

# **Unit 2 – Special Contracts**

**B.COM (P)-Semester 2**

Faculty-  
Section A- Nupur Tyagi

## **Topics to be covered**

### Contract of indemnity – (Section 124,125)

- Definitions and essentials
- Rights of indemnity holder
- Time of commencement to indemnifier's liability

### Contract of guarantee - (Section 126-147)

- Definitions and essentials
- Distinction between indemnity and guarantee
- Kings of guarantee
- Nature and extent of surety's liability
- Rights of surety
- Discharge of surety

### Contract of bailment - (Section 148-171)

- Definitions and essentials
- Kinds
- Rights and duties of Bailor and Bailee
- Lien and its types

### Contract of pledge - (Section 172-181)

- Definitions and essentials
- Difference with bailment
- Rights and duties of pawner and Pawnee
- Pledge by non-owners

### Contracts of agency – (Section 182-238)

- Definitions and essentials
- Principal agent relationship
- Creation of agency
- Extent of agents authority
- Delegation of authority: sub agent and substitute agent
- Liability of principal
- Personal liability of agent towards third party

## CONTRACT OF INDEMNITY

Contract of indemnity meaning is a special kind of contract. The term 'indemnity' literally means "security or protection against a loss" or compensation. According to **Section 124** of the Indian Contract Act, 1872 "A contract by which one party promises to save the other from loss caused to him by the conduct of the promisor himself, or by the conduct of any other person, is called a contract of indemnity."

Example: P contracts to indemnify Q against the consequences of any proceedings which R may take against Q in respect of a certain sum of money.

## OBJECTIVE OF CONTRACT OF INDEMNITY

The objective of entering into a contract of indemnity is to protect the promisee against unanticipated losses.

## PARTIES TO THE CONTRACT OF INDEMNITY

A contract of indemnity has two parties.

1. The promisor or indemnifier
2. The promisee or the indemnified or indemnity-holder

**The promisor or indemnifier:** He is the person who promises to bear the loss.

**The promisee or the indemnified or indemnity-holder:** He is the person whose loss is covered or who are compensated.

In the above-stated example,

- P is the indemnifier or promisor as he promises to bear the loss of Q.
- Q is the promisee or the indemnified or indemnity-holder as his loss is covered by P.

## **ESSENTIALS OF CONTRACT OF INDEMNITY**

1. **PARTIES TO A CONTRACT:** There must be two parties, namely, promisor or indemnifier and the promisee or indemnified or indemnity-holder.
2. **PROTECTION OF LOSS:** A contract of indemnity is entered into for the purpose of protecting the promisee from the loss. The loss may be caused due to the conduct of the promisor or any other person.
3. **EXPRESS OR IMPLIED:** The contract of indemnity may be express (i.e. made by words spoken or written) or implied (i.e. inferred from the conduct of the parties or circumstances of the particular case).
4. **ESSENTIALS OF A VALID CONTRACT:** A contract of indemnity is a special kind of contract. The principles of the general law of contract contained in Section 1 to 75 of the Indian Contract Act, 1872 are applicable to them. Therefore, it must possess all the essentials of a valid contract.
5. **NUMBER OF CONTRACTS:** In a contract of Indemnity, there is only one contract that is between the Indemnifier and the Indemnified.

## **RIGHTS OF PROMISEE/ THE INDEMNIFIED/ INDEMNITY HOLDER**

As per Section 125 of the Indian Contract Act, 1872 the following rights are available to the promisee/ the indemnified/ indemnity-holder against the promisor/ indemnifier, provided he has acted within the scope of his authority.

1. **RIGHT TO RECOVER DAMAGES PAID IN A SUIT**  
**[SECTION 125(1):** An indemnity-holder has the right to recover from the indemnifier all damages which he may be compelled to pay in any suit in respect of any matter to which the contract of indemnity applies.
2. **RIGHT TO RECOVER COSTS INCURRED IN DEFENDING A SUIT**  
**[SECTION 125(2):** An indemnity-holder has the right to

recover from the indemnifier all costs which he may be compelled to pay in any such suit if, in bringing or defending it, he did not contravene the orders of the promisor, and acted as it would have been prudent for him to act in the absence of any contract of indemnity, or if the promisor authorized him to bring or defend the suit.

3. **RIGHT TO RECOVER SUMS PAID UNDER COMPROMISE**  
**[SECTION 125(3)]**: An indemnity-holder also has the right to recover from the indemnifier all sums which he may have paid under the terms of any compromise of any such suit, if the compromise was not contrary to the orders of the promisor, and was one which it would have been prudent for the promisee to make in the absence of any contract of indemnity, or if the promisor authorized him to compromise the suit
4. **RIGHT TO SUE FOR SPECIFIC PERFORMANCE**- The indemnity holder is entitled to sue for specific performance if he has incurred absolute liability and the contract covers such liability.

### **COMMENCEMENT OF LIABILITY OF PROMISOR/ INDEMNIFIER**

Indian Contract Act, 1872 does not provide the time of the commencement of the indemnifier's liability under the contract of indemnity. But different High Courts in India have held the following rules in this regard:

- Indemnifier is not liable until the indemnified has suffered the loss.
- Indemnified can compel the indemnifier to make good his loss although he has not discharged his liability.

In the leading case of Gajanan Moreshwar vs. Moreshwar Madan(1942), an observation was made by the judge that “ If the indemnified has incurred a liability and the liability is absolute, he is entitled to call upon the indemnifier to save him from the liability and pay it off”.

Thus, Contract of Indemnity is a special contract in which one party to a contract (i.e. the indemnifier) promises to save the other (i.e. the indemnified) from loss caused to him by the conduct of the promisor himself, or by the conduct of any other person. Section 124 and 125 of the Indian Contract Act, 1872 are applicable to these types of contracts.

## CONTRACT OF GUARANTEE

**Contract of Guarantee means a contract to perform the promises made or discharge the liabilities of the third person in case of his failure to discharge such liabilities.**

As per section 126 of Indian Contract Act, 1872, a contract of guarantee has three parties: –

**Surety:** A surety is a person giving a guarantee in a contract of guarantee. A person who takes responsibility to pay a sum of money, perform any duty for another person in case that person fails to perform such work.

**Principal Debtor:** A principal debtor is a person for whom the guarantee is given in a contract of guarantee.

**Creditor:** The person to whom the guarantee is given is known as the creditor.

For example, Mr. X advances a loan of 25000 to Mr. Y and Mr. Z promise that in case Mr. Y fails to repay the loan, then he will repay the same. In this case of a contract of guarantee, Mr. X is a Creditor, Mr. Y is a principal debtor and Mr. Z is a Surety.

## ESSENTIAL

### 1. Essentials of valid contract

2. Consideration for guarantee
3. Competency of the parties
4. Existence of a recoverable debt
5. No misrepresentation or concealment of facts
6. Conditional liability of surety
7. Concurrence of all the three parties
8. Mode of creation of contract

### **KINDS OF GUARANTEE**

1. Retrospective or prospective
2. Specific or continuing
3. Entire or partial debt

### **REVOCATION OF CONTINUING GUARANTEE**

1. By notice
2. By death of surety

### **NATURE AND EXTENT OF SURETY'S LIABILITY**

1. Secondary
2. Contingent or dependent
3. Arises immediately on the default of the principal debtor

4. Co-extensive
5. Entitled to limit his liability
6. Continuing guarantee
7. Where the original contract between the principal debtor and creditor become void or voidable

## **RIGHTS OF SURETY**

1. Against the principal debtor
  - a. Right of subrogation
  - b. Right of indemnity
  - c. Right to insist the principal debtor to honour his obligation
  - d. Right to securities with the creditor
  
2. Against the creditor
  - a. Right to request the creditor to proceed against the debtor
  - b. Right of set off
  - c. Right to benefit of creditor's securities
  - d. Right to require the employer to terminate the employees services
  - e. Right to share reduction
  
3. Against co-sureties
  - a. When liable to contribute equally

- b. Bound to pay in different sums
- c. Right to share benefits of securities
- d. Effect of release of surety

## **DISCHARGE OF SURETY**

1. By revocation
  - a. By notice
  - b. By death of surety
  - c. By novation
2. By act or conduct of creditor
  - a. Variation in the terms of the contract
  - b. Release or discharge of principal debtor
  - c. Compounding with or giving time to the principal debtor
  - d. Creditors act or omission impairing surety eventual remedy
  - e. Loss of security
3. By invalidation of contract of guarantee
  - a. Obtained by misrepresentation
  - b. Obtained by concealment
  - c. Co-sureties does not join
  - d. Lacks essential element of a valid contract

### *Exceptions*

- a. Agreement made with third person
- b. Mere forbearance to sue
- c. Release of one co-surety
- d. Death or insolvency of principal debtor

## **CONTRACT OF BAILMENT AND PLEDGE**

The word “Bailment” has been derived from the French word “ballier” which means “to deliver”. Bailment etymologically means ‘handing over’ or ‘change of possession’. As per Section 148 of the Act, bailment is the delivery of goods by one person to another for some purpose, upon a contract, that the goods shall, when the purpose is accomplished, be returned or otherwise disposed of according to the directions of the person delivering them. The person delivering the goods is called the “bailor”. The person to whom they are delivered is called the “bailee”.

Example: Where ‘X’ delivers his car for repair to ‘Y’, ‘X’ is the bailor and ‘Y’ is the bailee.

Example: X delivers a piece of cloth to Y, a tailor, to be stitched into a suit. It is contract for bailment.

### **Essentials**

The essential elements of a contract of bailment are—

(a) Contract: Bailment is based upon a contract. The contract may be express or implied. No consideration is necessary to create a valid contract of bailment.

(b) Delivery of goods It involves the delivery of goods from one person to another for some purposes. Bailment is only for moveable goods and never for immovable goods or money. The delivery of the possession of goods is of the following kinds:

i. Actual Delivery: When goods are physically handed over to the Bailee by the bailor.

Eg: delivery of a car for repair to workshop

ii. Constructive Delivery: Where delivery is made by doing anything that has the effect of putting goods in the possession of the Bailee or of any person authorized to hold them on his behalf.

Eg: Delivery of the key of a car to a workshop dealer for repair of the car.

(c) Purpose: The goods are delivered for some purpose. The purpose may be express or implied.

(d) Possession: In bailment, possession of goods changes. Change of possession can happen by physical delivery or by any action which has the effect of placing the goods in the possession of Bailee. The change of possession does not lead to change of ownership. In bailment, bailor continues to be the owner of goods as there is no change of ownership. Where a person is in custody without possession he does not become a Bailee.

For example, servants of a master who are in custody of goods of the master do not become bailees

Similarly, depositing ornaments in a bank locker is not bailment, because ornaments are kept in a locker whose key are still with the owner and not with the bank. The ornaments are in possession of the owner though kept in a locker at the bank.

(e) Bailee is obliged to return the goods physically to the bailor. The goods should be returned in the same form as given or may be altered as per bailor's direction. It should be noted that exchange of goods should not be allowed. The Bailee cannot deliver some other goods,

even not those of higher value. Deposit of money in a bank is not bailment since the money returned by the bank would not be identical currency notes.

### **Kinds**

On the basis of benefit derived, bailment can be classified into two types:

- Exclusive benefit of bailor
- Exclusive benefit of bailee

On the basis of reward, bailment can be classified into two types:

- **Gratuitous Bailment:** The word gratuitous means free of charge. So a gratuitous bailment is one when the provider of service does it gratuitously i.e. free of charge such bailment would be either for the exclusive benefits of bailor or bailee.
- **Non-Gratuitous Bailment:** Non gratuitous bailment means where both the parties get some benefit i.e. bailment for the benefit of both bailor & bailee

### **Duties of bailor**

The duties of bailor are spelt out in a number of Sections [Section 150, 158, 159, 164

These are enumerated hereunder:

- 1. Bailor's duty to disclose faults in goods bailed [Section 150]:**  
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 extraordinary risks; 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 goods bailed.

Example 1: 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.

Example 2: 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.

The condition for the liability of the bailor are:

- a. The bailor should have the knowledge of the defect and the bailee should not be aware
- b. The defect in the goods must be such as exposes the bailee to extraordinary risks or materially interferes with the use of goods.

In *Hyman & Wife v. Nye & Sons* (1881), A hired from B a carriage along with a pair of horses and a driver for a specific journey. During the journey a bolt in the under-part of the carriage broke away. As a result of this, the carriage became upset and A was injured. It was held that B was liable to pay damages to A for the injury sustained by him. The court observed that it was the bailor's duty to supply a carriage fit for the purpose for which it was hired. Sometimes, the goods bailed are of dangerous nature (e.g., explosives). In such cases it is the duty of the bailor to disclose the nature of goods. [Great Northern Ry'.case (1932)]

**2. Duty to pay necessary expenses [Section 158]:** Where, by the conditions of the bailment, the goods are to be kept or to be carried, or to have work done upon them by the bailee for the bailor, and the bailee is to receive no remuneration (gratuitous bailment), the bailor shall repay to the bailee the necessary expenses incurred by him and any extraordinary expenses incurred by him for the purpose of the bailment. However, in case of non-gratuitous bailment the bailor is liable to pay the extraordinary expenses.

Example: A hired a taxi from B for the purpose of going to Gurgaon from Noida, during the journey, a major defect occurred in the engine. A had to pay ` 5000 as repair charges. These are the extraordinary expenses and it is the bailor's duty to bear such expenses. However, the usual and ordinary expenses for petrol, toll tax etc are to be borne by the bailee itself.

**3. Duty to indemnify the Bailee for premature termination**

**[Section 159]:** The bailor must compensate the bailee for the loss or damage suffered by the bailee that is in excess of the benefit received, where he had lent the goods gratuitously and decides to terminate the bailment before the expiry of the period of bailment.

**4. Bailor's responsibility to bailee [Section 164]:** The bailor is responsible to the bailee for the following:

a. **Indemnify 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 directions, respecting them (defective title in goods).

b. **It is the duty of the bailor to receive back the goods** when the bailee returns them after the time of bailment has expired or the purpose of bailment has been accomplished. If the bailor refuses to take delivery of goods when it is offered at the proper time the bailee can claim compensation for all necessary expenses incurred for the safe custody. Example: X delivered his car to S for five days for safe keeping. However, X did not take back the car for one month. In this case, S can claim the necessary expenses incurred by him for the custody of the car.

- 1. Take reasonable Care of the goods (Section 151 & 152):** In all cases of bailment, 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.

Example 1: If X bails his ornaments to 'Y' and 'Y' keeps these ornaments in his own locker at his house along with his own ornaments and if all the ornaments are lost/stolen in a riot 'Y' will not be responsible for the loss to 'X'. If on the other hand 'X' specifically instructs 'Y' to keep them in a bank, but 'Y' keeps them at his residence, then 'Y' would be responsible for the loss [caused on account of riot].

Example 2: A deposited his goods in B's godown. On account of unprecedented floods, a part of the goods were damaged. It was held that, B is not liable for the loss (Shanti Lal V. Takechand).

Exception: Bailee when not liable for loss, etc., of thing bailed [Section 152]: The bailee, in the absence of any special contract, is not responsible for the loss, destruction or deterioration of the thing bailed, if he has taken the amount of care of it described in section 151.

- 2. Not to make inconsistent use of goods (section 153 & 154):** As per Section 154, if the bailee makes any use of the goods bailed, which is not according to the conditions of the bailment, he is liable to make compensation to the bailor for any damage arising to the goods from or during such use of them.

Example 1: 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.

Example 2: 'A' hires a horse in Kolkata from B expressly to march to Varanasi. '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 for the injury to the horse.

As per Section 153, 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.

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

**3. Not to mix the goods (Section 155, 156 and 157):** Bailee is not entitled to mix up the goods bailed with his own goods except with the consent of the bailor.

- If he, with the consent of the bailor, mixes the goods bailed with his own goods, both the parties shall have an interest in proportion to their respective shares in the mixture thus produced (**Sec. 155**).
- If the bailee, without the consent of the bailor, mixes the goods bailed with his own goods and the goods can be separated or divided, the property in the goods remains in the parties respectively bailee is bound to bear the expenses of separation and division and any damage arising from the mixture (**Sec. 156**).

Example: A bails 100 bales of cotton marked with a particular mark to B. B, without A's consent, mixes the 100 bales with other bales of his own, bearing a different mark; A 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.

- 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 to deliver them back, the bailor is entitled to compensation by the bailee for loss of the goods (**Sec. 157**).

Example: A bails a barrel of Cape flour worth ` 4500 to B. B, without A's consent, mixes the flour with country flour of his own, worth only ` 2500 a barrel. B must compensate A for the loss of his flour

#### **4. Return the goods (Section 160 & 161):**

It is the duty of 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. [**Section 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. [**Section 161**]

Example – X delivered books to Y to be bound. Y promised to return the books within a reasonable time. X pressed for the return of the book. But Y, failed to deliver them back even after the expiry of reasonable time. Subsequently the books were burnt in an accidental fire at the premises of Y. In this case Y was held liable for the loss.

- 5. Return an accretion from the Goods [Section 163]:** 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.

Example: A leaves a cow in the custody of B. The cow gives birth a calf. B is bound to deliver the calf as well as the cow to A

- 6. Not to setup Adverse Title:** Bailee must not set up a title adverse to that of the bailor. He must hold the goods on behalf of and for the bailor. He cannot deny the title of the bailor.

### Rights of Bailor

Rights of Bailor: **Broadly rights of bailor are also the duty of the bailee** (under Sec. 151,154,155 and 157) In addition to that, the bailor has the following other rights also.

- Right of termination of bailment – Sec 153
- Right to demand the goods back – Sec 159
- Right to demand the return of goods on completion of bailment – Sec 160
- Right to claim any increase or profit – Sec 163
- Right to file a suit against the wrong doer – Sec 180

### Rights of Bailee

Rights of bailee: **As a matter of fact, all the duties of the bailor are the rights of the bailee.** In addition to that, the bailee has the following other rights also.

- Right to claim compensation in case of faulty goods (Sec. 150)
- Right to claim extraordinary expenses (Sec. 158)
- Right of indemnification in case of gratuitous bailment [Section 159]
- Right of indemnification in case of defective title [Section 164]

- Right to Deliver the Goods to any one of the Joint Bailors [Section 165]
- Right to deliver the goods to the bailor in good faith (Sec. 166)
- Right to Apply to Court to Decide the Title to the Goods/Interplead[Section 167]
- Right to claim damages in case of bailor's refusal to receive back the goods
- Right of lien for payment of services [Section 170]
- Suit by bailor & bailee against wrong doers [Section 180]
- Apportionment of relief or compensation obtained by such suits [Section 181]

### **Right of lien and its types**

#### **1. Bailee's particular lien [Section 170]:**

Where the bailee has, in accordance with the purpose of the bailment, rendered any service involving the exercise of labour or skill in respect of the goods bailed, he has, in the absence of a contract to the contrary, a right to retain such goods until he receives due remuneration for the services he has rendered in respect of them.

Example 1: 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.

Example 2: 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.

- In accordance with the purpose of bailment if the bailee by his skill or labour improves the goods bailed, he is entitled for remuneration for such services. Towards such remuneration, the bailee can retain the goods bailed if the bailor refuses to pay the remuneration. Such a right to retain the goods bailed is the right of particular lien. He however does not have the right to sue.

Where the bailee delivers the goods without receiving his remuneration, he has a right to sue the bailor. In such a case the particular lien may be waived.

- The particular lien is also lost if the bailee does not complete the work within the time agreed.

## **2. General lien of bankers, factors, attorneys and policy brokers [Section 171]:**

Bankers, factors, attorneys of a High Court and policy brokers may, in the absence of a contract to the contrary, retain, as a security for a general balance of account any goods bailed to them; but no other persons have a right to retain, as a security for such balance, goods bailed to them, unless there is an express contract to the effect.

- Bankers, factors, policy brokers and attorneys of law have a general lien in respect of goods which come into their possession during the course of their profession.
- For instance, a banker enjoys the right of a general lien on cash, cheques, bills of exchange and securities deposited with him for any amounts due to him. For instance, 'A' borrows ` 500/- from the bank without security and subsequently again borrows another `1000/- but with security of say certain jewellery. In this illustration, even where 'A' has returned `1000/- being the second loan, the banker can retain the jewellery given as security to the second loan towards the first loan which is yet to be repaid.
- Under the right of general lien the goods cannot be sold but can only be retained for dues. The right of lien can be waived through a contract.

## Pledge

**“Pledge”, “pawnor” and “pawnee” defined [Section 172]:** The bailment of goods as security for payment of a debt or performance of a promise is called “pledge”. The bailor is in this case called the “pawnor”. The bailee is called the “pawnee”.

Pledge is a variety or specie of bailment.

It is bailment of goods as security for payment of debt or performance of a promise. The person who pledges [or bails] is known as pledgor or also as pawnor, the bailee is known as pledgee or also as pawnee. In pledge, there is no change in ownership of the property.

Under exceptional circumstances, the pledgee has a right to sell the property pledged. Section 172 to 182 of the Indian Contract Act, 1872 deal specifically with the bailment of pledge.

Example: A lends money to B against the security of jewellery deposited by B with him i.e. A. This bailment of jewellery is a pledge as security for lending the money. B is a pawnor and A is a pawnee.

**ESSENTIALS OF PLEDGE:** Since Pledge is a special kind of bailment, therefore all the essentials of bailment are also the essentials of the pledge. Apart from that, the other essentials of the pledge are:

- a. There shall be a bailment for security against payment or performance of the promise,
- b. The subject matter of pledge is goods,
- c. Goods pledged for shall be in existence,
- d. There shall be the delivery of goods from pledger to pledgee,

## **Pawnee's rights**

Rights of Pawnee can be classified as under the following headings:

**1. Right to retain the pledged goods [Section 173]:** The pawnee may retain the goods pledged, not only for payment of the debt or the performance of the promise, but 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.

Example: Where 'M' pledges stock of goods for certain loan from a bank, the bank has a right to retain the stock not only for adjustment of the loan but also for payment of interest.

**2. Right to retention of subsequent debts [Section 174]:** The Pawnee shall not, in the absence of a contract to that effect, retain the goods pledged for any debt or promise other than the debt or promise for which they are pledged; but such contract in the absence of anything to the contrary, shall be presumed in regard to subsequent advances made by the Pawnee.

**3. Pawnee's right to extraordinary expenses Incurred [Section 175]:** The pawnee is entitled to receive from the pawnor extraordinary expenses incurred by him for the preservation of the goods pledged. For such expenses, however, he does not have the right to retain the goods.

**4. Pawnee's right where pawnor makes default [Section 176]:** If the pawnor makes 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 a 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.

## Duties of the Pawnee

Pawnee has the following duties:

- a. Duty to take reasonable care of the pledged goods
- b. Duty not to make unauthorized use of pledged goods
- c. Duty to return the goods when the debt has been repaid or the promise has been performed
- d. Duty not to mix his own goods with goods pledged
- e. Duty not to do any act which is inconsistent with the terms of the pledge
- f. Duty to return accretion to the goods, if any.

## Rights of Pawnor

As the bailor of goods pawnor has all the rights of the bailor-

### **Enforcement of Pawnee's duties**

- **Right to redeem [Section 177]:** 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.

## Duties of Pawnor

Pawnor has the following duties:

- a. The pawnor is liable to pay the debt or perform the promise as the case may be.
- b. It is the duty of the pawnor to compensate the Pawnee for any extraordinary expenses incurred by him for preserving the goods pawned.
- c. It is the duty of the pawnor to disclose all the faults which may put the pawnee under extraordinary risks.

- d. If loss occurs to the pawnee due to defect in pawnors title to the goods, the pawnor must indemnify the pawnee.
- e. If the Pawnee sells the good due to default by the pawnor, the pawnor must pay the deficit.

### **Pledge by non-owners**

Ordinarily, it is the owner of the goods, or any person authorized by him in that behalf, who can pledge the goods. But in order to facilitate mercantile transactions, the law has recognised certain exceptions. These exceptions are for bonafide pledges made by those persons who are not the actual owners of the goods, but in whose possession the goods have been left.

- a. **Pledge by mercantile agent [ Section 178]:** Where a mercantile agent is, with the consent of the owner, in possession of goods or the documents of title to goods, any pledge made by him, when acting in the ordinary course of business of a mercantile agent, shall be as valid as if he were expressly authorised by the owner of the goods to make the same; provided that the pawnee acts in good faith and has not at the time of the pledge notice that the Pawnor has no authority to pledge.
- b. **Pledge by person in possession under voidable contract [Section 178A]:** When the pawnor has obtained possession of the goods pledged by him under a contract voidable under section 19 or section 19A, but the contract has not been rescinded at the time of the pledge, the pawnee acquires a good title to the goods, provided he acts in good faith and without notice of the pawnor's defect of title.
- c. **Pledge where pawnor has only a limited interest [Section 179]:** Where a person pledges goods in which he has only a limited interest, the pledge is valid to the extent of that interest.

- d. Pledge by a co-owner in possession:** Where the goods are owned by many person and with the consent of other owners, the goods are left in the possession of one of the co-owners. Such a co-owner may make a valid pledge of the goods in his possession.
- e. Pledge by seller or buyer in possession:** A seller, in whose possession, the goods have been left after sale or a buyer who with the consent of the seller, obtains possession of the goods, before sale, can make a valid pledge, provided the pawnee acts in good faith and he has no knowledge of the defect in title of the pawnor.

For example, A buys a cycle from B. But leaves the cycle with the seller. B then pledges the cycle with C, who does not know of sale to B, and acted in good faith. This is valid pledge

## Difference between bailment and pledge

S.no	Basis of Distinction	Bailment	Pledge
1	<i>Meaning</i>	Transfer of goods by one person to another for some specific purpose is known as bailment	Transfer of goods from one person to another as security for repayment of debt is known as the pledge.
2	<i>Terms Applicable</i>	The person delivering the goods under a contract of bailment is called as "Bailor". The person to whom the goods are delivered under a contract of bailment is called as "Bailee"	The person who delivers the good as security is called the "Pawnor". The person to whom the goods are delivered as security is called the "pawnee"
3	<i>Purpose</i>	Bailment may be made for any purpose (as specified in the contract of bailment, eg: for safe custody, for repairs, for processing of goods)	Pledge is made for the purpose of delivering the goods as security for payment of a debt, or performance of a promise.
4	<i>Consideration</i>	The bailment may be made for consideration or without consideration	Pledge is always made for a consideration.
5	<i>Right to sell the goods</i>	The bailee has no right to sell the goods even if the charges	The pawnee has right to sell the goods if the
		of bailment are not paid to him. The bailee's rights are limited to suing the bailor for his dues or to exercise lien on the goods bailed	pawnor fails to redeem the goods.
6.	<i>Right to use of goods</i>	Bailee can use the goods only for a purpose specified in the contract of bailment and not otherwise.	Pledgee or Pawnee cannot use the goods pledged.

## **CONTRACT OF AGENCY**

According to Section 182 of the Contract Act an 'Agent' is a person employed to do any act for another or to represent another in dealings with third persons. The person for whom such act is done, or who is so represented, is called the 'principal'.

Thus,

It is clear from the definition, that an agent is a connecting link between his principal and third parties.

### **Principles of Agency**

Contracts of agency are based on two important principles, namely:

- Whatever a person can do personally shall also be allowed to be done through an agent except in case of contracts involving personal services such as painting, marriage, singing, etc.
- He who does not act through a duly authorized agent does it by himself, i.e., the act of the agent are considered the acts of the principal (Sec. 226)

### **Essential features of contract of agency**

- Agreement between agency and principal
- Competency of principal
- Competency not required for an agent
- Contractual relationship
- Creation of legal relations
- Consideration not required
- Intention of the person to act

## Creation of agency

Agency may be created under the following ways:

1. By Express Agreement (Section 186) - According to section 186 of the Indian Contract Act, 1872, the contract of agency may be express or implied. Express in the sense, it may be oral or in writing. It is a practice in many cases, to appoint agents by using the power of attorney on a stamped paper.
2. By Implied Agreement (Section 187): Section 187 defines express and implied authority as follows-

An authority is said to be express when it is given by words spoken or written. An authority is said to be implied when it is to be inferred from the circumstances of the case; and things spoken or written, or the ordinary course of dealing, may be accounted circumstances of the case.”

An Implied Agency may be created from the conduct, situation or relationship of the parties. It may be inferred from the circumstances of the case. Implied agency includes:

- a. Agency by Estoppel - It is based on the ‘Doctrine of Estoppel’. If the principal by his conduct or statement leads another person to believe that a person is his agent, he cannot deny him as his agent later. Eg- ‘A’ says ‘B’ in the presence of ‘C’ that he is the agent of ‘C’. If ‘C’ does not deny the statement, he cannot deny ‘A’ as his agent later.
- b. Agency by Holding Out- It is branch of the Agency by Estoppel. If one person knowingly admits another to act on his behalf and allows him to do so, later he cannot deny the act of that person. If he does not want to do so he should express his objection to that act immediately.

Example: 'A' allowed his wife 'B' to manage his property and to mortgage it. A is bound by her acts.

- c. Agency by necessity- Agency of necessity is created in case of emergencies. In these cases, the persons who perform their services as agents do not seek prior permission or appointment from the principals. The principals are also in certain difficult situations and they could not give their assent or refusal, but accept the services rendered by such persons. Therefore, law confers authority on a person to act as an agent for another, without the consent of that person (principal). Such an agency is called 'Agency by Necessity'.

Cases where agency by necessity may arise:

- When an agent exceeds his authority in an emergency (Sec. 189)
- Relationship between husband and wife-
  - Living together
  - Living separately
- Carrier of goods acting as Bailee does anything to protect or preserve the goods

3. By ratification - As per Section 196 of the Indian Contract Act, agency by ratification is said to arise when a person, on whose behalf the acts are done without his knowledge or authority, expressly or impliedly accept such acts.

Essentials of Ratification (Sec.196-200)

- a. Full knowledge

- b. Whole transaction
- c. No damage to 3rd parties
- d. Act on behalf of other person
- e. Existence of Principal
- f. Within reasonable time
- g. Lawful acts
- h. Acts within Principal's power
- i. Communication

4. By Operation of law- Agency by operation of law arises where the law treats one person as an agent of another.

### **Nature and extent of Agent's authority**

1. Actual or real Sec. 188 –

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.

#### *Illustrations*

(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 shipbuilder. B may purchase timber and other materials, and hire workmen, for the purpose of carrying on the business.

2. Ostensible or apparent
3. In emergency Sec. 189

### **Delegation of authority**

Sec. 190. An agent cannot lawfully employ another to perform acts which he has expressly or impliedly undertaken to perform personally, unless by the ordinary custom of trade a sub-agent may, or, from the nature of the agency, a sub-agent must, be employed.

Exceptions:

1. Express consent of principal
2. Implied consent of principal
3. Nature of agency
4. Custom of trade
5. Ministerial acts
6. Unforeseen emergencies

**Sub agent- Sec. 191.** A "sub-agent" is a person employed by, and acting under the control of, the original agent in the business of the agency.

Relationship between sub agent and principal

Sec. 192. **Where a sub-agent is properly appointed,**

- The principal is, so far as regards third person, represented by the sub-agent, and is bound by and responsible for his acts, as if he were an agent originally appointed by the principal.
- Agent's responsibility for sub-agent.-

- The agent is responsible to the principal for the acts of the sub-agent.
- Sub-agent's responsibility.-The sub-agent is responsible for his acts to the agent, but not to the principal, except in case of fraud or wilful wrong.

**Sec. 193 Where a sub-agent is improperly appointed,**

Where an agent, without having authority to do so, has appointed a person to act as a sub-agent,

- the agent stands towards such person in the relation of a principal to an agent, and is responsible for his acts both to the principal and to third persons;
- The principal is not represented by or responsible for the acts of the person so employed,
- The sub agent is not responsible to the principal.

**Substituted agent – Sec. 194.** Where an agent, holding an express or implied authority to name another person to act for the principal in the business of the agency, has named another person accordingly, such person is not a sub-agent, but an agent of the principal for such part of the business of the agency as is entrusted to him.

**Illustrations**

(a) 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.

(b) 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.

Sec. 195. In selecting such agent for his principal, an agent is bound to exercise the same amount of discretion as a man of ordinary prudence would exercise in his own case; and, if he does this, he is not responsible to the principal for the acts or negligence of the agent so selected.

### Illustrations

(a) 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.

(b) 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

## Liability of principal

### **1. Agent Acting for a Named Principal**

The rights and liabilities of a named principal for the acts of his agent may be discussed as below:

#### **a. Acts of an Agent within the Scope of his Authority**

If an act is carried on by an agent within his authority, his acts are binding on the principal. However, the act done should be lawful.

**Example:** A authorized his agent, B, to collect money on his behalf. B received from C a sum of money due to A. This receipt of

money is binding on *A*, and *C* is discharged from his obligation to pay this amount to *A*.

### **b. Acts of an Agent Exceeding his Authority**

It can be discussed under two heads as shown below:

1. **Where the work can be separated** – Where an agent exceeds his agency to do the work of the principal, the principal is bound by that part of the work which is within his authority if it can be separated from the part of the work which is beyond his authority.

**Example:** *A*, owner of a ship and cargo, authorizes *B* to procure an insurance policy for Rs.4,000 on the ship. *B* procures a policy for Rs.4,000 on the ship and another for Rs.6,000 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.

2. **Where the work cannot be separated** – When an agent does more than what he is authorized to do, and such act cannot be separated from that which is within his authority, the principal is not bound by the transaction. He is in such a case entitled to repudiate the whole transaction. So if the agent does something in excess of his powers, the transaction is not binding on the principal.

**Example:** *A* authorized *B*, an agent to buy 500 sheeps.

But *B* purchased 500 sheeps and 200 lambs, for a sum of Rs.6,000. In this case, the principal may repudiate the whole transaction.

### **c. Notice Given to Agent**

The principal is bound by the notice given to the agent in the course of business. Thus, the knowledge of the agent is the knowledge of the principal.

However, if the knowledge is not acquired by the agent in the course of his employment, it cannot be imputed to the principal. Further, if

the agent had committed a fraud on the principal, the rule of this section will not apply.

**Example:** *X* engaged *Y*'s agent to insure him against loss of eye-sight for \$500 in case of total loss of eye-sight and \$250 in case of loss of only one eye. At the time of the insurance, it appeared that *X* was in fact a one-eyed man. Held, the knowledge of the agent that *X* was one-eyed man should be attributed to the company and that *X* could recover \$500 when he lost the other eye.

#### **d. Liability by Estoppel**

The principal is liable for the unauthorized acts of the agent, if the principal has created an impression on the third party by his conduct, that the agent has the authority to do such acts.

**Example:** *A*, an owner of a house held out that *B*, the auctioneer had authority to sell the house. *B* sold the house by auction to a third party for an amount less than the amount authorized by *A*. It was held that the purchaser is not affected by *A*'s instructions to the auctioneer not to sell below a certain price.

#### **e. Liability for Misrepresentation or Fraud**

The principal is liable for the misrepresentation or fraud committed by his agent while acting in the course of his business. It is immaterial whether the misrepresentation or fraud has been committed for the benefit of the principal or of the agent himself.

**Example:** *A* offered to buy a residential flats consisting of number of flats in it and enquired *C*, the property manager of *B*, whether all the tenants were paying their rents regularly. *C* informed *A* that the tenants were paying rents regularly with immaterial exceptions. This statement turned out to be false. *B* was held liable for fraud because his agent (property manager) who knew the real facts had made a false statement.

## **2. Agent Acting for an Unnamed Principal**

When an agent contracts, as an agent for a principal but does not disclose his name, the principal is liable for the contract of the agent. But the unnamed principal should be in existence at the time of the contract and the acts must be within the scope of agent's authority.

**Example:** *A* appointed *B* as his agent to purchase some goods. *B* entered into an agreement with *C* for purchasing those goods. *B* signed the agreement as a broker "*to my principal*" but did not disclose the name of the principal. Here, *B* is not personally liable because he contracted in the capacity of an agent.

However, the agent is personally liable if he declines to disclose the identity of the principal when asked by the third parties.

## **3. Agent Acting for an Undisclosed Principal**

In case of an agent acting for an undisclosed principal, the mutual rights and liabilities of the agent, principal and the third party are as follows:

### **a. Rights and Liabilities of Agent**

Here agent contracts in his own name. So he is bound by the contract. He is personally liable to the third party also. On such contracts, he can sue and be sued in his own name because in the eyes of law he is the real contracting party. In such cases, the principal and the agent have their respective rights against each other.

### **b. Rights and Liabilities of Principal**

The principal has the right to intervene and require the performance of the contract from the third party. In such cases, the other party may sue either the principal or the agent or both. The principal if he likes may also require the performance of the contract from the other party. But in such a case, he should

allow, the benefit of all payments made by the third party to the agent, to the third party.

**Example:** *A* contracted with *B*, a shopkeeper, to purchase furniture. *A* advanced a part payment of the price to *B*. Afterwards, *A* discovered that *B* is the agent of *C*. In this case, *C* may ask *A* to perform the contract. But he must account for the advance money received by his agent *B*.

### **c. Rights and Liabilities of Third Party**

If the third party has discovered that there is a principal, he may file a suit against the principal, or his agent or both. In such a case, the third party must allow the principal, the benefit of all payments received by him from the agent.

**Example:** *A* sold 100 bales of cotton to *B* on credit. Afterwards, *A* discovered that *B* was acting as an agent of *C*. In this case, *A* may sue either *B* or *C*, or both for the performance of the contract.

## **Personal Liability of Agent Sec. 230**

Sec. 230. 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.

Presumption of contract to contrary.-Such a contract shall be presumed to exist in the following cases:-

- (1) Where the contract is made by an agent for the sale or purchase of goods for a merchant resident abroad;
- (2) Where the agent does not disclose the name of his principal;
- (3) Where the principal, though disclosed, cannot be sued.

An agent is not personally liable for the contracts entered into by him on behalf of his principal unless there is a contract to the contrary. Such a contract is presumed in the following circumstances.

- i.** Where the Contract Expressly Provides
- ii.** Where the Agent Acts for a Foreign Principal
- iii.** Where the agents acts for an unnamed principal
- iv.** Where the principal cannot be sued
- v.** Where the Agent Contracts in Excess of his Authority
- vi.** Where the Agent Acts for an Undisclosed Principal
- vii.** Where the Trade Usage or Customs makes him Personally Liable
- viii.** Where the Agent Acts for a Non-existing Principal
- ix.** Where an Agent Receives or Pays Money by Mistake or Fraud
- x.** Where the Agent Signs the Negotiable Instruments in his own Name
- xi.** Pretended Agent
- xii.** Where the Agent's Authority is Coupled with Interest