11 TERMINATION OR DISCHARGE OF CONTRACTS

METHODS OF TERMINATION

When the obligation created by a contract come to an end, the contract is said to be discharged or terminated. A contract may be discharged or terminated in any of the following ways :

I. By performance of the promise or tender.
II. By mutual consent cancelling the agreement or substituting a new agreement in place of the old.
III. By subsequent impossibility of performance.
IV. By operation of law—i.e., death, insolvency, or merger.
V. By lapse of time.
VI. By material alteration without the consent of the other parties.
VII. By breach made by one yearly.

The rules regarding termination of contracts are discussed below.

I. TERMINATION BY PERFORMANCE

The obligations of a party to a contract come to an end when he performs his promise. Performance by all the parties, of the respective obligations, puts an end to the contract completely. This is the normal and natural mode of discharging a contract.

The *offer of performance* or tender has the same effect as performance. If a party to a contract offers to perform his promise but the offer is not accepted by the other party, the obligations of the first party are terminated.

II. TERMINATION BY MUTUAL AGREEMENT

By agreement of all parties, a contract may be cancelled or its terms altered or a new agreement substituted for it. Whenever any of these things happen, the old contract is terminated.

"If the parties to a contract agree to substitute a new contract for it, or to rescind or alter it, the original contract need not be performed."—Sec. 62.

Termination by mutual agreement may occur in any one of the following ways.

Novation

Novation occurs when a new contract is substituted for an existing contract, either between the same parties or between different parties. The definition was given by Lord Selborne in a House of Lords case, *Scarf v. Jardine.*"[1] Anson however, is of opinion that novation can only take place by agreement between the parties. "Novation cannot be compulsory."[2]

It is now held that novation may occur by two ways, viz., (i) change of parties and (ii) a substitution of a new contract in place of the old.

Examples :

(*i*) *A* is indebted to *B* and *B* to *C*. By mutual agreement *B*'s debt to *C* and *A*'s debt to *B* is cancelled and *C* accepts *A* as his debtor. There is novation.

(*ii*) On an amalgamation of two companies into a new company, the creditors of the old companies can enforce their claims against the new company. The new company is substituted for the old companies.

(*iii*) *A* owes *B* 1,000 rupees under a contract. *B* owes *C* 1,000 rupees. *B* orders *A* to credit *C* with 1,000 rupees in the books, but *C* does not assent to the arrangement. *B* still owes *C* 1,000 rupees, and no new contract has been entered into.

(*iv*) *P* lent *D* Rs. 2,000. Afterwards the parties agreed that *D* will repay to *P* Rs. 1,000 and a certain amount of ornament at a certain date. The former agreement is replaced by the latter. There is novation.

Alteration

Alteration of a contract means change in one or more of the terms of a contract. Alteration is valid if it is done with the consent of all the parties to the contract.

In Alteration there is change in the terms of the contract but no change of the parties to it. In Novation there may be change of parties.

Remission

Remission may be defined as the acceptance of less than what was contracted for. According to Section 63 of Contract Act, "Every promisee may dispense with or remit, wholly or in part, the performance of the promise made to him, or may extend the time for such performance, or may accept instead of it any

[1] (1882) 7 App. Cases 345 [2] Anson, *Law of Contract*, ch. XI

satisfaction which he thinks fit." So in India a promisee may remit or give up a part of his claim and a promise to do so is binding ever though there is no consideration for doing so.

Examples :

(*i*) *A* owes *B* Rs. 5,000. *A* pays to *B* and *B* accepts in full satisfaction for the whole debt. Rs. 2,000. The old debt is discharged.

(*ii*) *A* promises to paint a picture for *B*. *B* afterwards forbids him to do so. *A* is no longer bound to perform the promise.

(*iii*) *A* owes *B*, under a contract, a sum of money, the amount of which has not been ascertained. *A* without ascertaining the amount gives to *B*, and *B*, in satisfaction thereof, accepts the sum 2,000 rupees. This is a discharge of the whole debt whatever may be its amount.

(*iv*) *H. K.* was liable to pay Rs. 27 lakhs. His estate was taken over by a committee to administer it. The committee offered to pay Rs. 20 lakhs to the creditor in full satisfaction and he accepted the offer. But afterwards the creditor sued the debtor for the balance viz., Rs. 7 lakhs. The Supreme Court held the case is covered by Sec. 63 and he is not entitled to sue. *Kapur Chand Godha* v. *Mir Nawab Himayatali Khan.*[1]

Accord and Satisfaction

These two terms are used in English law. According to English law, a promise to accept less than what is due under an existing contract, is not supported by any consideration and is therefore unenforceable. But an exception is made where the smaller sum is actually paid (or the smaller obligation actually performed) and accepted by the promisee. In such cases the old contract is discharged by what is called *accord and satisfaction.* Accord means the promise to accept less than what is due under the old contract. Satisfaction means the payment or the fulfilment of the smaller obligation. An accord is unenforceable ; but an accord followed by satisfaction discharges the pre-existing obligation.

Example :

P owes *Q* Rs. 5,000. *Q* agrees to accept Rs. 2,000 in full satisfaction of his claim. This promise is unenforceable in English law. But when Rs. 2,000 is actually paid and accepted, there is accord and satisfaction and the original debt is discharged.

The doctrine of accord and satisfaction is not applied in India. According to Section 63, a promise may dispense with or remit

[1] AIR (1963) Supreme Court 250

wholly or in part, the performance of the promise made to him. Therefore if the promise agrees to accept Rs. 2,000 in full satisfaction of a claim for Rs. 5,000 the promise is enforceable.

Rescission

Rescission means cancellation of all or some of the terms or a contract. The rescission of a contract may occur under various circumstances :

1. It may be done by mutual consent.—Sec. 62.
2. Where a party to a contract fails to perform his obligation, the other party can rescind the contract without prejudice to his rights to receive compensation for breach of contract.
3. In a voidable contract, one of the parties has the option of rescinding it.

Section 66 of the Indian Contract Act provides that, "The rescission of a voidable contract may be communicated or revoked in the same manner, and subject to the same rules, as apply to the communication or revocation of a proposal."

Rescission may be by act of party. It is not necessary, save in exceptjonal cases, to file a suit for the purpose.

Examples :

(*i*) *P* promises to deliver certain goods to *Q* on a certain date. Before the date of performance *P* and *Q* mutually agree that the contract will not be performed. The parties have rescinded the contract.

(*ii*) *X* was induced to enter into a agreement by coercion. He can rescind the agreement.

Suit for Rescission : Section 35 of Specific Relief Act (Act 1 of 1877) provides that, "Any person interested in a contract in writing may sue to have it rescinded." The court may grant rescission in the following cases :

(*a*) When the contract is voidable or terminable by the plaintiff.

(*b*) Where the contract is unlawful for causes not apparent on its face and the defendant is more to blame than the plaintiff.

(*c*) Where a decree for specific performance of a contract of sale, or of a contract to take a lease, has been made and the purchaser or the lessee makes default in payment of the purchase money or other sums which the court has ordered him to pay.

Waiver

Waiver means the abandonment of a right. A party to a

contract may waive his rights under the contract. Thereupon the other party is released from his obligations.

Merger

When a superior right and an inferior right coincide and meet in one and the same person, the inferior right vanishes into the superior right. This is known as merger.

Example :

A man holding property under a lease, buys the property. His rights as a lessee vanish. They are merged into the rights of ownership which he has now acquired.

III. SUBSEQUENT OR SUPERVENING IMPOSSIBILITY

Pre-contractual Impossibility

A contract which at the time it was entered into was impossible to perform, is void *ab initio* and creates no rights and obligations, *e.g.*, a promise to ride a horse to the sun.

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 the contract *becomes void.* This is known as the doctrine of *Supervening Impossibility.* It is also known as the Doctrine of Frustration. (See pages 124-126)

"A contract to do an act which, after the contract is made, becomes impossible, or, by reason of some event which the promisor could not prevent, unlawful, becomes void when the act becomes impossible or unlawful."—Sec. 56, para 2.

Grounds of Frustration. Supervening impossibility may occur in many ways, some of which are explained below :

1. Destruction of an object

In the case *Taylor* v. *Caldwell.*[1] Blackburn J. observed as follows. "In contracts in which the performance depends on the continued existence of a given person or thing, a condition is implied that the impossibility of performance arising from the perishing of the person or thing shall excuse the performance".

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[1] (1863) 122 E. R. 299

Examples :

(*a*) A music hall was let for a series of concerts on certain days. The hall was burnt down before the date of the first concert. The contract becomes void. *Taylor* v. *Caldwell.* (See p. 119)

(*b*) A person contracted to deliver 200 tons of potatoes from a particular field. The potatoes were destroyed by a pest through no fault of the party. The contract was held to be discharged. *Howell* v. *Coupland.*[1]

(*c*) There was an agreement between the owner of a theatre and a producer, to exhibit a picture. The Municipal authorities issued order to demolish the theatre because it was unsafe. Neither of the parties knew that. Held, the contract was discharged. *V. L. Narasu* v. *P. S. V. Iyer.*[2]

2. Change of law

The performance of a contract may become unlawful by a subsequent change of law. In such cases, the original contract becomes void.

Examples :

(*i*) *M* sold to *N* a specified parcel of wheat in a warehouse. Before delivery, the wheat was requisitioned by the Government under statutory powers. The delivery being now legally impossible, the contract was discharge. *Re Shipton, Anderson & Co.*[3]

(*ii*) *X*, who was governed by Hindu Law and who already had a wife promises to marry *Y*. Then the Special Marriage Act is passed prohibiting polygamous marriage. The contract to merry becomes void.

3. Failure of Pre-conditions

When a contract is entered into on the basis of the continued existence of a certain state of things, the contract is discharged if the state of things changes.

This principle has been supported in some cases on the ground that every agreement presumes the existence of a certain state of things on the basis of which the agreement was entered into. The continued existence of the same state of things is a *condition precedent* to the performance of the contract. Obviously the contract fails if there is a failure of the condition precedent.

Examples :

(*i*) *A* & *B* contract to marry each other. Before the time fixed for the marriage, *A* goes mad. The contract becomes void. [Illustration (b) of Section 56].

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[1] (1876) 1 O. B. D. 258

[2] I. L. R. (1953) Mad. 831

[3] (1915) 3 K. B. 676

(*ii*) *H* hired a room from *K* for two days with the object (as both parties knew) of using the room to view the coronation procession of Edward VII although the contract continued no reference to the procession. Owing to the King's illness the procession was abandoned. Held, that the contract was discharged and *H* was excused from paying rent for the room as the existence of the procession was the basis of the agreement. *Krell* v. *Henry*.[1]

(*iii*) *A* contracts to take cargo for *B* at a foreign port. *A's* Government afterwards declares war against the country in which the port is situated. The contract becomes void when war is declared. [Illustration (d) of Section 56. See also para 5, below.]

4. Death or Incapacity for personal services

Where the personal qualification of a party is the basis of the contract the contract is discharged in cases of death or personal incapacity.

Examples :

(*i*) *G* contracts to act at a theatre for six months in consideration of a sum paid in advance by *H*. On several occasions *G* is too ill to act. The contract to act on these occasions becomes void.

(*ii*) A piano player was prevented from performing by a dangerous illness. Held, the contract is discharged because the player could have insisted on performing when she was unfit to do so. *Robinson* v. *Davison*.[2]

(*iii*) A seaman was interned owing to war. His contract of service was discharged. *Herloek* v. *Beal*.[3]

(*iv*) A music-hall artist was called up for army service. His contract of service was discharged. *Morgan* v. *Manser*.[4]

5. Outbreak of War

A contract entered into during war with an alien enemy is void *ad initio*. A contract entered into before the war commenced between citizens of countries subsequently at war, remains suspended during the pendency of the war. After the termination of the war, the contract revives and may be enforced.

The above rules regarding the effect of war on contracts were formulated by English judicial decisions and are applicable to India. But the following exceptions are to be noted :

(*i*) In India there may be a valid contract with an enemy alien during war, if the Central Government specifically permits it.

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[1] (1903) 2 K. B. 740
[2] (1871) L. R. 6 Ex. 269
[3] (1916) 1 A.C. 486
[4] (1948) 1 K. B. 184

(*ii*) Contracts entered into before the outbreak of the war will be cancelled and not merely suspended, if they amount to aiding the enemy in the pursuit of war, *Eshosito* v. *Bowden*[1]; or if they are of such a character that they cannot remain suspended *e.g.*, when the contract involves the continuous performance of mutual duties.

Exceptions

Some illustrations are given below of cases which *do not* come within the principle of Supervening Impossibility.

1. *Difficulty of performance* : Difficulty does not excuse performance.

Examples :

(*i*) *A* sold *B* a certain quantity of Finland timber to be delivered between July and September, 1914. No deliveries were made before August when war broke out and transport was disorganised so that *A* could not bring any timber from Finland. Held *B* was not concerned with the way in which *A* was going to get timber and therefore the impossibility of getting timber from Finland did not excuse performance. *Blackburn Bobbin Co.* v. *Allen & Sons*.[2]

(*ii*) The appellants agreed to sell to the respondents a quantity of groundnuts to be shipped from Sudan to Hamburg during November or December, 1956. On November 2nd, the Suez Canal was closed and remained closed for the next five months. The appellants refused to perform the contract claiming that it had been frustrated by the closure of the canal. The House of Lords held there was no frustration, since it would still be possible to ship the nuts to Hamburg around the Cape of Good Hope. *Tsakiroglou & Co. Ltd.* v. *Noblee Thori G. m. b. H.*[3]

2. *Commercial impossibility* : A wholesale dealer's contract to deliver goods is not discharged because a manufacturer has not produced the goods concerned. Similarly increase of wages or prices of raw materials, unseasonable weather or lack of adequate profits do not excuse performance. The reason is that if the parties did not stipulate to the contrary, they must have intended to take the risk of occurrences like these.

Example :

In July 1946, the appellants entered into a contract with the respondents to build 78 houses for a fixed sum £ 94,424. Owing

[1] (1857) 7 E & B 783
[2] (1918) 2 K. B. 467
[3] (1962) A.C. 93

to an unexpected shortage of skilled labour and of certain materials the contract took twenty-two months to complete instead of the eight months expected, and cost sum £1,15,000. The appellants contended that the contract had been frustrated and that they were entitled to claim on a quantum meruit for the cost actually incurred. The House of Lords held that the performance of the contract was more onerous but did not discharge the agreement. The situation was still within the scope of the contract. *Davis Contractors Ltd.* v. *Fareham U.D.C.*[1]

3. *Strikes, lock-outs, civil disturbances and riots* : These events do not terminate contracts unless there is a clause in the contract providing that in such cases the contract is not to be performed or that the time of performance is to be extended.

Examples :

(*i*) The lessee of certain salt pans, failed to repair them according to the terms of his contract, on the ground of a strike of the workmen. Held, a strike of workmen is not sufficient reason to excuse performance of a term of the contract. *Hari Laxman* v. *Secretary of State for India*.[2]

(*ii*) A contract was entered into between two London merchants for the sale of certain Algerian goods. Owing to riots and civil disturbances in that country, the goods could not be brought. Held, no excuse for non-performance of the contract. *Jacob* v. *Credit Lyonnais*.[3]

4. *Failure of one of the objects* : When there are several purposes for which a contract is entered into, failure of one of the objects does not terminate the contract.

Example :

X agreed to let out a boat to *Y* for the purpose of viewing a naval review to be held on the occasion of the Coronation of Edward VII *and to cruise round the fleet*. Owing to the king's illness the naval review was abandoned but the fleet was assembled and the boat could have been used to cruise round the fleet. Held the contract was *not* terminated. *Herne Boy Steamboat Co.* v. *Hutton*.[4]

The Effects of Supervening Impossibility

1. Section 56 (para 2) provides that when the performance of a contract becomes subsequently impossible or illegal, the contract becomes void.

2. Section 65 provides that when a contract becomes void, any person who has received any advantage under it must restore

[1] (1956) A. C. 696
[2] (1928) 30 Bom. L. R. 49
[3] 12 Q. B. D. 589
[4] (1903) K. B. 740

it, or make compensation for it, to the person from whom he received it. [See under Restitution, p. 140]

3. Section 56 (para 3) provides that, "where one person has promised to do something which he knew, or with reasonable diligence, might have known, and which the promisee did not know to be impossible or unlawful, such promisor must make compensation to such promisee for any loss which such promisee sustains through the non-performance of the promise."

Example :

P contracts to marry *B* being already married to *C*, and being forbidden by the law to which he is subject to practice polygamy. *P* must make compensation to *B* for any loss caused to her by the non-performance of his promise.

THE DOCTRINE OF FRUSTRATION

Definition

When the common object of a contract can no longer be carried out, the court may declare the contract to be at an end. This is known as the Doctrine of Frustration. Anson says, "Most legal systems make provision for the discharge of a contract where, subsequent to its formation, a change of circumstances renders the contract legally or physically impossible of performance."

The law relating to this subject, as in England and India respectively, is stated below.

English Law

Before 1863 a contract, excepting an illegal agreement, was enforced literally. All the parties of a contract had an absolute obligation to perform it. The Doctrine of Frustration emerged after 1863 through court decisions.

In a very old case, decided in 1647, the facts were as follows ; A person *J* got a lease of land from *P* on a rental basis. Then a German Prince seized the land and it was not possible for *J* to use it. The landlord *P* sued for rent. The Court held that *J* must carry out all the terms on the contract including the payment of rent. *Paradine* v. *Jane*.[1] This case illustrated the rigours of English Law.

[1] (1647) Aleyn 26

Later on many exceptions to the Doctrine of Frustrations were made and on various grounds the court gave relief to aggrieved persons. In the following cases English courts accepted that the contract came into an end : (1) Destruction of an object (2) Change of Law (3) Failure of Pre-conditions (4) Death or Personal Incapacity and (5) Outbreak of War. The cases on those subjects have been cited above. (Pages 119-121)

Basis of the Doctrine : In English courts various theories have been put forward at different times as to the basis of discharge of contracts by Frustrations.[1] The theories are summarised briefly.

(1) *The implied terms* : In some cases it has been held that every contract contained an implied term that a particular thing or state of things should continue to exist. The continued existence of the same state of things is a condition precedent to performance of the contract. Example : *Krell* v. *Henry.* (See p. 121)

(2) *Disappearance of the foundation of the contract* : If the goods which are the subject of the contract are destroyed without any fault of the parties, the contract should terminate. *Taylor* v. *Caldwell.* (See p. 119)

(3) *The just and reasonable solution* : In *British Movietonews Ltd.* v. *London and District Cinemas Ltd.*,[2] the House of Lords based the doctrine upon the principles of construction or interpretation of documents. Where the court gathers as a matter of construction that the contract itself contained impliedly or expressly a term, according to which it would stand discharged on the happening of certain circumstances, the dissolution of the contract would take place under the terms of the contract itself.

(4) *Change in the obligation* : "Frustration occurs whenever the law recognizes that without default of either party a contractual obligation has become incapable of being performed because the circumstances in which performance is called for would render it a thing radically different from that which was undertaken by the contract." Per Lord Radcliffe. *Davis Contractors, Ltd.* v. *Fareham U. D. C.* (See p. 123)

Limits : In English law there are certain limits of the Doctrine of Frustration.

(*a*) If the frustration is self-induced by the party (e.g. negligent acts) the contract is not frustrated.

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[1] Anson, *Law of Contract*, p. 464 [2] (1952) A. C. 166

(*b*) The frustrating event should defeat the common intention of the parties. There cannot be frustration on one side only.

Example :

Blackburn Bobbin Co. v. *Allen and Sons.* (See. p. 122)

Effects : In English law frustration produces the following effects : (*a*) The contract terminates automatically and immediately. It is void and not voidable only. (*b*) All future obligations are discharged. (*c*) Some reliefs have been given in England by the Law Reform (Frustrated Contracts) Act 1943.

Example :

Some English merchants contracted to sell machinery to Polish buyers. Before delivery was due, Germany occupied Poland. It was held that the contract was discharged by frustration. *Fibrosa etc.* v. *Fairbairn etc.*[1]

Indian Law

In *Satyabrata Ghosh* v. *Mugniram Bangur and Co. and Another*,[2] the Supreme Court of India discussed the English cases relating to frustration and came to the following conclusions :

The doctrine of frustration of contract comes into play when a contract becomes impossible of performance, after it is made, on account of circumstances beyond the control of the parties. It comes within the purview of Sec. 56 of the Indian Contract Act. The word 'impossible' in this section has not been used in the sense of physical or literal impossibility. The performance of an act may not be literally impossible but it may be impracticable and useless from the point of view of the object and purpose which the parties had in view ; and if an untoward event or change of circumstances totally upsets the very foundation upon which the parties rested their bargain, it can be said that the promisor finds it impossible to do the act which he promised to do. (See section 56, pp. 119-120)

Examples :

(*i*) An agreement was entered into for the sale of land subject to the condition that the seller would do some development work on the land. Before the work could be completed the land was requisitioned by the Government for war purposes. Held, the contract was *not frustrated*. *Satyabrata Ghose* v. *Mugniram Bangur & Co. and Another.* (See above).

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[1] (1943) A.C. 32 [2] (1954) S. C. A. 187 (Supreme Court)

(*ii*) There was a contract for sale of goods relating to the Nizam's Jewellery Trust on taking delivery of goods upon payment. Meanwhile the courts restrained the sale by an injunction. The contract of sale must be deemed to be frustrated. *M/s Shanti Vijay & Co. etc.* v. *Princess Fatima Fouzia and others.*[1]

IV. TERMINATION BY OPERATION OF LAW

A contract terminates by operation of law in case of death, insolvency, and merger.

Death—In contracts involving personal skill or ability, death terminates the contract. In other cases, the rights and liabilities pass on to the legal representatives of the dead man.

Insolvency—Upon insolvency, the rights and liabilities of the insolvent are, with certain exceptions, transferred to an officer of the court, known as the Official Assignee in Calcutta and other presidency towns and as Official Receiver in other areas.

Merger—See p. 119.

V. LAPSE OF TIME

Contracts may be terminated by lapse of time. In civil suits the obligations and liabilities in contracts are barred by limitation. The provisions of law are stated in the Limitation Acts.

VI. TERMINATION BY MATERIAL ALTERATION

If the document containing the terms of a contract is *materially altered* by a party to the contract, *without the consent* of the other *parties*, the contract is discharged and cannot be enforced any more.

The term 'material alteration' means a change which affects or alters, in a significant manner, the rights and liabilities of the parties.[2]

Example :

A change in the amount of money to be paid ; the time of payments ; the place of payment ; the names of the parties etc.

These changes involve tampering with the document wherein the terms of the contract have been written down. A document which has been tampered with in such a way is not admissible

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[1] AIR (1980) Supreme Court 17

[2] Halsbury's Laws of England (Fourth Edition), para 1378

in evidence and the contract recorded there naturally becomes unenforceable.

If an alteration (by erasure, interlineation, or otherwise) is made in a material part of a deed, after its execution, without the consent of the party or parties liable under it, the deed is rendered void from the time of the alteration. *Loonkaran Sethia etc.* v. *Mr. Ivan E. John & others etc.*[1]

An alteration which does not affect the rights and liabilities of the parties or which are made to carry out the common intention of the parties has no effect on the validity of the contract.

Example :

Correcting a clerical error in figures, correcting the spelling of a name etc. (See under, 'Law relating to Negotiable Instruments'. Ch. 3).

VII. TERMINATION BY BREACH OF CONTRACT

When a contract is broken by one party, the other party or parties are freed from the obligation of performing the contract. They can also take the remedial measures to which they are entitled.

Breach of contract may arise in two ways : (*i*) by anticipatory breach and (*ii*) by actual breach or present breach.

Anticipatory Breach of Contract

Anticipatory breach of contract occurs when a party repudiates his liability under the contract *before the time for performance is due* or when a party by his own act *disables himself* from performing the contract.

Examples :

(*i*) *C* enters into a contract to supply *B* with certain articles on the 1st of June. Before 1st June he informs *B* that he will not be able to supply the goods.

(*ii*) *W* agrees to sing at *L*'s theatre on and from a certain date. Before that date she enters into a long term contract to sing at a different theatre.

(*iii*) *X* agrees to marry *Y*. Before the agreed date of marriage, he marries *Z*.

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[1] AIR (1977) Supreme Court 336

Consequences of Anticipatory Breach

When anticipatory breach occurs, the aggrieved party can take the following steps :

(*i*) He can treat the contract as discharged, so that he is no longer bound by any obligations under the contract ; and,

(*ii*) He can immediately adopt the legal remedies available to him for breach of contract, *viz.*, file a suit for damages or specific performance or injunction.

Anticipatory breach of contract does not by itself discharge the contract. The contract is discharged only when the aggrieved party chooses to treat it as discharged, *i.e.*, when he accepts the repudiation of the contract. If he does not accept the repudiation the contract continues to exist and may be performed by the other party, if possible. But if the repudiation is not accepted and subsequently an event happens which discharges the contract legally (*e.g.*, a supervening impossibility) the aggrieved party loses his right to sue for damages.

Examples :

(*i*) *D* agrees to employ *H* as a courier, the service to commence from 1st June. On 1st May he informs *H* that his services will not be required. On 11th May *H* files a suit for damages. He is entitled to do so even though the date of performance of the contract has not arrived. *Hochster* v. *De la Tour.*[1]

(*ii*) *X* agreed to load a cargo of wheat on *R*'s ship at Odessa within a certain number of days. When the ship arrived *R* refused to load the cargo. *Y* did not accept the refusal and continued to demand a cargo. Before the last date of loading had expired the Crimean War broke out, rendering the performance of the contract illegal. Held, the contract was discharged and *Y* cannot sue for damages. *Avery* v. *Bowden.*[2]

(*iii*) The defendant promised to marry the plaintiff upon his father's death ; but during his father's life time he renounced the contract. Held, the plaintiff was entitled to sue without waiting the father's death. *Frost* v. *Knight.*[3]

Actual Breach of Contract

Actual breach of contract occurs when during the performance of the contract or at the time when the performance of the contract is due, one party either fails or refuses to perform his obligations under the contract.

The refusal of performance may be *express* (i.e., by word

[1] (1853) 2 E & B 678
[2] (1856) 5 E & B 714
[3] (1872) L. R. 7 Ex. 111

or by writing) or *implied* (i.e., by conduct of the party or by non-action) or abstaining from doing something.

Examples :

(*i*) *D* agrees to deliver to *B*, 5 tons of sugar on 1st June. He fails to do so on 1st June. There is breach of contract by *D*.

(*ii*) *P* agrees to deliver to *Q* 5 tons of sugar on 1st June. On 1st June he tenders the sugar but *Q* (for no valid reason) refuses to accept delivery. There is breach by *Q*.

(*iii*) *C* agreed to supply a railway company with 3,900 tons of railway chairs. After 1787 tons had been delivered the company told *C* that no more will be required. There is breach of contract by the company. *Cort v. Ambergate Railway Company.*[1]

Remedies of Breach of Contract

When a breach of contract occurs, the aggrieved party or the injured party becomes entitled to the following reliefs :

1. *Rescission of the contract* : The aggrieved party is freed from all his obligations under the contract. (See p. 118)

Examples :

(*i*) *C* promises to deliver 5 tons of sugar to *B* on a certain date and *B* promises to pay the price on receipt of the goods. *C* does not deliver the goods on the appointed day. *B* need not pay the price.

(*ii*) *A* contracts with *B* to repair *B*'s house. *B* neglects or refuses to point out to *A* the place, in which his house requires repair. *A* is excused for the non-performance of the contract if it is caused by such neglect or refusal. (Illustration of Sec. 67)

2. *Suit for Damages* : The aggrieved party is entitled to receive compensation for any loss or damage caused to him by the breach of contract and can file a suit for getting a decree for damages.

3. *Suit upon Quantum Meruit* : When a contract has been partly performed the aggrieved party can, under certain circumstances, file a suit for the price of the services performed before breach of contract.

4. *Specific performance of the contract* : In certain special cases the court can direct a party to perform the contract according to the agreed terms.

5. *Injunction* : Under certain circumstances the court can issue an order upon a party whereby he is prohibited from doing something which amounts to a breach to contract.

The provisions of law regarding the reliefs listed above are discussed below.

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[1] (1851) 17 Q. B. 127

DAMAGES

When a contract is broken the injured party can claim damages from the other party. Damages allowed by the courts may be of different types as follows :

Compensatory Damages

Compensatory damages are damages calculated in such a way as to compensate or make up the loss suffered by a party. They can also be called Ordinary Damages.

Special Damages — See page 133.

Nominal Damages, Contemptuous Damages

Where the court finds that the party has not actually suffered much damage or when the court is of opinion that the breach complained of was too insignificant or petty ; the court allows a paltry sum for damages to the plaintiff. These are called nominal damages or contemptuous damages.

Exemplary, Punitive or Vindictive Damages

The court may allow damages exceeding the actual loss suffered by way of punishment. These are called exemplary, punitive or vindictive damages. Such damages are unusual. In English courts exemplary damages are usually given in cases of breach of contract of marriage and against bankers refusing to pay traders' cheques where there are sufficient funds of the trader in the bank. *Addis* v. *Gramophone and Co.*[1]

Example :

A scurrilous libel was committed by an author and its publisher against a distinguished naval officer. The officer sued for damages in an English Court. He was awarded £15,000—compensatory and £25,000/-exemplary damages, against both defendants. The Court of Appeal (presided by Lord Denning) did not interfere with the decision of the trial court. *Broome* v. *Cassell and Co.*[2]

RULES REGARDING THE AMOUNT OF DAMAGES

The principles

The principles, to be followed by the courts in determining the amount of damages, are laid down in Sections 73 to 75 of the Contract Act.

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[1] (1909) A. C. 488 [2] (1971) 2 All E. R. 187

Section 73 (para 1) provides that in cases of breach of contract the injured party is entitled to receive compensation for any loss or damage which arose naturally from the breach or which the parties knew to be likely to arise from the breach.

"When a contract has been broken, the party who suffers by such breach is entitled to receive, from the party who has broken the contract, compensation for any loss or damage caused to him thereby, which naturally arose in the usual course of things from such breach, or which the parties knew, when they made the contract, to be likely to result from the breach of it."—Sec. 73, para 1.

Rules

The rules on the subject of amount of damages can be summarised as follows :

1. Actual loss

Ordinarily, the aggrieved party is entitled to recovery by way of compensation, only the *actual loss* suffered by him.

2. Natural and usual loss

In calculating actual loss, the court will take into account only such loss as may be *fairly and reasonably* considered as arising *naturally* and in the *usual course of things* from the breach. Remote damages *i.e.*, damages for remote consequences are usually not allowed.

Examples :

(*i*) *X*, a carrier, was entrusted with the delivery of a machine part (breakage of a crankshaft) to *Y*, a manufacturer. The delivery was delayed. *Y* claimed from *X* compensation for the wages of workers and depreciation charges which were incurred during the period the factory was idle for the delayed delivery and for loss of profits which might have been made if the factory was working. The first two items were allowed because they were natural consequences of the breach. The last item, loss of profits was disallowed because it was a remote consequence. *Hadley* v. *Baxendale*.[1]

(*ii*) *A* contracts to sell and deliver 50 maunds of saltpetre to *B*, at a certain price to be paid on delivery. *A* breaks his promise. *B* is entitled to receive from *A* by way of compensation the sum if any by which the contract price falls short of the price for which *B* might have obtained 50 maunds of saltpetre of like quality at the

[1] (1854) 9 Ex. 341

time when the saltpetre ought to have been delivered. [Illustration (a) to Sec. 73]

(*iii*) *A* contracts to pay a sum of money to *B* in a day specified. *A* does not pay the money on that day. *B* in consequence of not receiving the money on that day is unable to pay his debts and is totally ruined. *A* is not liable to make good to *B* anything except the principal sum he contracted to pay, together with interest upto the day of payment. [Illustration (n) to Sec. 73]

(*iv*) *A* hires *B*'s ship to go to Bombay, and there take on board, on the first of January a cargo which *A* is to provide, and to bring it to Calcutta, the freight to be paid when earned. *B*'s ship does not go to Bombay but *A* has opportunities of procuring suitable conveyance for the cargo upon terms as advantageous as those on which he had chartered the ship. *A* avails himself of those opportunities, but is put to trouble and expense in doing so. *A* is entitled to receive compensation from *B* in respect to the trouble and expense. [Illustration (b) to Sec. 73]

3. Special damages

The court may allow remote damages *i.e.*, damages not arising naturally from the breach, if such damages may reasonably be supposed to have been in the contemplation of both the parties at the time they made the contract.

Damages coming within this category are sometimes called, "Special Damages".

Examples :

(*i*) *A* delivers to *B*, a common carrier, a machine to be conveyed without delay to *A*'s mill *informing B that his mill is stopped for want of the machine*. *B* unreasonably delays the delivery of the machine and *A*, in consequence, losses a profitable contract with the government. *A* is entitled to receive from *B*, by way of compensation, the average amount of profits which would have been made by the working of the mill during the time that delivery of it was delayed, but not the loss sustained through the loss of the government contract. [Illustation (i) to Sec. 73]

(*ii*) *P* bought from *L* some copra cake. *P* sold the cake to *B*, who sold it to various dealers who in turn sold it to farmers, who used it for feeding cattle. The copra cake was poisonous and the cattle fed on it died. The various buyers filed suits against their sellers and obtained damages. The various sellers filed suits against *P* and obtained damages. *P* claimed from *L* the damages and costs he had to pay. Held, as it was within the contemplation of the parties that the copra cake was to be used for feeding cattle. *L* was liable to pay damages. *Pinnock Bros. v. Lewis & Peat Ltd.*[1]

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[1] (1923) 1 K. B. 690

4. Restitution and Compensation

The general rule is that, subject to the rules stated above, the injured party is to be placed in the same financial position as he would have been in, if the other party had duly carried out the contract. "If a contract is broken, law will endeavor, so far as money can do it, to place the injured party in the same position as if the contract has been performed."

It follows that damages are given for restitution and compensation. Damages are not given with the object of punishment, except in certain special cases, *e.g.*, breach of contract of marriage.

Generally, in Sale Contracts, damages are given on the basis of the differences between the contract price and the market price.

See example (*iii*), page 106.

5. Costs

The injured party is entitled to get the costs of getting the decree for damages.

6. Minimisation of loss

It is the duty of the injured party to minimise the loss as much as possible. The law imposes on the plaintiff the duty of taking all reasonable steps to mitigate the loss consequent on the breach, and debars him from claiming any part of the damages which is due to his neglect to take such steps. *Jamal* v. *Moola Dawood Sons & Co.*[1]

Example :

The plaintiff took a shop on lease and paid an advance. The defendant could not give him possession and the plaintiff chose to do no business for 8 months though there were other shops available in the vicinity. Held, he was entitled only to refund of his advance as his duty was to minimise damages and he could have done so by taking another shop. *Neki* v. *Pirbhu*.[2]

7. Effect of a penalty clause

If in a contract a sum of money is named as the amount to be paid in case of breach, or if the contract contains any stipulation by way of penalty for failure to perform the

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[1] (1916) 43 I. A. 6 [2] 100 I. C. 662

obligations, the court will allow *reasonable compensation, not exceeding the sum named.*—Sec. 74.

Example :

A contracts with *B* to pay *B* Rs. 1000 if he fails to pay *B* Rs. 500 on a certain day. *A* fails to pay *B* Rs. 500 on that day. *B* is entitled to recover from *A* such com-pensation, not exceeding Rs. 1000, as the court considers reasonable.

8. Difficulty of assessment

Difficulty of calculating damages is no ground for refusing damages. The court must make an assessment of loss and pass a decree for it.

Example :

H organised a beauty competition in which 50 ladies were to be selected by votes of the readers of certain newspapers. *H* would select 12 out of the 50 and secure theatrical jobs for them. *C* was one of the 50 and by *H*'s breach of contract was prevented from being present when the final selection was made. Held, *C* was entitled to damages even though it was difficult to calculate them. *Chaplin* v. *Hicks.*[1]

Liquidated Damages and Penalty

A contract sometimes contains a clause in which a sum of money is named as the amount payable in case of breach of contract. In such cases the question arises whether the courts of law will accept this figure as the measure of damage.

English Law : According to English law, the amount of money payable is interpreted either as liquidated damages or as a penalty. It is considered to be liquidated damages when the amount is fixed by the parties on the basis of a *reasonable* estimate of the *probable* actual *loss* which a party will suffer in case of breach. On the other hand, the amount fixed is considered to be a penalty if it is *not* based upon a reasonable calculation of actual loss but is fixed by way of *punishment* and as a *threat.* Suppose that a contractor agrees to complete the building of a house by 1st June and promises to pay Rs. 50 per day as damages for each day of default beyond the prescribed day of completion. If the figure Rs. 50 was arrived at after calculating the actual loss which the house-owner will suffer for the breach of contract, it is liquidated damages. If the actual

[1] (1911) 2 K. B. 786

damage is considerably less and the amount was fixed in order to threaten the contractor it is a penalty.

In case of liquidated damages, English courts allow only the amount stipulated, never more or less even though it is shown that the actual loss is different from the amount mentioned. Penalty clauses, however, are treated as invalid. The court allows only reasonable compensation by way of damages.

Indian Law : In India, the distinction between liquidated damages and penalty is not recognised. Section 74 of the Contract Act lays down that if the parties have fixed what the damages will be, the courts will never allow more. But the court may allow less. A decree is to be passed only for reasonable compensation, not exceeding the sum named by the parties.

Exception : There is one exceptional case provided for by Section 74. When any person enters into any bail bond or similar instrument or gives any bond (to the Central Government or any State Government) for the performance of any public duty, he shall be liable, upon breach of the condition of any such instrument, to pay the whole sum mentioned therein. In this case it is not necessary to calculate the actual loss.

Examples :

(*i*) *A* contracts with *B* to pay *B* Rs. 1000 if he fails to pay *B* Rs. 500 on a given day. *A* fails to pay *B* Rs. 500 on that day. *B* is entitled to recover from *A* such compensation, not exceeding Rs.1,000, as the Court considers reasonable. [Illustration 'a' in Section 74]

(*ii*) *A* borrows Rs. 100 from *B* and gives him a bond for Rs. 200 payable by five yearly instalments of Rs. 40, with a stipulation that, in default of payment of any instalment, the whole shall become due. This is a stipulation by way of penalty. [Illustration 'g' in Section 74]

(*iii*) The appellants, sold tyres and tubes, to the respondents who contracted not to resell them, at a price below the manufacturers' list prices. The respondents further agreed to pay £5 by way of liquidated damages for every breach of this agreement. They sold a tyre at less than the list price. The House of Lords held that the sum fixed was a pre-estimate of the damage and not a penalty. *Dunlop Pneumatic Tyre Co. Ltd* v. *New Garage and Motor Co. Ltd.*[1]

(*iv*) The defendant agreed not to sell any one of the plaintiffs' cars below the listed price. For every breach he was to pay £250, as 'agreed damages'. The Court of Appeal of England held that this was a penalty. *Ford Motor Co.* v. *Armstrong.*[2]

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[1] (1915) A. C 79 [2] (1915) 31 T. L. R. 267

Can increased interest be called as penalty ?

A stipulation that increased interest will be paid from the date of default of performance may be considered a penalty clause and disallowed by the courts. If simple interest is payable and there is a condition in the agreement that the debtor will have to pay compound interest on failure to pay at the specified date, the condition will be considered penalty.

When can interest be claimed ?

Interest can be claimed and awarded for any debt or damages. The rules regarding interest were formerly laid down in the Interest Act of 1839. This Act was repealed in 1978 and was replaced by the Interest Act of 1978 (Act No. 14 of 1978). The important rules of the Act of 1978, regarding interest for debt and damages, are stated below : (1) there must be a debt or a sum certain ; (2) it must be payable at a certain time or otherwise ; (3) these debts or sums must be payable by virtue of some written contract at a certain time ; (4) there must have been a demand in writing stating that interest will be demanded from the date of demand ; and (5) the rate of interest must not exceed the current rate of interest. The phrase "the current rate of interest" means the highest of the maximum rates at which interest may be paid on different classes of deposits given or issued by the rules of the Reserve Bank of India.

The rules, stated above, do not apply to any debt or damages on which (*a*) interest is payable as of right; by virtue of any agreement ; and (*b*) when such payment of interest is barred by virtue of an express agreement. The rules do not apply to (*a*) compensation for dishonour under the Negotiable Instruments Act ; and (*b*) rules under the Code of Civil Procedure. The Court can award interest upon interest.

QUANTUM MERUIT

Definition

The phrase "Quantum Meruit" means "as much is merited". A person can, under certain circumstances, claim payment for work done or goods supplied without any contract and in cases where the original contract has terminated by breach of contract by one party or has become void for some reason. This is known as the Doctrine of Quantum Meruit.

Rules

The rules regarding the Doctrine of Quantum Meruit are stated below.

1. Where there is a breach of contract, the injured party is entitled to claim reasonable compensation for what he has done under the contract.

Examples :

(*i*) *P* agreed to write a book to be published by instalments in a magazine owned by *C*. After a few instalments were published, the magazine was abandoned. *P* is entitled to get damages for breach of contract and payment quantum meruit for the part already published. *Planche* v. *Colburn*.[1]

(*ii*) The plaintiff agreed to erect certain building but failed to complete the contract. The defendant completed the building himself, using the materials left on the site by the plaintiff. It was held that the plaintiff could not recover for the work done, but he was entitled to recover the value of the materials used. *Sumpter* v. *Hedges*.[2]

2. When a contract is discovered to be unenforceable for some technical reason, any person who had done something under the contract, is entitled to reasonable compensation. The case is proved for by Section 65 of the Act. (See p. 140)

Example :

C was employed as managing director of a company by the board of directors of the company under a written contract. The contract was found to be void because the directors who constituted the board were unqualified. *C* actually worked as managing director for some time. It was held that he was entitled to remuneration as quantum meruit. *Craven-Ellis* v. *Canons Ltd*.[3]

3. In certain cases the law presumes an implied agreement to pay for services rendered, for example, when work is done or goods are supplied by a person without any intention to do so gratuitously and the benefit of the same enjoyed by the other party. This case is provided for by Section 70 of the Contract Act. (See p. 142)

Example :

A, a trader leaves certain goods with *B* by mistake, not intending to do so gratuitously. *B* uses the goods. He must pay for them.

4. Where a contract is not divisible into parts and a lump sum of money is promised to be paid for the entire work, part

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[1] (1831) 8 Bing 14 [2] (1898) 1 Q. B. 673
[3] (1936) 2 K. B. 403

performance does not entitle a party to claim payment quantum meruit.

Example :

A sailor was appointed on a ship for a voyage from Jamaica to Liverpool on a lump sum payment of 30 guineas. He died when only two-thirds of the voyage was completed. Held, his legal representatives could not recover anything. *Curter* v. *Powell.*[1]

5. Nothing can be recovered for quantum meruit when there is no evidence of an excess or implied promise to pay for work already done.

6. A person guilty of breach of contract cannot claim payment on quantum meruit.

SPECIFIC PERFORMANCE

Under certain circumstances, a person aggrieved by breach of contract can file a suit for specific performance, *i.e.*, for an order by the court upon the party guilty of breach of contract directing him to perform what he promised to do. Specific performance is a discretionary remedy which is allowed only in a limited number of cases. Rules regarding the granting of this relief are contained in the Specific Relief Act of 1877.

Generally speaking specific performance is directed only in cases where monetary compensation is not an adequate remedy. For example, in contract for the sale of a particular house or some rare article, monetary compensation is not enough because the injured party will not be able to get an exact substitute in the market. In such cases specific performance may be directed.

Specific performance is not allowed in cases where monetary compensation is an adequate relief. It is also not allowed in contracts of a personal nature, *e.g.*, a contract to marry or a contract to paint a picture. Where it is not possible for the court to supervise the performance of the contract, *e.g.*, a building contract, specific performance is not granted.

INJUNCTION

Injunction means an order of the court. In cases of breach of contract, the injured party can, under certain circumstances,

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[1] 101 E. R. 573

get a negative injunction, *i.e.*, an order prohibiting a party from doing something. Injunctions are usually granted to enforce negative stipulations in cases where damages are not adequate relief. It is particularly appropriate in cases of anticipatory breach of contract.

Examples :

(*i*) *G* agreed to buy the whole of the electric energy required for his house from a certain company. This was interpreted as a promise not to buy electricity from any other company. He was therefore restrained by an injunction from buying electricity from any other company. *Metropolitan Electric Supply Company* v. *Ginder*.[1]

(*ii*) *N*, a film actress agreed to act exclusively for Warner Bros. for one year. During the year she contracted to act for *X*. Held, she could be restrained by an injunction from acting for *X*. *Warner Bros.* v. *Nelson*.[2] It is to be noted that in this case an order directing *N* to act for Warner Bros. (specific performance of the contract) was not passed because the contract was of a personal nature and performance could not have been supervised by the courts.

RESTITUTION OF BENEFIT

Section 64 of the Contract Act provides that when a person, at whose option a contract is voidable, rescinds such contract, he must restore to the other party any benefit which he may have received from him. For example, when a contract for the sale of a house is avoided on the ground of undue influence, any money received on account of the price must be refunded.

Section 65 provides that when an agreement is *discovered to be void* or when a contract *becomes void*, any person who has received any advantage under such agreement or contract is bound to restore it or to make compensation for it, to the person from whom he received it.

This section applies to contracts 'discovered to be void' and contracts which 'becomes void'. It does not apply to contracts which are known to be void. Thus if *A* pays Rs. 100 to *B* to beat *C*, the money is not recoverable.

The expression 'become void' is interpreted liberally. In *Muralidhar Chatterjee* v. *The International Film Co.*[1] it was held that when one party rescinds a contract for the default of another he is entitled to damages (if he has suffered any) but he must

[1] (1901) 2 Ch. 799 [2](1937) 1 K.B. 209

restore to the other party any advantage he has received under the contract.

Examples :

(*a*) *A* pays *B* Rs. 1000 in consideration of *B*'s promising to marry *C*, *A*'s daughter. *C* is dead at the time of the promise. The agreement is void but *B* must repay *A* Rs. 1000.

(*b*) *A*, a singer contracts with *B* the manager of a theatre to sing at his theatre for two nights in every week during the next two months, and, *B* engages to pay her a hundred rupees for each night's performance. On the sixth night *A* wilfully absent herself from the theatre and *B*, in consequence, rescinds the contract. *B* must pay *A* for the five nights on which she had sung. (*B* can of course claim damages against *A* for breach of contract.)

EXERCISES

1. State the circumstances under which a contract is said to be discharged. (Page 115)
2. Discuss the circumstances under which a contract can be terminated by consent of the parties. (Pages 115-119)
3. What do you understand by 'Novation' ? What is the difference between Alteration and Novation ? (Page 116)
4. Discuss the effect of supervening impossibility in the performance of a contract. (Pages 119-124)
5. Explain the Law of Frustration of Contract. Give illustrations. (Pages 124-127)
6. Define : Special Damages ; Exemplary Damages ; Nominal Damages. (Pages 131-133)
7. Describe the rules for determination of compensation payable in case of breach of contract. (Pages 128-134)
8. Explain 'Anticipatory breach of contract'. What are the consequences of the breach ? (Page 128)
9. What are the consequences of breach of a contract ? (Pages 129 -30)
10. State the remedies allowed to the aggrieved person in case of breach of contract. (Pages 128-130)
11. Explain the terms 'Penalty' and 'Liquidated Damages' clearly indicating the difference between the two. (Pages 134-136)
12. What is the effect of a contract on : (*i*) Strike, Lock-out and Riots, (*ii*) Material alteration, and (*iii*) Lapse of time ? (Para 3, page 123, 127)

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[1] AIR (1943) Privy Council 34

13. Write notes on : (*a*) Alteration, (*b*) Remission, (*c*) Accord and Satisfaction, (*d*) Rescission, (*e*) Waiver, (*f*) Merger, (*g*) Quantum Meruit.

[(*a*) 116, (*b*) 116, (*c*) 117, (*d*) 118, (*e*) 118-119, (*f*) 119, (*g*) 137-139]

14. Problem :

(*a*) *A* pays Rs. 10,000 to *B* in consideration of *B*'s promise to marry *C*. *A*'s daughter. *C* dies and the marriage does not take place. Can *A* claim a refund of the money from *B*? Discuss fully. (Example (*a*) page 141)

(*b*) *A* agreed to let his hall to *B*, for some public entertainment on 1st December, 1965. On 28th November, 1965 the hall was destroyed by accidental fire. Discuss the respective right of *A* and *B*. (Example (*a*) page 120)

(*c*) A debtor agreed to pay compound interest on failure to pay simple interest at the due date. Is it liquidated damage or penalty ? (Page 137)

15. Objective questions. Give short answers :

(*i*) Write two ways of termination of Contract. (Pages 115)

(*ii*) Write two remedies of breach of contract. (Page 130)

(*iii*) State the different damages which can be given for breach of contract. (Pages 131-132)

12 QUASI-CONTRACTS

DEFINITION AND EXPLANATION

When one person obtains a benefit at the expense of another and the circumstances are such that he ought, equitably, to pay for it, the law will compel payment, even though there is no contract between the parties by which payment is promised. The parties will be put in the same position as they would have occupied if there was a contract between them. Such cases are called quasi-contracts because the relationship between the parties in such cases resembles those created by contracts. Sections 68-72 of the Contract Act describe the cases which are to be deemed quasi-contracts under the Indian law.

1. Necessaries for incapable persons

"If a person, incapable of entering into a contract, or any one whom he is legally bound to support, is supplied by another person with necessaries suited to his condition in life, the person who has furnished such supplies is entitled to be reimbursed from the property of such incapable person."—Sec. 68. (See Page 51)

Examples :

(*i*) *A* supplies *B*, a lunatic with necessaries suitable to his condition in life. *A* is entitled to be reimbursed from *B*'s property.

(*ii*) *A* supplies the wife and children of *B*, a lunatic with necessaries suitable to their condition in life. *A* is entitled to be reimbursed from *B*'s property.

This section covers the case of necessaries supplied to a minor and other incapable persons (*e.g.*, a lunatic) and to persons whom the incapable person is bound by law to maintain (*e.g.*, his wife and minor children). The things supplied must come within the category of necessaries. The price to be paid is reasonable price—not the price which the incapable person might have "agreed to" (legally speaking an incapable person cannot agree to anything). Only the property of the incapable person is liable. He is not personally liable.

2. Reimbursement of interested persons

"A person who is interested in the payment of money which

another is bound by law to pay, and who therefore pays it, is entitled to be reimbursed by the other."—Sec. 69.

Requisites : The provisions of section 69 are as follows :

1. The payment is to be given to a person interested.
2. The payment is for the protection of his own interest.
3. The person is entitled to repayment.
4. The party must be bound to pay by law.

Examples :

(*i*) *B* holds land in Bengal on a lease granted by *A*, the zamindar. The revenue payable by *A* to the Government being in arrear, his land is advertised for sale by the Government. Under the revenue law, the consequence of such sale will be annulment of *B*'s lease. *B* to prevent the sale and the consequent annulment of his own lease, pays to the Government the sum due from *A*. *A* is bound to make good to *B* the amount so paid. (Illustration to Sec 69).

(*ii*) *X*'s goods were wrongfully attached in order to realise arrears of Government revenue due by *Y*. *X* pays the amount to save the goods from sale. *X* is entitled to recover the money from *Y*. *Tulsa Kunwar* v. *Jageshar Prasad*.[1]

(*iii*) A, Hindu mother incurred expenses for her daughter's marriage. She is entitled to recover the expenses from the other members of the Hindu Joint Family. *Vaikuntam* v. *Kallapiram*.[2]

3. Benefit of non-gratuitous act

"Where a person lawfully does anything for another person, or delivers anything to him, not intending to do so gratuitously, and such other person enjoys the benefit thereof, the latter is bound to make compensation to the former in respect of, or to restore, the thing so done or delivered."—Sec. 70.

The three ingredients to support the cause of action under Section 70 are these : First, the goods are to be delivered lawfully or anything has to be done for another person lawfully. Second, the thing done or the goods delivered is so done or delivered "not intending to do so gratuitously." Third, the person to whom the goods are delivered "enjoys the benefit thereof." *Union of India* v. *Sita Ram Jaiswal*.[3]

Examples :

(*a*) *A*, a tradesman, leaves goods at *B*'s house by mistake. *B* treats the goods as his own. He is bound to pay for them.

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[1] (1906) 28 All 563 [2] (1900) 23 Mad. 512

[3] AIR (1977) Supreme Court 329

(*b*) *A* saves *B*'s property from fire. *A* is not entitled to compensation from *B* if the circumstances show that he intended to act gratuitously.

(*c*) *A* contractor, on the request of an officer of the State of West Bengal, constructed a *Katcha* road, office, kitchen etc, for the clerks. The State accepted the works but tried to evade liability because no contract had been concluded according to the formalities of the Government of India Act. Since the State had enjoyed the benefit of the works, the Supreme Court decreed the contractor's claim. *State of West Bengal* v. *B. K. Mondal & Sons.*[1]

(*d*) A person supplied spare motor parts and the Pune Corporation accepted the goods. But the corporation said that the contract of sale was not according to the Bombay Municipal Corporation Act. The claim was decreed by Supreme Court. *Pillo Dhunjishaw* v. *Municipal Corporation of the city of Poona.*[2]

4. Finder of goods

"A person who finds goods belonging to another and takes them into his custody, is subject to the same responsibility as a bailee."—Sec. 71 (See pp. 168-169)

5. Delivery by mistake or under coercion

"A person to whom money has been paid, or anything delivered by mistake or under coercion, must repay or return it."—Sec. 72.

"The section in terms does not make any distinction between a mistake of law or mistake of fact. The term 'mistake' has been used without any qualification or limitation whatever." *Sales-tax Officer, Banaras* v. *Kanhaiya Lal Mukund Lal Saraf.*[3]

Examples :

(*a*) *A* and *B* jointly owe 100 rupees to *C*. *A* alone pays the amount to *C*, and *B*, not knowing this fact, pays 100 rupees over again to *C*. *C* is bound to repay the amount to *B*.

(*b*) A railway company refuses to deliver up certain goods to the consignee, except upon the payment of an illegal charge for carriage. The consignee pays the sum charged in order to obtain the goods. He is entitled to recover so much of the charge as was illegally excessive.

(*c*) *A* certain amount of sales-tax was paid by a firm under the U. P. Sales Act under a mistake of law. The firm was allowed to get back the money. See case of *Kanaiya Lal Saraf.* above.

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[1] AIR (1962) Supreme Court 779 [2] AIR (1970) Supreme Court 1201
[3] AIR (1959) Supreme Court 135

Compensation in case of Quasi Contracts

Under the Contract Act Section 73, para 3, provides the compensation for loss and damages under the Quasi Contracts. The relevant provision under the Act is quoted below :

"*Compensation for failure to discharge obligation resembling those created by contract* : When an obligation resembling those created by contract has been incurred and has not been discharged, any person injured by the failure to discharge it is entitled to receive the same compensation from the party in default, as if such person had contract to discharge it and had broken his contract.

Explanation : In estimating the loss or damage arising from a breach of contract, the means which existed of remedying the inconvenience caused by the non-performance of the contract must be taken into account."

EXERCISES

1. What is a quasi-contract ? Give some examples of quasi-contract. (Page 143)
2. State the law regarding the following : (a) Necessaries ; (b) Finder of goods. (Pages (*a*) 143, (*b*) 146, 168)
3. *A* supplies food to *C* who is a lunatic. *C* has assets worth Rupees One lac. On non-payment, can *A* proceed against the assets of *C* ? Would your answer be the same if *C* instead of being a lunatic is an infant ? (Examples (*ii*) page 143)
4. Objective questions. Give short answers.
   (*i*) Write two examples of quasi-contracts. (Page 143)
   (*ii*) *X*, an infant in a school bought eleven fancy waistcoats from *Y*. He was at the time adequately provided with clothing. Can *Y* get the price for the waistcoats.
   (See *Nash* v. *Inman*, Page 51)

13 INDEMNITY AND GUARANTEE

CONTRACTS OF INDEMNITY

Definition

Section 124 of the Contract Act defines a contract of indemnity as a contract by which one party promises to save the other party from loss caused to him by the conduct of the promisor himself, or by the conduct of any other person. *P* contracts to indemnify *Q* against the consequences of any proceeding which *R* may take against *Q* in respect of a certain sum of Rs. 200. This is a Contract of Indemnity. *P* is called the *Indemnifier* and *Q* the *Indemnity-holder.*

Characteristics

Characteristics (or the requisites) of a Contract of indemnity are as follows :

1. A contract of guarantee must satisfy all the essential elements of a contract. For example, the object must be lawful, there must be free consent etc.

2. The Contract may be *express or implied.* An express contract is by word or by writing. An implied contract of indemnity comes from the circumstances of the case or the relationship between the parties.

3. Section 69 implies a promise to indemnify (See p. 144)

Definition not exhaustive

Section 124 of the Indian Contract Act does not give an exhaustive definition of contracts of indemnity. This section includes (*i*) only *express promises* to indemnify and (*ii*) only those cases where the loss arises from the conduct of the promisor or of any other person. It does not include (*i*) *implied* promises to indemnify and (*ii*) cases where loss arises from accidents and events not depending on the conduct of any person.

It has been held in a number of cases in India that a duty to indemnify may arise by operation of law even in the absence of express agreements. A promise to indemnify may be either

express or implied from the circumstances of the case. The illustration given above is an example of an *express promise* to indemnify. The following is an example of an *implied promise* to indemnify.

A broker forged the signature of the holder of a Government promissory note and endorsed it to the Bank of India. The bank got the note renewed from the Government. The holder sued the Government and recovered damages. The Government sued the bank for indemnity. The Privy Council decreed the suit, quoting with approval the following observations of Lord Halsbury : "It is a general principle of law that when an action is done by one person at the request of another which act is not in itself manifestly tortious to the knowledge of the person doing it, and such act turns out to be injurious to the rights of a third party, the person doing it is entitled to indemnity from him who requested that it should be done." *Secretary of State etc.* v. *Bank of India.*[1]

Under English law, contracts of indemnity cover a much wider field than that included in section 124 of the Indian Contract Act. In England contracts of indemnity include promises, express and implied, to indemnify a person from loss caused by events or accidents which may not depend upon the conduct of any person. In a Bombay case it was held that, "Sections 124 and 125 of the Contract Act are not exhaustive of the law of indemnity and the courts here would apply the same equitable principles that the courts in England do." *Gajanan* v. *Moreshar.*[2]

Rights of the Indemnity-holder

Section 125 of the Contract Act lays down that the indemnity-holder is entitled to get from the indemnifier :

1. all damages which he may be compelled to pay in any suit in respect of any matter to which the promise to indemnify applies ;

2. all costs which he may be compelled to pay in such suits (provided he acted prudently or with the authority of the indemnifier) ; and

3. all sums which he may have paid upon compromise of such suit (provided the compromise was prudent or was authorised by the indemnifier).

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[1] (1938) 65 I. A. 286 (Privy Council) [2] (1942) Bom 402, 670

Comments : It has been held that the rights of the Indemnity-holder, under Section 125, are not exhaustive. The indemnity-holder may be entitled to other equitable reliefs also.

Bombay and Nagpur High Courts have held the indemnifier will be liable only after the actual loss was incurred. But according to the High Courts of Calcutta, Madras and A'lahabad, the indemnity-holder can compel payment from the indemnifier even before he (the indemnity-holder) has met his liability. *Osman Jamal & Sons* v. *Gopal.*[1]

CONTRACTS OF GUARANTEE

Definition

A contract of guarantee is a contract to perform the promise or discharge the liability, of a third person in case of his default.—Sec. 126. *P* lends Rs. 5,000 to *Q* and *R* promises to *P* that if *Q* does not pay the money *R* will do so. This is contract of guarantee. *Q* is called the *Principal Debtor, P the Creditor,* and *R* the *Guarantor* or the *Surety.*

Classification

Contracts of guarantee may be of three types: (1) for payment to the Creditor to the Principal Debtor by the Guarantor ; (2) payment of price for goods sold, and (3) 'fidelity guarantee' i.e. to discharge the liability of a person for good conduct of a service-holder.

A contract of guarantee may be for (1) a future debt or obligation or for (2) an existing debt.

A guarantee can also be (1) a Simple Guarantee or (2) a Continuing Guarantee (see p. 152)

Essentials of a Valid Guarantee

1. A contract of guarantee must satisfy all the essential elements of a contract. (For example, the object must be lawful ; there must be free consent etc.) But the following points are to be noted.

2. A contract of guarantee may be either oral or written.—Sec 126.

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[1] (1919) 56 Cal 262

3. In a contract of guarantee there are three parties i.e., the creditor, the principal debtor and the surety. All the parties must join the contract.

4. In a contract of guarantee, the primary liability is that of principal debtor. The liability of surety arises only when there is a default of the principal debtor. Therefore, the liability of the surety is secondary.

5. In a contract of guarantee the principal debtor may be a minor. In this case the surety is liable to pay even though the minor may not be. The contract will be enforced as between the surety and the creditor.

6. *Consideration* : In a contract of guarantee, the consideration received by the principal debtor is taken to be sufficient consideration for the surety. "Anything done, or any promise made, for the benefit of the principal debtor may be sufficient consideration to the surety for giving guarantee."—Sec.127.

Examples :

(*i*) *B* requests *P* to sell and deliver to him goods on credit. *P* agrees to do so, provided *C* will guarantee the payment of the price of goods. *C* promises to guarantee the payment in consideration of *P*'s promise to deliver the goods. This is a sufficient consideration for *C*'s promise.

(*ii*) *P* sells and delivers goods to *B*. *C* afterwards requests *P* to forbear to sue *B* for the debt for a year and promises that if he does so, *C* will pay for them in default of payment by *B*, *P* agrees to forbear as requested. This is a sufficient consideration for *C*'s promise.

(*iii*) *P* sells and delivers goods to *B*. *C* afterwards, without consideration agrees to pay for them in default of *B*. The agreement is void.

Contracts of Guarantee which are invalid

A contract of guarantee is invalid in the following cases :

1. *Misrepresentation* : Any guarantee which has been obtained by means of misrepresentation made by the creditor, or with his knowledge and assent, concerning a material part of the transaction, is invalid.—Sec. 142.

2. *Concealment* : Any guarantee which the creditor has obtained by means of keeping silence as to material circumstances is invalid.—Sec. 143.

Examples :

(*a*) *D* engages *B* as clerk to collect money for him. *B* fails to account for some of his receipts, and *D* in consequence calls upon him to

furnish security for his duly accounting. *C* gives his guarantee for *B*'s duly accounting. *D* does not acquaint *C* with *B*'s previous conduct. *B* afterwards makes default. The guarantee is invalid.

(*b*) *G* guarantees to *C* payment for iron to be supplied by him to *B* to the amount of 2000 tons. *B* and *C* have privately agreed that *B* should pay five rupees per ton beyond the market price, such excess to be applied in liquidation of an old debt. This agreement is concealed from *G*. *G* is not liable as a surety.

3. *When Co-surety does not join* : Where a person gives a guarantee upon a contract that the creditor shall not act upon it until another person has joined in it as co-surety, the guarantee is not valid if that other person does not join.—Sec. 144.

4. *Lack of essential elements* : A contract of guarantee is invalid if it lacks one or more of the essential elements of a contract (*e.g.*, if there is want of free consent or if the object is illegal).

DIFFERENCES BETWEEN INDEMNITY AND GUARANTEE

1. In a contract of indemnity, there are *two parties* : the indemnifier and the indemnity-holder. In a contract of guarantee there are *three parties* : the creditor, the principal debtor, and the surety.

2. In a contract of indemnity it is necessary to have only one contract, i.e., between the indemnity-holder and the indemnifier ; in a contract of guarantee it is necessary to have three contracts, between the parties, i.e., between the creditors, the principal debtors and the surety.

3. In a contract of indemnity, the liability of the indemnifier is *primary* ; in a contract of guarantee, the liability of the surety is *secondary i.e.*, the surety is liable only if the principal debtor fails to perform his obligations.

4. In a contract of guarantee there is an existing debt or duty, the performance of which is guaranteed by the surety. In a contract of indemnity, the liability of the indemnifier arises only on the *happening of a contingency.*

5. In a contract of indemnity the indemnifier can sue only the indemnity-holder for his loss, because there is no contract between the indemnified and other parties unless there is an assignment on his favour ; in a contract of guarantee the surety can proceed against principal debtor.

6. In a contract of guarantee the surety, after he discharges the debt owing to the creditor, can proceed *against the principal debtor*; in a contract of indemnity the loss falls on the *indemnifier* except in certain special cases.

CONTINUING GUARANTEE

Definition

A guarantee which extends to a series of transactions is called a *Continuing Guarantee.* (Sec. 129). A guarantee covering a single transaction may be called a *Simple Guarantee* or *Specific Guarantee.*

Examples :

(*i*) *D*, in consideration that *B* will employ *C* in collecting the rents of *B*'s zamindari, promises *B* to be responsible, to the amount of 5,000 rupees, for the due collection and payment by *C* of those rents. This is a continuing guarantee.

(*ii*) *P* guarantees payment to *B* a tea dealer, to the amount of Rs. 1000 for any tea he may from time to time supply to *C*. *B* supplies *C* with tea to the value of Rs. 1000 and *C* pays *B* for it. After-wards *B* supplies *C* with tea to the value of Rs. 2000. *C* fails to pay. The guarantee given by *P* was a continuing guarantee, and he is accordingly liable to *B* to the extent of Rs. 1000.

(*iii*) *P* guarantees payment to *B* of the price of five sacks of flour to be delivered by *B* to *C* to be paid for in a month. *B* delivers five sacks to *C*, *C* pays for them. Afterwards *B* delivers four sacks to *C*, which *C* does not pay for. The guarantee given by *P* was not a continuing guarantee, and accordingly he is not liable for the price of the four sacks.

How a Continuing Guarantee is Revoked

A continuing guarantee is revoked under the following circumstances.

1. *By notice of revocation by the surety* : The notice operates to revoke the surety's liabilities as regards transactions entered into after the notice. He continues to be liable for transactions entered into prior to the notice.—Sec. 130.

2. *By the death of the surety* : "The death of the surety operates, in the absence of a contract to the contrary, as a revocation of a continuing guarantee, so far as regards future transactions."—Sec. 131.

The estate of the surety is liable for all transactions entered

into prior to the death of the surety unless there was a contract to the contrary. It is not necessary that the creditor must have notice of the death.

A continuing guarantee is *terminated* under the same circumstances under which a surety's liability is discharged. (See below.)

THE EXTENT OF THE LIABILITY OF THE SURETY

Surety's Liability

The liability of the surety is co-extensive with that of the principal debtor, unless it is otherwise provided by the contract.—Sec. 128.

Example :

G guarantees to *B* the payment of a bill of exchange by *C*, the acceptor. The bill is dishonoured by *C*. *G* is liable not only for the amount of the bill but also for any interest and charges which may have become due on it.

A creditor is not bound first to proceed against the principal debtor. He can sue the surety without suing the principal debtor or without making the principal debtor a co-defendant. When the principal debtor is a minor, the surety alone is liable to the creditor.

Liability of two persons, primarily liable, not affected by arrangement between them that one shall be surety on other's default

Where two persons contract with a third person to undertake a certain liability, and also contract with each other that one of them shall be liable only on the default of the other, the third person not being a party to such contract, the liability of each of such two persons to the third person under the first contract is not affected by the existence of the second contract, although such third person may have been aware of its existence.—Sec. 132.

Example :

A and *B* made a joint and several promissory note to *C*. *A* makes it, in fact, as surety for *B* and *C* knows this as the time when the note is made. The fact that *A*, to the knowledge of *C* made the note as surety for *B*, is no answer to a suit by *C* against *A* upon the note.

WHEN IS A SURETY DISCHARGED FROM LIABILITY ?

The liability of a surety under a contract of guarantee comes to an end under any one of the following circumstances :

1. Notice of revocation

In the case of a continuing guarantee, a notice by the surety to the creditor stating that he will not be responsible, will revoke his liability as regards all future transactions. He will remain liable for all transactions entered into prior to the date of the notice.—Sec. 130.

2. Death of surety

In the case of a continuing guarantee the death of a surety discharges him from all liabilities as regards transactions after his death unless there is a contract to the contrary.—Sec. 131.

3. Variation of contract

Any variance, made without the surety's consent in the terms of the contract between the principal debtor and the creditor, discharges the surety as to transactions subsequent to the variance.—Sec. 133.

Examples :

(*a*) *A* becomes surety to *C* for *B*'s conduct as a manager in *C*'s bank. Afterwards *B* and *C* contract, without *A*'s consent, the *B*'s salary shall be raised and that he shall become liable for one-fourth of the losses on overdraft. *B* allows a customer to overdraw, and the bank loses a sum of money. *A* is discharged from his suretyship by the variance made without his consent, and is not liable to make good this loss.

(*b*) *C* agrees to appoint *B* as his clerk to sell goods at a yearly salary, upon *A*'s becoming surety to *C* for *B*'s accounting for moneys received by him as such clerk. Afterwards, without *A*'s knowledge or consent, *C* and *B* agree that *B* should be paid by a commission on the goods sold by him and not by a fixed salary. *A* is not liable for subsequent misconduct of *B*.

(*c*) *A* gives to *C* a continuing guarantee to the extent of 3,000 rupees for any oil supplied by *C* to *B* on credit. Afterwards *B* becomes embarrassed, and without the knowledge of *A*, *B* and *C* contract that *C* shall continue to supply *B* with oil for ready money and that the payments shall be applied to the then existing debts between *B* and *C*. *A* is not liable on his guarantee for any goods supplied after this new arrangement.

(*d*) *C* contracts to lend *B* 5,000 rupees on the 1st March. *A* guarantees repayment. *C* pays the 5,000 rupees to *B* on the 1st January. *A* is discharged from his liability, as the contract has been varied inasmuch as *C* might sue *B* for the money before the 1st March.

4. Release or discharge of principal debtor

The surety is discharged by any contract between the creditor and the principal debtor, by which the principal debtor is released, or by any act or omission of the creditor, the legal consequence of which is the discharge of the principal debtor.—Sec. 134.

Effect of Debt Relief Acts : The Madras High Court held that if the liability of the principal debtor is reduced under the provisions of an Act for debt relief, the surety is liable only for the reduced amount. *Subramania Chettiar* v. *M. P. Narayanswami Gounder*.[1] The Nagpur and the Kerala High Courts have held similar decisions.

Examples :

(*a*) *G* gives a guarantee to *C* for goods to be supplied by *C* to *B*. *C* supplies goods to *B* and afterwards *B* becomes embarrassed and contracts with his creditors (including *C*) to assign to them his property in consideration of their releasing him from their demands. Here *B* is released from his debt by the contract with *C* and *G* is discharged from his suretyship.

(*b*) *A* contracts with *B* to grow a crop of sugarcane on *A*'s land and to deliver it to *B* at fixed rate, and *C* guarantees *A*'s performance of this contract. *B* diverts a stream of water which is necessary for irrigation of *A*'s land and thereby prevent him from raising the crops. *C* is no longer liable on his guarantee.

(*c*) *D* contracts with *B* for a fixed price to build a house for *B* within a stipulated time. *B* supplying the necessary timber. *C* guarantees *D*'s performance of the contract. *B* omits to supply the timber. *C* is discharged from his suretyship.

5. Arrangement with principal debtor

A contract between the creditor and the principal debtor, by which the creditor makes a composition with, or promises to give time to, or not to sue, the principal debtor, discharges the surety, unless the surety assents to such contract.—Sec. 135.

With a third person

But where a contract to give time to the principal debtor

[1] AIR (1951) Mad. 48

is made by the creditor with a third person, and not with the principal debtor, the surety is not discharged.—Sec. 136.

Example :

C, the holder of an overdue bill of exchange drawn by *D* as surety for *B*, and accepted by *B*, contracts with *M* to give time to *B*. *D* is not discharged.

6. Creditor's forbearance to sue does not discharge surety

Mere forbearance on the part of the creditor to sue the principal debtor or to enforce any other remedy against him does not, in the absence of any provision in the guarantee to the contrary, discharge the surety.—Sec. 137.

Examples :

(*i*) *B* owes to *C* a debt guaranteed by *G*. The debt becomes payable. *C* does not sue *B* for a year after the debt has become payable. *G* is not discharged from his suretyship.

(*ii*) Failure to sue the principal debtor until recovery is barred by Statute of Limitation does not operate as a discharge of the surety. *Mohant Singh* v. *Ba Yi*.[1]

7. Release of one co-surety

Where there are co-sureties, a release by the creditor of one of them does not discharge the others; neither does it free the surety so released from his responsibility to the other sureties.—Sec. 138.

8. Act or omission impairing surety's eventual remedy

If the creditor does any act which is inconsistent with the rights of the surety, or omits to do any act which his duty to the surety requires him to do and the eventual remedy of the surety himself against the principal debtor is thereby impaired, the surety is discharged.—Sec. 139.

Examples :

(*a*) *B* contracts to build a ship for *C* for a given sum, to be paid by instalments as the work reaches certain stages. *S* becomes surety to *C* for *B*'s due performance of the contract. *C*, without the knowledge of *S*, prepays to *B* the last two instalments. *S* is discharged by the prepayment.

(*b*) *C* lends money to *B* on the security of a joint and several promissory note made in *C*'s favour by *B* and by *S* as surety for *B*, together with a bill of sale of *B*'s furniture, which gives power to *C* to sell

[1] AIR (1939) P. C. 410 (Privy Council)

the furniture, and apply the proceeds in discharge of the note. Subsequently, *C* sells the furniture, but, owing to his misconduct and wilful negligence, only a small price is realised. *S* is discharged from liability on the note.

(*c*) *S* puts *M* as apprentice to *B*, and gives a guarantee to *B*, for *M*'s fidelity. *B* promises on his part that he will, at least once a month, see *M* make up the cash. *B* omits to see this done as promised, and *M* embezzles. *S* is not liable to *B* on his guarantee.

9. Loss of security

If the creditor loses or parts with any security given to him by the principal debtor at the time the contract to guarantee was entered into, the surety is discharged to the extent of the value of the security, unless the surety consented to the release of such security.—Sec. 141.

10. Miscellaneous

A contract of guarantee is invalid if it is obtained by means of misrepresentation (Sec. 142), silence as to material circumstances (Sec. 143), or if a co-surety fails to join according to the terms of the contract (Sec. 144). See pp. 150-151.

THE RIGHTS OF THE SURETY

A surety has the following rights :

Against the Principal Debtor

1. *Right of Subrogation* : Upon payment of performance of all that he is liable for, he is invested with all the rights which the creditor had against the principal debtor.—Sec. 140.

2. *Right to Indemnity* : In every contract of guarantee there is implied promise by the principal debtor to indemnify the surety ; and the surety is entitled to recover from the principal debtor whatever sum he has rightfully paid under the guarantee, but no sums which he has paid wrongfully.—Sec. 145.

Examples :

(*a*) *B* is indebted to *C* and *A* is surety for the debt. *C* demands payment from *A*, and on his refusal sues him for the amount. *A* defends the suit, having reasonable grounds for doing so, but is compelled to pay the amount of the debt with costs. He can recover from *B* the amount paid by him for costs, as well as the principal debt.

(*b*) *C* lends *B* a sum of money and *A*, at the request of *B* accepts a bill of exchange drawn by *B* upon *A* to secure the amount. *C*, the

holder of the bill, demands payment of it from *A*, and on *A*'s refusal to pay, sues him upon the bill. *A* not having reasonable grounds for so doing, defends the suit, and has to pay the amount of the bill and costs. He can recover from *B* the amount of the bill, but not the sum paid for costs, as there was no real ground for defending the action.

(*c*) A surety settled with the creditor by paying a sum smaller than the amount guaranteed. Held, he can recover only what he paid. *Reed* v. *Norris*.[1]

Against the Creditor

Right of Security : A surety is entitled to the benefit of every security which the creditor has against the principal debtor at the time when the contract of suretyship is entered into. Whether the surety knows of the existence of security or not is immaterial.—Sec. 141.

"The expression 'security' in Section 141 is not used in any technical sense ; it includes all rights which the creditor had against the property of the principal debtor at the date of contract." *State of M. P.* v. *Kaluram*.[2]

Examples :

(*a*) *C* advances to *B* his tenant, 2000 rupees on the guarantee of *A*, *C* has also a further security for the 2000 rupees by a mortgage of *B*'s furniture. *B* cancels the mortgage. *B* becomes insolvent, and *C* sues *A* on his guarantee. *A* is discharged from liability to the amount of the value of the furniture.

(*b*) *C*, a creditor whose advance to *B* is secured by a decree, receives also a guarantee for that advance from *A*. *C* afterwards takes *B*'s goods in execution under the decree, and then, without the knowledge of *A*, withdraws the execution. *A* is discharged.

(*c*) *A* is surety for *B*, makes a bond jointly with *B* to *C*, to secure a loan from *C* to *B*. Afterwards, *C* obtains from *B* a further security for the same debt. Subsequently, *C* gives up the further security. *A* is not discharged.

Against the Co-surety—See Below.

CONTRIBUTION BETWEEN CO-SURETIES

Definition

Where several persons guarantee a debt or duty, they are called co-sureties.

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[1] 2 Bing 361 [2] AIR (1967) Supreme Court 1105

Co-sureties liable to contribute equally

Where two or more persons are co-sureties for the same debt or duty, either jointly or severally, and whether under the same or different contracts, and whether with or without the knowledge of each other, the co-sureties in the absence of any contract to the contrary, are liable as between themselves, to pay each an equal share of the whole debt, or of that part of it which remains unpaid by the principal debtor.—Sec. 146.

Examples :

(*a*) *A*, *B* and *C* are sureties to *D* for the sum of 3,000 rupees lent to *E*. *E* makes default in payment. *A*, *B* and *C* are liable as between themselves, to pay 1000 rupees each.

(*b*) *A*, *B* and *C* are sureties to *D* for sum of 1000 rupees lent to *E* and there is a contract between *A*, *B* and *C* that *A* is to be responsible to the extent of one-quarter, *B* to the extent of one-quarter, and *C* to the extent of one-half. *E* makes default in payment. As between the sureties *A* is liable to pay 250 rupees, *B* 250 rupees and *C* 500 rupees.

Liability of Co-sureties bound in different sums

Co-sureties who are bound in different sums are liable to pay equally as far as the limits of their respective obligations permit.—Sec. 147.

Examples :

(*a*) *A*, *B* and *C* as sureties for *D*, enter into three several bonds, each in a different penalty, namely *A* in the penalty of 10,000 rupees, *B* in that of 20,000 rupees, *C* in that of 40,000 rupees, conditioned for *D*'s duly accounting to *E*. *D* makes default to the extent of 30,000 rupees. *A*, *B* and *C* are each liable to pay 10,000 rupees.

(*b*) *A*, *B* and *C*, as sureties for *D*, enter into three several bonds each in a different penalty, namely *A* in the penalty of 10,000 rupees, *B* in the that of 20,000 rupees, *C* in that of 40,000 rupees, conditioned for *D*'s duly accounting to *E*. *D* makes default to the extent of 40,000 rupees. *A* is liable to pay 10,000 rupees, and *B* and *C* 15,000 rupees.

Release of one co-surety — See para 7, p. 156.

EXERCISES

1. Define a contract of indemnity. Distinguish between a contract of guarantee and a contract of indemnity. (Pages 147, 150)
2. Discuss the nature and extent of the liability of a surety. (Page 153)

3. State the law relating to continuing guarantee. (Page 152)
4. What are the rights of a surety against the principal debtor and against the co-sureties. (Pages 157-159)
5. Explain the rule that between co-sureties there is equality of the burden and benefit. (Pages 158-159)
6. *Problems* : (*a*) *B* owes to *C* a debt guaranteed by *A*. The debt becomes payable. *C* does not sure for a year after the debt has become payable. Is *A* discharged from his suretyship ? Give reasons. (Example (*i*) page 156)
   (*b*) *P* sells and delivers goods to *B*. *C* afterwards, without consideration, agrees to pay for them in default of *B*. Is the agreement valid ? Give reasons. (Example (*iii*), page 150)
7. Objective question. Give short answer.
   (*i*) Give an example of continuing guarantee. (Page 152)

(14) BAILMENT AND PLEDGE

DEFINITION AND FEATURES

Definition of Bailment

"A bailment is the delivery of goods by one person to another for some purpose, upon a contract that they shall, when the purpose is accomplished be returned or otherwise disposed of according to the directions of the persons delivering them".— Sec. 14.

The person delivering the goods it called the *Bailor*. The person to whom they are delivered is called the *Bailee*. The transaction is called *Bailment*.

Examples :

(*i*) *P* lends his book to *Q*.
(*ii*) *P* delivers a pen to *Q* for repair.
(*iii*) *P* gives *Q* his watch as security for a loan.
In all these cases *P* is the bailor and *Q* is the bailee.

Characteristic Features or the Requisites of Bailment

Bailment has the following characteristic features :

1. *Delivery* : It is delivery of goods by one person to another.

2. *Purpose* : The goods are delivered for some purpose.

3. *Return* : It is agreed, that when the purpose is accomplished the goods are to be returned or otherwise disposed of according to the direction of the bailor.

4. *Contract* : Bailment arises from express or implied contract. In case of finder of goods bailment arises by implication of law.

5. *Ownership* : In bailment the bailor continues to be the owner of the goods. Therefore bailment does not cause any change of ownership.

6. *Movable goods* : Bailment is concerned with only movable goods. Money is not included in the category in movable goods. A deposit of money is not bailment.

Deposit of money in a bank does not constitute bailment. The relationship between depositor and the bank is that of borrower and the lender.

7. *Possession* : A person already in possession of the goods may become a bailee by a subsequent agreement, express or implied.

Example :

X is a seller of motor cars, having several cars in his possession. *Y* buys a car and leaves the car in the possession of *X*. After the sale is complete, *X* becomes a bailee, although originally he was the owner.

Delivery to bailee how made

"The delivery of goods to the bailee may be made by doing anything which has the effect of putting the goods in the possession of the intended bailee or of any person authorised to hold them on his behalf".—Sec. 149.

Different kinds of Bailment

Bailments may be classified into ; (1) *Gratuitous Bailments* and (2) *Bailment for Reward.*

A gratuitous bailment is one in which neither the bailor, nor the bailee is entitled to any remuneration, *e.g.*, loan of an article *gratis* ; safe custody without charge, etc.

A bailment for reward is one where either the bailor or the bailee is entitled to a remuneration, *e.g.*, a motor car let out for hire ; goods given to a carrier for carriage at a price ; articles given to a person for being repaired for a remuneration ; pawn, etc.

DUTIES OF THE BAILEE

1. Duty of reasonable care

The bailee is bound to take as much care of the goods bailed to him as a man of ordinary prudence would, under similar circumstances, take of his own goods of the same bulk, quality and value as the goods bailed.—Sec. 151.

The degree of care to be taken by a bailee is that of a man of ordinary prudence. If he takes that amount of care, he will not be held responsible for loss, destruction or deterioration of the goods bailed. (Sec. 152). The degree of care required from the bailee is the same whether the bailment is for reward or is gratuitous.

There may be a special contract between the bailor and the bailee by which the bailee is required to take a higher degree

of care or under which he is responsible for compensating in full for loss, destruction or deterioration of the goods. Such special terms are usually incorporated in contracts of carriage.

2. Bailee's liability for negligence of servants

A bailee is liable for damages caused by negligence of the servants about the use or custody of the things bailed, when acting in course of their employment. But the bailee is not liable for damages caused by the acts or default of third person which cannot be prevented by ordinary diligence. The bailee is also not liable for unauthorised acts of his servants outside the scope of their employment. *Sanderson* v. *Collins.*[1]

3. Unauthorised use of goods

If the bailee makes unauthorised use of goods bailed, *i.e.*, uses them in a way not authorised by the terms of the bailment, he is responsible for all damages to the goods and must pay compensation to the bailor. This liability arises even if the bailee is not guilty of any negligence, and even if the damage is the result of accident.—Sec. 154.

Examples :

(*i*) *A* lends a horse to *B* for his own riding only. *B* allows *C*, a member of his family, to ride the horse. *C* rides with care, but the horse accidentally falls and is injured. *B* is liable to make compensation to *A* for the injury done to the horse.

(*ii*) *A* hires a horse in Calcutta from *B* expressly to march to Benares, *A* rides with due care, but marches to Cuttack instead. The horse accidentally falls and is injured. *A* is liable to make compensation to *B* or the injury to the horse.

4. Mixture of Bailor's goods with the Bailee's

If the bailee mixes up his own goods with those of the bailor, the following rules apply :

(*a*) "If the bailee, with consent of the bailor, mixes the goods of the bailor with his own goods, the bailor and the bailee shall have an interest, in proportion to their respective shares, in the mixture thus produced."—Sec. 155.

(*b*) "If the bailee, without the consent of the bailor mixes the goods of the bailor with his own goods, and the goods can

[1] (1904) 1 K. B. 628

be separated or divided, the property in the goods remains in the parties respectively; but the bailee is bound to bear the expense of separation or division, and any damage arising from the mixture."—Sec. 156.

Example :

D bails 100 bales of cotton marked with a particular mark to *B*. *B* without *D*'s consent mixes the 100 bales with other bales of his own, bearing a different mark. *D* is entitled to have his 100 bales returned, and *B* is bound to bear all the expenses incurred in the separation of the bales, and any other incidental damage.

(*c*) "If the bailee, without the consent of the bailor, mixes the goods of the bailor with his own goods, in such a manner that it is impossible to separate the goods bailed from the other goods and deliver them back, the bailor is entitled to be compensated by the bailee for the loss of the goods."—Sec. 157.

Example :

D bails superior flour worth Rs. 45 to *B*. *B*, without *D*'s consent mixes the flour with inferior flour of his own, worth only Rs. 25. *B* must compensate *D* for the loss of his flour.

5. Duty of returning goods

"It is the duty of the bailee to return or deliver according to the bailor's directions, the goods bailed, without demand, as soon as the time for which they were bailed has expired, or the purpose for which they were bailed has been accomplished."—Sec. 160.

"If, by the default of the bailee, the goods are not returned, delivered or tendered at the proper time, he is responsible to the bailor for any loss, destruction or deterioration of the goods from that time."—Sec. 161.

Example :

G agreed to carry certain goods of *B* expeditiously. The driver of the van which was carrying the goods, left the van unattended for one hour for lunch. During that time the goods were stolen, *B* filed a suit for damages against *G*. Held, the carrier has a duty *viz*., to deliver the goods or return them. The carrier could not do so. The van driver's departure constitutes a fundamental breach of the contract to carry the goods forthwith to the destination. Damages were awarded. *Bontex Knitting Works Ltd.* v. *St. John Garage*.[1]

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[1] (1944) 2 All E. R. 690

6. Accretion to the goods bailed

"In the absence of any contract to the contrary, the bailee is bound to deliver to the bailor, or according to his directions, any increase or profit which may have accrued from the goods bailed."—Sec. 163.

Example :

C leaves a cow in the custody of *B* to be taken care of. The cow has a calf. *B* is bound to deliver the calf as well as the cow to *C*.

7. Liabilities of Innkeeper and Hotelkeepers

In England Innkeepers were governed by the Common Law. They were regarded as insurers, *i.e.*, loss of or damages to customer's goods had to be fully made up, except certain special cases. This rule was applied in Bombay High Court in an old case (1886). It is now held that the liabilities of innkeepers and hotel-keepers are as bailees and are governed by Sections 151 and 152 of the Contract Act. (See para 1, p. 162) *Rampal Sing* v. *Murray & Co.*[1]; *Jan & Son* v. *Cameron.*[2]

8. Liabilities of Carriers — See Book V, Ch 1.

DUTIES OF THE BAILOR

1. Bailor's duty to disclose faults in goods bailed

"The bailor is bound to disclose to the bailee faults in the goods bailed, of which the bailor is aware, and which materially interfere with the use of them, or expose the bailee to extra-ordinary risk, and, if he does not make such disclosure, he is responsible for damage arising to the bailee directly from such faults.

If the goods are bailed for hire, the bailor is responsible for such damage, whether he was or was not aware of the existence of such faults in the good bailed."—Sec. 150.

Examples :

(*i*) *A* lends a horse which he knows to be vicious to *B*. He does not disclose the fact that the horse is vicious. The horse runs away, *B* is thrown and injured. *A* is responsible to *B* for damage sustained.

(*ii*) *A* hires a carriage of *B*. The carriage is unsafe, though *B* is not aware of it, and *A* is injured. *B* is responsible to *A* for the injury.

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[1] (1899) 22 All 164 [2] (1922) 44 All 735

2. Payment of expenses in Gratuitous Bailments

"Where by the conditions of the bailment, the bailee is to receive no remuneration, the bailor shall repay to the bailee the necessary expenses incurred by him for the purpose of the bailment."—Sec. 158.

3. Responsibility for breach of warranty of title

The bailor is responsible to the bailee for any loss which the bailee may sustain by reason that the bailor was not entitled to make the bailment, or to receive back the goods or to give direction respecting them.—Sec. 164.

Example :

A gives *B*'s car to *C* for use without *B*'s knowledge of permission. *B* sues *C* and receives compensation. *C* is entitled to recover his losses from *A*.

BAILEE'S RIGHTS

1. Enforcement of rights

The bailee can, by suit, enforce the duties of the bailor.

2. Bailment by several joint owners

"If several joint owners of goods bail them, the bailee may deliver them back to, or according to the directions of, one joint owner without the consent of all, in the absence of any agreement to the contrary."—Sec. 165.

3. Bailee not responsible on re-delivery to bailor without title

"If the bailor has no title to the goods, and the bailee, in good faith, delivers them back to, or according to directions of the bailor, the bailee is not responsible to the owner in respect of such delivery."—Sec. 166.

4. Bailee's Particular Lien

Lien means the rights to retain property until some debt or claim is paid. The right of lien is given by law in certain cases. Lien may be of two types : General Lien and Particular Lien. General lien means the right to retain *all* the goods of the other party until *all* the claims of the holder are paid. Particular lien means the right to retain particular goods until claims on account of those goods are paid.

A bailee has a particular lien, when he has rendered any service upon an article and is entitled to some remuneration for it according to the terms of the contract between him and the other party. The following limitations upon the bailee's particular lien are to be noted.—Sec. 170.

(*i*) The particular lien is available only if the service rendered by the bailee is one involving the *exercise of labour* or *skill* in respect of the goods bailed. There is no lien for custody charges or other charges for work not involving labour or skill.

(*ii*) The right of lien cannot be exercised until the services have been performed in full. When a bailee has done only a part of the work contracted for he cannot claim lien for part payment.

(*iii*) The lien cannot be claimed if there is an agreement to pay the money on a future date.

(*iv*) The lien can be exercised only so long as the goods are in the possession of the bailee. If possession is lost for any reason, the lien is also lost.

Examples :

(*i*) *A* delivers a rough diamond to *B*, a jeweller, to be cut and polished, which is accordingly done. *B* is entitled to retain the stone till he is paid for the services he has rendered.

(*ii*) *A* gives cloth to *B*, a tailor, to make into a coat, *B* promises *A* to deliver the coat as soon as it is finished, and to give a three months' credit for the price. *B* is not entitled to retain the coat until he is paid.

5. Bailee's General Lien

Section 171 provides that bailees coming within the following categories have a general lien : bankers, factors, wharfingers, attorneys of High Court, and policy brokers. Such bailees can retain all goods of the bailor so long as anything is due to them. The general lien in all these cases may not exist if there is a contract to the contrary. Bailees failing in categories other than those mentioned above may have a general lien if there is an express agreement to that effect.

BAILOR'S RIGHTS

1. Enforcement of rights

The bailor can enforce by suit all the liabilities or duties of the bailee.

2. Act inconsistent with the terms

"A contract of bailment is voidable, at the option of the bailor, if the bailee does any act with regard to the goods bailed inconsistent with the conditions of the bailment."—Sec. 153.

Example :

A lets to *B*, for hire, a horse his own riding. *B* drives the horse in carriage. This is, at the option of *A*, a termination of the bailment.

3. Restoration of goods lent gratuitously

When goods are lent gratuitously, the bailor can demand their return whenever he pleases, even though he lent it for a specified time or purpose. But if the bailee in such cases had acted in such a manner that the return of the goods before the stipulated time would cause loss greater than the benefit which he has received, the bailor must indemnify him for the loss if he compels an immediate return.—Sec. 159.

TERMINATION OF BAILMENT

A contract of bailment terminates under the following circumstances :

1. *Efflux of time* : If the bailment is for a stipulated period, the bailment terminates as soon as the stipulated period expires.

2. *Fulfilment of purpose* : If the bailment is for a specific purpose, the bailment terminates as soon as the purpose is fulfilled.

3. *Act inconsistent with the terms* : If the bailee does any act, with regard to the goods bailed, which is inconsistent with the terms of the bailment, the bailment terminates.—Sec. 153.

4. *Goods lent gratuitously* : A gratuitous bailment can be terminated any time but if premature termination causes any loss to the bailee, the bailor must indemnify the bailee.—Sec. 159.

5. *Death* : A gratuitous bailment terminates upon the death of either the bailor or the bailee.—Sec. 162.

RIGHTS AND DUTIES OF FINDER OF GOODS

Rights

A finder of goods is in the position of a bailee if he takes charge of the goods. (See p. 132) The rights of the finder of goods can be summarised as follows.—Sections 168 and 169 :

1. *Possession* : He can retain possession of the goods against everybody except the true owner.

2. *Compensation and Lien* : He is entitled to be compensated for the trouble and expense incurred by him to preserve the goods and to find out the owner. He has a lien upon the goods for the payment of these sums *i.e.*, he can refuse to return the goods until they are paid.

3. *Reward* : He cannot file a suit for the expense he has incurred but can sue for any reward which the owner might have offered for the return of the goods lost.

4. *Sale* : If the goods found are commonly the subject-matter of sale and if the owner cannot with reasonable diligence be found or if he refuses to pay the lawful charges of the finder, the goods can be sold provided the following further conditions are fulfilled—

(*a*) When the thing is in danger of perishing or of losing the greater part of its value.

(*b*) When the lawful charges of the finder amount to two-thirds of its value.

Duties and Obligations

The finder of goods is a bailee. Therefore, he has the following duties and obligations : (*i*) He must take reasonable care of the goods (Sec. 151). (*ii*) He must not mix the finder's goods with his own goods (Secs. 155-157). (*iii*) The goods must be returned to the real owner (Secs. 160 & 161). (*iv*) If there is an accretion to the goods bailed, it must be given to the real owner (Sec. 163). (*v*) He must not use the goods for his purpose. (*vi*) He must try to find out the true owner of the goods.

SUITS BY BAILEES OR BAILORS AGAINST WRONG-DOERS

1. Right to interplead

If a person, other than the bailor, claims the goods bailed, he may apply to the courts to stop delivery of the goods bailed and to decide the title to the goods.—Sec. 167.

2. Suit by bailor or bailee against wrong-doer

If a third party wrongfully deprives the bailee of the use of the goods bailed or does them any injury, the bailee is entitled

to use all such remedies as the owner of the goods might have used. Either the bailee or the bailor may file a suit against the third party in such cases.—Sec. 180.

3. Apportionment of relief or compensation obtained by such suits

Whatever is obtained by way of relief or compensation in any such suits shall, as between the bailor and the bailee be dealt with according to their respective interests.—Sec. 181.

BAILMENTS BY WAY OF PLEDGE OR PAWN

Definition

The bailment of goods as security for payment of a debt or performance of a promise is called *Pledge* or *Pawn*. The bailor in this case is called the *Pledgor* or the *Pawnor*. The bailee is called the *Pledgee* or the *Pawnee*.—Sec. 172.

Difference between Bailment and Pledge

Pledge is a particular kind of bailment. The difference between Pledge and other kinds of bailment lies in the purpose or objective of the transaction. The purpose of a pledge is to provide security for a debt or the performance of a promise. In other kinds of bailment there are other purposes for example, repair, safe-custody etc. The pledgor and the pledgee have certain special rights and duties.

When can a non-owner make a valid Pledge ?

The owner of goods can always make a valid pledge. In the following cases, one who is not an owner can make a valid pledge.

1. Mercantile Agent

A mercantile agent who is, with the consent of the owner, in possession of the goods or of the documents of title to goods, can make a valid pledge of the goods while acting in the ordinary course of business of a mercantile agent. Such a pledge will be valid even if the agent had no authority to pledge, provided that the pawnee acts in good faith and has not at the time of the pledge any notice that the pawnor has no authority to pledge.—Sec. 178.

2. Possession under a voidable contract

A person having possession of goods under a voidable contract can make a valid pledge of the goods so long as the contract is not rescinded. The pawnee gets a good title to the goods provided he acts in good faith and without notice of the pawnor's defect of title.—Sec. 178A.

Example :

A gets an ornament by inducing the owner to sell it to him by undue influence. Before the contract is rescinded by the owner, he pawns it to *B*. *B* will get a good title to the ornament provided he acted in good faith and was unaware of *A*'s defective title.

3. Pawnor with a limited interest

Where a person pledges goods in which he has only a limited interest, the pledge is valid to the extent of that interest.—Sec. 179.

4. Possession with co-owner

If one of several co-owners is in sole possession of the goods with the consent of the owners, he can make a valid pledge of the goods.—Sec. 30 (1). Sale of Goods Act.

RIGHTS OF PLEDGEE OR PAWNEE

1. Right of Retainer

"The pawnee can retain the goods pledged not only for payment of the debt or the performance of the promise, but also for the interest of the debt and all necessary expenses incurred by him in respect of the possession or for the preservation of the goods pledged."—Sec. 173.

2. Retainer for subsequent advance

The pawnee's lien is a particular lien, *i.e.*, he cannot retain the goods for any debt other than the debt for which the security was given unless there is an express contract to the contrary. If the pawnee makes fresh advances to the same debtor it will be presumed that the debtor has agreed to create on the goods already pledged a lien for the fresh advance.—Sec. 174

3. Extraordinary expenses

The pawnee is entitled to receive from the pawnor extraordinary expenses incurred by him for the preservation of the goods pledged.—Sec. 175.

4. Pawnee's right where pawnor makes default

"If the pawnor makes a default in payment of the debt, or performance, at the stipulated time of the promise, in respect of which the goods were pledged, the pawnee may bring a suit against the pawnor upon the debt or promise, and retain the goods pledged as collateral security ; or, he may sell the thing pledged on giving the pawnor reasonable notice of the sale.

If the proceeds of such sale are less than the amount due in respect of the debt or promise, the pawnor is still liable to pay the balance. If the proceeds of the sale are greater than the amount so due, the pawnee shall pay over the surplus to the pawnor.—Sec. 176.

RIGHTS OF PLEDGOR

1. Defaulting pawnor's right to redeem

"If a time is stipulated for the payment of the debt, or performance of the promise, for which the pledge is made, and the pawnor makes default in payment of the debt or performance of the promise at the stipulated time, he may redeem the goods pledged at any subsequent time before the actual sale of them ; but he must, in that case, pay, in addition, any expenses which have arisen from his default."—Sec. 177.

2. Preservation and maintenance

The pledgor can enforce the preservation and proper maintenance of the goods pledged.

3. Protection of debtors

The pledgor as a debtor has various rights given to him by statutes enacted for the protection of debtors *e.g.*, the Moneylenders Acts.

EXERCISES

1. Define bailment. State the degree of care to be taken by a bailee. What are the duties of the bailee ? (Pages 161-165)
2. What is a pledge ? What are the rights of a pawnee ? (Pages 170-172)
3. Can a person other than the true owner make a valid pledge of goods ? (Page 170)

4. Define bailment. State the rights and liabilities of a finder of goods. (Pages 161, 168-169)
5. Explain 'Bailment'. What are the rights of the parties in case of accretion during the period of bailment? (Pages 161, 165)
6. State the pawnee's rights when the pawnor makes default. (Pages 171-172)
7. Write notes on the following :
   (*a*) Mixture of bailor's goods with the bailee's. (Page 163)
   (*b*) Negligence of servants. (Para 2, page 163)
   (*c*) Liabilities of Hotel-keepers. (Para 7, page 165)
   (*d*) Right of Retainer. (Para 1 & 2, page 171)
8. Distinguish between :
   (*i*) Bailor and Bailee. (Page 161)
   (*ii*) Finders of goods and Bailee. (Pages 161, 168)
   (*iii*) Bailment and Pledge. (Page 170)
   (*iv*) Bailee's Particular Lien and Bailee's General Lien. (Pages 166-167)
9. Objective questions. Give short answers :
   (*i*) "A deposit of money in a bank is not bailment." True or false ? (Para 6, page 161)
   (*ii*) "A bailee has a duty to return the goods bailed." True or false ? (Para 5, page 164)
   (*iii*) Give three examples of termination of bailment. (Page 168)
   (*iv*) What is 'Pawn' ? (Page 170)
10. Problems :
   (*a*) *A* lends his horse to *B* for his own riding only. *B* allows *C*, a member of his family to ride the horse. *C* rides with care, but the horse accidentally fails and is injured. What remedy has *A* against *B* ? (Example (*i*), page 163)
   (*b*) *A* hires a motor car of *B*. The car is unsafe, though *B* is not aware of it, and *A* is injured. Is *B* responsible to *A* for the injury ? (Example (*ii*), page 165)
   (*c*) *A* kept some valuable ornaments in the custody of *B*, his neighbour, *B* kept *A*'s ornaments along with his own. *A*'s ornaments as well as *B*'s ornaments were lost on account of carelessness of *B*. Can *A* hold *B* responsible for his loss ? (Para 1, page 162)
   (*d*) *A* leaves a cow in the custody of *B* to be taken care of. The cow has given birth to a calf. Who is entitled to the calf ? (Para 6, page 165)

15 LAW OF AGENCY

DEFINITIONS

Definition and Nature of Agency

"An 'Agent' is a person employed to do any act for another or to represent another in dealings with third persons."—Sec.182.

The person for whom such act is done, or who is so represented, is called the *Principal*. *P* appoints *X* to buy 50 bales of cotton on his behalf. *P* is the principal and *X* is his *Agent*. The relationship between *P* and *X* is called *Agency*.

Power of Attorney

An Agent may be appointed by the Principal, executing a written and stamped document. Such a document is called Power of Attorney. There are two kinds of Power of Attorney : General and Special. A general power is one by which the agent is given an authority to do certain general objectives, e.g., managing an estate or a business. A special or particular power may be appointed by which an agent is authorised to do a specific thing, e.g., selling some goods. A man dealing with a particular agent is bound to find out the limits of the authority by which the authority of the agent can act accordingly.

Enforcement and consequences of Agent's contracts

The function of an agent is to bring about contractual relations between the principal and third parties. Usually agents are appointed with specific instructions and authorised to act within the scope of their instructions. Acts of the agent within the scope of the instructions bind the principal as if he has done them himself. There is a legal maxim regarding agency *viz*., *'Quit facit per alium facit per se'*, which means—"He who does through another does by himself." The act of an agent is the act of the principal.

"Contracts entered into through an agent, and obligations arising from acts done by an agent, may be enforced in the same manner and will have the same legal consequences, as if the

contracts had been entered into and the acts done by the principal in person."—Sec. 226.

Examples :

(*a*) *A* buys goods from *B*, knowing that he is an agent for their sale, but not knowing who is the principal. *B*'s principal is the person entitled to claim from *A* the price of the goods, and *A* cannot in a suit by the principal, set off against the claim a debt due to himself from *B*.

(*b*) *A*, being *B*'s agent with authority to receive money on his behalf, receives from *C* a sum of money due to *B*. *B* is discharged of his obligation to pay the sum in question to *B*.

The Test of Agency

Agency exists whenever a person can bind another by acts done on his behalf. When this power does not exist the relationship is not one of agency. Thus a wife is not the agent of the husband except under special circumstances and for special purposes. But the constituted attorney of a person is his agent for the purposes mentioned in the power of attorney.

Agent and Servant

The differences between an Agent and a Servant were discussed in the case *Lakhminarayan Ram Gopal & Sons* v. *Hyderabad Government.*[1] The points are summarised below.

1. An agent is to exercise his authority in accordance with the principal's instructions ; but he is not subject to the principal's direct control or supervision. A servant has to act according to the orders of the master in every particular.

2. An agent is appointed and employed to bring the principal into contractual relationship with third parties. The servant cannot do that.

3. An agent can bind the principal to the third parties. A servant cannot do so.

4. The mode of remuneration of an agent may vary, including a commission on the basis of the work done. A servant is generally paid through wages.

5. An agent is liable for wrong done within the scope of his authority. A master is liable for the wrong of his servant if it is committed in course of the servant's employment.

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[1] AIR (1954) Supreme Court 364

6. An agent may work for several principals. A whole-time servant serves only one master.

7. A servant can, however, be appointed as an agent for some purposes.

Agent and an Independent Contractor

A person who undertakes to do something for another is called an independent contractor, if the manner of doing the thing is left to him. An independent contractor does not represent the other contracting party nor can he bind him by contracts entered into with others. An agent is one who acts according to the instructions of the principal and can bind the principal by entering into contracts with other persons within the scope of his authority.

Agent and Bailee

The differences between an Agent and a Bailee are summarised below.

1. The bailee has possession of goods of the bailor. An agent may not have possession of any goods or property of the principal.

2. The bailee has no power to create any contractual relationship with the third party. An Agent has that authority.

3. Under certain circumstances a bailee may act as an agent.

Who can appoint an Agent ?

"Any person who is of the age of majority according to the law to which he is subject, and who is of sound mind, may employ an agent."—Sec. 183.

Who may be an Agent ?

Any person may be an agent, even a minor. A minor acting as agent can bind the principal to third parties. But a minor is not himself liable to his principal.—Sec. 184.

Joint Principals

Several principals can jointly appoint *one* agent. The agent can act in respect of those affairs in which all the co-principals are jointly interested. The Power of Attorney, by virtue of which the agent was created, has to be strictly construed and what it authorized depend on the terms and the purposes for which it

was executed. *Syed Abdul Khader* v. *Rami Reddy and others.*[1] The Supreme Court in the judgment quoted Halsbury, "co-principals may jointly appoint an agent to act for them and in such case become jointly liable to him and may jointly sue him."[2]

Consideration in Agency Contracts

No consideration is necessary to create an agency (Sec. 185). The acceptance of the office of an agent is regarded as sufficient consideration for the appointment. The agency contract generally provides for the amount of remuneration payable by the principal to the agent.

DIFFERENT CLASSES OF AGENTS

The relationship between the principal and agent and the extent of the authority of the latter are matters to be determined by agreement of the parties.

There are, however, certain well-known varieties of agency contracts where the powers and duties of the agent are settled by usage and custom of trade recognised by the courts of law. Some of these particular kinds of agency-contracts, together with their legal incidents are described below.

1. Broker

A broker is one who brings buyers and sellers into contract with one another. His duties are at an end when the parties are brought together. The contract of sale and purchase is entered into directly by the parties. The broker does not keep the goods or the property of the principal in his possession.

2. Factor

A factor is a mercantile agent with whom goods are kept for sale. He has got discretionary powers to enter into contracts of sale with third parties. He has a general lien on the goods for money due to him as agent.

3. A Commission Agent

A commission agent is one who secures buyers for a seller of goods and sellers for a buyer of goods in return for a

[1] AIR (1979) Supreme Court 553

[2] Halsbury's Laws of England, vol I, 4th Ed., para 726

commission on the sale. A commission agent may have possession of the goods or not. His position is very similar to that of a broker.

4. Auctioneer

An auctioneer is one who is authorised to sell goods of his principal by auction. He has a particular lien on the goods for his remuneration. He has the goods in his possession and can sue the buyer in his own name for the purchase price. An auctioneer acts in a double capacity. Up to the moment of sale he is the agent of the seller. After the sale he is the agent of the buyer. An auctioneer has implied authority to sell the goods without any restriction. Therefore a sale by him in violation of instructions is binding on the owner. If the owner directs the auctioneer not to sell below a reserve price and the auctioneer sells it below the price the sale is binding on the owner except in cases where the buyer knew that there was a limitation on the auctioneer's authority.

5. A Del Credere Agent

A del credere agent is one who, for extra remuneration, guarantees the performance of the contract by the other party. If the other party fails to pay the price or otherwise causes damage to the principal, the *del credere* agent must pay compensation to the principal.

6. General Agent and Particular Agent

A general agent is one who represents the principal in all matters concerning a particular business. A particular agent is one who is appointed for a specific purpose *e.g.*, to sell a particular article. Factors and commission agents are usually general agents.

METHODS OF CREATING AGENCY

Agency may be created in any one of the following ways:

1. Agency by Express Agreement

A contract of agency may be created by express agreement. The agreement may be either oral or written. It is usual in many cases to appoint agents by executing a formal power of attorney on a written and stamped document.

2. Agency by Implied Agreement

An agency agreement may be implied under certain circumstances from the conduct of the parties or the relationship between them. Agency by estoppel and agency of necessity are cases of implied agency.

3. Agency by Estoppel or by Holding Out

Agency may be created by estoppel. When a man has by his conduct or statements induced others to believe that a certain person is his agent, he is precluded from subsequently denying it. Thus an agency is created by implication of law.

Examples :

(*i*) *Y* allows his servant *X* to buy goods for him on credit regularly. On one occasion the servant buys some goods not ordered by his master, on credit. *Y* is responsible to the shopkeeper for the price because *X* will be deemed to be his agent by estoppel.

(*ii*) *P* employed *X* a broker, to buy hemp for him and at *P*'s request it was kept in a warehouse in *X*'s name. *X* without *P*'s authority sold the hemp. Held, *P* was bound by the sale because he had allowed *X* to assume the apparent right of disposing of the hemp in the ordinary course of business. *Pickering* v. *Bush*.[1]

There are three possible cases of agency by estoppel :

(*a*) A person can be held out as an agent although he is actually not so—*Example* (*i*) above.

(*b*) A person acting as an agent may be held out as having more authority than he actually has—*Example* (*ii*) above.

(*c*) A person may be held out as agent after he has ceased to be so.

Section 237 provides as follows : "When an agent has, without authority, done acts or incurred obligations to third persons on behalf of his principal, the principal is bound by such acts or obligations if he has by his words or conduct induced such third persons to believe that such acts or obligations were within the scope of the agent's authority."

Examples :

(*a*) *A* consigns goods to *B* for sale and gives him instructions not to sell under a fixed price. *C*, being ignorant of *B*'s instructions, enters into a contract with *B* to buy the goods at a price lower than the reserved price. *A* is bound by the contract.

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[1] (1812) 15 East 38

(*b*) *A* entrusts *B* with negotiable instruments endorsed in blank. *B* sells them to *C* in violation of private orders from *A*. The sale is goods.

4. Agency of Necessity

Circumstances sometimes force a person to act on behalf of another without any express authority from him. In such cases an agency of necessity is said to be created.

Three conditions must be satisfied before an agency can be created by necessity: (*a*) It must be impossible to get the principal's instructions. (*b*) There must be an actual necessity for acting on his behalf. *(c)* The agent of necessity must act honestly in the interest of the parties concerned.

Examples :

(*i*) The captain of a ship finds himself in a distant port without money. The owner cannot be communicated with. The captain can pledge the ship for obtaining money. He will be considered the agent of the owner by necessity.

(*ii*) *A* horse, sent by a train, arrived at a station with nobody to receive it. The railway company fed the horse. Held, the railway company was an agent of necessity and was entitled to recover the money from the owner. *G N. Ry* v. *Swaffield*.[1]

Husband and Wife

A wife is an agent of necessity, having power to pledge her husband's credit for necessaries of life, when she is not properly provided for by him or when she has been deserted by the husband. But if the husband gives her a sufficient allowance, she has no authority to pledge his credit and can never be the agent of necessity. In *Gray (Miss) Ltd.* v. *Cathcart*[2] a wife was supplied with clothes of the value of £ 215 by a shopkeeper. The shopkeeper sued the husband. It was found that the husband was giving the wife an allowance of £ 960 per year. It was held that the husband was not liable to pay the dues of the shopkeeper.

The general rule is that the wife is not the agent of her husband and the husband is not the agent of his wife. But one of them may be the agent of the other by express appointment, by holding out, by ratification, or because of necessity.

5. Agency by Ratification

Ratification means the subsequent adoption and acceptance

[1] (1874) L. R. 9 Ex. 132 [2] (1922) 38 T.L.R. 562

of an act originally done without instructions or authority. *P* buys ten maunds of wheat on behalf of *Q*. *Q* did not appoint *P* as his agent and did not instruct him to buy wheat for him. *Q* may, upon hearing of the transaction, accept it. If he does so, the act is ratified and *P* becomes his agent with retrospective effect.

Effect of ratification : "Where acts are done by one person on behalf of another, but without his knowledge or autl ority, he may elect to ratify or to disown such acts. If he ratifies them, the same effects will follow as if they had been performed by his authority."—Sec. 196.

Ratification may be express or implied, *i.e.*, it may be by express words or by conduct.—Sec. 197.

Examples of implied ratification :

(*i*) *D*, without authority, buys goods for *B*. Afterwards *B* sells them to *C* on his own account. *B*'s conduct implies a ratification of the purchase made by *D* for him.

(*ii*) *D*, without *B*'s authority lends *B*'s money to *C*. Afterwards *B* accepts interest on the money from *C*. *B*'s conduct implies a ratification of the loan.

Ratification when validly made is retrospective in operation, *i.e.*, it relates back and dates from the time when the agent entered into the contract.

Conditions : To be valid, a ratification must fulfil the following conditions :

1. The agent must expressly contract as agent. A man cannot enter into a contract in his own name and later shift it on to a third party.
2. The act to be ratified must be a lawful one. There can be no ratification of an illegal act or an act which is void.
3. Ratification must be made within a reasonable time.
4. No valid ratification can be made by a person whose knowledge of the facts of the case is materially defective.—Sec. 198.
5. Ratification must be of the whole contract. There cannot be partial ratification and partial rejection.—Sec. 199.
6. For valid ratification, the agent must have a principal who is in actual existence at the time of the contract. *Example*—a company cannot ratify a contract entered into by a promoter on its behalf before the company came into existence by incorporation.

7. The principal must have contractual capacity at the date of the contract and at the date of the ratification.
8. Ratification is not valid where the effect of ratification is to subject a third person to damages or of terminating any right or interest of a third person.—Sec. 200.

Examples :

(*i*) *A*, not being authorised thereto by *B*, demands on behalf of *B*, the delivery of a chattel, the property of *B*, from *C* who is in possession of it. This demand cannot be ratified by *B*, so as to make *C* liable for damages for his refusal to deliver.

(*ii*) *A* holds a lease from *B*, terminable on three months' notice. *C*, an unauthorised person, gives notice of termination to *A*. The notice cannot be ratified by *B*, so as to be binding on *A*.

AGENT'S AUTHORITY

Express and implied authority

"The authority of an agent may be expressed or implied."—Sec.186.

The authority is said to be express when it is given by words spoken or written. The authority is said to be implied when it is to be inferred from the circumstances of the case. The inference as to implied authority, may be drawn from things spoken or written, or the ordinary course of dealing between the parties and others.—Sec. 187.

Example :

A owns a shop in Serampur, living himself in Calcutta, and visiting the shop occasionally. The shop is managed by *B*, and he is in the habit of ordering goods from *C* in the name of *A* for the purposes of the shop, and of paying for them out of *A*'s funds with *A*'s knowledge, *B* has an implied authority from *A* to order goods from *C* in the name of *A* for the purposes of the shop.

Extent of agent's authority

"An agent having an authority to do an act has authority to do every lawful thing which is necessary in order to do such act.

An agent having an authority to carry on a business has authority to do every lawful thing necessary for the purpose, or usually done in the course of conducting such business."—Sec. 188.

Examples :

(*a*) *A* is employed by *B*, residing in London, to recover at Bombay a debt due to *B*. *A* may adopt any legal process necessary for the purpose of recovering the debt and may give a valid discharge for the same.

(*b*) *A* constitutes *B* his agent to carry on his business of a ship-builder. *B* may purchase timber and other materials, and hire workmen, for the purpose of carrying on the business.

Authority in an emergency

"An agent has authority, in an emergency to do all such acts for the purpose of protecting his principal from loss as would be done by a person of ordinary prudence, in his own case, under similar circumstances."—Sec. 189.

Examples :

(*a*) An agent for sale may have goods repaired if it be necessary.

(*b*) *A* consigns provisions to *B* at Calcutta with directions to send them immediately to *C* at Cuttack. *B* may sell the provisions at Calcutta, if they will not bear the journey to Cuttack without spoiling.

What happens when the agent exceeds his authority ?

When the authority is separable : "When an agent does more than he is authorized to do, and when the part of what he does, which is within his authority, can be separated from the part which is beyond his authority, so much only of what he does as is within his authority, is binding as between him and his principal."—Sec. 227.

Example :

A, being owner of a ship and cargo, authorizes *B* to procure an insurance for 4,000 rupees on the ship. *B* procures a policy for 4,000 rupees on the ship, and another for the like sum on the cargo. *A* is bound to pay the premium for the policy on the ship, but not the premium for the policy on the cargo.

When the authority cannot be separated : "Where an agent does more than he is authorized to do and what he does beyond the scope of his authority cannot be separated from what is within it, the principal is not bound to recognize the transaction."—Sec. 228.

Example :

A, authorizes *B* to buy 500 sheep for him. *B* buys 500 sheep and 200 lambs for one sum of 6,000 rupees. *A* may repudiate the whole transaction.

When the principal is bound by unauthorized acts of agent. The principal may be bound by unauthorized acts of the agent in two cases : (*i*) Where by the rule of estoppel the principal is precluded from denying the authority of the agent. (See cases cited under "Agency by Estoppel", p. 179.) (*ii*) Where an agency has been terminated, but notice of termination has not been received by the other parties concerned (See pp. 188-189)

Effects of notice to agent or information obtained by agent

Any notice given to or information obtained by the agent (provided it be given or obtained in the course of the business transacted by him for the principal) shall have the same legal consequences as if it has been given to or obtained by the principal.—Sec. 229.

Examples :

(*a*) *A* is employed by *B* to buy from *C* certain goods of which *C* is the apparent owner, and buys them accordingly. In the course of the treaty for the sale, *A* learns that the goods really belonged to *D*, but *B* is ignorant of that fact. *B* is not entitled to set-off a debt owing to him from *C* against the price of the goods.

(*b*) *A* is employed by *B* to buy from *C* goods of which *C* is the apparent owner, *A*, was before he was so employed, a servant of *C* and then learnt that the goods really belonged to *D*, but *B* is ignorant of that fact. In spite of the knowledge of his agent, *B* may set-off against the price of the goods a debt owing to him from *C*.

Representation as to Liability

When a person who has made a contract with an agent induces the agent to act upon the belief that the principal only will be held liable, he cannot subsequently hold the agent liable on the contract. Similarly if a person induces the principal to act on the belief that the agent only will be held liable, he cannot afterwards hold the principal liable on the contract.—Sec. 234.

Pretended Agents

A person untruly representing himself to be the authorized agent of another, and thereby inducing a third person to deal with him as such agent, is liable, if his alleged employer does not ratify his acts, to make compensation to the other in respect of any loss or damage which he had incurred by so dealing.—Sec. 235.

A pretended agent has no authority to act as agent. When the other party to the contract suffers damage as a result of such want of authority, he can sue the agent for breach of warranty of authority. The pretended agent is liable to pay damages under the Law of Torts. The liability arises even when the agent acted innocently.

Example :

A firm of solicitors were instructed by a client to defend a suit. Subsequently the client became insane (and the solicitors' authority as agent terminated by law). The solicitors in ignorance of the fact took steps to defend the suits. Held, the solicitors were personally liable for the cost of the other side, as on a breach of warranty of authority. *Yonge* v. *Toynbee*.[1]

A person with whom a contract has been entered into in the character of agent, is not entitled to require the performance of it if he was in reality acting, not as agent, but on his own account.—Sec. 236.

Misrepresentation and Fraud by Agents

Misrepresentations made, or frauds committed, by agents acting in the course of their business for their principals, have the same effect on agreements made by such agents as if such misrepresentations or frauds had been made or committed by the principals.

But misrepresentations made, or frauds committed, by agents, in matters which do not fall within their authority, do not affect their principals.—Sec. 238.

Examples :

(*i*) *A*, being *B*'s agent for the sale of goods, induces *C* to buy them by a misrepresentation, which he was not authorised by *B* to make. The contract is voidable, as between *B* and *C*, at the option of *C*.

(*ii*) *A*, the captain of *B*'s ship, signs bills of lading without having received on board the goods mentioned therein. The bills of lading are void as between *B* and the pretended consignor.

(*iii*) A solicitor's managing clerk had authority to transact conveyancing business on behalf of his employer. He induced a client, who was an old lady, to sign a conveyance of her properties to himself. With the help of the document the clerk sold the properties to another and decamped with the proceeds. Held, that as the clerk was acting in course of the business of the solicitor, the solicitor must make good the loss of the lady. *Lloyd* v. *Grace Smith & Co.*[2]

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[1] (1910) 1 K.B. 215 [2] (1912) A.C. 716

SUB-AGENT AND CO-AGENT

Rule

The general rule is that an agent cannot appoint an agent. (*"Delegatus non potest delegare."*) "An agent cannot lawfully employ another to perform acts which he has expressly or impliedly undertaken to perform personally."—Sec. 190.

Exceptions

But there are two exceptions to this rule. An agent can appoint an agent (*i*) when it is permitted by the custom of the trade with which the agency is concerned ; and (*ii*) when it is necessary because of the nature of the agency.

Sub-agent

An agent appointed by an agent is called a sub-agent. "A sub-agent is a person employed by, and acting under the control of, the original agent in the business of the agency."—Sec. 191.

The consequences of the appointment of a sub-agent are stated below :

1. A sub-agent is appointed by and acts under the control of the original agent.—Sec. 191.
2. The principal is represented by the sub-agent and is bound by and responsible for his acts as if he was an agent appointed by the principal.—Sec. 192.
3. The agent is responsible to the principal for the acts of the sub-agent.—Sec. 192.
4. The sub-agent is responsible for his acts to the agent. The sub-agent is not responsible to the principal except in case of fraud and wilful wrong.—Sec. 192.
5. Where an agent improperly appoints a sub-agent, the agent is responsible for his acts both to the principal and to third parties. The principal in such cases is not represented by the sub-agent nor is he responsible for the acts of the sub-agent.—Sec. 193.

Co-agent

A co-agent is a person appointed by the agent according to the express or implied authority of the principal, to act *on behalf of the principal* in the business of the agency.—Sec. 194.

Such a person is an agent of the principal and is responsible to him. A co-agent is sometimes called a Substituted Agent.

In case of a co-agent there is direct privity of contract between the principal and the co-agent. There is no direct privity of contract between the principal and the sub-agent, except in cases of fraud and wilful wrong-doing.

Examples :

(*i*) *A* directs *B*, his solicitor, to sell his estate by auction, and to employ an auctioneer for the purpose. *B* names *C*, an auctioneer, to conduct the sale. *C* is not a sub-agent, but is *A*'s agent for the conduct of the sale.

(*ii*) *A* authorizes *B* a merchant in Calcutta to recover the moneys due to *A* from *C & Co.* *B* instructs *D* a solicitor, to take legal proceedings against *C & Co.* for the recovery of the money. *D* is not a sub-agent but is solicitor for *A*.

An agent in appointing a co-agent must exercise the same amount of discretion as a man of ordinary prudence would exercise in his own case. If he does this he is not responsible to the principal for acts of negligence of the co-agent.—Sec. 195.

Examples :

(*i*) *A* instructs *B*, a merchant, to buy a ship for him. *B* employs a ship surveyor of good reputation to choose a ship for *A*. The surveyor makes the choice negligently and the ship turns out to be unseaworthy and is lost. *B* is not, but the surveyor is, responsible to *A*.

(*ii*) *A* consigns goods to *B*, a merchant for sale. *B* in due course, employs an auctioneer in good credit to sell the goods of *A* and allows the auctioneer to receive the proceeds of the sale. The auctioneer afterwards becomes insolvent without having accounted for the proceeds. *B* is not responsible to *A* for the proceeds.

TERMINATION OF AGENCY

An agency may be terminated by *act of parties or by operation of law.* The different possible circumstances leading to the termination of agency are enumerated below.—Sections 201-210.

Termination by act of parties

Revocation and Renunciation : The principal may, by notice, revoke the authority of the agent. The agent may similarly, by notice, renounce the business of agency.

Revocation and renunciation can be express or may be implied from the conduct of the parties.

Example :

A empowers *B* to let *A*'s house. Afterwards *A* lets it himself. There is an implied revocation of *B*'s authority.

Compensation for revocation or renunciation : Where there is an express or implied agreement to continue the agency for any length of time, and the contract of agency is revoked or renounced without sufficient cause, compensation must be paid to the injured party.—Sec. 205.

Irrevocable agency : The principal cannot revoke the authority of the agent in the following cases :

1. When the agent has an interest in the subject-matter of the contract, his authority cannot be revoked so as to prejudice that interest. This is known as *agency coupled with interest.*—Sec. 202.

Examples :

(*i*) *A* gives authority to *B* to sell *A*'s land to pay himself out of the proceeds, the debts due to him from *A*. *A* cannot revoke this authority, nor can it be terminated by his insanity or death.

(*ii*) *A* consigns 1000 bales of cotton to *B*, who has made advances to him on such cotton, and desires *B* to sell the cotton, and to repay himself out of the price, the amount of his own advances. *A* cannot revoke this authority, not is it terminated by his insanity or death.

2. The authority of the agent cannot be revoked once it has been exercised so as to bind the principal.

3. When the agent has partially exercised his authority, the principal cannot by revocation affect the acts already done.

II. Termination by operation of Law

An agency may terminate by operation of law in any of the following ways :

1. *Efflux of time* : When the agency is for a fixed period of time, it terminates on the expiry of that time.

2. *Performance of the object* : Where the agency is for a particular object, it terminates when the object is accomplished or when the accomplishment becomes impossible.

3. *Determination of subject-matter.* When the subject-matter of the agency comes to an end, the agency terminates.

4. *Death or insanity of the principal or agent* : Death or insanity of the principal or the agent, terminates the agency. In case of a company, its winding up and in case of a firm, its dissolution has the same effect.

5. *Insolvency of the principal* : If the principal is adjudicated an insolvent, the agency terminates. But insolvency of the agent does not terminate the agency.

6. *The principal becoming an alien enemy* : If the principal and the agent belong to different countries and war breaks out between the two countries, the contract of agency is terminated.

7. *Termination of the sub-agent's authority* : The sub-agent's authority comes to an end when the agent's authority terminates.

When termination of agent's authority takes effect

The termination of the authority of an agent takes effect, as regards the agent from the time it becomes known to him. As regards third parties it becomes effective when it becomes known to them.—Sec. 208.

Examples :

(*i*) *A* directs *B* to sell goods for him, and agrees to give *B* five per cent commission on the price fetched by the goods. *A* afterwards, by letter, revokes *B*'s authority, *B* after the letter is sent, but before he receives it, sells the goods for 100 rupees. The sale is binding on *A*, and *B* is entitled to five rupees as his commission.

(*ii*) *A*, at Madras, by letter directs *B* to sell for him some cotton lying in a warehouse in Bombay, and afterwards by letter, revokes his authority to sell, and directs *B* to send the cotton to Madras. *B*, after receiving the second letter enters into a contract with *C*, who knows of the first letter, but not of the second, for the sale to him of the cotton. *C* pays *B* the money, with which *B* absconds. *B*'s payment is good as against *A*.

(*iii*) *A* directs *B*, his agent, to pay certain money to *B*. *A* dies and *D* takes out probate to his will. *B* after *A*'s death but before hearing of it, pays the money to *C*. The payment is good as against *D*, the executor.

AGENT'S DUTIES TO PRINCIPALS

1. *Agent's duty in conducting principal's business* : An agent is bound to conduct the business of his principal according to the directions given by the principal, or, in the absence of any such directions, according to the custom which prevails in doing business of the same kind at the place where the agent conducts such business. When the agent acts otherwise, if any loss be sustained he must make it goods to his principal, and, if any profit accrues, he must account for it.—Sec. 211.

Examples :

(*a*) *A*, an agent engaged in carrying on for *B* a business, in which it is the custom to invest from time to time, at interest, the moneys which may be in hand, omits to make such investment. *A* must make good to *B* the interest usually obtained by such investments.

(*b*) *B*, a broker, in whose business it is not the custom to sell on credit, sells goods of *A* on credit to *C*, whose credit at the time was very high. *C*, before payment, becomes insolvent. *B* must make good the loss to *A*.

2. *Skill and diligence required from agent* : An agent is bound to conduct the business of the agency with as much skill as is generally possessed by persons engaged in similar business unless the principal has notice of his want of skill.

The agent is always bound to act with reasonable diligence, and to use such skill as he possesses ; and to make compensation to his principal in respect of the direct consequences of his own neglect, want of skill or misconduct, but not in respect of loss or damages which are indirectly or remotely caused by such neglect, want of skill, or misconduct.—Sec. 212.

Examples :

(*a*) *A*, a merchant in Calcutta, has an agent *B*, in London to whom a sum of money is paid on *A*'s account, with orders to remit. *B* retains the money for a considerable time. *A*, in consequence of not receiving, the money, becomes insolvent. *B* is liable for the money and interest from the day on which it ought to have been paid according to the usual rate, and for any further direct loss.—as *e.g.*, by variation of rate of exchange—but not further.

(*b*) *A*, an agent for the sale of goods, having authority to sell on credit, sells to *B* on credit, without making the proper and usual enquiries as to the solvency of *B*. *B*, at the time of such sale, is insolvent. *A* must make compensation to his principal in respect of any loss thereby sustained.

(*c*) *A*, an insurance broker, employed by *B* to effect an insurance on a ship, omits to see that the usual clauses are inserted in the policy. The ship is afterwards lost. In consequence of the omission of the clauses nothing can be recovered from the underwriters. *A* is bound to make good the loss to *B*.

(*d*) *A*, a merchant in England, directs *B*, his agent at Bombay, who accepts the agency, to send him 100 bales of cotton by a certain ship. *B* having it in his power to send the cotton, omits to do so. The ship arrives safely in England. Soon after her arrival the price of cotton rises. *B* is bound to make good to *A* the profit which he might have made by the 100 bales of cotton at the time the ship arrived, but not any profit he might have made by the subsequent rise.

(*e*) *K* employed *W* to sell a house. On 29th May *W* received an offer of £6,150 from *E* and communicated it to *K* who directed him to accept it "subject to contract". On 3rd June *D* offered £6,750 but this offer was not communicated to *K*. On 8th June a written contract was entered into between *K* and *E*. *K* sued *W* for breach of duty in not communicating *D*'s offer. Held, there was breach of duty and *W* was directed to pay to *K* the difference between the two prices. *Keppel* v. *Wheeler*.[1]

3. *Agent's duty to render accounts* : An agent is bound to render proper accounts to his principal on demand, or periodically if so provided in the agreement.—Sec. 213.

4. *Agent's duty to communicate to principal* : It is the duty of an agent, in cases of difficulty, to use all reasonable diligence in communicating with his principal, and in seeking to obtain his instructions.—Sec. 214.

5. *Agent not to deal on his own account* : If an agent deals on his own account in the business of the agency, without first obtaining the consent of his principal and acquainting him with all material circumstances which have come to his own knowledge on the subject, the principal may repudiate the transaction, if the case shows either that any material fact has been dishonestly concealed from him by the agent, or that the dealings of the agent have been disadvantageous to him.—Sec. 215. The agent has a duty to avoid conflict of interest between the agent and the principal.

Examples :

(*a*) *A* directs *B* to sell *A*'s estate. *B* buys the estate for himself in the name of *C*. *A*, on discovering that *B* has brought the estate for himself, may repudiate the sale, if he can show that *B* has dishonestly concealed any material fact, or that the sale has been disadvantageous to him.

(*b*) *A* directs *B* to sell *A*'s estate. *B*, on looking over the estate before selling it, finds a mine on the estate which is unknown to *A*. *B* informs *A* that he wishes to buy the estate for himself; but conceals the discovery of the mine. *A* allows *B* to buy, in ignorance of the existence of mine. *A*, on discovering that *B* knew of the mine at the time he bought the estate, may either repudiate or adopt the sale at his option.

6. *Principal to get benefit of agent's dealings* : If an agent, without the knowledge of his principal, deals in the business of the agency on his own account, instead of on account of his

[1] (1927) 1 K.B. 577

principal, the principal is entitled to claim from the agent any benefit which may have resulted to him from the transaction.—Sec. 216. The agent has a duty not to make secret profits.

Example :

A directs *B*, his agent, to buy a certain house for him. *B* tells *A* it cannot be brought, and buys the house for himself. *A* may, on discovering that *B* has brought the house, compel him to sell it to *A* at the price he gave for it.

Agent's duty to pay sums received for principal : The agent is bound to pay to his principal all sums received on his account after deducting therefrom his dues on account of remuneration and expenses.—Sec. 218.

8. *Principal's death or insanity* : When an agency is terminated by the principal dying or becoming of unsound mind, the agent is bound to take on behalf of the representatives of his late principal, all reasonable steps for the protection and preservation of the interests entrusted to him.—Sec. 209.

9. *Miscellaneous* : The Agent has other duties also. The agent must give all information to the principal. He must not delegate his authority. He must avoid the clash between his duty and self-interest. He should be loyal to the principal. He must not set up an adverse title against the principal. He is not entitled to remuneration in certain circumstances.

PRINCIPAL'S DUTIES TO AGENT

1. *Agent to be indemnified against consequences of lawful acts* : The principal is bound to indemnify the agent against the consequences of all lawful acts done by such agent in exercise of the authority conferred upon him.—Sec. 222.

Examples :

(*a*) *B*, at Singapore, under instructions from *A* of Calcutta contracts with *C* to deliver certain goods to him. *A* does not send the goods to *B*, and *C* sues *B* for breach of contract. *B* informs *A* of the suit, and *A* authorised him to defend the suit. *B* defends the suit, and is compelled to pay damages and costs, and incurs expenses. *A* is liable to *B* for such damages, costs and expenses.

(*b*) *B*, a broker at Calcutta, by the orders of *A*, a merchant there contracts with *C* for the purchase of 10 casks of oil for *A*. Afterwards *A* refuses to receive the oil, and *C* sues *B*. *B* informs *A*, who repudiates the contract altogether. *B*, defends, but unsuccessfully, and has to pay damages and costs and expenses. *A* is liable to *B* for such damages, costs and expenses.

2. *Agent to be indemnified against consequences of acts done in good faith* : Where one person employs another to do an act, and the agent does the act in good faith, the employer is liable to indemnify the agent against the consequences of that act, though it causes an injury to the rights of third persons.—Sec. 223.

Examples :

(*a*) *A*, a decree-holder and entitled to execution of *B*'s goods, requires the officer of the Court to seize certain goods, representing them to be the goods of *B*. The officer seizes the goods and is used by *C*, the true owner of the goods. *A* is liable to indemnify the officer for the sum which he is compelled to pay to *C*, in consequence of obeying *A*'s directions.

(*b*) *B*, at the request of *A*, sells goods in the possession of *A*, but which *A* had not right to dispose of. *B* does not know this and hands over the proceeds of the sale to *A*. Afterwards *C*, the true owner of the goods, sues *B* and recovers the value of the goods and costs. *A* is liable to indemnify *B* for what he has been compelled to pay to *C* and for *B*'s own expenses.

3. *Non-liability for criminal acts* : But where one person employs another to do an act which is *criminal*, the employer is not liable to the agent, either upon an express or an implied promise, to indemnify him against the consequences of that act.—Sec. 224.

Examples :

(*a*) *A* employs *B* to beat *C*, and agrees to indemnify him against all consequences of the act. *B* thereupon beats *C*, and has to pay damages to *C* for so doing. *A* is not liable to indemnify *B* for those damages.

(*b*) *B*, the proprietor of a newspaper publishes, at *A*'s request, a liable upon *C* in the paper, and *A* agrees to indemnify *B* against the consequences of the publication, and all costs and damages of any action in respect thereof. *B* is sued by *C* and has to pay damages, and also incurs expenses. *A* is not liable to *B* upon the indemnity.

4. *Compensation for principal's neglect* : The principal must make compensation to his agent in respect of injury caused to such agent by the principal's neglect or want of skill.—Sec. 225.

Example :

A employs *B* as a bricklayer in building a house and puts up the scaffolding himself. The scaffolding is unskilfully put up and *B* is in consequence hurt. *A* must make compensation to *B*.

PRINCIPAL'S RIGHTS

1. *Compensation* : The principal is entitled to compensation for any breach of duty by the agent.

2. *Agent's duties* : The agent's duties are the principal's rights.

3. *Revocation* : The principal can revoke the agent's authority, subject to certain conditions.

AGENT'S RIGHTS

1. *Enforcement of rights* : The agent can enforce all the duties of the principal. The principal's duties are the agent's rights.

2. *Agent's Right of Retainer* : An agent may retain, out of any sums received on account of the principal in the business of the agency, all moneys due to himself in respect of advances made or expenses properly incurred by him in conducting such business, and also such remuneration as may be payable to him for acting as agent.—Sec. 217.

3. *When agent's remuneration becomes due* : In the absence of any special contract, the agent's remuneration does not become due until he has completed the act for which he was appointed agent. But an agent may detain moneys received by him on account of goods sold, although the whole of the goods consigned to him for sale may have been sold, or although the sale may be actually complete.—Sec. 219.

4. *Agent not entitled to remuneration for business misconducted* : An agent who is guilty of misconduct in the business of the agency is not entitled to any remuneration in respect of that part of the business which he has misconducted.—Sec. 220.

Examples :

(*a*) *A* employs *B* to recover Rs. 100,000 and to lay it out on good security. *B* recovers, Rs. 100,000 and lays out Rs. 90,000 on good security but lays out Rs. 10,000 on bad security whereby *A* loses Rs. 2,000. *B* is entitled to remuneration for recovering Rs. 100,000 and for investing Rs 90,000. He is not entitled to any remuneration for investing Rs. 10,000 and must make good the loss of Rs. 2,000 to *A*.

(*b*) *A* employs *B* to recover Rs. 1,000 from *C*. Through *B's* misconduct the money is not recovered. *B* is entitled to no remuneration for his services, and must make good the loss.

5. *Agent's Lien* : In the absence of any contract to the contrary, an agent is entitled to retain goods, papers and other

property, whether movable or immovable of the principal, received by him, until the amount due to himself for commission, disbursements and services in respect of the same has been paid or accounted for to him.—Sec. 221.

PERSONAL RESPONSIBILITY OF AGENT

It is provided by Section 230 that, in the absence of any contract to that effect, an agent cannot personally enforce contracts entered into by him on behalf of his principal, nor is he personally bound by them.

But if there is an agreement to that effect, express or implied, the agent may enforce the contract and may also be *personally liable* on it. Such a contract *shall be presumed to exist* in the following cases :

1. *Foreign principal* : Where the contract is made by an agent for the sale or purchase of goods for a merchant resident abroad.
2. *Undisclosed principal* : Where the agent does not disclose the name of his principal.
3. *When principal cannot be sued* : Where the principal, though disclosed, cannot be sued (for example, if he is a foreign sovereign or a foreign State).

The agent is also personally responsible in the following cases :

4. *Fictitious person or a non-existent person* : If the principal does not exist. *Example* : When a promoter makes a contract for a company which has not yet been registered.
5. *Unauthorised Acts* : Agent acting beyond the principal's authority.—Secs. 227, 228. (p. 183)
6. *Misrepresentation or fraud by agent* : An agent is personally responsible if he makes misrepresentations or frauds acting in course of the business of the principal.—Sec. 238. (p. 185)
7. *Pretended agents* : A pretended agent does not have authority. When the other party to the contract suffers damage, he can sue the agent for breach of warranty of authority. The pretended agent is liable to pay damages under the Law of Torts. The liability arises even when the agent acted innocently.—Sec.235.

8. *Representation as to liability* : If a person induces the principal to act on the belief that the agent only will be held liable, he cannot afterwards hold the principal liable on the contract.—Sec. 234.

Right of person dealing with agent personally liable : In cases where the agent is personally liable, a person dealing with him may hold either him or his principal, or both of them liable.—Sec. 233.

CONTRACTS WITH AN UNDISCLOSED PRINCIPAL

An agent may enter into a contract with a person without disclosing the name of the principal. The legal consequences of contracts with undisclosed principal are as follows :

1. *Principal may require performance of the contract* : If an agent makes a contract with a person who neither knows, nor has reason to suspect, that he is an agent, his principal may require the performance of the contract. But the other contracting party has, as against the principal, the same right as he would have had as against the agent if the agent had been principal.—Sec. 231. (Para 1)

2. *Other party may refuse to fulfil the contract* : If the principal discloses himself before the contract is completed, the other contracting party may refuse to fulfil the contract, if he can show that, if he had known who was the principal in the contract, or if he had known that the agent was not a principal, he would not have entered into the contract.—Sec. 231. (Para 2)

3. *Performance is subject to the rights and obligations between agent and the other party* : Where one man makes a contract with another, neither knowing nor having reasonable ground to suspect that the other is an agent, the principal, if he requires the performance of the contract, can only obtain such performance subject to the rights and obligations subsisting between the agent and the other party to the contract.—Sec. 232.

Example :

A, who owes Rs. 500 to *B*, sells Rs. 1,000 worth of rice to *B*. *A* is acting as agent for *C* in the transaction, but *B* has no knowledge nor reasonable ground of suspicion that such is the case. *C* cannot compel *B* to take the rice without allowing him to set off *A*'s debt.

4. *Agent is personally liable*. In contracts with an undisclosed principal, the agent is, in the absence of a contract to the contrary, personally liable on the contract. The other party

may hold either the agent or the principal or both liable.—Sec. 233.

Example :

A enters into a contract with *B* to sell him 100 bales of cotton, and afterwards discovers that *B* was acting as agent for *C*. *A* may sue either *B* or *C*, or both, for the price of the cotton.

EXERCISES

1. In what ways an agency can be created ? (Pages 178-182)
2. What are the different ways an agency can be terminated ? (Pages 187-189)
3. When is a Principal bound by the unauthorised acts of his Agent? (Pages 182-183)
4. State the duties of the principal to his agent. (Pages 192-193)
5. State the duties of an agent to the principal. (Pages 189-192)
6. State the respective rights and duties of a principal and an agent, when the principal is undisclosed. (Pages 196-197)
7. Explain the instances when an agent can be made personally liable in respect of contracts entered into by him on behalf of the principal. (Pages 195-196)
8. Explain the following terms : (*a*) Principal (*b*) Agent (*c*) Power of Attorney (*d*) A Del Credere Agent (*e*) Sub-agent and Co-agent (*f*) Ratification (*g*) Agency of necessity. (Pages (*a*) 174, (*b*) 174, (*c*) 174, (*d*) 178, (*e*) 186, (*f*) 180, (*g*) 180)
9. Distinguish between :
   (*i*) Agent and Servant. (Page 175)
   (*ii*) Agent and Contractor. (Page 176)
   (*iii*) Agent and Bailee. (Page 176)
   (*iv*) Express authority and Implied authority of agent. (Page 182)
   (*v*) Sub-agent and Co-agent. (Page 186)
   (*vi*) Agent and Pretended agent. (Page 184)
10. Objective questions. Give short answers.
    (*i*) "An agent can be appointed orally." True or false ? (Page 178)
    (*ii*) State three varieties of agency contracts. (Page 177)
    (*iii*) Give three examples of how agency can be created. (Page 178)
    (*iv*) "The wife is not the agent of her husband". True or false ? (Page 180)
    (*v*) Give three examples of termination of agency. (Page 187)
    (*vi*) "An agent is bound to render accounts to the principal. "True or false ? (Page 191)
    (*vii*) Give two exceptions to the rule "an agent cannot appoint an agent". (Page 186)