

SPECIAL CONTRACTS

CONTRACT OF INDEMNITY

(Sec 124 of Indian Contract Act)- wherein a person promises to save another from loss caused to him.

1. by the act of promisor himself or
2. by act of other party.

Eg: 'A' contracts to indemnify 'B' against the consequences of any proceedings which 'C' may take against 'B' in respect of sum of Rs.200 advanced by 'C' to 'B'. In consequence, when 'B' is called upon to pay the sum of money to 'C' fails to do so; 'C' would be able to recover the amount from 'A'.

Essentials:

1. Promise between the two parties- promise should be express promise.
2. Protection against loss- promise should be to protect the other party from loss caused to him.
3. By promisor himself or other person- Loss may be caused by promisor himself or by any other person. It does not include loss caused by natural reasons which are beyond human control, fire, perils of sea etc.

Contracts of insurance are not indemnity contracts under Indian Law.

2 parties:

1. Indemnifier (who makes promise to make good the loss caused to another party)
2. Indemnity-holder/indemnified(whose loss is made good)

Rights of Indemnity- holder (Sec 125): the promisee acting within the scope of his authority is entitled to recover from the promisor-

- (1) **All damages**- which he was compelled to pay in any suit in respect of matter to which promise of indemnity applies.
- (2) **All costs**- if in bringing/defending such suit he did not contravene the orders of the promisor and he acted as it would have been prudent for him to act in absence of any indemnity.
- (3) **All sums**- which he may have paid under the terms of any compromise of any such suit, if promisor authorised him to compromise the suit.

Case: Bihal Chandra v Chatur Sen AIR 1967 All 506: where seller promised to the purchaser to indemnify him against dues, if any, it was **held** that such indemnity clause would include only then existing dues and not those subsequently imposed though retrospectively.

Duties of Indemnity-holder = Rights of Indemnifier:

- to act in accordance of the orders of the indemnifier;
- to act as a man of ordinary prudence;
- To bring all the material facts to the knowledge of the indemnifier.

Case: Osman Jamal & Sons ltd v Gopal Purushottam 1928 ILR 56 Cal 262: held indemnity is not necessarily given by repayment after payment. Indemnity requires that the party to be indemnified shall never be called upon to pay.

CONTRACT OF GUARANTEE (Sec 126)

A contract to perform a promise or discharge the liability of third person in case third person makes a default.

Eg: 'A' says to 'C' "lend money at interest to B and if B fails to pay back, I shall".

Here 'A' is guarantor/surety; 'B' is principal debtor; 'C' is creditor.

3 parties:

- **Surety:** who gives guarantee; person who undertakes liability of third person.
- **Principal debtor:** person who borrows the money.
- **Creditor:** to whom guarantee is given.

3 types of contract:

1. Between principal debtor and creditor
2. Between surety and creditor
3. Between principal debtor and surety

2 types of guarantee:

- (a) Specific Guarantee: when surety is liable for a particular transaction only.
- (b) Continuing Guarantee: when liability of surety extends to a series of transaction in future; **Eg:** promise of surety to produce the debtor in court from time to time as and when required.

- Continuing guarantee can be revoked at any time by the surety as to future transactions by giving a notice to creditor; except in case where continuing relationship is established.

Eg: 'A' becomes surety of 'C' for B's conduct as manager in C's bank and 'B' is appointed on faith of this guarantee. Now 'A' cannot revoke the continuing guarantee so long as 'B' is the manager since a continuing relationship has been established.

- On death of surety, continuing guarantee is revoked for all the future transactions in absence of any contract to the contrary.

Liability of surety is co-extensive i.e. up to the same extent as that of principal debtor. (Sec 128).

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

Who must creditor sue first?

Case: Bank of Bihar v Damodar Prasad AIR 1969 SC 297: wherein the defendant guaranteed a bank loan. On default, the defendant was sued. The trial court held that bank shall enforce the guarantee only after having exhausting its remedies against the principal debtor. Patna H.C. confirmed the decree. But SC held that it is on the **discretion of creditor** whether to first sue the principal debtor or the creditor first. The very object of guarantee is defeated if the creditor is asked to postpone his remedies against the surety.

Case: Union of India v Manku Narayan (1987)2 SCC 335: held that creditor must first proceed against the mortgaged property and then against the surety for the balance.

Discharge of surety's liability:

Variance in terms of contract: between principal debtor and creditor without the consent of surety.

Eg: 'A' stands as surety for the rent payable by 'B' to 'C' for C's house. If 'B' and 'C' agree on a higher rent without the consent of 'A', then 'A' is discharged from his liability.

Discharge of principal debtor: the surety is discharged if the principal debtor is discharged by a contract or by act or omission.

Eg: 'A' contracts with 'B' to build a house for him. 'C' stands as surety for 'B'. If 'A' discharged 'B' from his obligation to build the house, 'C' will also stand discharged.

Compromise: if a compromise takes place between creditor and principal debtor without the consent of surety, surety stands discharged.

Act/omission of creditor: which adversely affects the rights of surety, then surety gets discharged.

Creditor loses the security: if creditor loses the security, surety gets discharged.

Rights of surety:

1. Against principal debtor:

- Right of subrogation (Sec 140): on the failure of principal debtor to pay the debt---surety pays off--- then surety comes into the position of a creditor and has all the rights which are available to a creditor against principal debtor.
- Right to indemnity (Sec 145): there is an implied promise on behalf of debtor to indemnify the surety after surety pays off his debts.

2. Against the creditor (Sec 141): when surety pays off the debt on default of principal debtor---- surety acquires some rights against creditor which are available to principal debtor:

- Right to securities
- Right to share reduction
- Right to set-off

3. Against co-sureties (Sec 146): in case of more than one surety---if one of them pays off the debt—then such surety has right to get contribution from all the sureties; release of one surety does not discharge others.

CONSIDERATION for past debt: The section says that “anything done...for the benefit of principal debtor” is good consideration. But will “anything done” include things done before the guarantee is given? _

Case: Gulam Husain v Faiyaz Ali AIR 1940 Oudh 346: answered in affirmative. A lessee was to pay the sum due by certain instalments. After a few days a person become the surety of lessee. Court **held** that the bond was not without consideration.

CONTRACT OF BAILMENT (Sec 148)

Bailment: an act of delivering goods by one person to another for some purpose. Herein delivery of a thing is given but ownership is not transferred.

Eg: giving of cloth to tailor for stitching a shirt.

Bailor: the person delivering the goods.

Bailee: the person to whom they are delivered.

There is a contract between bailor and bailee wherein they agree that after the purpose is fulfilled, the goods will either be returned to the bailor or delivered to any other person as per orders of the bailor.

Case: Ultzen v Nicolls (1894) 1 QB 92 wherein an old customer went into a restaurant, a waiter took his coat and hung it on a hook behind him. When the customer was about to leave, the coat went missing. **Held** that though what the waiter did might be no more than an act of voluntary courtesy towards the customer, yet the restaurant was held liable as bailee.

Case: Ram Gulam v Govt of UP AIR 1950 All 206: the plaintiff's ornaments, having been stolen, were recovered by the police and while in police custody, were stolen again. The plaintiff's action against the state for loss was dismissed. **Held** that the ornaments were not made over to govt under any contract therefore the govt never occupied the position of bailee and is not liable.

RIGHTS OF BAILOR

- 1. Right to rescind the contract (Sec 153)**- if bailee contravenes the terms of the contract.
- 2. Right to claim damages (Sec 154)**- if bailee uses the thing in contravention of terms of contract and the thing bailed gets damaged.
- 3. Right to get things back (Sec 160)**- after completion of the object for which the thing was bailed or after the completion of time.
- 4. Right to claim damages on mixture of goods by bailee (Sec 155, 156, 157)**- if the things get mixed by the bailee with his own goods.
- 5. Right to get increase or profit from the goods bailed (Sec 163)**- in the absence of a contract to the contrary, the bailee is bound to deliver to the bailor any increase or profit which may have accrued from the goods bailed.

Eg: 'A' leaves a cow in the custody of 'B'. The cow has a calf while in B's custody. 'B' is bound to deliver the calf as well as cow to 'A'.

DUTIES OF BAILOR

1. To disclose all the faults in the goods bailed (Sec 150)
2. Liability to pay necessary expenses (Sec 158)
3. To indemnify the bailee (Sec 164)

RIGHTS OF BAILEE

(A) To claim damages (Sec 150) – if bailee is injured or is put to loss because of the defect in the goods bailed.

(B) Right to get expenses (Sec 158) – which the bailee has to incur for the maintenance of the thing bailed.

(C) Right of lien (Sec 170) – right to keep the thing bailed with him until bailor makes the payment due to him.

DUTIES OF BAILEE

- (a) Duty to take good care of the goods bailed (Sec 151, 152)- care as expected from an ordinary prudent man.
- (b) Not to act in contravention of the terms of bailment (Sec 153)
- (c) Not to make unauthorised use of goods (Sec 154)- if he does so and loss is caused to the thing bailed, then bailee is liable to bailor.
- (d) Not to mix bailed goods with his own goods (Sec 155, 156, 157) without the consent of bailor.
- (e) To return goods (Sec 160, 161, 163) after completion of the time or after completion of the object for which thing was bailed.

PLEDGE (Sec 172)

A pledge is a form of bailment, the only difference being that there is a delivery of goods as security for a debt or promise. Pledge is only of movables.

Essentials:

1. Transfer of possession of thing- essential ingredient
2. Pawnee must hold legal possession over the thing. He is not the owner but it is not only custody.
3. Delivery of thing can be actual or constructive.

Delivery by attornment: When goods are in possession of third person and the pawnor directs the third person to hold them on pledgee's (pawnee's) behalf, that is enough delivery.

1. Delivery of goods is made for securing a debt or for performance of a promise. (particular purpose)
2. Pledge is in connection with movables.

Case: Morvi Merchantile Bank v Union of India AIR 1965 SC 1954: certain goods were consigned with the railways to “self” from Bombay for transit to Okhla. The consigner endorses the railway receipts to the appellant bank against an advance of Rs.20,000. The goods having been lost in the transit, the bank as endorsee of the railway receipts and pawnee of goods sued the Railways for the loss. **Held** that delivery of railway receipts was the same thing as delivery of goods therefore it was valid pledge and pawnee was entitled to sue for the loss.

RIGHTS OF PAWNEE

1. **Right to lien** (Sec 173, 174) till payment of dues is made to him by the pawnor. (Particular lien)
2. **Right to recover extraordinary expenses** (Sec 175) for preservation of the thing pledged.
3. **Where pawnor makes default** (Sec 176) default in making payment or in performing the promise, pawnee has right to file a suit for recovering the amount; to retain the goods with him; to sell the goods after due notice.

PLEDGE BY PERSON OTHER THAN THE OWNER

General rule: a thing can be validly pledged only by the owner of the goods.

Exceptions: sometimes possessor of the goods can pledge them.

By mercantile agent (Sec 178)- an agent who has such authority from his principal to sell goods for the purpose of sale or to buy goods or to raise money for security of goods. Such person can with the consent of the owner pledge goods in ordinary course of business provided

- the pawnor acts in good faith and
- has no notice at the time of the pledge that the pawner has no authority to pledge

By person holding possession under a voidable contract (Sec 178A)- voidable at the option of the lawful owner on the ground of fraud, misrepresentation, coercion or undue influence provided

- Contract has not been rescinded at the time of pledge.

Case: Phillips v Brooks Ltd. (1919)2 KB 243: a fraudulent person induced the plaintiff to give him a valuable ring in return for his cheque which later proved worthless. Before the fraud was discovered, the ring was pledged with the defendant. Pledge was **held valid** because it was made by a person in possession under a voidable contract.

By person holding limited interest in the thing pledged (Sec 179)- whenever a person has limited interest in the goods in his possession, he has unconditional authority to charge at least that interest.

By co-owner in possession- if one of several joint owners of goods is in sole possession of the goods with the consent of the rest of the owners, he can make a valid pledge of the goods.

AGENCY

Agent (Sec 182): a person employed to do any act for another; or to represent another in dealings with third person.

Agent has power to represent his principal in dealings with third persons.

The essential point: agent makes his principal answerable to third persons for his acts because whatever he does in that capacity he does for and on behalf of the principal and not his own behalf.

Representative character and derivative authority -----distinguishing feature of an agent.

Principal: the person for whom such act is done; or who is so represented.

Contract of agency: the relationship that exists between agent and principal.

Eg: 'A' authorizes 'B' to collect rent of the properties belonging to 'A' and to look after his properties. Here, 'A' = principal; 'B' = agent; the relationship between 'A' and 'B' is agency.

Case: Krishna v Ganapathi AIR 1955 Mad 648: held that every person who acts for another is not his agent...it is only when he acts as a representative of the other in business negotiations, between that other and third person, that he is an agent. Representative character and derivative authority are the distinguishing features of an agent.

ESSENTIAL FEATURES of contract of agency:

1. Principal should be competent to contract (Sec 183): since agency is a contract of employment, i.e. principal should not be minor, unsound mind and should not be disqualified by law.
2. Capacity to become an agent (Sec 184): An agent incurs no personal liability while contracting for his principal; therefore it is not necessary that he should be competent to contract. Thus a minor can be appointed as an agent but he will not be responsible for any of his act.

3. Consideration is not necessary (Sec 185): Contract of agency is an exception to general rule contained in Sec 25 which provides that an agreement without consideration is void.
4. Liability of Principal: Principal is answerable and liable for the acts of the agent to the third party since the agent acts for and on behalf of the principal and not on his own behalf.

Case: Unit Trust of India v Ravinder Kumar Shukla AIR 2005 SC 3528, a cheque was sent by UTI by registered post, but it was not received by the payee. There was no understanding with or request by the payee that it should be sent by post. Held- that the post office acted as the agent of UTI. Liability for non-delivery was that of the UTI and not the post office.

Creation of agency (modes)

(i) By agreement: an agent can be appointed expressly or impliedly; it can be by words spoken or written.

Eg: 'A' owns a shop and 'B' manages the shop. Though 'A' being the owner orders purchases for the shop, 'B' by virtue of his position can also purchase as an agent.

Case: Delhi Electric Supply Undertaking v Basanti Devi (1999) 8 SCC 229: under Salary Saving Scheme adopted by LIC of India, the employer (DESU) was authorized by LIC to collect premium amount from the salary of an employee and forward it to LIC. Thus DESU became an agent of LIC for that purpose. Thus, on failure of DESU to collect premium whereby the policy was about to lapse on the death of the employee, LIC was held liable to make payment under the policy.

(ii) By ratification: It is necessary when the agent acts without the knowledge or approval of the principal; the principal can later ratify/approve the act of the agent and thus become bound by the acts of the agent. If he does not ratify the act, the agent is answerable to the third party for his acts.

Rules of ratification:

a) Ratification can be done only by a person, for whom the act was done, professing him to be a principal.

- b) Ratification dates back to the date of the act.
- c) It can be express or implied by the acts of the principal.
- d) Ratification must be of whole act and cannot be of a part of it.
- e) Ratification cannot be done to cause injustice to the third party.
- f) Ratification cannot be done if the principal ratifying is in knowledge of facts which are materially defective.
- g) Illegal and void acts cannot be ratified.

(iii) By estoppel: when principal by his own acts places an agent in such a situation that an ordinary prudent person is justified in presuming that such agent has authority to perform a particular act; the principal is estopped from denying the agent's acts against the third person.

Eg: In presence of 'B', 'A' tells 'C' that he is an agent of 'B' and 'B' remains silent on it. 'C', believing 'A' to be agent of 'B', gives a loan of Rs.1000 to 'A'. Here 'B' cannot escape his liability as principal and is liable to pay Rs.1000 to 'C'.

(iv) By necessity: When a person is not appointed as an agent but under certain circumstances one has to do some act for another which are necessary.

Conditions which enable a person to act as agent of necessity:

- Inability to communicate with the principal,
- Act should be reasonably necessary,
- Act should be bonafide in the interest of the party concerned

Eg: An occasion for a person to act as agent of necessity arises when an injured person is in urgent need of medical attendance. Any person acting on his behalf may call the services of a doctor. The injured person is bound to pay charges of the services.

(v) By law: employment of any agent by any authority authorized by law to make the employment (not necessarily by principal only).

- Eg: when a company is first formed, its original directors are its agent by operation of law.

- Eg: a statute may empower the court to appoint a person to act on behalf of another and so enable the court to create relation of principal and agent.

Duties of agent:

To execute mandate: to carry out the work for which he is appointed.

Effect of failure: he will be absolutely liable to principal for any loss.

To follow instructions: agent is bound to conduct the business according to the instructions of the principal.

Eg: an estate agent cannot make binding contract on behalf of his principal with third party.

Effect of failure: agent must make good any loss suffered by principal and if any profit accrues to agent, he must account for it.

To take reasonable care and skill:

Case: Bank of Bihar v Tata Scob Dealers AIR 1960 Cal 475: a bank was instructed to collect a certain amount on principal's behalf and remit it to him. There was no specific instruction as to the manner of remittance. The bank sent the amount by draft placed in a letter sent by ordinary post. Bank was held negligent in sending the amount like that.

Effect of failure: if principal suffers any loss, agent has to compensate him, but not in respect of any loss which is caused indirectly by such neglect, want of skill or misconduct.

To avoid conflict of interest: if agent deals on his own account in business of agency, without first obtaining the consent of principal, the principal may repudiate the transaction if---it was a material fact which was dishonestly concealed from him, and such dealing caused disadvantage to him.

Eg: 'A' discovers a mine on principal's estate and without disclosing this fact buys estate for himself. Principal may repudiate the transaction.

Not to make secret profit: agent shares a fiduciary relationship with principal, therefore he must act in good faith.

Secret profit = any advantage obtained by agent over and above his agreed remuneration and which he would not have been able to make but for his position as an agent.

To maintain account: he is bound to render proper account to his principal on demand.

Not to delegate: (Delegatus non potest delegare)

DELEGATUS NON POTEST DELEGARE (Sec 190)

= a delegated authority cannot further delegate.

=when principal appoints an agent for some purpose, such agent cannot for that purpose appoint a sub-agent.

=confidence in a particular person employed is at the core of the contract.

=Sub-agent: a person appointed by an agent and to whom principal's work is delegated.

Eg: 'A' appoints 'B' for looking after his business believing in the efficiency of 'B' but 'B' appoints 'C' for executing that work. 'A' is not liable for the acts of 'C' (sub-agent).

Exceptions:

1. Nature of work: sometimes the nature of work is such that it becomes necessary for the agent to appoint a sub-agent.

Eg: an agent authorized to file a suit may engage a lawyer.

Trade custom: a sub-agent may be appointed if there is ordinary custom of trade to that effect.

Eg: architects generally appoint surveyors.

Ministerial action: an agent cannot delegate acts which require personal or professional skills; but he can delegate the acts which are purely ministerial in nature.

Eg: authority to sign.

Principal's consent: principal may expressly/implicitly allow the agent to appoint a sub-agent.

RIGHTS OF AGENT

a) Right to claim remuneration (Sec 219-220): agent is entitled to remuneration for performance of his act. If principal declines—agent is entitled to damages which will be equal to remuneration which he would have earned if transaction had been duly completed.

- Payment is not due until completion of act
- Agent guilty of misconduct is not entitled to remuneration

b) Right to lien (Sec 221): till the amount due to himself for commission and services has been paid to him, the agent can retain goods, property of the principal received by him, in absence of contract to the contrary.

c) Right to recover loss (Sec 225): loss caused to agent due to negligence or lack of skill on the part of principal.

Eg: 'A' employs 'B' as bricklayer in building a house and puts up scaffolding himself. The scaffolding is put up unskillfully and 'B' is hurt. 'A' must make compensation to 'B'.

Relation between agent and sub-agent

Improper delegation: (Sec 193) means when delegation is not authorized, i.e. when none of the exceptions apply to it.

Effect: ---principal is not bound by the acts of the sub-agent.

---sub-agent is not responsible to the principal.

---here agent stands in the position of the principal towards that sub-agent.

---agent is responsible for his acts towards third party.

Proper delegation: (Sec 192) when sub-agent is properly appointed according to the exceptions stated above.

Effect: ---principal is bound by the acts of sub-agent.

---there is no privity of contract between principal and sub-agent.

---agent is responsible to principal for acts of sub-agent.

---sub-agent is responsible to the agent for his acts.

---in case of fraud/willful wrong only, sub-agent is responsible to principal.

Note: sub-agent is bound by all the duties of an ordinary agent. His rights cannot go beyond those of an agent.

Substituted agent = a person appointed by the agent with express/implicit authority of the principal.

= he is another agent of the principal (whereas sub-agent is agent of the agent)

Eg: 'A' directs 'B' (solicitor) to sell his estate by auction and to employ an auctioneer for the purpose. 'B' names 'C', an auctioneer, to conduct the sale.

Here 'A'=principal; 'B'=agent, 'C'=substituted agent

Relation between substituted agent and principal:

---substituted agent is also an agent of principal

---he is responsible to principal and not to the agent

---agent is not responsible to principal for the acts of substituted agent.

TERMINATION OF AGENCY

1) Revocation of authority of agent: (Sec 207)---express/implicit conduct of principal.

Eg: 'A' empowers 'B' to let A's house. Afterwards 'A' himself lets it. This is an implied revocation.

---Principal cannot revoke after authority has been partly exercised. (Sec 204)

---reasonable notice must be given of such revocation to the agent, otherwise any damage caused to the agent must be made good by the principal.

2) Renunciation by agent: (Sec 206) agent may himself renounce the business of agency.

---if agency is for a fixed period—agent will have to compensate principal for any premature renunciation without sufficient cause.

---a reasonable notice of renunciation is necessary, otherwise agent will have to make good any loss suffered by the principal.

3) Completion of business: (Sec 201) when the business is completed, agency automatically and by operation of law is terminated.

Eg: authority of agent appointed to sell goods terminates when sale is completed.

4) Expiry of time: (Sec 201) agency automatically ends on expiry of its term.

Eg: where agency was to run a petrol pump for a specified period, it was held that agent was bound to vacate the premises on expiry of that period.

Case: Turner v Goldsmith (1891)1 QB 544: an agent was appointed by a shirt manufacturer as a canvasser and traveller for 5 years. The principal's factory was burned down by a chance fire while there were still 3 years for the agency to terminate. The principal never resumed business and ended the agency. Principal was held liable in damages as the agency was created for a definite term.

5) Death/insanity of principal or agent: (Sec 201) agency automatically terminates on death of principal or agent. But acts done by agent before death will remain binding.

6) Insolvency of principal: (Sec 201) agency ends on the principal being adjudicated insolvent.

Effects of termination (Sec 208)

Termination of agency:

Between principal and agent----the authority of agent ends when he comes to know of the termination.

Eg: where authority of agent to sell goods is revoked, but he sells the goods before receiving letter of revocation, the sale is valid.

As regards third person---- agency does not terminate until they come to know of the fact of termination.

Termination of sub-agency (Sec 210):

Once authority of an agent terminates---authority of sub-agent appointed by him also terminates.

Agent's duty on termination (Sec 209):

= to protect principal's interest where principal has died or has become a person of unsound mind.