue for interest.

**Unpaid Seller's Lien:**

- No stipulation as to credit
- Expiry of credit period
- Insolvency of buyer

**Auction of Sale:**

An auction of sale is a public sale where people will compete in purchasing the property by offering advancing prices and the property is given to the highest bidder.

**Rules of Auction of sale:**

- Where goods are put up for sale in lots.
- The sale is complete when the hammer falls.
- The seller may reserve expressly the right to bid.
- If he bids without reserving the right to do, such bidding becomes fraudulent.
- If the original bidder fails to pay, the auctioneer can re-sell.

## 1.4 NEGOTIABLE INSTRUMENTS ACT 1881

**Negotiable instruments:**

Negotiable instruments are writings that can be transferred from person to person as a substitute for money or an instrument of credit.

E.g., Promissory note, Bill of Exchange.

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- Negotiation is transferring ownership of negotiable instrument to another party.
- An endorsement is the signature of the owner made on the back of an instrument.
- Holders in due course acquire rights superior to those of the original owner.

**Parties to Negotiable Instruments:**

✓ <b>Payee</b>	✓ <b>Bearer</b>
✓ <b>Drawer</b>	✓ <b>Holder</b>
✓ <b>Drawee</b>	✓ <b>Holder in due course</b>
✓ <b>Acceptor</b>	✓ <b>Endorser</b>
✓ <b>Maker</b>	✓ <b>Endorsee</b>

**1.4.1 Nature or characteristics or Essential**

- Easy Transferability
- Title to transferee
- Right to file suit
- Notice of transfer
- Presumption
- Procedure for suits
- Number of transfer
- Rule of evidence
- Exchange.

**Presumption as to Negotiable Instruments:**

- Consideration
- Date
- Time of acceptance
- Transfer
- Order of Endorsement
- Stamping

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- Holder in due course
- Proof of protest

**Different kinds of Negotiable Instruments**

- Promissory note
- Bill of Exchange
- Cheque
- Pay Order
- Demand draft
- Hundi
- Railway receipt
- Delivery note
- Dividend warrants
- Debentures etc.....

**Differences between Promissory Note and Bill of Exchange:**

S. No.	Promissory Note	Bill of Exchange
1.	It contains a promise to pay and is presented for payment without any previous acceptance by the maker.	It is required to be accepted either by the drawee or by someone else on his behalf, before it can be presented for payment.
2.	It cannot be made payable to the maker himself. The maker and the payee cannot be the same person.	The drawer and payee or the drawee and the payee may be the same person.
3.	In the case of a promissory note there are only two parties, the maker and the payee.	There are three parties, drawer, drawee and payee.
4.	A promissory note can never be conditional.	A bill of exchange cannot be drawn conditionally, but it can be accepted conditionally with the consent of the holder.

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5.	In case of dishonour no notice of dishonour is required to be given by the Holder	A notice of dishonour must be given in case of dishonour of Bill of Exchange.
6.	It contains an order to pay.	

**Differences between Cheque and Bill of Exchange:**

S. No.	Cheque	Bill of Exchange
1.	<b>Drawee:</b> Cheque can be drawn only on a banker.	The drawee may be any person.
2.	<b>Time of payment:</b> A cheque is payable on demand.	A bill may be drawn payable on demand or on expiry of certain period after date or sight.
3.	<b>Grace period:</b> Cheque is payable on demand and no grace period is allowed.	While calculating maturity three days grace is allowed.
4.	<b>Notice of dishonour:</b> Notice of dishonour is not necessary.	A notice of dishonour is required.
5.	<b>Acceptance:</b> A cheque is not required to be presented for acceptance. It needs to be presented only for payment.	Bills have to be presented for acceptance and it is better to present them for acceptance even when it is not essential to do so.
6.	<b>Crossing:</b> A cheque may be crossed.	A bill of exchange cannot be crossed.
7.	<b>Validity period:</b> A cheque is usually valid for a period of six months.	A bill may be drawn for any period.

**1.4.2 Transfer of negotiable instruments and liability of parties**

- Maker primarily liable
- Maker must pay according to the terms of the note
- Liability of 2 or more makers
- Payee's existence, etc.

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**Transfer by Assignment or Negotiation:**

S. No.	Transfer by Assignment	Transfer by Negotiation
1.	The transfer of rights under a contract.	The transfer of a negotiable instrument by a person other than the issuer.
2.	It transfers the rights of the transferor (assignor) to the transferee (assignee).	The person to whom the instrument is transferred becomes the holder.

**Kinds of endorsement:**

- Blank or general endorsement – where endorsee simply puts his signature on the back of the instrument without writing name of the person in whose favour the instrument is endorsed.
- Special or full endorsement – An endorsement with the direction to pay amount mentioned in the instrument to a specified person or his order & the endorser writes his signature under it.
- Partial endorsement – When an endorser is willing to transfer to an endorsee only a part of the amount of the instrument. Such an endorsement does not operate as a negotiation of the instrument.

**The instrument is therefore payable to the bearer:**

- Restrictive endorsement – An endorsement is said to be restrictive if it prohibits or restricts the further negotiability of the instrument. The holder of such an instrument can only receive the payment but he **cannot negotiate it further**. An instrument can be made restrictive only by expressed words.
- Conditional endorsement – It **limits the liability** of the endorser. E.g. “Pay A or order on his marrying B”.

**1.4.3 Enforcement of secondary liability**

He engages merely that the bill will be accepted or paid or both, according to its tenor, and that he will pay only when:

- It is dishonoured.
- And the necessary proceedings of dishonour are duly taken.
  - The liability of the drawer is subject to the two conditions and attaches only upon their fulfilment.

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- The drawer, by merely drawing the bill and signing his name in the bill as such drawer, without more, impliedly engages to be so secondarily liable, as if he has incorporated the provisions of Section 61 in the bill.
- If the bill is not paid, accordingly, the drawer becomes liable for the payment of its value to the holder provided that notice of dishonour is given.

### **To whom drawer is secondarily liable:**

- If any of the endorsers intervening between the holder and the drawer is compelled to pay by the holder, the drawer will be compelled and liable to pay to that endorser.
  - Holder in due course
  - Special rules for cheques and drafts
  - Discharge of negotiable instruments

### **Discharge of Negotiable Instruments:**

The term discharge in relation to negotiable instruments has two connotations, viz.

1. discharge of the instrument, and
2. discharge of one or more parties from liability on the instrument.

A negotiable instrument is said to be discharged when it becomes completely useless, i.e. no action on that will lie, and it cannot be negotiated further. After a negotiable instrument is discharged, the rights against all the parties thereto come to an end, and no party, even a holder in due course, can claim the amount of the instrument from any party thereto. Discharge of the party primarily and ultimately liable on the instrument results in the discharge of the instrument itself. For example, in the following cases the instrument is deemed to be discharged.

1. When the party primarily liable on the instrument (i.e., the maker of the note, acceptor of the bill or drawee bank) makes the payment in due course to the holder at or after maturity (Sec. 78). A payment by a party who is secondarily liable does not discharge the instrument because in that case the payer holds it to enforce it against prior endorsers and the principal debtor.
2. When a bill of exchange which has been negotiated is, at or after maturity held by the acceptor in his own right, the instrument is discharged (Sec. 90).
3. When the party primarily liable becomes insolvent, the instrument is discharged and the holder cannot make any other prior party liable thereon. Notice that in the case of insolvency, the acceptor or maker is unable to pay and it is only on refusal to pay that the instrument is deemed to be dishonoured and prior parties can be made liable there on. Similarly, an instrument stands discharged when the primary party liable is discharged by material alteration in the instrument (Sec. 87), or by lapse of time making the debt time barred under the Limitation Act.

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4. When the holder cancels the instrument with an intention to release the party primarily liable thereon from the liability, the instrument is discharged and ceases to be negotiable (Sec. 82).

**Discharge of One or More Parties**

A party is said to be discharged from his liability when his liability on the instrument comes to an end. When only some of the parties to a negotiable instrument are discharged, the instrument continues to be negotiable and the undischarged parties remain liable on it. Thus the discharge of one or more parties to an instrument does not discharge the instrument and the rights under it can still be enforced against those parties who continue to be liable thereon. One or more parties to a negotiable instrument is/are discharged from liability in the following ways:

**1. By cancellation:**

When the holder of a negotiable instrument deliberately cancels the name of any of the party (by drawing a line through the name) liable on the instrument with an intent to discharge him from liability thereon, such party and all endorser's subsequent to him, who have a right of action against the party whose name is so cancelled, are discharged from liability. Thus, if the maker's or acceptor's name has been cancelled the liability of other parties to the instrument, who must have obviously become parties there to subsequent to the maker or acceptor and as such must be in the position of sureties to him, comes to an end, which in effect discharges or cancels the instrument itself. But if the name of an endorser has been cancelled then all the endorsers subsequent to him will be discharged but those prior to him will remain liable. Section 40 contains a similar provision, according to which if the holder, without the consent of the endorser, destroys or impairs the endorser's remedy against a prior party, the endorser is discharged from liability.

**2. By release:**

If the holder of a negotiable instrument releases any party to the instrument by any method other than cancellation of names (i.e. by a separate agreement of waiver, release, or remission), the party so released and all parties subsequent to him, who have a right of action against the party so released, are discharged from liability.

**3. By payment:**

When the party primarily liable on the instrument makes the payment in due course to the holder at or after maturity, all the parties to the instrument stand discharged, because the instrument as such is discharged by such payment.

**4. By allowing drawee more than 48 hours to accept:**

If the holder of a bill of exchange allows the drawee more than forty eight hours, exclusive of public holidays, to consider whether he will accept the same, all previous parties not consenting to such allowance are thereby discharged from liability to such holder.

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**5. By taking, qualified acceptance:**

If the holder of a bill agrees to a qualified acceptance all prior parties whose consent is not obtained to such an acceptance are discharged from liability.

**6. By not giving notice of dishonour:**

Any party to a negotiable instrument (other than the party primarily liable) to whom notice of dishonour is not sent by the holder is discharged from liability as against the holder, unless the circumstances are such that no notice of dishonour is required to be sent.

**7. By non-presentment for acceptance of a bill**

When a bill of exchange is payable certain period after sight, its holder must present it for acceptance to the drawee within a reasonable time after it is drawn. If he makes a default in making such presentment, the drawer and all endorsers who were liable towards such a holder are discharged from their liability towards him.

**8. By delay in presenting cheque**

It is the duty of the holder of a cheque to present it for payment within reasonable time of its issue. If he fails to do so and in the meanwhile the bank fails causing damage to the drawer, the drawer is discharged as against the holder to the extent of the actual damage suffered by him.

**1.4.4 Holder in due course**

Holders in due course acquire rights superior to those of the original owner.

**Holder in due Course (Sec. 9)** "Holder in due course" means any person who became the possessor of a promissory note, bill of exchange or cheque payable to bearer, or the payee or endorsee thereof, without being aware that it is overdue or that there is a prior claim against it or without knowing that there is any defect in the title of the person from whom he derived his title.

**The essential requirements to become a holder in due course are:**

1. He must be a holder.
2. The holder must have paid a valuable consideration.
3. He must have become the holder of the negotiable instrument before its maturity.
4. He must take the negotiable instrument complete and regular on the face of it.
5. The holder must have obtained the instrument without a sufficient cause to believe that any defect existed in the title of the person from whom he has derived his title.

**1.4.5 Promissory note Meaning**

Sec.4 of the Act it as “an instrument in writing containing an unconditional undertaking, signed by the maker, to pay a certain sum of money only to, or to the order of, a certain person, or to the bearer of the instrument”. The promissory note is in short called as pronote.

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**The essentials of a valid promissory note:**

- It must be in writing
- It must contain an unconditional undertaking to pay
- It must be signed and delivered by the maker
- The sum payable must be definite
- The promise must be to pay money only
- The maker and payee must be a definite person
- It must be stamped as required by the Stamp Act.

**Bill of Exchange Meaning:**

Sec.5 of the negotiable Instruments Act defines it as “an instrument in writing, containing an unconditional order, signed by the maker, directing a certain person to pay a certain sum of money only to or to the order of, a certain person or to the bearer of the instrument”.

**The essentials of Bill of Exchange:**

- It must be in writing
- It must contain an order to pay
- The order must be unconditional
- It requires 3 parties i.e., drawer, drawee and payee.
- It must be signed by the drawer
- The sum payable must be certain
- The sum payable must be in legal
- It must be stamped.

**Cheques:**

- Section 6, defines it as “A cheque is a bill of exchange drawn on a specified banker & not expressed to be payable otherwise than on demand”.
- It is always drawn on a bank.
- It is payable to bearer on demand

**Parties to Cheque:**

- Drawer – who makes the cheque

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- Payee – to whom payment is to be made
- Drawee – Bank

**Meaning of Crossing of a Cheque:**

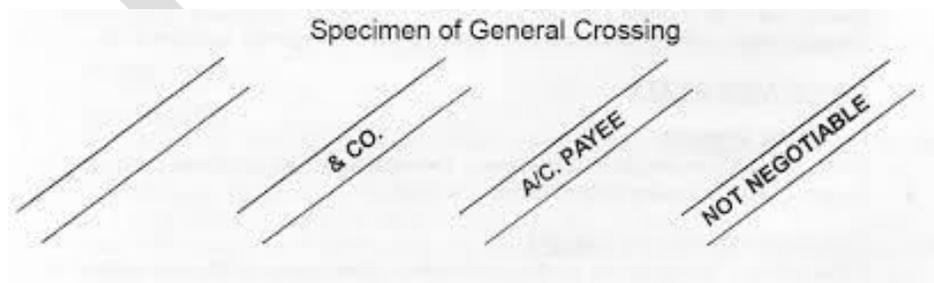
- Crossing of a cheque is a unique feature associated with a cheque affecting to a certain level the responsibility of the paying Banker and also its negotiable Character.
- Crossing of a Cheque is a direction to a particular Banker by the Drawer that Payment should not be made across the Counter. The payment on the crossed Cheque can be collected only through a Banker.
- Crossing of the Cheque is affected by drawing two parallel Transverse lines.
- The Cheque that is not crossed is an open Cheque.

**Types of cheque:**

- There are two types of cheques:
  - Open cheque – those which can be encashed across the counter of the bank. Liable to great risk if stolen or lost. Finder can get payment from bank.
  - Crossed cheque – which bears two transverse lines with or without the words “& co.”

**Various kinds of Crossing:**

1. General Crossing: - which bears across its face the words “& co.” or the words “not negotiable”. For general crossing two transverse lines on the face of cheque are essential. The paying banker shall pay only to a banker. There are two sloping parallel lines, marked across its face.
  - a. The cheque bears a short form "& Co." between the two parallel lines.
  - b. The cheque bears the words "A/c. Payee" between the two parallel lines.
  - c. The cheque bears the words "Not Negotiable" between the two parallel lines.



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2. Special or Restrictive Crossing: - When a particular bank's name is written in between the two parallel lines the cheque is said to be specially crossed. Where a cheque bears across its face an addition the name of banker either with or without the words "not negotiable". It contains:
- The name of the banker across the face of cheque.
  - With the words "not negotiable".
  - In addition to the bank name, the words "A/c. Payee Only", "Not Negotiable" may also be written. The payment of such cheque is not made unless the bank named in crossing is presenting the cheque. The effect of special crossing is that the bank makes payment only to the banker whose name is written in the crossing. Specially crossed cheques are safer than generally crossed cheques.



### **Why Crossing of Cheque is being used?**

- The important usefulness of a crossing cheque is that it cannot be covered at the counter but can be collected only by a bank from the drawee bank.
- Crossing provides a protection and safeguard to the owner of the cheque as by securing payment through a banker it can be easily detected to whose use the money is received. When the cheque is crossed, the paying banker shall not pay it except to a banker.
- In case of not negotiable crossing the person holding such a cheque gets no better title than that of his transferor and cannot suggest a better title to his own transferee. In case of 'account payee' only crossing, a direction is given to the collecting banker to collect cheque and to place the amount to the credit of the payee only.
- A special crossing makes the cheque safer than a general crossing because the payee or holder cannot receive payment except through the banker named on the cheque.

### **Who can cross a Cheque?**

- The drawer of a Cheque
- Holder of the Cheque
- The Banker in whose favour the cheque has been crossed special

## 1.5 GOODS AND SERVICES TAX (GST)

Goods & Services Tax is a comprehensive, multi-stage, destination-based tax that will be levied on every value addition.

In simple words, GST is an indirect tax levied on the supply of goods and services which was introduced in India on 1 July 2017. GST Law has replaced many indirect tax laws that previously existed in India.

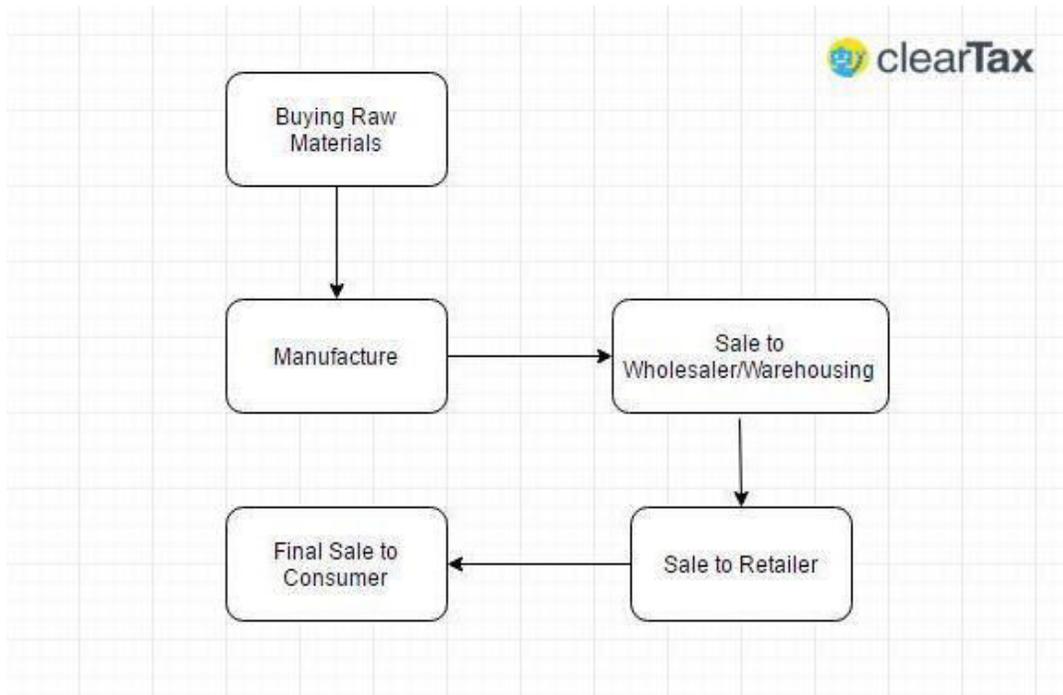
### 1.5.1 GST Levying Methods

#### Multistage

Let us consider the following case.

There are multiple change-of-hands an item goes through along its supply chain: from manufacture to the final sale to consumer.

- Purchase of raw materials
- Production or manufacture
- Warehousing of finished goods
- Sale of the product to the retailer
- Sale to the end consumer



Goods and Services Tax will be levied on each of these stages, which make it a multi-stage tax.

### **Destination-Based**

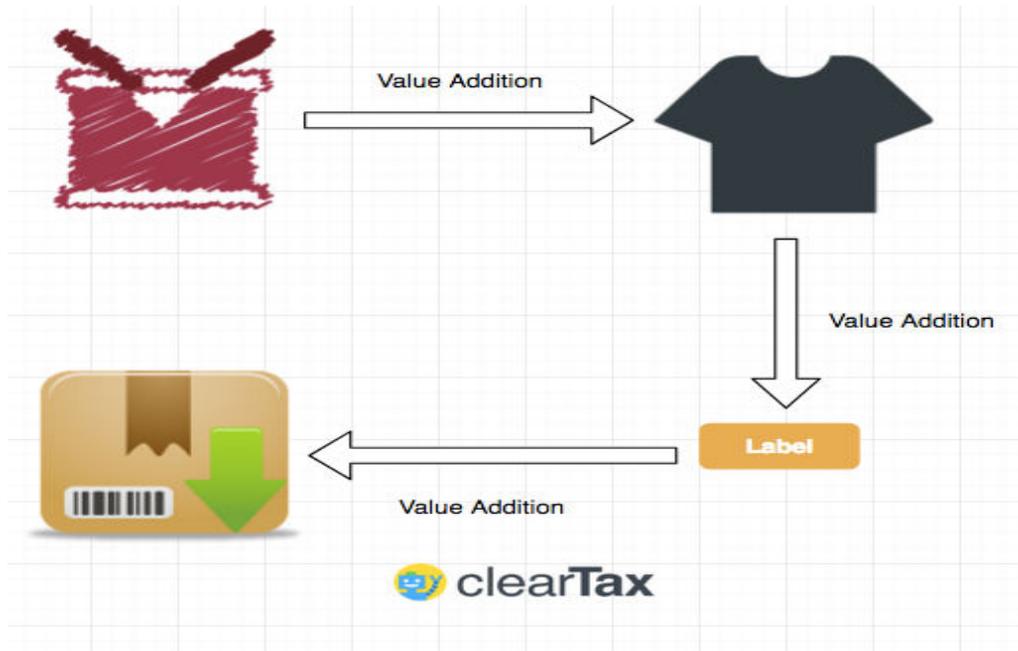
Consider goods manufactured in Rajasthan and are sold to the final consumer in Karnataka. Since Goods & Service Tax (GST) is levied at the point of consumption, in this case Karnataka, the entire tax revenue will go to Karnataka.

### **Value Addition**

The manufacturer who makes shirts buys yarn. The value of yarn gets increased when the yarn is woven into a shirt.

The manufacturer then sells the shirt to the warehousing agent who attaches labels and tags to each shirt. That is another addition of value after which the warehouse agent sells it to the retailer.

The retailer packages each shirt separately and invests in the marketing of the shirt thus increasing its value.



GST will be levied on these value additions i.e. the monetary worth added at each stage to achieve the final sale to the end customer.

### 1.5.2 Components of GST

There are 3 applicable taxes under GST: CGST, SGST & IGST.

CGST: Collected by the Central Government on an intra-state sale (Eg: Within Karnataka)

SGST: Collected by the State Government on an intra-state sale (Eg: Within Karnataka)

IGST: Collected by the Central Government for inter-state sale (Eg: Karnataka to Tamil Nadu)

### 1.5.3 GST rates

The government has opted for four slabs for both goods and services — 5%, 12%, 18% and 28%. In addition, several items face zero levy, while gold will attract 3% GST, a few items like aerated drinks, luxury cars and tobacco products are in the top bracket of 28% tax regime.

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**1.5.4 Advantages of GST**

**Advantages to the customer**

1. Huge number of items are either tax exempt or in 5% tax bracket.
2. Maximum benefits to the poor and the common man.
3. Will ensure that the poor get their due.
4. Consumers to benefit from increased competition

**Advantages for trade and industry**

1. Common procedures for registration, duty payment, return filing and refund of taxes
2. Seamless flow of tax credit from manufacturer to consumer eliminating cascading of taxes. (A cascade tax or cascading tax is a turnover tax that is applied at every stage in the supply chain, without any deduction for the tax paid at earlier stages)
3. More efficient neutralization of taxes to make our exports more competitive internationally.
4. Benefit of exemption/composition scheme for a large segment of small scale suppliers to make their products cheaper.

**Advantages to the economy**

1. To create a unified common National market.
2. To make India a manufacturing hub.
3. To boost investments and exports.
4. To generate more employment by increased economic activity.
5. Harmonization of laws, procedures and rates of tax across the country.

**1.5.5 Difference between VAT and GST**

Description	VAT	GST
Nature of Levy	Levied on goods	Levied on goods and services
Rates	The tax rates changes for each goods	Uniform rate in all states
Nature of tax	Multi-point destination-based system of taxation.	Destination based tax

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Input credit	Can be set-off only against the goods sold within the state	Set-off input credit against goods sold within the country
Indirect tax	VAT is levied as Separate Tax.	Summation of all indirect taxes which is levied by the Central Government

**1.5.6 How is GST calculated?**

In the case of Goods and Services Tax, the individual who has paid a tax already can claim credit for this tax when he submits his taxes.

Let's take a simple example,

A person sells the raw material at Rs 100 for which he pays a tax of 10%. The manufacturer purchases the raw material at Rs 110. He then makes a value addition of Rs 40 for which he pays a tax of 10% (i.e. 10% of 140 = 14 Rs). But as he has already paid the tax for the raw material, now he has to pay only for the value addition made by him (i.e. Rs 14 - Rs 10 = Rs 4). The next stage the wholesaler buys from the manufacturer and makes a value addition worth Rs 30. Now the cost becomes Rs 170 (Rs 140 + Rs 30). The tax of 10% is Rs 17. But as he has already paid the tax of the manufacturer and he has purchased the product at Rs 154, now he has to pay tax only for the value addition made by him (i.e. Rs 17 - Rs 14 = Rs 3)

Action	Cost	10% Tax	Actual liability	Total Cost
Raw material	100	10	10	110
Manufacturer (adds value) 40	140	14	4 (14-10)	154
Wholesaler (adds value) Rs 30	170	17	3 (17-14)	187
Total	170		17	187

## 1.6 REFERENCE

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