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FOR CA FOUNDATION EXAM PREPARATION

CA Foundation 2024 Suggested Answers · Paper 2 Business Laws

EXAM	YEAR	TYPE	SUBJECT
CA Foundation	2024	Suggested Answers	Paper 2 Business Laws

DATE

June 2024

SUGGESTED ANSWER JUNE 2024
FOUNDATION EXAMINATION

PAPER – 2: BUSINESS LAWS

*Question No. **1** is compulsory.*

*Attempt any **four** questions from the remaining **five** questions.*

Working notes should form part of the answers

Question 1

(a) *R owns an electronics store. P visited the store to buy a water purifier priced at ₹54,000/-. He specifically requested R for a purifier with a copper filter. As P wanted to buy the purifier on credit, with the intention of paying in 9 equal monthly instalments, R demands a guarantor for the transaction. S (a friend of P) came forward and gave the guarantee for payment of water purifier. R sold P, a water purifier of a specific brand. P made payment for 4 monthly instalments and after that became insolvent. Explain with reference to the Indian Contract Act, 1872, the liability of S as a guarantor to pay the balance price of water purifier to R.*

What will be your answer, if R sold the water purifier misrepresenting it as having a copper filter, while it actually has a normal filter? Neither P nor S was aware of this fact and upon discovering the truth, P refused to pay the price. In response to P's refusal, R filed the suit against S, the guarantor. Explain with reference to the Indian Contract Act 1872, whether S is liable to pay the balance price of water purifier to R? ***(7 Marks)***

(b) *A company, ABC limited as on 31.03.2023 had a paid-up capital of ₹ 1 lakh (10,000 equity shares of ₹ 10 each). In June 2023, ABC limited had issued additional 10,000 equity shares of ₹ 10 each which was fully subscribed. Out of 10,000 shares, 5,000 of these shares were issued to XYZ private limited company. XYZ is a holding company of PQR private limited by having control over the composition of its board of directors.*

Now, PQR private limited claims the status of being a subsidiary of ABC limited as being a subsidiary of its subsidiary i.e. XYZ private limited. Examine the validity of the claim of PQR private limited.

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State the relationship if any, between ABC limited & XYZ private limited as per the provisions of the Companies Act, 2013. ***(7 Marks)***

(c) *The Indian Partnership Act does not make the registration of firms compulsory, yet the consequences or disabilities of non-registration have a persuasive pressure for their registration. Still, there are come cases where non-registration of firm does not affect certain rights. Explain with reference to the provisions of the Indian Partnership Act, 1932.* ***(6 Marks)***

Answer

(a) As per section 126 of the Indian Contract Act, 1872, the contract of guarantee is defined as a contract to perform the promise or discharge the liability of a third person in case of his default.

In this case, S has given a guarantee for P's payment obligation towards R. When P defaulted after making four monthly instalments and became insolvent, S's liability as a guarantor will come into existence.

According to Section 128 of the Act, the liability of the surety is co-extensive with that of the principal debtor, unless it is otherwise provided by the contract.

Since P failed to pay the remaining instalments due to insolvency, S, as the guarantor, is liable to pay the balance price of the water purifier to R. In the given situation, S will have to pay the balance amount of ₹ 30,000 to R. [54,000-(4x6,000)]

In the second situation, R sold the water purifier misrepresenting it as having a copper filter, while it actually has a normal filter; this changes the situation significantly.

According to Section 142 of the Act, 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. Here, guarantee is obtained by means of misrepresentation made by the creditor (R), and therefore the guarantee is invalid.

Furthermore, under Section 143, any guarantee which the creditor has obtained by means of keeping silence as to material circumstances, is invalid.

Here R misrepresented the filter type and both P and S were unaware of this fact. The creditor (R) has obtained the guarantee by remaining silent as to material circumstances. Therefore, the guarantee obtained from S will be considered to be invalid.

Consequently, S cannot be held liable to pay the balance price of the water purifier to R.

(b) As per Section 2(46) of the Companies Act, 2013, holding company in relation to one or more other companies, means a company of which such companies are subsidiary companies.

Section 2(87) defines "subsidiary company" in relation to any other company (that is to say the holding company), means a company in which the holding company—

(i) controls the composition of the Board of Directors; or

(ii) exercises or controls more than one-half of the total voting power either at its own or together with one or more of its subsidiary companies.

In the instant case, as on 31.03.2023, ABC Limited had a paid-up capital of ₹ 1 lakh (10,000 equity shares of ₹ 10 each). In June 2023, ABC Limited issued additional 10,000 equity shares, which was fully subscribed. Post-issue, the total paid-up capital of ABC Limited is ₹ 2 lakhs (20,000 equity shares of ₹10 each).

Out of these, 5,000 shares were issued to XYZ Private Limited. Since XYZ Private Limited holds only 25% of the shares in ABC Limited, it does not have control of more than one-half of the total voting power of ABC Limited. Hence, XYZ Private Limited cannot be considered as a subsidiary company of ABC Limited in terms of the second criteria stated above, that of controlling of voting power.

XYZ Private Limited is the holding company of PQR Private Limited by having control over the composition of its Board of Directors. But since XYZ Private Limited cannot be termed as a subsidiary company of ABC Limited, PQR Private Limited cannot claim the status of being a subsidiary of ABC Limited in terms of the first criteria, that of controlling of the composition of directors.

As per section 2(6) of the Act, Associate Company in relation to another company, means a company in which that other company has a significant influence, but which is not a subsidiary company of the company having such influence and includes a joint venture company.

The expression "significant influence" means control of at least twenty per cent of total voting power, or control of or participation in business decisions under an agreement.

In terms of the above provision, the relationship between ABC Limited and XYZ Private Limited can be of an Associate Company.

Since XYZ Private Limited holds more than 20 percent of voting power in ABC Limited, it can be considered as an Associate Company of ABC Limited.

(c) The Indian Partnership Act, 1932 does not make the registration of firms compulsory nor does it impose any penalty for non-registration. However, under Section 69, non-registration of partnership gives rise to a number of disabilities. Although registration of firms is not compulsory, yet the consequences or disabilities of non-registration have a persuasive pressure for their registration.

Exceptions: Non-registration of a firm does not, however affect the following rights:

1. The right of third parties to sue the firm or any partner.
2. The right of partners to sue for the dissolution of the firm or for the settlement of the accounts of a dissolved firm, or for realization of the property of a dissolved firm.
3. The power of an Official Assignees, Receiver of Court to release the property of the insolvent partner and to bring an action.
4. The right to sue or claim a set-off if the value of suit does not exceed ₹ 100 in value.
5. The right to suit and proceeding instituted by legal representatives or heirs of the deceased partner of a firm for accounts of the firm or to realise the property of the firm.

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Question 2

(a) Sony, a friend of Priya wanted to buy her two-wheeler. Priya agreed to sell her two-wheeler to Sony and it was decided that price of her two-wheeler will be fixed by Priya's father, who is an auto dealer. Priya immediately handed over the keys to Sony. However, Priya's father refused to fix the price as he did not want Priya to sell her vehicle. Priya expressed her inability to sell the two-wheeler to Sony and asked for return, but Sony refused to return the same. Explain-

(i) Can Priya take-back the vehicle from Sony?

(ii) Will your answer be different, if Priya had not handed over the vehicle to Sony? ***(7 Marks)***

(b) Ram wants to incorporate a company in which he will be the only member. According to provisions of the Companies Act, 2013, what type of company can be incorporated? What are the salient features of this type of company?

(7 Marks)

(c) A LLP is a new form of legal business entity with limited liability. It's an alternative corporate business vehicle that only gives the benefits of limited liability at low compliance cost but allows its partners the flexibility of organizing their internal structure as a traditional partnership. Keeping in view of above, define the following characteristics of LLP.

(i) Body Corporate

(ii) Mutual Agency

(iii) Foreign LLPs

(iv) Artificial legal person ***(6 Marks)***

Answer

(a) Ascertainment of price (Section 9 of the Sale of Goods Act, 1930):

By virtue of Section 9, the price in a contract of sale may be-

(1) fixed by the contract, or

(2) agreed to be fixed in a manner provided by the contract, e.g., by a valuer, or

(3) determined by the course of dealing between the parties.

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Agreement to sell at valuation (Section 10):

Section 10 provides for the determination of price by a third party.

1. Where there is an agreement to sell goods on the terms that price is to be fixed by the valuation of a third party and that third party either does not or cannot make such valuation, the agreement is thereby avoided.

   However, a buyer who has received and appropriated the goods, must pay a reasonable price for them.

2. In case the third party is prevented from making the valuation by the default of either party, the party not at fault may maintain a suit for damages against the party in fault.

   (i) In the instant case, Priya handed over the keys of her two-wheeler to Sony and it was decided between them that price of the vehicle will be fixed by Priya's father. However, Priya's father refused to fix the price as he did not want Priya to sell her vehicle. As the keys have already been handed over to Sony, Priya cannot take back the keys from Sony and Sony shall pay reasonable price to Priya for the two-wheeler.

   (ii) If Priya had not handed over the vehicle to Sony, the contract could have been avoided as Priya's father refused to fix the price of the vehicle.

(b) (a) Section 2(62) of the Companies Act, 2013 defines one person company (OPC) as a company which has only one person as a member.

Ram wants to incorporate a company in which he will be the only member. Hence, he can incorporate an One person Company.

According to section 3(1)(c) of the Companies Act, 2013, OPC is a private limited company with the minimum paid up share capital as may be prescribed and having one member.

OPC (One Person Company) – salient features

- Only one person as member.
- Minimum paid up capital – no limit prescribed.

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- The memorandum of OPC shall indicate the name of the other person, who shall, in the event of the subscriber's death or his incapacity to contract, become the member of the company.
- The other person whose name is given in the memorandum shall give his prior written consent in prescribed form and the same shall be filed with Registrar of companies at the time of incorporation.
- Such other person may be given the right to withdraw his consent.
- The member of OPC may at any time change the name of such other person by giving notice to the company and the company shall intimate the same to the Registrar.
- Any such change in the name of the person shall not be deemed to be an alteration of the memorandum.
- Only a natural person who is an Indian citizen whether resident in India or otherwise and has stayed in India for a period of not less than 120 days during the immediately preceding financial year.
    - shall be eligible to incorporate an OPC;
    - shall be a nominee for the sole member of an OPC.
- No person shall be eligible to incorporate more than one OPC or become nominee in more than one such company.
- No minor shall become member or nominee of the OPC or can hold share with beneficial interest.
- Such Company cannot be incorporated or converted into a company under section 8 of the Act. Though it may be converted to private or public companies in certain cases.
- Such Company cannot carry out Non-Banking Financial Investment activities including investment in securities of any body-corporate.
- If One Person Company or any officer of such company contravenes the provisions, they shall be punishable with fine which may extend to ten thousand rupees and with a further fine

which may extend to one thousand rupees for every day after the first during which such contravention continues.

Here the member can be the sole member-cum-director.

(c) Body corporate: Section 2(1)(d) of the LLP Act, 2008 provides that a LLP is a body corporate formed and incorporated under this Act and is a legal entity separate from that of its partners and shall have perpetual succession. Therefore, any change in the partners of a LLP shall not affect the existence, rights or liabilities of the LLP.

Section 3 of LLP Act, 2008, provides that a LLP is a body corporate formed and incorporated under this Act and is a legal entity separate from that of its partners.

Mutual Agency: No partner is liable on account of the independent or un-authorized actions of other partners, thus individual partners are shielded from joint liability created by another partner's wrongful business decisions or misconduct. In other words, all partners will be the agents of the LLP alone. No one partner can bind the other partner by his acts.

Foreign LLPs: Section 2(1)(m) defines foreign limited liability partnership "as a limited liability partnership formed, incorporated, or registered outside India which established as place of business within India". Foreign LLP can become a partner in an Indian LLP.

Artificial Legal Person: A LLP is an artificial legal person because it is created by a legal process and is clothed with all rights of an individual. It can do everything which any natural person can do, except of course that, it cannot be sent to jail, cannot take an oath, cannot marry or get divorce nor can it practice a learned profession like CA or Medicine. A LLP is invisible, intangible, immortal (it can be dissolved by law alone) but not fictitious because it really exists.

Question 3

(a) (i) P, Q and R formed a partnership agreement to operate motor buses along specific routes for a duration of 12 years. After operating the business for four years, it was observed that the business incurred losses each year. Despite this, P is determined to continue the business for the remaining Period. Examine with reference to the Indian Partnership Act, 1932, can P

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insist to continue the business? If so, what options are available to Q and R who are reluctant to continue operating the business? ***(4 Marks)***

(ii) *A and B operate a textile merchant business in partnership. Mr. A finances the business and is a sleeping partner. In the regular course of business, B acquires certain fabric goods belonging to C. However, B is aware that these goods are stolen property. Despite this knowledge, B proceeds to purchase and sell some of these stolen goods. Moreover, B records proceeds from these sales in the firm's books. Now, A wants to avoid the liability towards C, on the grounds of misconduct by B. In the light of the provisions of the Indian Partnership Act, 1932 discuss the liability of A and B towards C.* ***(3 Marks)***

(b) (i) *XYZ is a company incorporated under the Companies Act, 2013.*

The paid up share capital of the company is held by others as on 31.03.2024 in as under:

(1)	*Government of India*	*20%*
(2)	*Life Insurance Corporation of India (Public Institution)*	*8%*
(3)	*Government of Tamil Nadu*	*10%*
(4)	*Government of Rajasthan*	*10%*
(5)	*ABC Limited (owned by Government Company)*	*15%*

As per above shareholding, state whether XYZ limited be called a government company under the provisions of the Companies Act, 2013.

(4 Marks)

(ii) *M and N holding 70% and 30% of the shares in the company. Both died in an accident. Answer with reference to the provisions of the Companies Act, 2013, what will be the legal effect on the company as both the members have died?* ***(3 Marks)***

(c) *Explain in brief with reference to the provisions of the Indian Contract Act, 1872, what are the rights enjoyed by Surety against the Creditor, the Principal Debtor and Co-Sureties?* ***(6 Marks)***

Answer

(a) (i) Section 40 of the Indian Partnership Act, 1932, gives right to the partners to dissolve the partnership by agreement with the consent of

all the partners or in accordance with a contract between the partners. 'Contract between the partners' means a contract already made.

Also, according to section 44, the Court may, at the suit of a partner, may dissolve a firm on various grounds including where the business of the firm cannot be carried on except at a loss (in future also).

In the instant case, P wants to continue the partnership business despite the losses incurred over the past four years and Q and R are reluctant to continue operating the business due to continuous losses.

Here, P can insist on continuing the business if the partnership agreement does not specifically provide such a right to one or more partner / partners since Section 40 specifies that with the consent of all the partners or in accordance with a contract between the partners the firm can be dissolved.

Options available to Q and R

Mutual Agreement to Dissolve the Partnership: Q and R can propose to P that the partnership be dissolved by mutual agreement. If P agrees, the partnership can be dissolved amicably.

Dissolution by the Court: If P does not agree to dissolve the partnership mutually, Q and R can approach the court for an order under Section 44.

(ii) According to Section 25 of the Indian Partnership Act, 1932, every partner is jointly and severally liable for all acts of the firm done while he is a partner.

As per section 26, the firm is liable to the same extent as the partner for any wrongful act or omission of a partner while acting:

(a) in the ordinary course of the business of the firm, or

(b) with the authority of the partners.

Section 27 provides that the firm is liable if a partner, acting within the scope of his apparent authority, receives money or property from a third party and misapplies it, or if the firm in the course of its business receives money or property and the same is misapplied while it is in the custody of the firm.

In the instant case, both A and B are liable to C for the wrongful acts committed by B. A cannot avoid liability merely on the grounds of being a sleeping partner.

(b) (i) Under the Companies Act, 2013, a Government company is defined in Section 2(45) as a company in which not less than 51% of the paid-up share capital is held by:

- The Central Government, or
- Any State Government or Governments, or
- Partly by the Central Government and partly by one or more State Governments,

And includes a company which is a subsidiary company of such a Government company.

In the instant case, total Government Shareholding is 40% [i.e. 20% (Government of India) + 10% (Government of Tamil Nadu) + 10% (Government of Rajasthan)] = 40%

The holding of the Life Insurance Corporation of India i.e. 8% and ABC Limited i.e. 15%, total amounting to 23% cannot be taken into account while counting the prescribed limit of 51%.

Since the total shareholding held by the Central Government and State Governments combined is 40%, which is less than 51%, XYZ Limited does not qualify to be a Government company under the provisions of the Companies Act, 2013.

(ii) **One of the features of a company is that it has perpetual succession.** As per this feature, members may die or change, but the company goes on till it is wound up on the grounds specified by the Companies Act, 2013. The shares of the company may change hands infinitely but that does not affect the existence of the company. Since a company is an artificial person created by law, law alone can bring an end to its life. Its existence is not affected by the death or insolvency of its members.

In the instant case, on the death of M and N, who are holding 70% and 30% shares in the Company, the existence of the company is not

affected, since the shares held by M and N will be legally transmitted to their legal heirs.

(c) In terms of the provisions of the Indian Contract Act, 1872, the surety enjoys the following rights:

(a) Rights against the creditor;

(b) Rights against the principal debtor;

(c) Rights against co-sureties.

Right against the Creditor

(a) Surety's right to benefit of creditor's securities [Section 141]: 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 such security or not; and, if the creditor loses, or, without the consent of the surety, parts with such security, the surety is discharged to the extent of the value of the security.

(b) Right to set off: If the creditor sues the surety, for payment of principal debtor's liability, the surety may have the benefit of the set off, if any, that the principal debtor had against the creditor.

(c) Right to share reduction: The surety has right to claim proportionate reduction in his liability if the principal debtor becomes insolvent.

Right against the principal debtor

(a) Rights of subrogation [Section 140 of the Indian Contract Act, 1872]: Where, a guaranteed debt has become due, or default of the principal debtor to perform a guaranteed duty has taken place, the surety, upon payment or performance of all that he is liable for, is invested with all the rights which the creditor had against the principal debtor.

This right is known as right of subrogation. It means that on payment of the guaranteed debt, or performance of the guaranteed duty, the surety steps into the shoes of the creditor.

(b) Implied promise to indemnify surety [Section 145]: In every contract of guarantee there is an implied promise by the principal

debtor to indemnify the surety. The surety is entitled to recover from the principal debtor whatever sum he has rightfully paid under the guarantee, but not sums which he paid wrongfully.

Rights against co-sureties

"Co-sureties (meaning)- When the same debt or duty is guaranteed by two or more persons, such persons are called co-sureties"

(a) **Co-sureties liable to contribute equally (Section 146):** Unless otherwise agreed, each surety is liable to contribute equally for discharge of whole debt or part of the debt remains unpaid by debtor.

(b) **Liability of co-sureties bound in different sums (Section 147):** The principal of equal contribution is, however, subject to the maximum limit fixed by a surety to his liability. Co-sureties who are bound in different sums are liable to pay equally as far as the limits of their respective obligations permit.

Question 4

(a) (i) Mr. J entered into an agreement with Mr. S to purchase his house for ₹ 20 lakh, within three months. He also paid ₹ 50,000/- as token money. In the meanwhile, in an anti-encroachment drive of the local administration, Mr. S's house was demolished. When Mr. J was informed about the incident he asked for the refund of token money.

Referring to the relevant provisions of the Indian Contract Act, 1872 state whether Mr. J is entitled to the refund of the amount paid.

(4 Marks)

(ii) Rama directs Shyam to sell laptops for him and agrees to give Shyam eleven percent (11%) commission on the sale price fixed by Rama for each laptop. As Government of India put restrictions on import of Laptops, Rama thought that the prices of laptops might go up in near future and he revokes Shyam's authority for any further sale. Shyam, before receiving the letter at his end sold 5 laptops at the price fixed by Rama. Shyam asked for 11% commission on the sale of 5 Laptops for ₹ 1 lakh each. Explain under the provisions of the Indian Contract Act, 1872:

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(1) *Whether sale of laptops after revoking Shyam's authority is binding on Rama?*

(2) *Whether Shyam will be able to recover his commission from Rama, if yes, what will be the amount of such commission?* ***(3 Marks)***

(b) *A promissory note, payable at a certain period after sight, must be presented to the maker thereof for payment. Under which scenarios presentment for payment is not necessary and the instrument is dishonoured at the due date for presentment according to the provisions of the Negotiable Instrument Act. 1881?* ***(7 Marks)***

(c) *Describe in brief about the following Regulatory bodies of the Government of India: -*

(i) *Securities and Exchange Board of India*

(ii) *Reserve Bank of India*

(iii) *Insolvency and Bankruptcy Board of India* ***(6 Marks)***

Answer

(a) (i) According to section 56 of the Indian Contract Act, 1872, an agreement to do an act impossible in itself is void.

Contract to do act afterwards becoming impossible or unlawful: 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.

According to section 65 of the Indian Contract Act, 1872, 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.

In the instant case, Mr. J entered into a contract with Mr. S to purchase his house for ₹ 20 lakh, with a token payment of ₹ 50,000. The agreement included a condition that the sale would be completed within three months. Before the completion of the sale, the house was demolished by the local administration. This event made it impossible for Mr. S to sell the house to Mr. J as agreed.

In this situation, Mr. J is required to refund ₹ 50,000 token money paid to Mr. S, as the contract to sell the house has become void due to the demolition of the house by the local administration, as a result of which it becomes impossible to sell the house on the part of S.

(ii) **When termination of agent's authority takes effect as to agent, and as to third persons [Section 208 of the Indian Contract Act, 1872]:** The termination of the authority of an agent does not, so far as regards the agent, take effect before it becomes known to him, or, so far as regards third persons, before it becomes known to them.

In the instant case,

(1) The revocation of Shyam's authority becomes effective only when it is communicated to and received by Shyam. Since Shyam had not received the revocation letter at the time of selling the laptops, his authority to sell on behalf of Rama was still valid. Hence, the sale of laptops conducted by Shyam is binding on Rama.

(2) Shyam is entitled to receive his commission for the sales made while he still had the authority to sell. Since he sold the laptops before receiving the revocation, he is entitled to his commission as per the initial agreement with Rama.

Amount of Commission: Shyam sold 5 laptops at the price fixed by Rama, which is ₹1 lakh each. The total sales amount to ₹5 lakh. The agreed commission rate is 11% i.e. ₹ 55,000.

(b) As per Section 76 of the Negotiable Instruments Act, 1881:

No presentment for payment is necessary, and the instrument is dishonoured at the due date for presentment, in any of the following cases:

(a) (i) If the maker, drawee or acceptor intentionally prevents the presentment of the instrument, or

(ii) if the instrument being payable at his place of business, he closes such place on a business day during the usual business hours, or

(iii) if the instrument being payable at some other specified place, neither he nor any person authorised to pay it attends at such place during the usual business hours, or

(iv) if the instrument not being payable at any specified place, he cannot after due search be found;

(b) as against any party sought to be charged therewith, if he has engaged to pay notwithstanding non-presentment;

(c) as against any party if, after maturity, with knowledge that the instrument has not been presented—

- he makes a part payment on account of the amount due on the instrument,
- or promises to pay the amount due thereon in whole or in part,
- or otherwise waives his right to take advantage of any default in presentment for payment;

(d) as against the drawer, if the drawer could not suffer damage from the want of such presentment.

(c) (i) The Securities and Exchange Board of India (SEBI):

- It is the regulatory body
- for securities and commodity market in India
- under the ownership of Ministry of Finance within the Government of India.
- It was established on 12 April, 1988 as an executive body and was given statutory powers on 30 January, 1992 through the SEBI Act, 1992.

(ii) Reserve Bank of India (RBI):

- It is India's Central Bank and regulatory body responsible for regulation of the Indian banking system.
- It is under the ownership of Ministry of Finance, Government of India.
- It is responsible for the control, issue and maintaining supply of the Indian rupee.
- It also manages the country's main payment systems and works to promote its economic development.

- Bharatiya Reserve Bank Note Mudran (BRBNM) is a specialised division of RBI through which it prints and mints Indian currency notes (INR) in two of its currency printing presses located in Nashik (Western India) and Dewas (Central India).
- RBI established the National Payments Corporation of India as one of its specialised division to regulate the payment and settlement systems in India.
- Deposit Insurance and Credit Guarantee Corporation was established by RBI as one of its specialised division for the purpose of providing insurance of deposits and guaranteeing of credit facilities to all Indian banks.

(iii) Insolvency and Bankruptcy Board of India (IBBI)-

- It is the regulator for overseeing insolvency proceedings and entities like Insolvency Professional Agencies (IPA), Insolvency Professionals (IP) and Information Utilities (IU) in India.
- It was established on 1 October 2016 and given statutory powers through the Insolvency and Bankruptcy Code, which was passed by Lok Sabha on 5th May 2016.
- It covers Individuals, Companies, Limited Liability, Partnerships and Partnership firms. The new code will speed up the resolution process for stressed assets in the country.
- It attempts to simplify the process of insolvency and bankruptcy proceedings.
- It handles the cases using two tribunals like NCLT (National Company Law Tribunal) and Debt Recovery Tribunal.

Question 5

(a) PTC Hotels in Bombay decided to sell their furniture by auction sale. For this purpose, they appointed RN & Associates as auctioneer. They invited top ten renowned Architects in Bombay for bidding. A right to bid was not notified by them. Furniture was put up in lots for sale. It was decided that for every lot of furniture there will be a reserve price. On 25th Feb 2024, Auction sale was started at 10.am in the lawn of PTC Hotels Bombay. For a

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special lot of furniture three parties came for bidding Mr. Neel, Mr. Raj and Mr. Dev on behalf of their respective companies. Bidding was as follows:

Mr. Neel	*₹5.70 lakh*
Mr. Raj	*₹4.85 lakh*
Mr. Dev	*₹6.10 lakh*

The sale was completed in favour of Mr. Neel by RN & Associates by fall of hammer. Mr. Dev's Bid was rejected on ground that Right to bid was reserved and company of Mr. Dev was not invited to bid.

For another bid of Italian Furniture was made by two parties as follows:

Mr. Dheer	*₹15 lakh*
Mr. Madhu (on behalf of R N & Associates)	*₹15.20 lakh*

Sale was completed in favour of Mr. Dheer instead of Mr. Madhu.

Mr. Dev and Mr. Madhu argued that auction sale was not lawful. Give your opinion with reference to provisions of the Sale of Goods Act, 1930 whether Auction Sale will be considered lawful or not? ***(7 Marks)***

(b) "Dissolution of partnership doesn't mean dissolution of firm". Do you agree with this statement? State any three situations where court can dissolve the partnership firm. ***(7 Marks)***

(c) Where a party to a contract refuses altogether to perform, or is disabled from performing his part of it, the other party has a right to rescind it. Discuss this statement and the effects of such refusal under the provisions of The Indian Contract Act, 1872. ***(6 Marks)***

Answer

(a) An 'Auction Sale' is a mode of selling property by inviting bids publicly and the property is sold to the highest bidder. Section 64 of the Sale of Goods Act, 1930 regulates the legal requirements for the sale by auction.

In terms of the provisions of the above Section, following are some of the requirements, which *inter alia* are required to be complied with for conduct of a valid auction sale-

(i) Where the goods are sold in lots: Where the goods are put up for sale in lots, each lot is *prima facie* deemed to be subject of a separate contract of sale.

(ii) Right to bid may be reserved: Right to bid may be reserved expressly by or on behalf of the seller and where such a right is expressly reserved, but not otherwise, the seller or any one person on his behalf may bid at the auction.

(iii) Where the sale is not notified by the seller: Where the sale is not notified to be subject to a right to bid on behalf of the seller, it shall not be lawful for the seller to bid himself or to employ any person to bid at such sale, or for the auctioneer knowingly to take any bid from the seller or any such person; and any sale contravening this rule may be treated as fraudulent by the buyer.

(iv) Reserved price: The sale may be notified to be subject to a reserve or upset price;

In the first Auction sale, the rejection of Mr. Dev's bidding was not justified since the information as to the right to bid was not expressly given. Therefore, this auction sale was unlawful.

In auction sale of lot 2, since right to bid was not notified, it shall not be lawful for the seller to bid himself or to employ any person to bid at such sale. Therefore, auction made in favour of Mr. Dheer will be considered lawful.

(b) Dissolution of partnership doesn't mean dissolution of firm. According to Section 39 of the Indian Partnership Act, 1932, the dissolution of partnership between all partners of a firm is called the 'dissolution of the firm'.

Thus, the dissolution of firm means the discontinuation of the legal relation, the dissolution of firm means the discontinuation of the legal relation existing between all the partners of the firm. But when only one or more partners retires or becomes incapacitated from acting as a partner due to death, insolvency or insanity, the partnership, the relationship between such a partner and other is dissolved, but the rest may decide to continue.

In such cases, there is in practice, no dissolution of the firm. The particular partner goes out, but the remaining partners carry on the business of the firm, it is called dissolution of partnership. In the case of dissolution of the firm, on the other hand, the whole firm is dissolved. The partnership terminates as between each and every partner of the firm.

Important note: Different mode of presentation to an answer

Dissolution of partnership doesn't mean dissolution of firm. This statement can be proved with the help of some points of distinction between both of them, which are as follows:

Dissolution of Firm Vs. Dissolution of Partnership

S. No.	Basis of Difference	Dissolution of Firm	Dissolution of Partnership
1.	**Continuation of business**	It involves discontinuation of business in partnership.	It does not affect continuation of business. It involves only reconstitution of the firm.
2.	**Winding up**	It involves winding up of the firm and requires realization of assets and settlement of liabilities.	It involves only reconstitution and requires only revaluation of assets and liabilities of the firm.
3.	**Order of court**	A firm may be dissolved by the order of the court.	Dissolution of partnership is not ordered by the court.
4.	**Scope**	It necessarily involves dissolution of partnership.	It may or may not involve dissolution of firm.
5.	**Final closure of books**	It involves final closure of books of the firm.	It does not involve final closure of the books of the firm.

SUGGESTED ANSWER

BUSINESS LAWS

Dissolution By the Court (Section 44 of the Indian Partnership Act, 1932):

Court may, at the suit of the partner, dissolve a firm on any of the following grounds:

(a) **Insanity/unsound mind:** Where a partner (not a sleeping partner) has become of unsound mind, the court may dissolve the firm on a suit of the other partners or by the next friend of the insane partner. Temporary sickness is no ground for dissolution of firm.

(b) **Permanent incapacity:** When a partner, other than the partner suing, has become in any way permanently incapable of performing his duties as partner, then the court may dissolve the firm. Such permanent incapacity may result from physical disability or illness etc.

(c) **Misconduct:** Where a partner, other than the partner suing, is guilty of conduct which is likely to affect prejudicially the carrying on of business, the court may order for dissolution of the firm, by giving regard to the nature of business. It is not necessary that misconduct must relate to the conduct of the business. The important point is the adverse effect of misconduct on the business. In each case nature of business will decide whether an act is misconduct or not.

(d) **Persistent breach of agreement:** Where a partner other than the partner suing, wilfully or persistently commits breach of agreements relating to the management of the affairs of the firm or the conduct of its business, or otherwise so conduct himself in matters relating to the business that it is not reasonably practicable for other partners to carry on the business in partnership with him, then the court may dissolve the firm at the instance of any of the partners. Following comes in to category of breach of contract:

- Embezzlement,
- Keeping erroneous accounts
- Holding more cash than allowed
- Refusal to show accounts despite repeated request etc.

(e) **Transfer of interest:** Where a partner other than the partner suing, has transferred the whole of his interest in the firm to a third party or has allowed his share to be charged or sold by the court, in the recovery of arrears of land revenue due by the partner, the court may dissolve the firm at the instance of any other partner.

(f) **Continuous/Perpetual losses:** Where the business of the firm cannot be carried on except at a loss in future also, the court may order for its dissolution.

(g) **Just and equitable grounds:** Where the court considers any other ground to be just and equitable for the dissolution of the firm, it may dissolve a firm. The following are the cases for the just and equitable grounds-

(i) Deadlock in the management.

(ii) Where the partners are not in talking terms between them.

(iii) Loss of substratum.

(iv) Gambling by a partner on a stock exchange.

(c) An anticipatory breach of contract is a breach of contract occurring before the time fixed for performance has arrived. When the promisor refuses altogether to perform his promise and signifies his unwillingness even before the time for performance has arrived, it is called Anticipatory Breach.

Anticipatory breach of a contract may take either of the following two ways:

(a) Expressly by words spoken or written, and

(b) Impliedly by the conduct of one of the parties.

Section 39 of the Indian Contract Act deals with anticipatory breach of contract and provides as follows:

"When a party to a contract has refused to perform or disable himself from performing, his promise in its entirety, the promisee may put an end to the contract, unless he has signified, but words or conduct, his acquiescence in its continuance."

Effect of anticipatory breach: The promisee is excused from performance or from further performance. Further he gets an option:

(1) To either treat the contract as "rescinded and sue the other party for damages from breach of contract immediately without waiting until the due date of performance;

or

(2) He may elect not to rescind but to treat the contract as still operative and wait for the time of performance and then hold the other party responsible for the consequences of non-performance. But in this case, he will keep the contract alive for the benefit of the other party as well as his own, and the guilty party, if he so decides on re-consideration, may still perform his part of the contract and can also take advantage of any supervening impossibility which may have the effect of discharging the contract.

Question 6

(a) Mr. Y issued a cheque for ₹ 10,000 to Mr. Z which was dishonoured by the Bank because Y did not have enough funds in his account and has no authority to overdraw. Examine as per the provisions of the Negotiable Instruments Act, 1881 whether-

(i) Mr. Y is liable for dishonour of cheque, if yes, what are the consequences for such an offence?

(ii) What would be your answer if Y issued a cheque as a donation to Mr. Z? ***(7 Marks)***

(b) Explain the term Wagering agreement in the light of the Indian Contract Act, 1872. Also, explain some transactions resembling with wagering transaction but which are not void.

OR

(b) What is the meaning of contingent contract? Write briefly its essentials. Also, explain any three rules relating to enforcement of a contingent contract. ***(6 Marks)***

(c) J, a wholesaler of premium Basmati rice delivered on approval 100 bags of rice of 10 kg each to a local retailer, on sale or returnable basis within a month of delivery. The next day the retailer sold 5 bags of rice to a regular customer K. A week later K informed the retailer that the quality of rice was not as per the price.

SUGGESTED ANSWER

FOUNDATION EXAMINATION: JUNE 2024

The retailer now wants to return all the rice bags to J, including the 4 bags not used by K. Can the retailer do so?

Also briefly describe the provisions underlying in this context of the Sale of Goods Act, 1930, ***(7 Marks)***

Answer

(a) Dishonour of Cheque for Insufficiency, Etc., of funds in the accounts [Section 138 of the Negotiable Instruments Act, 1881]

Where any cheque drawn by a person on an account maintained by him with a banker—

- for payment of any amount of money
- to another person from that account
- for the discharge, in whole or in part, of any debt or other liability, [A cheque given as gift or donation, or as a security or in discharge of a mere moral obligation, or for an illegal consideration, would be outside the purview of this section]
- is returned by the bank unpaid,
- either because of the—
    - amount of money standing to the credit of that account is insufficient to honour the cheque, or
    - that it exceeds the amount arranged to be paid from that account by an agreement made with that bank,

such person shall be deemed to have committed an offence and shall, be punished with imprisonment for a term which may extend to two years, or with fine which may extend to twice the amount of the cheque, or with both.

In the instant case,

(i) Since Y's cheque was dishonoured by the Bank due to insufficiency of funds in his account, he shall be deemed to have committed an offence and shall, be punished with imprisonment for a term which may extend to two years, or with fine which may extend to Rs. 20,000, or with both.

(ii) A cheque given as gift or donation, or as a security or in discharge of a mere moral obligation, or for an illegal consideration, would be outside the purview of this section. Hence, if Y issued a cheque as a donation to Mr. Z, he shall not be liable under section 138 of the Act.

(b) Wagering agreement (Section 30 of the Indian Contract Act, 1872): An agreement by way of a wager is void. It is an agreement involving payment of a sum of money upon the determination of an uncertain event. The essence of a wager is that each side should stand to win or lose, depending on the way an uncertain event takes place in reference to which the chance is taken and in the occurrence of which neither of the parties has legitimate interest.

Transactions resembling with wagering transaction but are not void

(i) **Chit fund:** Chit fund does not come within the scope of wager (Section 30). In case of a chit fund, a certain number of persons decide to contribute a fixed sum for a specified period and at the end of a month, the amount so contributed is paid to the lucky winner of the lucky draw.

(ii) **Commercial transactions or share market transactions**: In these transactions in which delivery of goods or shares is intended to be given or taken, do not amount to wagers.

(iii) **Games of skill and Athletic Competition**: Crossword puzzles, picture competitions and athletic competitions where prizes are awarded on the basis of skill and intelligence are the games of skill and hence such competitions are valid.

(iv) **A contract of insurance:** A contract of insurance is a type of contingent contract and is valid under law and these contracts are different from wagering agreements.

OR

(b) Essentials of a contingent contract

(a) The performance of a contingent contract would depend upon the happening or non-happening of some event or condition. The condition may be precedent or subsequent.

(b) The event referred to as collateral to the contract. The event is not part of the contract. The event should be neither performance promised nor a consideration for a promise.

(c) The contingent event should not be a mere 'will' of the promisor. The event should be contingent in addition to being the will of the promisor.

(d) The event must be uncertain. Where the event is certain or bound to happen, the contract is due to be performed, then it is a not contingent contract.

Definition of 'Contingent Contract' (Section 31 of the Indian Contract Act, 1872)

"A contract to do or not to do something, if some event, collateral to such contract, does or does not happen".

Rules Relating to Enforcement of a contingent contract:

The rules relating to enforcement of a contingent contract are laid down in **sections 32, 33, 34, 35 and 36 of the Act.**

(a) **Enforcement of contracts contingent on an event happening:** Section 32 says that "where a contingent contract is made to do or not to do anything if an uncertain future event happens, it cannot be enforced by law unless and until that event has happened. If the event becomes impossible, such contracts become void".

(b) **Enforcement of contracts contingent on an event not happening:** Section 33 says that "Where a contingent contract is made to do or not do anything if an uncertain future event does not happen, it can be enforced only when the happening of that event becomes impossible and not before".

(c) **A contract would cease to be enforceable if it is contingent upon the conduct of a living person when that living person does something to make the 'event' or 'conduct' as impossible of happening.**

Section 34 says that "if a contract is contingent upon as to how a person will act at an unspecified time, the event shall be considered to have become impossible when such person does anything which

renders it impossible that he should so act within any definite time or otherwise than under further contingencies".

(d) **Contingent on happening of specified event within the fixed time:** Section 35 says that Contingent contracts to do or not to do anything, if a specified uncertain event happens within a fixed time, becomes void if, at the expiration of time fixed, such event has not happened, or if, before the time fixed, such event becomes impossible.

(e) **Contingent on specified event not happening within fixed time:** Section 35 also says that - "Contingent contracts to do or not to do anything, if a specified uncertain event does not happen within a fixed time, may be enforced by law when the time fixed has expired, and such event has not happened or before the time fixed has expired, if it becomes certain that such event will not happen".

(f) **Contingent on an impossible event (Section 36):** Contingent agreements to do or not to do anything, if an impossible event happens are void, whether the impossibility of the event is known or not to the parties to the agreement at the time when it is made.

(c) According to Section 24 of the Sales of Goods Act, 1930, in case of delivery of goods on approval basis, the property in goods passes from seller to the buyer:-

(i) When the person to whom the goods are given either accepts them or does an act which implies adopting the transaction.

(ii) When the person to whom the goods are given retains the goods without giving his approval or giving notice of rejection beyond the time fixed for the return of goods and in case no time is fixed after the lapse of reasonable time.

In the given case, J (seller) has delivered on approval 100 bags of rice of 10 kg each to local retailer (buyer) on sale or returnable basis within a month of delivery. Out of these 100 bags, the local retailer sold 5 bags to K (customer). It implies that the local retailer has accepted 5 bags out of 100.

SUGGESTED ANSWER

FOUNDATION EXAMINATION: JUNE 2024

A week later, local retailer received the complaint of some defect in the rice bags, so, he wanted to return all the bags to the J (seller).

According to the above provisions, the local retailer is entitled to return only 95 bags to the J (seller) and not those 4 bags which are not used by K. Because, as per clause (i) above, the local retailer has already sold 5 bags, signifying that he has done an act which implies adopting the transaction relating to those 5 bags.