

BA4105

LEGAL ASPECTS OF BUSINESS

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COURSE OBJECTIVE:

□ The objective of this course is to familiarize the students with various laws that will help them to refine their understanding of how law affects the different aspects of business.

UNIT I COMMERCIAL LAW

9

THE INDIAN CONTRACT ACT 1872

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

THE SALE OF GOODS ACT 1930 Nature of Sales contract, Documents of title, risk of loss, Guarantees and Warranties, performance of sales contracts, conditional sales and rights of an unpaid seller -

NEGOTIABLE INSTRUMENTS ACT 1881: Nature and requisites of negotiable instruments. Types of negotiable instruments, liability of parties, holder in due course, special rules for Cheque and drafts, discharge of negotiable instruments.

UNIT II COMPANY LAW AND COMPETITION ACT

9

COMPANY ACT 1956&2013 Major principles – Nature and types of companies, Formation, Memorandum and Articles of Association, Prospectus, Power, duties and liabilities of Directors, winding up of companies, Corporate Governance.

Competition Act 2002 - Introduction, Definitions, Enquiry into Certain Agreements and Dominant Position of Enterprise and Combinations.

UNIT III INDUSTRIAL LAW

9

An Overview of Factories Act - Payment of Wages Act - Payment of Bonus Act - Industrial Disputes Act.

UNIT IV CORPORATE TAX & GST

9

Corporate Tax Planning, Corporate Taxes and Overview of Latest Developments in Indirect tax Laws relating to GST:An introduction including constitutional aspects, Levy and collection of CGST & IGST, Basic concept of time and value of supply, Input tax credit, Computation of GST Liability, Registration, Tax Invoice, Credit & Debit Notes, Electronic Way bill, Returns, Payment of taxes including Reverse Charge

UNIT V CONSUMER PROTECTION ACT AND INTRODUCTION OF CYBER LAWS

9

Consumer Protection Act – Consumer rights, Procedures for Consumer grievances redressal, Types of consumer Redressal Machineries and Forums-- Cyber crimes, IT Act 2000 and 2002,Cyber Laws, Introduction of IPR Intellectual Property Laws- Introduction, Legal Aspects of Patents, Filing of Patent Applications, Rights from Patents, Infringement of Patents, Copyright and its Ownership, Infringement of Copyright, Civil Remedies for Infringement.– Copy rights, Trade marks, Patent Act. Introduction, Right to Information Act, 2005.

TOTAL: 45 PERIODS

COURSE OUTCOMES:

1. Understand the fundamental legal principles in developing various contracts and commercial laws in the business world
2. Identify the common forms of business associations and elements of Corporate Governance
3. Develop insights regarding the laws related to industrial environment
4. Ability to understand the fundamentals of corporate tax and GST
5. Understand the role of consumer rights and cyber laws in the modern business environment



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UNIT-1

COMMERCIAL LAW

Business Law is a wide term and embraces all legal principles concerning business transactions. It is also known as the 'Commercial Law', 'Law Merchant' or 'Mercantile Law'.

Business Law consists of those legal rules, which govern and regulate the business activities, transactions and trade. It also encompasses the law relating to regulation of business associations and other incidental matters.

Definition

According to S R Davar, business law "means that branch of law which is applicable to or concerned with trade and commerce in connection with various mercantile or business transactions".

Scope of Business Law

The following legislation enacted by Indian Legislature from time to time is covered in the Indian Business Laws:

- a) The Indian Contract Act, 1872.
- b) The Negotiable Instruments Act, 1881.
- c) The Sale of Goods Act, 1930.
- d) The Indian Partnership Act, 1932.
- e) The Insurance Act, 1972.
- f) The Arbitration & Conciliation Act, 1996.
- g) The Law of Insolvency.
- h) Law Relating to Carriage of Goods.

Sources of Business Law

The main sources of Indian Business Law are as follows:

- a) **The English Mercantile Law** [Common Laws, Equity, Roman Laws and Case Laws],
- b) **Statutes of the Indian Legislature** [Supreme and Subordinate Legislation],
- c) **Judicial Decisions & Precedents** [Declaratory, Persuasive, Absolutely Authoritative & Conditionally Authoritative Precedents],
- d) **Customs and Usage.**

THE INDIAN CONTRACT ACT, 1872

In India, the law relating to contracts is contained in the INDIAN CONTRACT ACT, 1872. The Act came into force on the 1st day of September 1872, and it applies to the whole of India except the State of Jammu and Kashmir. The act does not deal with all the branches of law of contracts. The contracts relating to Partnership, Sale of Goods Act and Negotiable Instruments Act are outside the scope of the Indian Contract Act. The Indian Contract Act deals with:

1. The general principles applicable to all contracts;
2. The conditions, which are essential for making a valid contract;
3. The principles applicable to quasi contracts;
4. The principles, which are applicable to a few special contracts, namely,
 - a) *The contracts of indemnity,*
 - b) *The contracts of guarantee,*
 - c) *The contracts of bailment and agency,*
 - d) *The contracts of agency.*

The law of contracts deals with agreements, which can be enforced through law courts. Law of contracts is the most important branch of mercantile law. It affects every person in one way or the other, as all of us enter into some kind of contract everyday. The object of the law of contracts is to introduce definiteness in commercial and other transactions, and to ensure the realization of reasonable expectation of the parties, who enter into a contract.

CONTRACT

The word contract is derived from the Latin word “contractum” which means “drawn together”. It denotes a drawing together the minds of two or more persons to form a common intention giving rise to an agreement. A contract is an agreement enforceable by law, which offers personal rights and imposes personal obligations, which the law protects and enforces against the parties to the agreement.

DEFINITION

Section 2 (h) of the Indian Contract Act defines a contract as “an agreement enforceable by law”.

Therefore, a contract essentially consists of two elements:

1. **Agreement:** Section 2 (e) defines an agreement as, “*every promise and every set of promises forming the consideration for each other*”. In other words, an agreement is formed where one party makes the proposal and the other party accepts it.
2. **Enforceability:** Only an enforceable agreement can be called a contract. Section 10 of the Act defines “*All agreements are contracts if they are made by the free consent of parties competent to contract, for a lawful consideration and a lawful object, and are not hereby expressly declared to be void*”.

Sir William Anson observes, “A contract is an agreement enforceable at law made between two or more persons, by whom rights are acquired by one or more to acts or forbearances on the part of the other or others”.

ESSENTIAL ELEMENTS OF A VALID CONTRACT

The following are the essential elements of a contract, arrived at on the basis of a combined reading of Section 2(h) and Section 10 of the Indian Contract Act:

1. **Offer and Acceptance:** There must be a ‘lawful offer’ and ‘lawful acceptance’ of the offer, thus resulting in an agreement.

For example: If X offers to sell his Maruti Car to Y for Rs. 2,25,000 and Y agrees to pay X Rs. 2,25,000 for the Maruti Car. Here X is called the offeror or promisor and Y is the offeree or promisee.

2. **Consensus ad idem:** For a valid agreement, there must be a complete identity of minds between the contracting parties.

For example: A has two buffaloes but B is aware of only one of these. B proposes to buy the buffalo of which he is aware. A's Consents to sell the other buffalo. Since there is confusion in the minds of the parties, there is no consensus and hence no agreement follows.

3. **Free Consent:** The contracting parties must give their consent freely. It must not be given due to coercion, undue influence, fraud, misrepresentation or mistake. The absence of free consent would affect the legal enforceability of a contract.

For example: An illiterate woman executes a deed of gift under the impression that she is executing a deed authorizing her nephew to manage her agricultural land. The deed is not read or explained to her. Here, there is no consent, therefore no contract.

4. **Capacity of the parties:** The parties making the contract must be legally competent in the sense that each must be of the age of majority, of a sound mind, and not expressly disqualified from contracting (Section 11). An agreement by incompetent parties shall be a legal nullity.

For example: A, a minor, borrows Rs. 5,000 from B and executes a promissory note in B's favour. After attaining majority A executes a fresh promissory note in favour of B for this amount. B cannot sue on this promissory note as the agreement is void for lack of consideration.

5. **Lawful Consideration:** An agreement to be enforceable by law must be supported by consideration. Without consideration, a contract is regarded as a nudum pactum. Each of the contracting parties must give as well as get something. Moreover, the consideration must be lawful.

For example: X lets his house for being used as a gambling den. The agreement is illegal as the object of agreement is unlawful.

6. **Lawful object:** The object of the agreement must be lawful. It is considered unlawful if it is (i) illegal (ii) immoral, (iii) fraudulent, (iv) of a nature that, if permitted, it would defeat the provisions of any law, (v) causes injury to the person or property of another, or (vi) opposed to public policy.

For example: A promises to obtain a job for B in government service in consideration of Rs. 50,000. The agreement is void because it is forbidden by law.

7. **Not expressly declared void:** The agreement must not have been declared void by any law in force in India. The Act has itself declared void certain types of agreements such as those in restraint of marriage, or trade, or legal proceedings as well as wagering agreements.

8. **Intention to create legal relations:** There must be an intention among the parties that the agreement should be attached by legal consequences and create legal obligations.

For example: A wife withdraws a complaint against her husband under an agreement that husband will pay her allowance. Court held it as a binding contract.

9. **Certainty of meaning:** The terms of the agreement must be certain and unambiguous. Section 29 of the Act, “agreements the meaning of which is not certain or capable of being made certain are void”.

For example: A agrees to sell a car to B out of his 5 cars. There is nothing whatever to show which car was intended. The agreement is void for uncertainty.

10. **Legal formalities:** The agreement must comply with the necessary formalities as to writing, registration, stamping etc. if any required in order to make it enforceable by law.

CLASSIFICATION OF CONTRACTS

Section of the Act, which is called the ‘interpretation clause’, besides defining a contract in clause (h), also provides the basis for the classification of contracts.

Contracts may be classified as follows:

1. On the basis of Enforceability

a) **Valid Contract:** A contract which satisfies all the legal requirements laid down in Section 10 of the Act, is a valid contract. Such a contract creates rights in personem and is legally enforceable.

b) **Void Agreement:** Section 2(g) defines it as, “an agreement not enforceable by law is said to be void”. Such agreements are void ab initio which means that they are unenforceable right from the time they are made.

For example: X agrees with Y, in consideration of Rs. 100, to draw two parallel lines in such a way as to cross each other. The agreement is impossible to perform and, therefore void.

c) **Void Contract:** Section 2(j) provides that "a contract which ceases to be enforceable by law becomes void when it ceases to be enforceable." Following are the examples of such circumstances which render a contract void:

(i) Supervening impossibility or illegality as described in Section 56.

(ii) In the case of a voidable contract when the party whose consent is not free, repudiates the contract.

(iii) A contingent contract to do or not to do something on the happening of an event becomes void when the event becomes impossible (Section 32).

For Example: A agrees to sell 1000 tonnes of wheat to B @ Rs. 500 per tonne in case his ship reaches the port safely by 15th February. The ship fails to reach by the stipulated date. The contract between A and B is void.

d) **Voidable Contract:** According to Section 2(i), "An agreement which is enforceable by law at the option of one or more of the parties thereto, but not at the option of other or others, is a voidable contract."

In a voidable contract, a right or option is open to the aggrieved party i.e., the party whose consent is not free that either to repudiate the contract or to abide by it. Thus, a voidable contract continues to be valid and enforceable till it is repudiated by the aggrieved party.

For example: A threatens to kill B if he does not give him a loan of Rs. 50,000 for 25 years. B gives the loan. This is a voidable contract as consent of B is obtained by coercion.

- e) **Illegal agreement:** An agreement which is either prohibited by law or otherwise against the policy of law is an illegal agreement. Such an agreement is a nullity and is void ab initio.
- f) **Unenforceable Contract:** An unenforceable contract is that which is valid and enforceable, but for certain technical defects such as want of proof, expiry of the period within which enforceable, absence of writing, registration and attestation, insufficient stamp etc., it becomes unenforceable.

For example: If a document embodying a contract is understamped, the contract is unenforceable, but if the requisite stamp is affixed (if allowed), the contract becomes enforceable.

2. On the basis of mode of creation

- a) **Express Contract:** An express contract is that which is made in writing or by the words of mouth.

For example: A writes to B, 'I am prepared to sell my horse for a sum of Rs. 500. B accepts A's offer by a telegram. The contract will be termed as express contract.

- b) **Implied Contract:** An implied contract is one which arises out of acts or conduct of the parties or out of the dealings between them.

For example: A takes a seat in a bus. There is an implied contract that he will pay the prescribed fare for taking him to his destination.

- c) **Quasi Contract:** Under certain circumstances, law itself creates legal rights and obligations against the parties. These obligations are known as quasi contracts.

For example: A supplies B, a lunatic with necessaries suitable to his condition in life. A is entitled to be reimbursed from B's property.

3. On the basis of execution

- a) **Executed Contract:** When a contract has been completely performed, it is termed as executed contract, i.e., it is a contract where, under the terms of a contract, nothing remains to be done by either party.

For example: X sells a radio set to Y for Rs. 300. Y pays the price. Both the parties have performed their respective obligations, and therefore, it is an executed contract.

- b) **Executory Contract:** Where one or both the parties to the contract have still to perform their obligations in future, the contract is termed as executory contract.

For example: A agrees to paint a picture for B and B in consideration promises to pay A a sum of rupees one hundred. The contract is executory.

- c) **Unilateral Contract:** A unilateral contract is one sided contract in which only one party has to perform his promise or obligation to do or forbear.

For example: A, a coolie, puts B's luggage in the carriage. The contract comes into existence as soon as the luggage is put. It is now for B to perform his obligation by paying the charges to the coolie.

- d) **Bilateral Contract:** A bilateral contract is one in which both the parties have to perform their respective promises or obligations to do or forbear.

For example: A promises to sell his car to B after 15 day. B promises to pay the price on the delivery of the car. The contract is bilateral as obligations of both the parties are outstanding at the time of the formation of the contract.

Distinction between Void Agreement and Voidable Contract

Basis of Distinction	Void Agreement	Voidable Contract
1. Void/illegal	All void agreements need not necessarily be illegal.	All illegal agreements are always void.
2. Effect on collateral agreements	The collateral agreements do not become void.	The collateral agreements also become void.
3. Restoration of benefit received	If a contract becomes void subsequently, the benefit received must be restored to the other party.	The money advanced or thing given cannot be claimed back.

Distinction between Void Agreement and Voidable Contract

Basis of Distinction	Void Agreement	Voidable Contract
1. Void ab initio	It is void from the very beginning.	It is valid when made and continues to remain valid till it is repudiated by the aggrieved party.
2. Enforceability	It cannot be enforced by any party.	It continues to be enforceable if the aggrieved party does not repudiate the contract.
3. Right of third party	Third party does not acquire any rights.	A third party can acquire a valid title from a person claiming under such a contract.
4. Effect of lapse of reasonable time	Even on the expiry of a reasonable time, it can never become a valid contract.	On the expiry of a reasonable time, it may become a valid contract if the aggrieved party does not repudiate the contract within reasonable time.
5. Damages	The question of damages does not arise.	The aggrieved party can claim damages.

OFFER AND ACCEPTANCE

It is an established principle that an agreement arises only when an offer is made by one person and is accepted by the other person, to whom it is made. Thus, an offer and its acceptance is the starting point in the making of an agreement.

OFFER OR PROPOSAL

According to Section 2 (a) of the Indian Contract Act, 1872 defines a proposal as follows:

“When one person signifies to another his willingness to do or to abstain from doing anything, with a view to obtaining the assent of that other to such act or abstinence, he is said to make a proposal”.

The person making the proposal is called the ‘promisor or offeror’. The person to whom the proposal is made is called the ‘promisee or offeree’.

Example:

X says to Y, “I want to sell my car to you for Rs. 1, 00,000”. Here, “to sell car” is an offer or proposal. X who has made the offer is called offeror or promisor. Y to whom the offer has been made is called the offeree or promisee.

ESSENTIALS CHARACTERISTICS OF A VALID OFFER

- 1. The offer must be capable of creating legal relations:** An offer must intend to create legal relationship among the parties. If the parties have agreed that the breach of the agreement would not confer any right on either party to go to the court of law for enforcing the agreement, it will not be a valid offer.
- 2. The offer must be certain, definite and not vague:** The terms of the offer must be certain and unambiguous and not vague. If the terms of the offer are vague, no contract can be entered into because it is not clear as to what exactly the parties intended to do.
- 3. The offer must be communicated to the other party:** The offer must be communicated to the person to whom it is made. Thus, an offer accepted without its knowledge, does not confer any legal rights on the acceptor.
- 4. The offer must be made with a view to obtaining the consent of the offeree:** If a person merely makes a statement without any intention to be bound by it, then it is not a valid offer. Merely making an enquiry does not constitute an offer.
- 5. The offer must be distinguished from an answer to a question:** The terms of an offer should be clear so that there is no confusion whether it is a valid offer or an answer to a question. An answer to a question cannot be taken as an offer.
- 6. Invitation to an offer is not an offer:** Price lists, catalogues, display of goods in a show window, tenders, advertisements, prospectus of a company, an auctioneer's request for bids, etc., are instances of invitation to offer. In case of an invitation for an offer, there is no intention on the part of the person sending out the invitation to obtain the assent of the other persons to such an invitation.
- 7. The offer must be distinguished from mere statement of intention:** The terms of an offer should be clear so that there is no confusion whether it is a valid offer or a mere statement of intention. Such statement or declaration merely indicates that an offer may be made or invited in future.
- 8. Special conditions attached to an offer must also be communicated:** In such cases the rule is that the party shall not be bound by the conditions unless conditions printed are properly communicated.

9. **The offer may be positive or negative:** An offer to do something is a positive offer. And an offer not to do something is a negative offer.
10. **The offer may be express or implied:** An offer which is expressed by words, written or spoken, is called an express offer. The offer which is expressed by conduct, it is called an implied offer.
11. **The offer may be specific or general:** When an offer is addressed to a specific individual or a group of individuals, called it as specific offer. When an offer is addressed to an unascertained body of individuals or to the public at large, it is said to be a general offer.
12. **The offer should not contain a term the non-compliance of which would amount to acceptance:** One cannot say while making the offer that if the offer is not accepted by a certain time, it will be presumed to have been accepted.

DIFFERENT KINDS OF OFFERS

1. **Express offer:** An express offer is one which is made by words spoken or written.
2. **Implied offer:** An implied offer is one which is made otherwise than in words. In other words, it is inferred from the conduct of the person or the circumstance of the particular case.
3. **Specific offer:** A specific offer can be accepted only by that definite person or that particular group of persons to whom it has made.
4. **General offer:** A general offer is one which is made to the world at large or public in general.
5. **Standing or Open or Continuing offer:** An offer for a continuous supply of certain goods and services in any quantity at a certain price as and when required it will be termed as a standing or open offer.
6. **Counter offer:** A Counter offer is rejecting the original offer and making a new offer. The new offer is the counter offer.
7. **Cross offer:** Where identical offers are made by parties in ignorance of each other, the offers are said to be cross offers.

Lapses of offer [When does an offer come to an end]

Section 6 of the Act deals with the various modes of revocation of an offer. Accordingly, an offer may come to an end in any of the following ways:

1. **By communication of notice of revocation by the proposer:** The proposer can revoke or withdraw his offer at any time before the acceptor posts his letters of acceptance. A notice of revocation to be effective must be communicated to the acceptor.
2. **By lapse of prescribed time:** An offer lapses if acceptance is not communicated within the time prescribed in the offer, or if no time is prescribed, within a reasonable time.
3. **By non-fulfillment of a condition by acceptor:** A proposal comes to an end when the acceptor fails to fulfill a condition precedent to the acceptance of the proposal.
4. **By the death or insanity of the offeror:** A proposal comes to an end by the death or insanity of the offeror if the fact of the death or insanity comes to the knowledge of the acceptor before acceptance.

5. **By counter offer:** A proposal lapses if it has been rejected by the other party or a counter offer is made.
6. **By subsequent illegality or destruction of subject matter:** An offer lapses if it becomes illegal after it is made or which the subject matter is destroyed or substantially impaired before acceptance.
7. **By rejection:** An offer lapses if it has been rejected by the offeree. The rejection may be express i.e., by words spoken or written, or implied. Implied rejection is one; (a) where either the offeree makes a counter offer, or (b) where the offeree gives a conditional acceptance.

ACCEPTANCE

An acceptance is the manifestation by the offeree of his willingness to be bound by the terms of the offer. According to Section 2 (b) of the Act, “*When the person to whom the offer is made signifies his assent thereto, the proposal is said to be accepted. A proposal when accepted becomes a promise*”.

Example: *X offers to sell his car to Y for Rs. 1,00,000. Y agrees to buy the car for Rs. 1,00,000. Y's act is an acceptance of X's offer.*

ESSENTIAL AND LEGAL RULES FOR A VALID ACCEPTANCE

1. **The acceptance must be communicated:** An acceptance to be valid must be communicated to the proposer. If the person to whom the proposal is made remains silent and does nothing to show that he has accepted the proposal, no contract is formed.
2. **Acceptance must be absolute or unqualified:** Acceptance, in order to be binding, must correspond with all the terms of the offer. Offer must be accepted in toto. A qualified and conditional acceptance amounts to making of a counter offer which puts an end to the original offer and it cannot be revived by subsequent acceptance.
3. **Acceptance may be express or implied:** Acceptance given by words is known as express acceptance. But an acceptance given by conduct is said to be implied. Implied acceptance may arise from (a) doing of a particular act as prescribed in the offer, and (b) by accepting a benefit offered by the offeror.
4. **The acceptance must be given in some usual and reasonable manner:** It is another important legal rule of an acceptance that where no mode is prescribed, acceptance must be given in some usual and reasonable manner.
5. **The acceptance must be given before the lapse of offer:** A valid contract can arise only when the acceptance is given before the offer has elapsed or withdrawn.
6. **The acceptance cannot be implied from silence:** The offeror does not have the legal rights to say that if no answer is received within a certain time, the offer shall be deemed to have been accepted.
7. **Acceptance means acceptance of all the terms of the offer:** When an offer is accepted, it would mean acceptance of all the terms of offer. The acceptance of offer cannot be partial at all.
8. **If acceptance has been given conditional there will be no contract:** When an acceptance by a person is made conditional i.e., ‘subject to a formal contract’ or ‘subject to approval by

certain person – such as solicitors etc’, no contract will arise till a formal contract is entered into or consent of such persons is obtained.

COMMUNICATION AND REVOCATION OF OFFER AND ACCEPTANCE

When the contracting parties are facing each other, there is no problem of communication, because there is instantaneous communication of offer and acceptance.

Mode of Communication [Sec. 3]

Section 3 of the Act refers to the two modes of communication:

1. Communication by act, and
2. Communication by omission.

Act includes by conduct or by words, written or oral. So communication can be by letter, telegram, telephone etc. Omission includes conduct or forbearance on the part of one person which has the effect of communication.

When is Communication Complete [Sec. 4]

1. Communication of Offer

The communication of an offer is complete when it comes to the knowledge of the person to whom it is made.

2. Communication of Acceptance

Communication of an acceptance is complete:

- a) as against the proposer, when it is put in course of transmission to him so as to be out of the power of the acceptor to withdraw the same; and
- b) as against the acceptor, when it comes to the knowledge of the proposer.

3. Communication of Revocation

Revocation means “taking back” or “withdrawal”. It may be a revocation of offer or acceptance. The communication of a revocation is complete:

- a) as against the person who makes it, when it is put into a course of transmission to the person to whom it is made, so as to be out of the power of the person who makes it; and
- b) as against the person to whom it is made, when it comes to his knowledge.

CONSIDERATION

The consideration is one of the essential elements of a valid contract. The term ‘consideration’ may be defined as the price of the promise. This term is used in the sense of *quid pro quo* (i.e., something in return). Accordingly, an agreement which is not supported by consideration is a *nudum pactum* (a nude or a bare agreement), and the effect of a nude agreement is expressed in the legal maxim, *ex nudo pacto non oritur actio* meaning no cause of action arises from a bare agreement.

The most popular definition of consideration is given by *Lush J. in Currie vs Misa*. According to him, “A valuable consideration, in the sense of the law, may consist either in some right, interest, profit or benefit accruing to the one party, or some forbearance, detriment, loss or responsibility given, suffered, or undertaken by the other”.

Definition

Section 2 (d) of the Act defines consideration as under:

"When at the desire of the promisor, the promisee or any other person has done or abstained from doing, or does or abstains from doing, or promises or to do or abstain from doing something, such act or abstinence or promise is called a consideration for the promise".

ESSENTIALS OF CONSIDERATION

- 1. Consideration must move at the desire of the promisor:** The act or abstinence of the promisee or any other person must be done at the desire or request of the third party or voluntary acts would not constitute a valid consideration. The desire of the promisor may be express or implied from the conduct of the parties.
- 2. Consideration may move from the promisee or any other person:** It is not necessary that the consideration should proceed only from the promisee. Consideration furnished by a third party will also be valid if it has been done at the desire of the promisor. This is termed as 'Doctrine of Constructive Consideration'.
- 3. Consideration may be past, present or future:** The words, has done or abstained from doing, does or abstains from doing, or promises to do or to abstain from doing; indicate that the consideration may be past, present or future.
 - a) Past consideration:** When the present promise is based on the consideration already taken place (i.e., before the date of the promise), it is termed as consideration.
 - b) Present consideration:** When the promisor receives consideration simultaneously with his promise, it is termed as present consideration.
 - c) Future consideration:** When the consideration for a promise is rendered in future it is termed as future or executory consideration.
- 4. Consideration need not be adequate:** The consideration need not be adequate to the promise but it must be of some value in the eye of the law. According to explanation 2 to Section 25, an agreement to which the consent of the promisor is freely given is not void merely because the consideration is inadequate; but the inadequacy of the consideration may be taken into account by the Court in determining the question whether the consent of the promisor was freely given.
- 5. Consideration must be real and not illusory:** Consideration must be real and be of some value in the eyes of law. Consideration of the following type are not real:
 - (a) Physical impossibility:** For instance As promising to put life into B's dead wife should B pay him Rs. 500, is void for lack of physical possibility.
 - (b) Legal impossibility:** If consideration consists of something illegal, the agreement will be void.
 - (c) Uncertain consideration:** An uncertain or vague consideration will make the agreement void.
 - (d) Illusory consideration:** It consists of a promise to do something which a person is already bound to do by law or contract. It must be something more than what a promisee is already bound to do.

6. **Consideration must be lawful:** Section 23 of the Act which says that “every agreement of which the consideration is unlawful, is void”. It means that an agreement must be supported by lawful consideration.
7. **Consideration must not be illegal, immoral or opposed to public policy:** The consideration of an agreement is unlawful if:
 - a) it is forbidden by law; or
 - b) it is of such a nature that if permitted it would defeat the provisions of any law; or
 - c) it is fraudulent; or
 - d) it involves or implies injury to the person or property of another; or
 - e) the court regard it as immoral or opposed to public policy.

PRIVITY OF CONSIDERATION OR STRANGER TO CONSIDERATION

The term ‘privity of consideration’ means stranger to the consideration, or consideration given by any other person other than the promisee. A promise is enforceable so long as there is some consideration for it, and it is immaterial whether it is furnished by the promisee or other person even a stranger.

Example: *In Subramaniam Iyer vs. Lakshmi Ammal (1973) 2 SCC 54, A borrowed Rs. 40,000 from B as security for the loan. A executed a mortgage of his property in favour of B. Later on, A sold his property to C for Rs. 44,000. Out of this, A received Rs. 4,000 and allowed him to retain the balance of Rs. 40,000 in order to redeem the mortgage by paying the amount to B. B sued C for the recovery of the mortgage money. Held, B cannot succeed as he was not a party to the sale agreement.*

PRIVITY OF CONTRACT OR STRANGER TO CONTRACT

The term ‘privity of contract’ means stranger to a contract. As per the doctrine of privity of contract, a person, who is not a party to the contract, cannot sue for carrying out the promise made by the parties to the contract.

Example: *In Dunlop Pneumatic Tyre Co. Ltd. vs. Selfridge & Co. (1915), AC. 847, S bought tyres from the Dunlop Rubber Co. and sold them to D, a sub-dealer who agreed with S not to sell below Dunlop's list price and to pay to Dunlop £5 as damages on every tyre undersold. D sold two tyres at less than the list price and thereupon Dunlop sued him for breach. Held, Dunlop cannot maintain the suit as it was a stranger to the contract.*

EXCEPTIONS TO THE RULE OF STRANGER TO CONTRACT

1. **In case of Trusts:** When a trust is created, the beneficiary can enforce his rights given to him under the trust, even though he was not a party to the contract between the settler and the trustees.
2. **In case of marriage settlement, partition or other family arrangements:** Where a provision is made in a partition or family arrangement for the benefit of any member of the family, such a member may sue to enforce the agreement even though he is not a party to the agreement.

3. **Acknowledgement of payment:** Where the promisor acknowledges payment to a third party, either by conduct or otherwise, the latter can sue.
4. **In case of agency:** A contract entered into by an agent acting within the scope of his authority, can be enforced by the principal.
5. **In case of assignment of rights under a contract:** The assignee can enforce the benefits of the contract.
6. **Agreements relating to the land:** When any person purchases such land with the notice of rights and obligations of the owner, then he shall be bound by those rights and obligations although he was not a party to the agreement.

Rule of “No Consideration, No Contract”

According to Section 25, an agreement made without consideration is void. But gratuitous promise shall be enforceable by law if the promisee on the faith of such promise suffered a liability as suffering of detriment forms a valid consideration. According to Salmond and Winfield, a promise without consideration is a gift, one made for a consideration is a bargain.

Exceptions to the General Rule of “No Consideration, No Contract”

The following circumstances under which the agreement is valid and enforceable even if it is made without consideration:

1. **Agreements made on account of natural love and affection [Sec. 25 (1)]:** This clause lays down four essential requirements for the validity of an agreement made without consideration. They are
 - a) The agreement must be in writing;
 - b) It is registered under the law;
 - c) It is made on account of natural love and affection; and
 - d) It is between parties standing in a near relation to each other.

Example:

A, for natural love and affection, promised to give Rs. 1,000 to his son B. A put his promise to B in writing and registered it. This is valid contract.

2. **Promise to compensate for past voluntary services [Sec. 25 (2)]:** Such promise made without consideration is valid:
 - a) If the act was done voluntarily;
 - b) For the promisor or something which the promisor was legally bound to do;
 - c) The promisor must be in existence at the time when the act was done; and
 - d) The promisor must agree now to compensate the promise.

Example:

X finds Y's purse and gives it to him. Y promises to give Rs. 500 to X. This is a valid contract even though the consideration did not move at the desire of Y, the promisor.

3. Promise to pay time-barred debt [Sec. 25 (3)]: When a debtor makes a written and registered promise, under signature of his own or that of his agent, to pay a time-barred debt, no fresh consideration is needed. The following conditions must be satisfied for the application of this exception:

- a) The promise to pay must be definite and express;
- b) The promise must be in writing;
- c) The promise must be signed by the promisor or his authorized agent;
- d) The debt must be time-barred, i.e., the limitation period for the recovery of the debt, must be expired.

Example:

X owed Rs. 2,000 to Y. This debt was barred by Limitation Act i.e., the limitation period for the recovery of debt has already expired. X signed a written promise to pay Rs. 1,000 to Y on account of this debt. This is a valid contract.

4. Completed gift [Explanation 1 to Sec. 25]: The gifts actually made by a donor and accepted by the donee are valid even without consideration. Thus, a completed gift needs no consideration.

5. Contracts of agency [Sec. 185]: No consideration is necessary to create an agency.

6. Remission [Sec. 63]: No consideration is required for an agreement to receive less than what is actually due.

CAPACITY TO CONTRACT

One of the essential conditions for the enforceability of an agreement is that the concerned parties must be competent to enter into an agreement. The 'capacity to contract' means the competence (i.e., capability) of the parties to enter into a valid contract.

According to Sec. 11 of the Contract Act, "Every person is competent to contract who is of the age of majority according to the law to which he is subject, and who is of a sound mind, and is not-disqualified from contracting by any law to which he is subject".

PERSONS NOT COMPETENT TO CONTRACT

As per the statement of Section 11 of the Indian Contract Act, the following persons are not competent to contract, i.e., they are incapable of entering into a valid contract.

- (i) Minors;
- (ii) Persons of unsound mind; and
- (iii) Persons disqualified for contracting by any other law.

(i) MINORS

According to Section 3 of the Indian Majority Act, 1875, a person who has not completed his age of 18 years (majority), is considered to be a minor. In the following two cases, a person becomes major on completing the age of 21 years:

- a) Where a guardian of a minor's person or property has been appointed under the Guardians and Wards Act, 1890; and

- b) Where the superintendence of minor's property is assumed by a Court of Wards.

Rules Regarding Minor's Agreements

The law protects minor's rights because they are not mature and may not possess the capacity to judge what is good and what is bad for them. The position of a minor as regards his agreements may be stated as under:

1. **An agreement with or by a minor is void ab initio:** An agreement with a minor has been held to be void ab initio. It is not only void, but is absolutely void.
2. **A minor can be a promisee or a beneficiary:** A promissory note executed in favour of the minor can be enforced. He can draw, negotiate or endorse a negotiable instrument so as not to incur any liability upon himself.
3. **No ratification:** Since a contract with or by a minor is altogether void, he cannot ratify contracts entered into by him during his minority, even after attaining the majority. There can be no ratification of a contract void ab initio.
4. **No restitution:** Sometimes, the minor receives some property or money by falsely representing his age. In such cases, the minor can be asked to restore such property or money so long as the same is traceable in his possession.
5. **The liability of Minor's parents or guardian:** A contract made by the minor's parents or guardian or manager of his estate can be specifically enforced by or against the minor provided: (a) the contract is within the scope of authority of the parent, etc., and (b) it is for the benefit of the minor.
6. **No Estoppel:** Where a minor represents fraudulently or otherwise that he is of age and thereby induces another to enter into contract with him, he in an action founded on the contract, is not estopped from setting up infancy.
7. **Minor's property liable for necessaries:** Sometimes, a person supplies necessaries to a minor. In such cases, the supplier of necessaries can claim reimbursement from the property of minor.
8. **Minor's liability for tort:** A minor is liable for negligently causing any injury or damage, or for converting property that does not belong to him. But, he is not liable for a tort directly connected with a contract which as an infant he would be entitled to avoid. In other words, a person cannot convert a contract into a tort to enable him to sue an infant.
9. **Minor as an agent:** Minor can act as an agent and bind his principal by his acts without incurring any personal liability.
10. **Minor as a partner:** A minor cannot be a partner in a firm. But under Section 30 of the Partnership Act, he can be admitted to the benefits of partnership with the consent of all the members.
11. **Minor as an insolvent:** A minor cannot be declared insolvent because he is not competent to contract.

PERSONS OF UNSOUND MIND

According to Section 12 of the Indian Contract Act, defines the term 'Sound Mind' as follows:

“A person is said to be sound mind for the purpose of making a contract if at the time when he makes it, he is capable of understanding it, and of forming a rational judgement as to its effects upon his interests”.

Thus, if a person is not capable of both, he is said to have suffered from unsoundness of mind. Section 11 of the Act also specifically declares that persons of unsound mind are incompetent to enter into an agreement. The following persons are also considered to be the persons of unsound mind.

1. **Idiot:** An idiot is a person who has completely lost his mental faculties of thinking for rational judgement. All agreements, other than those for necessities of life, with idiots are absolutely void.
2. **Lunatics:** A lunatic is a person who is mentally deranged (disordered) due to some mental strain or other personal experience but who has some lucid intervals of sound mind.
3. **Drunken or intoxicated person:** A drunken or intoxicated person is a sane person who is delirious from fever or who is so drunk that he cannot understand the terms of a contract or form a rational judgement as to its effect on his interest.

PERSONS DISQUALIFIED BY ANY LAW

1. **Alien enemy:** "Alien" means a person who is not a citizen of India. During the continuance of war with the country to which an alien belongs, he becomes an alien enemy. In that situation, he can neither contract with an Indian subject nor can he file a suit in an Indian court. He can do so only after obtaining the permission of the Central Government. Contracts made before war may either be suspended or dissolved. They are dissolved if found to be against public policy or of benefit to the enemy.
2. **Insolvent:** When a person is declared as an insolvent, his property vests in the Official Receiver or Assignee. And the insolvent is deprived of his power to deal with the property, and sue and be sued on his behalf.
3. **Foreign Sovereigns, their Diplomatic Staff and Accredited representatives of Foreign States:** Such persons can enter into valid contracts and can enforce them in Indian courts. However, a suit cannot be filed against them, in the Indian courts, without the prior sanction of the central government.
4. **Joint Stock Company and Corporations incorporated under Special Acts:** A corporation or company, being an artificial person, and having a separate legal entity, can hold property; can purchase or sell property; and can sue or be sued in the Courts of Law. But it cannot enter into contracts which are strictly of personal nature.
5. **Felons or Convicts:** A convict cannot enter into a contract while he is undergoing imprisonment. This inability comes to an end on the expiration of the period of imprisonment or if he has been pardoned.

FREE CONSENT

In order to create a valid contract, there should be perfect identity of mind, i.e., “consensus ad idem” between the contracting parties regarding the subject matter of the contract. Section 10 of the Indian Contract Act laid down in clear terms free consent is one of the essentials of a valid contract.

CONSENT

According to Section 13 of the Act has defined consent as “two or more persons are said to consent when they agree upon the same thing in the same sense”. According to this section which has laid down the basic principle of consensus ad idem on which the law of contract is based, the parties to an agreement should have identity of minds regarding the subject matter of the agreement.

FREE CONSENT

If the consent is there but it is not free or real, then the contract will be voidable at the option of the contracting parties whose consent is not free. The word “free consent” is defined in Section 14 of the Contract Act as follows –

“Consent is said to be free when it is not caused by

1. *Coercion, as defined in Section 15; or*
2. *Undue influence as defined in Section 16; or*
3. *Fraud, as defined in Section 17; or*
4. *Misrepresentation, as defined in Section 18; or*
5. *Mistake, subject to the provisions of Sections 20, 21 and 22.*

Consent is said to be so caused when it would not have been given but for the existence of such coercion, undue influence, fraud, misrepresentation or mistake”.

COERCION [SEC. 15]

Coercion means compelling or forcing a person to enter into a contract under a pressure or threat. Section 15 of the Indian Contract Act defines coercion as “*the committing or threatening to commit, any act forbidden by the Indian Penal Code, or the unlawful detaining, or threatening to detain, any property, to the prejudice of any person whatsoever, with the intention of causing any person to enter into an agreement”.*

Example: X beats Y and compels him to sell his car for Rs. 50,000. Here, Y’s consent has been obtained by coercion because beating someone is an offence under the Indian Penal Code.

ESSENTIALS CHARACTERISTICS OF COERCION

- (a) **The committing of any act forbidden by Indian Penal Code:** When the consent of a person is obtained by committing any act which is forbidden by the Indian Penal Code, the consent is said to be obtained by coercion.
- (b) **The threatening to commit any act forbidden by Indian Penal Code:** If a person attempts to commit an act which is punishable under the Indian Penal Code, it leads to coercion, e.g., consent obtained at the pistol point, or by threatening to cause death or by intimidation.

- (c) **The unlawful detaining of any property:** If a person unlawfully detains the property of another person and forces him to enter into a contract, the consent is said to be induced by coercion.
- (d) **The threatening to detain any property unlawfully:** If a threat is given to detain any property of another person, this amounts to coercion.
- (e) **The act of coercion:** It must be done with the object of inducing or compelling any person to enter into an agreement.

EFFECTS OF COERCION

According to Section 19 states that, 'when the consent of a party to an agreement is obtained by coercion, the contract becomes voidable at the option of the party, i.e., such party can put an end to the contract if he so chooses'.

According to Section 72 of the Act, which is based on the principle of equitable restitution, a person to whom anything has been delivered or money paid under coercion must return or repay it.

UNDUE INFLUENCE [SEC. 16]

When a party enters into a contract under any kind of mental pressure, unfair influence or persuasion by the superior party, the undue influence is said to be employed. According to Section 16 (1) of the Act, a contract is said to be induced by undue influence, "*where the relations subsisting between the parties are such that one of the parties is in a position to dominate the will of the other, and uses that position to obtain an unfair advantage over the other*".

Presumption of undue influence

Section 16 (2), a person is deemed to be in a position to dominate the will of the other in the following cases:

- a) **Real or apparent authority:** Where he holds a real or apparent authority over the other, e.g., master and the servant, parent and child, Income Tax officer and assessee, etc.
- b) **Fiduciary relationship:** Fiduciary relation means a relation of mutual trust and confidence, e.g., guardian and the ward, solicitor and client, doctor and patient, guru and disciple, trustees and beneficiaries, etc.
- c) **Mental distress:** Where he contracts with a person whose mental capacity is temporarily or permanently affected by reason of age, illness, or mental or bodily distress.

BURDEN OF PROOF [SEC. 16 (3)]

Where a person who is in a position to dominate the will of another, makes a contract and the transaction appears to be unconscionable, the burden of proving that the contract has not been induced by undue influence shall lie on the person who is in a position to dominate the will of the other.

The presumption of undue influence can be rebutted or opposed by showing the following:

- (i) that full disclosure of all material facts was made;
- (ii) that the consideration was adequate; and

(iii) that the other party was in receipt of competent independent advice and his consent was free.

Distinction between Coercion and Undue Influence

Basis of Distinction	Coercion	Undue Influence
1. Nature of force	It involves physical force.	It involves moral pressure.
2. Relationship	Parties to a contract may or may not be related to each other.	Parties to a contract are related to each other under some sort of relationship.
3. Consent	Consent is obtained by giving a threat of an offence or committing an offence.	Consent is obtained by dominating the will.
4. Who can exercise	It can be exercised even by a stranger to the contract.	It can be exercised only by a party to a contract and not by a stranger.
5. Presumption	Coercion has to be proved by the aggrieved party alleging it in. It is not presumed by the law.	There is a presumption of undue influence in the case of certain relationship.
6. Restoration of benefit	The aggrieved party who is rescinding the contract has to return the benefit received to the other party.	The aggrieved party may or may not be required to return the benefit in whole or in part as per Court's direction.
7. Criminal element	It entails criminal liability.	It doesn't involve any criminal liability.
8. Place of use	The act or the threat amounting to coercion may be committed even outside India.	It must have been exercised in India.

FRAUD [Sec. 17]

The term 'fraud' may be defined as an intentional, deliberate or wilful misstatement of facts, which are material for the formation of a contract.

According to Section 17, "*fraud means and includes any of the following acts committed by a party to a contract or with his connivance or by his agent, with intent to deceive another party thereto or his agent, or to induce him to enter into the contract:*

- (a) *the suggestion, as to a fact, of that which is not true, by one who does not believe it to be true;*
- (b) *the active concealment of a fact by one having knowledge or belief of the fact;*
- (c) *a promise made without any intention of performing it;*
- (d) *any other act fitted to deceive;*
- (e) *any such act or omission as the law specially declares to be fraudulent".*

ELEMENTS OF FRAUD

On the basis of aforesaid definition of fraud, the essential elements of fraud are as follows:

1. **The act must have been committed by a party to the contract:** The fraud must be committed by a party to a contract or by anyone with his connivance or by his agent. Thus, the fraud by a stranger to the contract does not affect the validity of the contract.
2. **Acts committed may be of the following nature:**
 - a) **Suggestion of an untrue fact:** If a person knowingly states an untrue fact or fact which he does not believe to be true, it will be taken as a fraud on his part.
 - b) **Active concealment of a fact:** An active concealment is considered as a fraud when (i) there is a concealment of fact, and (ii) the concealment is active (i.e., all efforts are made to conceal fact), and (iii) the concealment is made by a party who has the knowledge of it.
 - c) **A promise made without any intention of performing it:** If a party while entering into a contract has no intention to perform his promise, it will be taken as a fraud on his part.
 - d) **Any other act fitted to deceive:** The expression 'act fitted to deceive' means any act which is done with the obvious intention of committing fraud. Thus, this clause covers all tricks and unfair ways which are used by cunning and clever people to cheat others.
 - e) **Any such act or omission which the law specially declares to be fraudulent:** Under the Transfer of Property Act, any transfer of immovable property with the intention of defrauding the creditors, is taken as a fraud.
3. **The act must have been committed with the intention of inducing the deceived party to act upon it:** It implies that the assertion should be such that it would necessarily influence and induce the other party to act.
4. **The act must have in fact deceived the other party:** If a person has committed a fraudulent act to deceive the other party, but the other party has not been actually deceived by his act, it will not be taken as a fraud on his part.
5. **Plaintiff must have suffered:** There is no fraud without damages, and therefore, to constitute fraud it is necessary that the plaintiff must have suffered some loss of money or money's worth or some other tangible detriment capable of assessment.

Mere silence is not a fraud

According to explanation to Section 17, "mere silence as to facts likely to affect the willingness of a person to enter into a contract is not fraud".

Example: *A sells, by auction, to B a horse which A knows to be unsound. A says nothing to B about the horse's unsoundness. This is not fraud by A.*

Exceptions

1. **Duty to Speak:** Mere silence amounts to fraud when the person keeping silent, is under a duty to speak. The duty to speak arises, where one party reposes trust and confidence in the other. The duty to speak arises in the following types of contracts:
 - a) **Contracts uberrimae fidei**, i.e., contracts of good faith such as contracts of insurance; contracts for the sale of immovable properties; contracts of marriage; contracts for the purchase of shares; family contracts, etc.
 - b) **Contracts of partnership:** Under the Partnership Act, partners are required to observe absolute good faith and to be just and faithful to each other.

- c) **Contracts of guarantee:** The creditor must disclose all material facts about the debtor to the surety.
 - d) Where the parties stand in fiduciary relationship to each other.
 - e) Contracts to marry.
2. **Where silence is equivalent to speech:** For instance, B says to A, "If you do not deny it, I shall presume that the horse is sound". A says nothing. Here A's silence is equivalent to speech. If the horse turns out to be vicious A can be held liable for fraud.
3. **Change of circumstances:** Sometimes a statement may be true when it is made but due to change in circumstances, it may become false subsequently. In such a case, it is the duty of the person to communicate the change in circumstances.

Effect of Fraud

1. **Right to rescind the contract:** The party whose consent was caused by fraud can rescind (cancel) the contract but he cannot do so in the following cases:
 - a) where silence amounts to fraud, the aggrieved party cannot rescind the contract if he had the means of discovering the truth with ordinary diligence;
 - b) where the party gave the consent in ignorance of fraud;
 - c) where the party after becoming aware of the fraud takes a benefit under the contract;
 - d) where an innocent third party before the contract is rescinded acquires for consideration some interest in the property passing under the contract;
 - e) where the parties cannot be restored to their original position.
2. **Right to insist upon performance:** The party whose consent was caused by fraud may, if he thinks fit, insist that the contract shall be performed and that he shall be put in the position in which he would have been if the representation made had been true.
3. **Right to claim damages:** The party whose consent was caused by fraud, can claim damage if he suffers some loss.

MISREPRESENTATION [Sec. 18]

The term 'Misrepresentation' means a false representation of fact made innocently or non-disclosure of a material fact without any intention to deceive the other party. A false representation made by a person may be either:

1. Innocent or unintentional, i.e., without any intention of deceiving the party.
2. Intentional or wilful or deliberate, i.e., with the intention of deceiving the party.

According to Section 18 defines the term 'misrepresentation' as follows:

"Misrepresentation" means and includes –

- i) the positive assertion, in a manner not warranted by the information of the person making it, of that which is not true, though he believes it to be true;
- ii) any breach of duty which, without any intent to deceive, gains an advantage to the person committing it, or anyone claiming under him, by misleading another to his prejudice, or to the prejudice of any one claiming under him;

iii) Causing, however innocently, a party to an agreement, to make a mistake as to the substance of the thing which is the subject of the agreement.

Essentials of Misrepresentation

1. There must be a representation or breach of duty.
2. The representation must be of facts material to the contract.
3. The representation must be untrue.
4. The representation must be made with a view to inducing the other party to enter into contract.
5. The other party must have acted on the faith of the representation.
6. The person making the representation honestly believes it to be true.

Acts Which Constitute Misrepresentation

Thus misrepresentation may be committed in any of the following ways:

1. **Unwarranted Statements:** If a person makes a statement of fact which is not warranted by his information, he is said to make a misrepresentation.
2. **Breach of Duty:** When a person commits a breach of duty without any intention to deceive the other party and thereby gains something while the other party loses, it will be termed as misrepresentation.
3. **Inducing Mistake about Subject Matter:** If a party to an agreement induces the other party, although innocently to commit a mistake as to the nature or quality of the subject matter of the agreement, he becomes guilty of misrepresentation.

Effects of Misrepresentation

The effect of misrepresentation is that it makes the contract voidable the option of the party whose consent is so obtained. And such party may put an end to the contract if he so chooses.

Exceptions

1. **Where the other party had the means of discovering the truth with ordinary diligence:** The party cannot complain of misrepresentation if he had the means of discovering the truth with ordinary means.
2. **Where the misrepresentation does not induce the other party to enter into contract, the contract is not voidable:** If the consent is given independently in spite of misrepresentation, the contract is not voidable.

Difference between Fraud and Misrepresentation

Fraud	Misrepresentation
1. There is misstatement or concealment of fact, deliberately made with the intention to deceive the other party or to induce him to enter into a contract.	1. The misstatement of fact is made innocently without any bad intention.
2. The fraud is intentional or wilful wrong. The person making an untrue statement knows that it is not true.	2. The misrepresentation is an innocent wrong. The person making the false statement believes it to be true.
3. In case of active fraud, the aggrieved party	3. The aggrieved party cannot rescind the

<p>has a right to rescind the contract.</p> <p>4. A fraud is a criminal act too.</p> <p>5. Not only is the contract voidable but it also gives rise to an independent action in tort for damages.</p> <p>6. The aggrieved party in addition to the normal remedies can claim also damages.</p>	<p>contract if it was possible for him with ordinary diligence to discover the truth.</p> <p>4. It is not a criminal act.</p> <p>5. It makes the contract voidable at the option of the party misrepresented.</p> <p>6. The aggrieved party cannot claim to damages.</p>
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MISTAKE

A mistake is said to have occurred where the parties intending to do one thing by error do something else. Mistake is an erroneous belief concerning something.

Example: *X engages Y as a teacher for his son appearing for IAS Preliminary. Y agrees to come daily 7. X think 7 a.m. but Y means 7 p.m. This is a bilateral mistake of fact but not essential and can be rectified. Therefore the agreement is valid.*

Kinds of Mistake

Mistake may be of two kinds: (I) Mistake of Law; and (II) Mistake of Fact.

(I) Mistake of Law: It may be of the following types:

a) Mistake of law of the country: It does not render the agreement void. This is based on the well established rule of law namely, ignorantia juris non excusat (i.e., ignorance of law is no excuse). Section 21 lays down that "a contract is not voidable because it was caused by a mistake as to any law in force in India".

b) Mistake of foreign law: The mistake of the foreign law has the same effect as a mistake of fact. Therefore, it renders the agreement void. Section 21 lays down that "a mistake as to a law not in force in India has the same effect as a mistake of fact".

(II) Mistake of Fact: Mistake of fact may be of two types –

- (1) Bilateral mistake; and
- (2) Unilateral mistake.

(1) Bilateral mistake: Where both the parties to an agreement are under a mistake as to matter of fact essential to the agreement, the agreement is void. An agreement shall be void if the following conditions are satisfied:

- (i) **Both the parties must be under a mistake:** This means the mistake must be mutual or common.
- (ii) **Mistake must relate to an essential fact:** It is necessary that the mistake must relate to a matter of fact which is essential to the agreement.

Types of Bilateral Mistake

The following types of bilateral mistake, which render the agreement void, are important from the subject point of view:

a) Mistake as to subject matter

Where both the parties working under a mistake relating to the subject matter of contract, the contract is void. It may be of the following types:

- (i) Mistake regarding existence of the subject matter: Where both the parties are under a mistake regarding the existence of the subject matter, the contract is void.
- (ii) Mistake regarding identity of the subject matter: If both, the parties are mistaken about the identity of subject matter, the contract shall be void.
- (iii) Regarding the title to the subject matter: If a person buys some property which neither party knew that it already belonged to the buyer, the contract will be void.
- (iv) Regarding the quantity of the subject matter: Where the quantity purchased is fundamentally, different from the quantity intended to be sold, there occurs mutual mistake which prevents the formation of an enforceable contract.
- (v) Regarding the quality of the subject matter: It occurs, where the subject matter is entirely different from that contemplated by the parties.
- (vi) Regarding the price of the subject matter: Where a seller while writing the price of the goods intending to write Rs. 2,250 by mistake writes Rs. 1250, the agreement is void.

b) Mistake as to the possibility of performance

Where the parties to an agreement believe that the agreement is capable of performance, while in fact it is not so, the agreement is treated as void. The impossibility may either be physical or legal.

(2) Unilateral mistake

The term unilateral mistake means where only one party to the agreement is under a mistake. A contract is not voidable merely because it was caused by one of the parties to it being under a mistake as to matter of fact.

Types of Unilateral Mistake

1. **Mistake about the identity of the parties to an agreement:** If there is a mistake regarding the identity of the person contracted with, even if the mistake is caused by fraud or misrepresentation of another party, the contract will be void.
2. **Mistake about the nature of the agreement:** If a party does not disclose the true nature of the document but fraudulently induces the other party to sign it who believes that he is signing some other document, in such a case there is no real agreement.

LEGALITY OF CONSIDERATION AND OBJECT

For a valid contract it is essential that the object or consideration of the agreement must be lawful. According to Sec. 23 of the Indian Contract Act, the objects and the consideration of an agreement shall be unlawful in the following cases:

1. **Where it is forbidden by law:** As a matter of fact, an act is forbidden by law, when it is punishable by criminal law of the country, or when it is prohibited by special legislation or by the regulations made by a competent authority under power derived from the legislature.

- 2. Where it defeats the provision of any law:** It is of such nature that, if permitted, it would defeat the provisions of law, e.g., purchase of land being sold for arrears of land revenue by the defaulter, or an agreement by a debtor not to raise the plea of limitation in a suit by the creditor.
- 3. Where it is fraudulent:** If the two parties agree to practice a fraud on third party, then the agreement between the parties is unlawful and void.
- 4. Where it is injurious either to the person or his property:** It involves or implies injury to the person or property of another, e.g., an agreement to indemnify a person against the consequences of publication of a libel.
- 5. Where it is regarded as immoral:** The term 'immoral' depends upon the standard of 'morality' prevailing at a particular place and time. If the consideration for the agreement is an act of sexual immorality, for example, illicit co-habitation and prostitution, the agreement is illegal.
- 6. Where it is opposed to public policy:** The agreements that are injurious to the public or which are against the public good or public welfare are void.

AGREEMENTS OPPOSED TO PUBLIC POLICY

Public policy is that principle of law which holds that no citizen can lawfully do that which has a tendency to be injurious to the public. An agreement is said to be opposed to public policy when it is injurious to the welfare of the society or it tends to prejudice the welfare of the society.

Following agreements have been declared by the Courts as opposed to public policy and they are as follows:

- 1. Trading with an alien enemy:** All agreements made with an alien enemy are illegal on the ground of public policy.
- 2. Agreement for stifling prosecution:** An agreement which seeks to absolve an offender of criminal liability or excuse him from prosecution or to withdraw a criminal case pending against him is known as an agreement stifling prosecution.
- 3. Maintenance and Champerty:** Any agreement which improperly promotes litigation is opposed to public policy. Such agreements may be either maintenance or Champerty.
- 4. Agreement for sale of public offices and titles:** The agreements for the sale or trafficking in public offices or to obtain public title like Padma Shree etc., are illegal on the ground of being opposed to public policy.
- 5. Marriage brokerage agreements:** Agreements to procure marriages for reward, or agreement to pay money to the parent or guardian of a minor in consideration of his consenting to give the child in marriage, are void.
- 6. Agreement in restraint of personal liberty:** An agreement which unduly restricts the personal liberty of any person is void on the ground of being opposed to public policy.
- 7. Agreement in restraint of parental rights:** An agreement which is inconsistent with the duties arising out of such guardianship is void as being opposed to public policy.
- 8. Agreements tending to create interest opposed to duty:** An agreement with a public servant which obliges him to do something which is inconsistent with his official duty, shall be void as being opposed to public policy.

9. **Agreements interfering with marital duties:** Any agreement which interferes with the performance of marital duties, it is void. For example, an agreement that the husband shall always live at the wife's house was held to be void.
10. **Agreements to vary the period of limitation:** Agreements, the object of which is to curtail or extend the period of limitation prescribed by the law of limitation, are void.
11. **Agreements to defraud creditors or revenue authorities:** The agreements, the object of which is to defraud the creditors or revenue authorities are void as being opposed to public policy.
12. **Agreement tending to create monopoly:** An agreement, the object of which is to create monopoly is illegal and void as being opposed to public policy.
13. **Agreement to commit a crime:** An agreement to indemnify a person against consequences of his criminal act is void as opposed to public policy. These act may be grouped under the following heads:
 - a) *Agreements in restraint of marriage [Section 26].*
 - b) *Agreements in restraint of trade [Section 27].*
 - c) *Agreements in restraint of legal proceedings [Section 28].*All these agreements will be discussed in detail in the next chapter on "Void Agreement".

VOID AGREEMENTS

According to Section 2 (g) of the Indian Contract Act, 1872, a void agreement is an agreement which is not enforceable by law. A void agreement does not create any legal rights and obligations. It is void-ab-initio (i.e., void from the very beginning) and without any legal effect. Agreements, which possess all the essential elements of a valid contract laid down in Section 10, must not have been expressly declares as void by any law in force in any country.

The following agreements have been expressly declared as void by the Indian Contract Act:

1. Agreements by incompetent persons [Section 11].
2. Agreements made under a mutual mistake [Section 20].
3. Agreements, the object or consideration of which is unlawful [Section 23].
4. Agreements, the object or consideration is partly unlawful [Section 24].
5. Agreements made without consideration [Section 25].
6. Agreements in restraint of marriage [Section 26].
7. Agreements in restraint of trade [Section 27].
8. Agreements in restraint of legal proceedings [Section 28].
9. Agreements the meaning of which is uncertain [Section 29].
10. Agreements by way of wager [Section 30].
11. Agreements to do impossible acts [Section 56].

Agreements from 1 to 5 have already been discussed in earlier chapters. The other agreements are discussed below:

AGREEMENTS IN RESTRAINT OF MARRIAGE [SECTION 26]

According to Sec. 26 of the Act, “every agreement in restraint of the marriage of any person, other than a minor, is void”. The law regards the marriage as the right of every person. Restriction on the freedom of people shall be against public policy and, therefore, void.

Example: *A promised to marry B only and none else, and to pay Rs. 2000 in default. A married C and B sued A for recovery of Rs. 2000. It was held that B could not recover anything because the agreement was in restraint of marriage. [Lowe vs. Peers]*

It may be noted that an agreement which provides for a penalty upon remarriage may not be considered as a restraint of marriage.

AGREEMENTS IN RESTRAINT OF TRADE [SECTION 27]

According to Sec. 27 of Indian Contract Act, 1872, “every agreement by which anyone is restrained from exercising a lawful profession, trade or business of any kind, is to that extent void”. This is because Article 19 (g) of the Constitution of India regards the freedom of trade and commerce as a right of every individual. Therefore, no agreement can deprive or restrain a person from exercising such a right.

Example: *In the case, Madhub Chander vs Raj Coomar, A and B were rival shopkeepers in a locality of Calcutta. A agreed to pay a sum of money to B if he would close his business in that locality. B closes his shop. On A’s refusal to pay the amount, the court held that the agreement was void under Sec. 27 of the Act.*

EXCEPTIONS

The following are the exceptions to the rule that ‘an agreement in restraint of trade is void’.

1. Statutory Exceptions

- a) **Sale of Goodwill:** An agreement which restrains the seller of a goodwill from carrying on a business is valid if all the following conditions are fulfilled:
 - (i) The seller should be restrained only from carrying on a similar business;
 - (ii) The restriction shall apply so long as the buyer or any person deriving title from him is carrying on a similar business;
 - (iii) The restraint should apply only within specified local limits.
 - (iv) The restraint must be reasonable having regard to the nature of the business.
- b) **Restrictions under Partnership Act:** The following restrictions are provided in the Partnership Act, 1932:
 - (i) **Restriction on existing partner [Section 11(2)]:** A partner shall not carry on any business other than that of the firm while he is a partner.
 - (ii) **Restriction on outgoing partner [Section 36(2)]:** An agreement by an outgoing partner with the continuing partners not to carry on a business similar to that of the firm within a specified period or within specified local limits shall not be void.
 - (iii) **Restriction in anticipation of dissolution [Section 54]:** Agreement amongst partners

that upon dissolution of the firm some or all of them shall not carry on similar business within a specified period or within specified local limits shall not be void.

- (iv) **Restriction in case of sale of goodwill of the firm [Section 55 (3)]:** Agreement by a partner upon sale of goodwill of the firm, with the buyer thereof not to carry on any similar business within a specified period or within specified local limits shall not be void.

2. Under Judicial Interpretations

- a) **Trade Combinations:** Trade combinations which have been formed to regulate the business or to fix prices are not void, but the trade combinations which tend to create monopoly and which are against the public interest are void.
- b) **Service Agreements:** Agreements of service often contain a clause by which the employee is prohibited from working anywhere else during the term of the agreement, such agreements are valid.
- c) **Sole Dealing Agreements:** An agreement to deal in the products of a single manufacturer or to sell the whole produce to a single dealer is valid if their terms are reasonable.

AGREEMENTS IN RESTRAINT OF LEGAL PROCEEDINGS [SECTION 28]

An agreement by which any party is restricted absolutely from enforcing his legal rights under or in respect of any contract is void to that extent. An agreement which interferes with the course of justice is void on account of its being opposed to public policy.

The following are the four kinds of agreements which are in restraint of legal proceedings, and are therefore, void:

- a) **Absolute restrictions from enforcing legal rights:** Any agreement that absolutely restricts a party to a contract from enforcing his contractual rights in ordinary tribunals is void.
- b) **Agreements curtailing the limitation period:** An agreement which limits the time within which an action may be brought so as to make it shorter than that prescribed by the Law of Limitation, is void because its object is to defeat the provisions of law.
- c) **An agreement which extinguishes the rights of a party.**
- d) **An agreement which discharges a party from liability.**

Exceptions

There are the following two exceptions to the rule laid down in Section 28:

1. Restraints for referring the future disputes to arbitration.
2. Restraints for referring the existing or present disputes to arbitration.

AGREEMENTS THE MEANING OF WHICH IS UNCERTAIN [SECTION 29]

An uncertain agreement is one, the terms of which are uncertain or not capable of being made certain without further agreement between the parties are void. An agreement with uncertain, ambiguous or vague terms is void because in such cases, courts may not give a practical meaning to the contract.

Example: A agreed to sell to B, 100 tons of oil. There is nothing whatever to show what kind of oil was intended. Therefore, the agreement is void for uncertainty.

AGREEMENTS BY WAY OF WAGER [SECTION 30]

The term 'wagering agreement' or 'wager' may be defined as an agreement in which one person agrees to pay certain amount of money to the other person on the happening or non-happening of a specified uncertain event.

Sir William Anson defines a wager as "a promise to give money or money's worth upon the determination or ascertainment of an uncertain event" and this definition was quoted by the Supreme Court in *Gherulal Parekh vs Mahadeo Das Maiya*.

Examples:

- i) X agrees with Y that if there is rain on a certain day X will pay Y Rs. 1000. If there is no rain Y will pay X Rs. 1000. The agreement is of a wagering nature.
- ii) A test match between India and Australia has ended in Kolkata today. Both A and B are ignorant of the result. A agrees with B to pay 1000 in case India wins and B agrees to pay A Rs. 1000 in case India does not win. The agreement is of a wagering nature.

Essential Features of a Wager Agreement

1. **Promise to pay money or money's worth:** There must be a promise to pay money or money's worth by one party to the other.
2. **Event:** The promise must be conditional on the happening or not happening of an event.
3. **Uncertainty of the event:** The agreement must be conditional upon the determination of an uncertain event. An event may be uncertain not only because it relates to future but because it is not yet ascertained to the knowledge of the parties.
4. **Mutual chances of gain or loss:** Each party must stand an equal chance to win or lose on the determination of the contemplated events.
5. **No control over the event:** Neither party should have control over the happening or non-happening of the event.
6. **Stake as the only interest:** Neither party should have any interest other than the sum or stake that he stands to win or lose.

Effects of Wagering Agreement

- a) Agreements by way of wager are void in India.
- b) Agreements by way of wager have been declared illegal in the states of Maharashtra and Gujarat.
- c) No suit can be filed to recover the amount won on any wager.
- d) Transactions which are collateral to wagering agreements are not void in India except the states of Maharashtra and Gujarat (Wagering agreements which are illegal).

Exceptions to Wager

The following transactions are not wagers:

1. **Horse race:** An agreement to contribute or subscribe towards any plate, prize or sum of money, the amount of rupees five hundred or more to be awarded to the winners of any horse race is a valid agreement and not a wager. In 1996, the Supreme Court has held horse races to be "games of skill" and not gambling.
2. **Crossword competitions:** Crossword puzzles are games of skill. But if in crossword competition, the winning of the prize depends upon the tallying of competitors' entry with the solution kept with the editor of the magazine, then it is a wagering transaction. According to the Prize Competition Act, 1955, prize competitions in games of skills are not wagers provided the amount of prize does not exceed Rs. 1000.
3. **Games of skill:** Picture puzzles, literary and athletic competitions, being based on skill and intelligence, are games of skill.
4. **Share market transactions:** In the share market if the intention is to take and give delivery of stocks and shares, it is a valid transaction.
5. **Contracts of insurance:** It is a contract in which an insurer, in consideration of a certain sum of money, undertakes to make good the loss of the insured arising on the happening of an uncertain specified event.
6. **Chit Fund:** In it, a certain number of persons contribute a fixed sum for a specified period which is made over to one of them at the end of a pre-determined period in accordance with an agreed plan. These are not wagers.

Difference Between Wagering and Contract of Insurance

1. Contract of insurance is valid and can be enforced in court of law, where as wagering agreement is void under section 30, without any legal effect.
2. In case of insurance contract, the assured has an insurable interest in the subject matter, while in the wagering agreements the parties have no interest in the agreement except the stake.
3. A contract of insurance except life insurance, is a contract of indemnity i.e., in the event of loss only actual loss is to be made good, whereas in wagering agreements the amount to be paid is decided beforehand.
4. A contract of insurance is based on scientific actuarial calculation of risks while wagering transactions are a pure gamble or game of chance.
5. A wager will arise only if one party losses and another gains while in insurance contract no winning or losing.
6. Insurance contracts are social security measures which are beneficial to the public while wagering transactions do not promote public welfare in any way, rather they encourage gambling which is injurious to the interest of public.

Commercial Transaction and Wager

An agreement for the actual sale and purchase of goods is not a wagering agreement. But sometimes it becomes difficult to determine whether a particular transaction is by way of wager or a genuine business transaction.

Lotteries

A lottery is a game of chance, therefore, an agreement to buy a lottery ticket, is a wagering agreement. If the lottery is authorized by Government, it does not cease to be a wagering transaction, the only effect of such sanction is that the persons conducting the lottery will not be prosecuted under the penal law.

CONTINGENT CONTRACT

A contract may be absolute or contingent.

Absolute Contract

An absolute contract is one in which the promisor binds himself to performance independent of any condition of contingency i.e., the promisor undertakes to perform the contract in all events.

Contingent contract

According to Section 31 of the Contract Act, a contingent contract “is a contract to do or not to do something, if some event, collateral to such contract does or does not happen”.

The performance of a contingent contract becomes due only upon the happening or non-happening of some future uncertain event. In simple words, it is a conditional contract. Contracts of insurance, indemnity and guarantee etc. are some of the important examples of contingent contracts.

Example: *A contracts to pay Rs. 10,000 to B if his (B's) house is burnt. This is a contingent contract as its performance is dependent upon an uncertain event (i.e., burning of B's house).*

Essentials of a Contingent Contract

A valid contingent contract must satisfy these essential requirements:

1. ***There must be a valid contract:*** It must fulfill the basic requirements of a valid contract between the parties.
2. ***The performance of the contract must be conditional:*** The performance of a contingent contract must depend upon the happening or non-happening of some future event.
3. ***The event must be uncertain:*** The future event, upon which the performance of a contract depends, must be an uncertain event.
4. ***The event must be collateral to the contract:*** The event must be independent or ancillary to the contract.
5. ***The event should not be the discretion of the promisor:*** The ‘mere will’ or ‘discretion’ of the promisor is not an event for the purpose of a contingent contract.

RULES REGARDING CONTINGENT CONTRACTS

1. **Contingent contracts dependent on the happening of future uncertain event:** Sec. 32 provides that “contingent contract to do or not to do anything if an uncertain future event happens cannot be enforced by law unless and until that event has happened. If the event becomes impossible such contracts become void.
2. **Contingent contracts dependent on the non-happening of future uncertain event:** Sec. 33 provides that “contingent contract to do or not to do anything if an uncertain future event does

not happen can be enforced when the happening of that event becomes impossible, and not before.

3. **Contingent contracts dependent on the future conduct of a living person:** According to Sec. 34, if a contract is contingent upon how a person will act at an unspecified time, the event shall be considered to 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.
4. **Contingent contracts dependent on the happening of specified uncertain event within a fixed time:** According to Sec. 35 (para. I), if a person is to perform something within a fixed time provided an uncertain event happens, then the person is bound to perform it, if such particular event happens within that time.
5. **Contingent contracts dependent on the non-happening of specified uncertain event within a fixed time:** Sec. 35 (para. II) provides that contingent contract 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.
6. **Contingent contracts dependent on the happening of an impossible event:** Sec. 36 provides that contingent contract 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.

Difference between Wager and Contingent Contract

Contingent Contract	Wagering Contract
1. It is perfectly valid and can be enforced in a Court of Law.	1. It is absolutely void and cannot be enforced in a Court of Law.
2. The parties have insurable interest in the happening or non-happening of the event.	2. The parties do not have insurable interest in the happening or non-happening of the event as such. Their main interest is in winning or losing.
3. In this case, the future uncertain event is merely collateral or incidental.	3. In this case, the uncertain event is the only determining factor.
4. There may not be reciprocal promises.	4. It consists of reciprocal promises.
5. All contingent contracts are not of a wagering nature, because all the contingent contracts are not void.	5. All wagering agreements are also contingent contracts because they are dependent on uncertain event.
6. In a contingent contract, the parties are interested in the occurrence or non-occurrence of the event.	6. In a wagering agreement, the parties are interested only for the stake.

QUASI CONTRACTS

Under the Law of Contracts, the contractual obligations are voluntarily undertaken by the contracting parties. However, under certain circumstances, a person may receive a benefit to which the law regards another person as better entitled or for which the law considers he should pay to the other person, even though there is no contract between the parties. Such relationships are called quasi-contracts, because, although there is no contract or agreement between the parties, they are put in the same position as if there were a contract between them.

Definition

Quasi contract is defined as “an obligation to pay a sum of money, whether liquidated or unliquidated, which arises independently of any contract, on the ground that in the circumstances of the case, it is considered by the law to be just debt”.

It is a debt or obligation constituted by the act of the law apart from any consent or intention of the parties or any privity of contract. These relationships are termed as quasi-contracts or constructive contracts under the English Law and “certain relations resembling those created by contracts” under the Indian Law.

A quasi-contract rests on the ground of equity that a person shall not be allowed to enrich himself unjustly at the expense of another. That is why the law of quasi-contracts is known as the law of restitution. Strictly speaking, a quasi-contract is not a contract at all. A contract is intentionally entered into. A quasi-contract, on the other hand, is created by law.

BASIS OF QUASI CONTRACTS

The quasi contracts are based on the maxim of ‘*nemo debet locuplatari ex liena justua*’, i.e., no man must grow rich out of another person’s costs. In other words, these are based on the equitable principle that a person shall not be allowed to enrich himself at the expense of another. Lord Mansfield explained the quasi-contracts on the principle that ‘Law as well as justice should try to prevent unjust enrichment’. The term ‘unjust enrichment’ means the enrichment of one person at the cost of another. The principle of ‘unjust enrichment’ requires, that

1. the defendant (against whom the case is filed) has been enriched by the receipt of a benefit.
2. the enrichment is at the expense of the plaintiff (i.e., who files the case).
3. the retention of the enrichment is unjust.

FEATURES OF QUASI-CONTRACTS

The salient features of a quasi-contract are as under:

- a) It is imposed by law and does not arise from any agreement.
- b) The duty of a party and not the promise of any party is the basis of such contract.
- c) The right under it is always a right to money and generally, though not always, to a liquidated sum of money.
- d) The right under it is available against specific person(s) and not against the world.
- e) A suit for its breach may be filed in the same way as in case of a complete contract.

KINDS OF QUASI CONTRACTS

The quasi contractual obligations are contained in Sections 68 to 72 of the Contract Act, 1872. These have been described below:

1. Supply of necessaries to persons incompetent to contract [Section 68]: The person who has supplied the necessaries to a person who is incompetent to contract or anyone who is dependent on such incompetent person, is entitled to claim their price from the property of such incapable person.

Example: *A supplies B, a lunatic, some necessaries suitable to the maintenance of his life. A is entitled to be reimbursed from B's property.*

The following conditions are necessary for the applicability of the provisions of Section 68:

- a) There must be the supply of necessaries to a person who is incompetent to contract such as a minor or a person of unsound mind or dependents of such incompetent person.
- b) The term 'necessaries' shall be construed in accordance with the situation in life of the incompetent person, the nature of goods, the extent of supplies, etc.
- c) The supplier can claim only reasonable value for the supplies made.
- d) The reimbursement of the price of goods supplied can be obtained from the property of the incompetent person who cannot be held personally liable.

2. Payment by an interested person [Section 69]: A person who is interested in the payment of money which another is bound by law to pay, and who, therefore, pays it, is entitled to be reimbursed by the other”.

Example: *X is bound by law to make a certain payment. Y is interested in such a payment, and he makes it, there will be a quasi contractual obligation of X to reimburse Y.*

In order to make Section 69 applicable, the following conditions must be satisfied:

- a) The plaintiff should be interested in making the payment in order to protect his own interest and the payment should not be voluntary one.
- b) The payment must be such as the other party was bound by law to pay.
- c) The payment must not be such as the plaintiff himself was bound to pay.

3. Liability to pay non-gratuitous acts [Section 70]: Where a person lawfully does anything for another person, or delivers anything to him not intending to do so gratuitously and such other person enjoys the benefits thereof, the latter is bound to make compensation to the former in respect of, or to restore, the things so done or delivered.

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

A claim under this Section can be made only when the following conditions are satisfied:

- a) The thing must have been done or delivered lawfully;
- b) The person who has done or delivered the thing, must not have intended to do so gratuitously; and

- c) The person for whom the act is done/to whom thing is delivered must have enjoyed the benefit of the act done/thing delivered.

4. Responsibility of a finder of goods [Section 71]: A person who finds goods belonging to another, and takes them into his custody, is subject to the same responsibility as a bailee.

Example: *X, a guest found a diamond ring at a birthday party of Y. X told Y and other guests about it. He has performed his duty to find the owner. If he is not able to find the owner he can retain the ring as bailee.*

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

Example: *A paid some money to B by mistake which was in fact due to C. In this case, B must repay the money to C as it had been paid under a bonafide mistake.*

DISCHARGE OF CONTRACT

Discharge of contract means termination of the contractual relations between the parties to a contract. A contract is said to be discharged when the rights and obligations of the contracting parties are extinguished and their relationship comes to an end.

VARIOUS MODES OF DISCHARGE

A contract may be discharged in the following ways:

- By performance of contract.
- By agreement.
- By lapse of time.
- By operation of law.
- By impossibility of performance.
- By committing breach of contract.

(1) DISCHARGE BY PERFORMANCE OF CONTRACT

Performance of a contract is one of the most usual ways of discharge of a contract when the parties to the contract fulfill their obligations under a contract, the contract is said to have been performed and the contract comes to an end. Performance of contract may be classified as:

- a) **Actual Performance:** A contract is said to be discharged by actual performance when the parties to the contract perform their promise in accordance with the terms of the contract.
- b) **Attempted Performance or Tender:** A contract is said to be discharged by attempted performance when the promisor has made an offer of performance (i.e., a valid tender) to the promisee but it has not been accepted by the promisee.

(2) DISCHARGE BY AGREEMENT

As contract emerges from an agreement of both parties, it may also be terminated by another agreement or consent of both parties. A contract can be discharged by mutual agreement in any of the following ways:

- a) **By novation (Substitution of a new contract):** Novation means substituting a new contract for the existing one, either between the same parties or between different parties, the consideration mutually being the discharge of the old contract. The novation may be of the following two types i.e., (i) novation involving change of parties, but the contract remaining the same (ii) novation involving substitution of a new contract, but parties remaining the same.
- b) **By alteration:** Alteration means change in one or more of the terms of a contract with the consent of all the parties. If any material alterations are made in the contract, the original contract will come to an end and in its place a new contract in an altered form comes into existence.
- c) **By rescission:** Rescission means cancellation of the contract. A contract may be rescinded by agreement between the parties at any time before it is discharged by performance or in some other way.
- d) **By remission:** The term 'remission' may be defined as the acceptance of lesser fulfillment of the terms of the promise, e.g., acceptance of a less sum of money where more is due.
- e) **By waiver:** When both the parties, by mutual consent, agree to abandon their respective rights, the contract need not be performed and the same is discharged. It is called waiver. To constitute a waiver, neither an agreement nor consideration is necessary.
- f) **By merger:** It takes place when an inferior right accruing to a party under a contract merges into a superior right accruing to the same party under the same or some other contract, e.g., a tenant buying the house in which he is a tenant.

(3) DISCHARGE BY LAPSE OF TIME

The Limitations Act, 1963 provides that a contract must be performed within the period of limitation. If the contract is not performed and the promisee fails to take any action within the period of limitation, then the contract is terminated or discharged by lapse of time.

(4) DISCHARGE BY OPERATION OF LAW

A contract may be discharged by operation of law in the following cases:

- a) **Death:** A contract involving the personal skill or ability of the promisor is discharged automatically on the death of the promisor.
- b) **Insolvency:** When a person is declared insolvent, he is discharged from his liability up to the date of his insolvency.
- c) **Unauthorized Material Alteration:** If any party makes any material alteration in the terms of the contract without the approval of the other party, the contract comes to an end.
- d) **Merger:** Where an inferior right accruing to a party in a contract merges into the superior rights accruing to the same party, the earlier contract is discharged.

(5) DISCHARGE BY IMPOSSIBILITY OF PERFORMANCE

A contract will be discharged when the performance of contract becomes impossible. The effects of impossibility of performance may be of the two types, namely,

- a) **Initial impossibility:** It is the impossibility which exists at the time of formation of contract. It makes the contract *void ab initio*, i.e., void from the very beginning.

b) Subsequent or supervening impossibility: Supervening impossibility means impossibility which does not exist at the time of making the contract but which arises subsequently after the formation of the contract and which makes the performance of the contract impossible or illegal.

Supervening impossibility is an excuse for the non-performance of the contract in the following cases:

- (i) ***Destruction of subject matter:*** If the subject-matter of a contract is destroyed after making the contract, without the default of either party, the contract is discharged.
- (ii) ***Death or personal incapacity:*** The contract is discharged on the death or incapacity or illness of a person if the performance of a contract depends on his personal skill or ability.
- (iii) ***Change of law:*** The contract is discharged if the performance of the contract becomes impossible or unlawful due to change in law after the formation of the contract.
- (iv) ***Non-occurrence or non-existence of particular state of thing:*** Where a contract is made on the basis of continued existence or occurrence of a particular state of things, the contract comes to an end if the state of things ceases to exist or changes.
- (v) ***Outbreak of war:*** The pending contracts at the time of declaration of war are either suspended or declared as void.

(6) DISCHARGE BY BREACH OF CONTRACT

A contract is said to be discharged by breach of contract if any party to the contract refuses or fails to perform his part of the contract or by his act makes it impossible to perform his obligation under the contract. Breach of contract is of two kinds, namely,

- a) Anticipatory breach of contract:** When a party to a contract refuses to perform his part of the contract, before the due date of performance, it is known as anticipatory or constructive breach of contract.
- b) Actual breach of contract:** Actual breach of contract occurs in the following two ways:
 - (i) ***On due date of performance:*** If a party to a contract fails to perform his obligation at the specified time, he is liable for its breach.
 - (ii) ***During the course of performance:*** If during performance of a contract, a party to it either fails or refuses to perform his obligation, there is said to be actual breach during performance of the contract.

FRUSTRATION

Frustration may be defined as the pre-mature termination of the contract owing to the change of circumstances which are entirely beyond the control of the parties.

REMEDIES FOR BREACH OF CONTRACT

A breach of contract occurs if any party refuses or fails to perform his part of the contract or by his act makes it impossible to perform his obligation under the contract. A breach of contract may arise in two ways, (a) anticipatory breach and (b) actual breach. A remedy is the course of action available to an aggrieved party (i.e., the party not at default) for the enforcement of a right under a contract. The various remedies available to an aggrieved party are as follows:

- Suit for rescission of the contract.
- Suit for damages.
- Suit for specific performance
- Suit for injunction
- Suit upon quantum meruit.
- Restitution.

I. RESCISSION OF THE CONTRACT

Rescission of a contract means annulment of it. When all or some of the terms of the contract are cancelled, rescission of a contract takes place. When there is a breach of contract by one party, the aggrieved party may rescind the contract and need not perform his part of the contract. The aggrieved party has to file a suit for rescission. When rescission is granted, the aggrieved party is absolved from all his obligations under the contract.

The court grants rescission in the following cases:

- a) Where the contract is voidable at the option of the plaintiff.
- b) Where the contract, is unlawful for causes not apparent on its face and the defendant is more to blame than the plaintiff.

The court, may, however, refuse to grant rescission, in the following cases:

- a) Where the plaintiff has expressly or impliedly ratified the contract; or
- b) Where owing to change in the circumstances of the contract, the parties cannot be restored to their original position; or
- c) Where the third parties have, during the subsistence of the contract, acquired right's in the contract in good faith and for value; or
- d) Where only a part of the contract is sought to be rescinded and such part is not severable from the rest of the contract.

II. SUIT FOR DAMAGES

“Damages” are monetary compensation allowed for loss suffered by the aggrieved party due to breach of contract. The object of awarding damages is not to punish the party at fault but to make good the financial loss suffered by the aggrieved party due to the breach of contract.

Types of Damages

- a) **General or ordinary damages:** These are the damages which are payable for the loss arising naturally and directly, in the usual course, from the breach of contract. In a contract for the sale of goods, the measure of ordinary damages is the difference between the contract price and the market price of such goods on the date of breach.
- b) **Special damages:** These are the damages which are payable for the loss arising due to some special or unusual circumstances.
- c) **Exemplary or punitive or vindictive damages:** These are the damages which are in the nature of punishment. The court may award these damages in case of:
 - i) Breach of contract to marry.

- ii) Wrongful dishonour of cheque by a banker in violation of Section 31 of the Negotiable Instruments Act. The damages are estimated on the basis of loss of prestige and goodwill of the customer. The rule applied in this case is that smaller the amount of cheque, the higher shall be the damages.
- d) **Nominal damages:** These are the damages which are very small in amount. Such damages are awarded simply to establish the right of the party to claim damages for the breach of contract even though the party has suffered no loss.
- e) **Liquidated damages and penalty:** When the amount of compensation fixed by an agreement between the parties to be paid in case of breach of contract is in the nature of a fair and honest pre-estimation of probable damages. It is called liquidated damages.

When the amount named in the contract at the time of its formation is disproportionate to the damages likely to accrue in the event of breach, it will be known as penalty.

Rules Regarding Determination of Damages

Section 73 of the Contract Act provides that when a contract has been broken the party who suffers by such breach, is entitled to receive, from the party who has broken the contract.

1. **The ordinary damages are recoverable:** The aggrieved party is entitled to receive such damages:
 - a) as may fairly and reasonably be considered to arise naturally from the breach; or
 - b) as may reasonably be supposed to have been in the contemplation of both the parties at the time of making of contract as the probable result of breach.
2. **Remoteness of damage:** Compensation shall not be granted for any remote or indirect damage. Damages are considered to be remote if they are not the necessary or probable consequence of breach or if they were not in the contemplation of the parties at the time when contract was made. Loss of profit is not to be taken in account in estimating damages unless otherwise agreed upon.
3. **Primary aim of damages:** The primary aim of the law of damages for breach of contract is to place the aggrieved party in the position which he would have occupied if the breach had not occurred.
4. **Special damages, i.e., damages in the contemplation of the parties:** Special damages which do not arise naturally from the breach cannot be recovered unless these were in the contemplation of the parties.
5. **Only compensation, no penalties:** Damages are allowed by way of compensation for the loss suffered and not by way of punishment except in the case of (a) breach of promise to marry, and (b) wrongful dishonour of a cheque by a bank.
6. **Nominal damages:** What the aggrieved party has not suffered any loss, the court may allow him nominal damages, in its discretion.
7. **Mental pain and suffering:** Damages are not allowed for injured feeling or mental pain except where (i) the breach was reckless, (ii) it caused bodily harm, and (iii) the defaulting party was

aware that breach would cause mental suffering.

8. **Duty to mitigate the loss:** It is the duty of the injured party to take all reasonable steps to mitigate the loss caused by the breach. He cannot seek damages for loss which are not due to breach but due to his own neglect to mitigate the loss.
9. **Difficulty of assessment:** Any difficulty in assessing damages shall not prevent the injured party from recovering them. The court must do its best to determine the amount of damages.
10. **Cost of decree:** The aggrieved party can recover the cost of getting the decree along with the damages.

III. SUIT FOR SPECIFIC PERFORMANCE

This means demanding the court's direction to the defaulting party to carry out the promise according to the terms of the contract. Specific performance of the contract may be directed by the court in the following circumstances:

- (i) Where actual damages arising from breach are not measurable.
- (ii) Where monetary compensation is not an adequate remedy.

Specific performance of an agreement will not be granted –

- a) Where the damages are considered as an adequate remedy;
- b) Where the contract is of personal nature, e.g. contract to marry;
- c) Where the contract is made by a company beyond its powers as laid down in its Memorandum of Association;
- d) Where the court cannot supervise the performance of the contract;
- e) Where one of the parties is a minor;
- f) Where the contract is inequitable to either party.

IV. SUIT FOR INJUNCTION

An injunction is an order of the court requiring a person to refrain from doing some act which has been the subject matter of contract. The power to grant injunction is discretionary and it may be granted temporarily or for an indefinite period.

V. SUIT UPON QUANTUM MERUIT

The word '*quantum meruit*' literally means "as much as is earned" or "according to the quantity of work done". When a person has begun the work and before he could complete it, if the other party terminates the contract or does something which makes it impossible for the other party to complete the contract, he can claim for the work done under the contract.

VI. RESTITUTION

Restitution means 'an act of restoration'. If a person has been unjustly enriched at the expense of the other party, he should restore the benefit received or compensate the other party.

COMPANY LAW

Unit - II

Definition, Nature and Kinds of a Company

Definition: A company is an Association (Voluntary) of many persons who contribute money or money's worth to a common stock & employs it in some common trade/ business and share the profit or loss arising them.

Nature/ Characteristics of a Company

1. An artificial person created by law

It is an artificial person, because it does not take birth but created by law.

2. Separate legal entity:

- An entity separate from its members
- It has an independent corporate existence
- The Company's money & property belong to them not to the shareholders

Eg. Salomon Vs. Salomon & Co. case

3. Limited liability: If the company limited by shares, the liability of the members is limited to the unpaid value of the share. (Eg. Face value: Rs.10, he paid Rs.7, yet to pay only Rs.3).

4. Perpetual succession

- The company never dies, nor does its life depends on the life of its members.
- The members may come and go but the company can go on forever (until dissolved), it continues to exist even if all its human members are dead.
- A company's exist persist irrespective of the change in the composition of its membership.

5. Common seal: The company seal acts as the official signature of the company

6. Transferability of shares: Company shares are subject to certain conditions, freely transferable.

7. Separate property: Being a separate person, company is able of owning, enjoying & disposing of property in its own name.

8. Capacity of sue: A company can sue and be sued in its own corporate name.

Kinds of Companies

I. Classification on the basis of incorporation

1. Statutory companies
2. Registered companies

II. Classification on the basis of liability

1. Companies with limited liability
 - a. Companies limited by shares
 - b. Companies limited by guarantee
2. Companies with unlimited liability

- III. Classification on the basis of Number of members
 - 1. A private companies
 - 2. A public companies
- IV. Classification on the basis of control
 - 1. Holding companies
 - 2. Subsidiary companies
- V. Classification on the basis of ownership
 - 1. Govt. companies
 - 2. Non- Govt. companies
- VI. Association not for profit
- VII. One man company

I. Classification on the basis of incorporation

- 1. **Statutory companies:** - Created by a special act of the legislature, Eg.RBI, SBI, etc.
 - These are mostly concerned with public utilities Eg. Railways.
- 2. **Registered companies:** -formed and registered under the companies' act 1956/2013.

II. Classification on the basis of liability

1. Companies with limited liability

a. Companies limited by shares

- Where the liability of the members of a company is limited to the amount of unpaid/paid on the shares.
- The liability can be enforced during the existence of the company as also during the winding up.

b. Company limited by guarantee

- The member's liability is limited to a fixed amount, which the members undertake to contribute to the assets of the company.

2. Unlimited company

- Every member is liable for the debts of the company
- Their liability is unlimited
- These may/may not have share capital

III. Classification on the basis of Number of members

- 1. **Private company** (close corporation): Sec.3 (1)(iii), defined, a private company has a minimum paid up capital of Rs.1,00,000 or more as prescribed and also.
 - a. Restricts the right to transfer its shares
 - b. Limited members (Max.200)
 - c. Prohibits any invitation to the public to subscribe for any shares/ debentures
 - d. Prohibits any acceptance of deposits from persons other than its members
 - e. Number of debenture holders in a private company may exceed 50
 - f. Joint holders of shares are treated as a single member

2. Public company

- Minimum paid up Rs.5 lakhs and maximum as prescribed
- Shares freely transferable
- It can invite the public to subscribe for shares

Distinction between a Public company and a Private company

S.N.	Particulars	Public	Private
1	Minimum capital	Rs.5,00,000	Rs.1,00,000
2	Minimum members	07	02 (1 person company)
3	Max. members	Unlimited	200
4	No. of Directors	Atleast 03	Atleast 02
5	Restriction on appointment of directors	Qualification approval from Registrar is must	It is not necessary
6	Restriction on invitation to subscribe for shares	Can invite the public	Prohibited to invite public
7	Transferability of shares & Debentures	Freely transferable	Restricted
8	Quorum	5 members must be present	2 members must be present
9	Managerial remuneration	Total remuneration should not exceed 11% on Net profit	No restriction (If it is not a subsidiary of a public co.)
10	“Limited” title	The word of “Limited” should be added followed by company name	The word of “Private Limited” should be added followed by company name
11	Special privileges	No such privileges to Public limited companies	It enjoy the following privileges: a. Need not issue prospectus b. Mini. 2 members enough c. May issue any kind of shares d. 2 directors enough e. Statutory meeting and reporting is not necessary f. No restriction on managerial remuneration (If it is a subsidiary of Public co. limited to 11% on NP) g. Can commence business immediately on incorporation

IV. Classification on the basis of Number of control

1. **Holding company:** If a company has control over the other company

2. **Subsidiary company:** If a company coming under the control of another company (Holding company) called subsidiary company.

Other conditions:

- Holding company must control the appointment and removal of the directors of the subsidiary companies
- Holding company must have the majority shares of the subsidiary company
- Subsidiary company of another subsidiary co. – must come under the Holding company.

Eg. **H** → **S** → **S1** → **S2**, Here **S1** and **S2** are the subsidiaries of **H**.

V. Classification on the basis of Ownership

1. **Govt. Company:** A company in which not less than 51% of the paid up share capital held by (a) The Central Govt. or (b) State Govt. or (c) Partly Central and partly by State.

Rules: - Appointment of auditors – Auditors should be appointed by Central Govt. on the advice of Auditor General of India.

- Audit report to be submitted to Auditor General of India
- Annual report to be placed before parliament
- 51% of paid up share should be held by the Govt.

2. **Foreign company:** Any company incorporated outside India, which has an established place of Business in India.

Rules:

a. Documents: Every foreign company, within 30 days of its establishment in India, shall file with the Registrar the following documents.

- Certificate copy of the Charter, AoA, MoA, etc.,
- Full address & Principal office
- A list of directors and Secretaries
- The name & address of any person reside in India

b. Books of Accounts – as Indian company

c. Obligation to furnish the country of incorporation

d. Documents to be delivered to registrar

- VI. **Association not for Profit:** The Central Govt. may grant a license to an association for

- Promoting commerce, science, religion, charity or any other useful object
- Using its profit for its objective and not for payment of dividend

- VII. **One Man Company (OPC –One Person Co.):** This is a company in which, one man holds the whole of the share capital of the company. Some dummy members may be appointed to satisfy the statutory requirements.

- VIII. **Illegal association:** If the number of members in an association/ orgn. exceeds the limit and it is not registered under the companies act 1956 is called an illegal company or association.

FORMATION OF A COMPANY

Formation of the company means incorporating or creating the company.

Project ‘MCA-21’ - Ministry of Corporate Affairs has launched a programme for managing the work relating to filing of documents, etc. with ROCs etc. and getting approvals from Ministry of Corporate Affairs. The physical filing of all forms has been discontinued and converted into electronic filing. This project is termed as Project ‘MCA-21’.

Incorporation of Company

1. Provisions relating to filing of applications, documents, inspection, etc., through electronic form

- Applications and required documents shall be filed through the electronic form and authenticated in such manner as may be specified in the rules.
- ‘Certificate Filing Centers’ (to be operated by professionally qualified persons/CA/ICWA/CS) will facilitate e-filing of documents.
- Every director will have to obtain DIN (Director’s Identification Number).
- Filing of forms and application will be through internet
- Payment of fees can be through internet through credit card/ net banking
- Office of ROC, Regional Director and Delhi HQ will process the documents and applications submitted electronically by companies.
- Issuance of certificated and approvals will continue to remain on paper. This will be dispatched by post or courier to applicant.

2. Documents to be filed with the Registrar: The following documents duly stamped together with the necessary fees are to be filed with the Registrar of Companies.

- a. The Memorandum of Association
- b. The Articles of Association
- c. Agreements & appointment of Managerial persons
- d. A list of directors
- e. A declaration about the formalities and should be signed by the following persons
 - i. An advocate of Supreme court/ High court
 - ii. An attorney
 - iii. Secretary or Chartered accountant
 - iv. A person named in articles as director
- f. Notice about the situation of the Registered office

3. Certificate of Incorporation

If the Registrar satisfied with the documents, which are submitted, he retains them and issues a “Certificate of Incorporation” (of the formation of the company), the Registrar is not required to carry out any investigation about the truthfulness of the given documents.

4. Conclusiveness of Certificate of Incorporation

A certificate of incorporation given by the Registrar is the conclusive evidence that means the company has fulfilled all the requirements - this is known as **Rule in Peel's case**.

Ref. case:

- The date mentioned in the certificate of Incorporation (CoI) is the date of the Birth of the company
- Even though the company got CoI, its illegal activities cannot be legalized

5. Effect of Registration

- The company becomes a distinct legal entity
- It acquires a perpetual succession
- It's property is not the property of its shareholders

6. Business commencement certificate

Private limited company can commence business immediately after its incorporation; but Public limited company can commence business after getting Business commencement certificate.

Promoter: He is a person do all the necessary preliminary work and takes preliminary essential decisions (such as whether it should be a private/ public co., capital, etc.).

Pre- incorporation/ Preliminary contracts

If any contracts agreed before incorporation (Before getting CoI) by the promoter is called Pre-incorporation or Preliminary contracts.

- The company is not liable for the acts of the promoters done before its incorporation

Conditions:

- Company not bound by pre-incorporation contracts
- Company cannot enforce pre-incorporation contract
- Promoters are personally liable.

Provisional contracts

It refers to contracts entered into by a public company after its incorporation but before it is to be issued the certificate of commencement of business.

MEMORANDUM OF ASSOCIATION

It is a fundamental document defines its **raison d'être** (i.e. reason for existence)

Features:

- a. It contains fundamental conditions
- b. Regulates the external affairs of the company
- c. Lays down the area of operation
- d. Reason for existence
- e. Possible scope of the company

Content of Memorandum of Association

1. **Name clause:** The name of a company followed by limitation/ private limited and its identity and symbol of its existence is given in the Memorandum of Association (MoA).

Rules/ Conditions:

- a. Undesirable name to be avoided
 - As per the opinion of the Central Govt. the company must avoid
 - i. Too similar to the name of another company
 - ii. Misleading
- b. Injunction if identical name adopted
- c. 'Limited' or 'Private Limited' as the last word of words of the name
- d. Prohibition of use of certain names – such as
 - i. Emblem and Name of United Nations Organisation, WTO, etc.,
 - ii. Indian National flag, the name, emblem, official seal etc.,
 - iii. Emblem and seal of Central & State Govt. and President of India
- e. Use of some key words according to authorized capital

S.N	Key word	Authorized Capital
1	Corporation	5 Crores
2	International, Global, Universal, Asia, Continental – being first word	1 Crore
3	Hindustan, India, Bharat – Being first word	50 Lakhs
4	Industries/ Udyog	1 Crore
5	Enterprise, Products, Business, Manufacturing	10 Lakhs

Publication of Name:

- Paint its name with address, it should be placed on the outside of the registered office
- It should be in legible character
- It should be used in all business letters, bill heads, invoices, receipts, etc.

2. The Registered office clause

Every company should have the registered office at the time of registration. All communications and notices are to be send to that address.

Notice of situation of the registered office and every change shall be given to Registrar within 30 days after the date of incorporation

In case of default, the director will be punished with fine of Rs.500 for every day during which the default continues.

3. The objects clause:

The objects clause of a company shall be clearly stated in Memorandum, it defines the scope of the company and any alteration could be made only as per the law.

It enables the subscriber to know the purpose of their investment and enables the creditors to know the persons involved in company activities.

The object clause in Memorandum of every company has to state (i) Main object and (ii) Other object.

4. The Capital clause

- The Registered/ authorized/ Nominal capital should be stated
- It also be stated the amount of shares, its type etc.

5. The Liability clause

The liability of its members is stated in this clause, whether they are limited by share or limited by guarantee.

6. The Association clause

- Declaration of all the directors & members/ subscribers is stated
- The names, addresses & description of the subscribers and number of shares taken by each one of them is mentioned

The MoA shall be signed by at least 7 subscribers in case of public company (2 in case of private company). Their signature shall be attested by at least 1 witness (the witness should not be the relative/ another subscriber).

Alteration of Memorandum – Alteration of Conditions:

1. Change of name

- The company may change its name with the approval of the Central Govt.
- Mere changing the word 'Private' to 'Public' or vice versa, need not get the approval
- The company may change its name by ordinary resolution and shall change its name within 12 months of its registration as per the direction of the Central Govt.
- If the company does not follow the direction given by the Govt., shall be punishable with fine of Rs.100 for every day during which the default continues.
- Where the company changes its name, the Registrar shall enter the new name & issue a fresh certificate of incorporation in new name.

2. Change of registered office

a. *Change of Registered office from one place to another within a state:*

- The company has to give an application to the Regional Director for getting confirmation order

- The Regional Director issues the order and it should be send to the Registrar within 2 months for getting approval.
- b. *Change of Registered office from one state to another*
-It is possible by passing a special resolution

3. Alteration of Objects

The objects of a company may be altered by special resolution, so as to enable the company:

- a. To carry on its business more economically or more efficiently
- b. To attain its main purpose by new/ improved means
- c. To enlarge its operation
- d. To amalgamate with any other company

4. Change in liability clause

- A company limited by shares/ guarantee cannot change its liability clause in the memorandum
- It is possible to give additional liability to its members

5. Change in capital clause: The Company may change in the capital clause about increase, reduction or re-organisation.

Doctrine of Ultra Vires (Ultra- Beyond; Vires- Power): It means that the company doing of the act is beyond the legal power and authority of the company. Ultra Vires act is void.

Ultra vires the directors: They do beyond their powers, but within the powers of the company

Ultra vires the articles: If an act or transaction is done beyond the articles.

Articles of Association

The Articles of association or Articles are the rules, regulations and bye-laws for the internal management of the affairs of a company.

Forms and Signature of Articles (Sec.30)

1. Printed
2. Divided into paragraphs
3. Signed by each members with one witness
4. Printed on computer laser printer and it should be accepted by the Registrar.

Contents of Articles

1. Share capital, rights of shareholders, payment of commissions etc.	10. General meetings and proceedings
2. Line on shares	11. Voting rights of members, proxies
3. Calls on shares	12. Directors appointment, remuneration, qualification, powers, etc.
4. Transfer of shares	13. Managers
5. Transmission of shares	14. Secretary
6. Forfeiture of shares	15. Dividend and reserves

7. Conversion of shares in to stocks	16. Accounts, audit and borrowing powers
8. Share warrants	17. Capitalisation of profits
9. Alteration of capital	18. Winding up

A public company may have its own Articles of association. If it does not have its own Articles, it may adopt Table A given in Schedule I to the Act.

Alteration of Articles: Companies have been given full power to alter their articles, unless otherwise it is restricted by any provision.

Procedure of alteration: - By passing special resolution

- Alterations should be informed to the Registrar within 30 days of its passing

Limitations to Alteration

1. Must not be inconsistent or go beyond with the companies act
2. Must not conflict with the Memorandum
3. Must not sanction any illegal
4. Must be for the benefit of the company
5. Must not increase the liability of members
6. Alteration by special resolution only
7. Approved of Central Govt. is must – when Public co. is converted to Private co.
8. Alteration leads to breach of contract is valid
9. Must not result in expulsion (removal) of a member
10. No power of the Tribunal to amend articles
11. Alteration may be with retrospective (show) effect

Doctrine of Indoor Management

The outsiders of company presume that all the activities of the company is being done regularly and within the scope of the MoA and AoA. This is known as “Doctrine of Indoor management” or “The rule in Royal British bank Vs. Turquand” or “Turquand rule”.

Case: Ref. Royal British Bank Vs. Turquand/ CL/N.D.Kapoor

Exception: 1. Knowledge of irregularity 2. Negligence 3. Forgery
4. Acts outside the scope of MoA & AoA

Memorandum of Association and Articles of Association – Distinction

Memorandum of Association	Articles of Association
1. It indicates the nature	1.It indicates the rules and regulations
2. It defines relationship with outside world	2. It defines relationship with Internal management of the company
3. It defines the scope of the company, the company can not go beyond	3. They are the rules for carrying out the objects of the company
4. It is a Supreme document	4. It is subordinate to the Memorandum
5. Every company must have its own memorandum	5. Company limited by shares need not have articles of its own – Table A applies
6. There are strict restrictions on its alteration	6. AoA can be altered by special resolution, but do not conflict with Memorandum and Companies act
7. Any act of the company is Ultra vires the memorandum is void	7. Any act of the company is Ultra vires to Articles may be confirmed by the shareholders.

PROSPECTUS

Any document inviting deposits from the public or inviting offers from the public for the subscription of shares or debentures of a company is a prospectus.

Private Company need not issue a Prospectus, because it is prohibited from making any invitation to the public to subscribe for any shares or debentures of the company.

Features

1. It is an Invitation/ Ad./ Circular to the public to subscribe for any shares or debentures of the company
2. It should be in writing (Ads. In TV/ Films is not a prospectus)
3. Invitation to the public – any invitation made to its friends or relatives to subscribe shares is not a prospectus
4. Offer to the public
5. Must be dated
6. Must be signed by the Directors and Registered to the Registrar.

Red- herring Prospectus or Information memorandum

It is a circular issued to the public prior to filling or issuing prospectus. Generally, it does not have complete particulars about price and number of shares to be issued.

Content of the Prospectus

The important content of Prospectus is as follows

A. Part I of Schedule II

1. General information

1.Name & Address of Reg. office	7.Date of Opening & Closing of issue
2.Consent of the Central Govt. about present issue and about its financial soundness	8.Name & address of Auditors and lead managers
3.Name of its Regional stock exchange	9.Name & Address of Trustee
4.Provision relating to punishment for fictitious application	10.Rating from CRISIL or any other agency
5.Declaration about refund of the issue, if Minimum subscription is not attained	11. Underwriting of the issue
6.Declaration about allotment of shares	

2. Capital structure of the company

- a. Authorised, Issued, subscribed and paid-up capital
- b. Size of present issue – its reservation (Preferential allotment)
- c. Paid up capital – after the present issue or after the conversion of debenture

3. Terms of the Present issue

- a. Terms of payment
- b. Rights of the instrument holder
- c. How to apply – availability of forms, etc.
- d. Any special tax benefits, if any.

4. Particulars of the Issue

- a. Object b. Project cost c. Sources of finance

5. Company management and project

1.History, objects and present business of the company	7.Collaboration agreement, if any
2.Promoters & their Background	8.Infrastructure facility for Raw material, power, water etc.
3.Subsidiary of the company	9.Schedule of implementation of project
4.Name & address of Directors	10.Nature of product & marketing etc.
5.Location of Project	11.Future prospectus and development
6.Plant, Machinery & Technology used	

6. Particulars about the company and its subsidiaries (Sister concerns)

7. Outstanding litigation relating to – (a) Operation and finance of the company
(b) Particulars of default, etc.

8. Management perception of risk factors – Reg. availability of raw materials, fluctuations in foreign exchange rate, marketing, etc.

B. Part II of Schedule II

1. General information

- Consent of Directors, Auditors, Advocates, Managers, Bankers & Registrar
- Expert's opinion
- Change of any directors of auditors, if any, in the last 3 years and its reasons
- Authority for the issue
- Procedure and time schedule for allotment and issue of certificates
- Name & address of Company secretary, Legal adviser, etc.

2. Financial information

- Report by the auditors – About profit and loss, Assets & liabilities and Rate of dividend paid by the company during the preceding 5 financial years.
- Reports by the Accountants – on the profits or losses of the business for the preceding 5 financial years and about the assets and liabilities of the business (Not more than 120 days before the date of issue of prospectus).

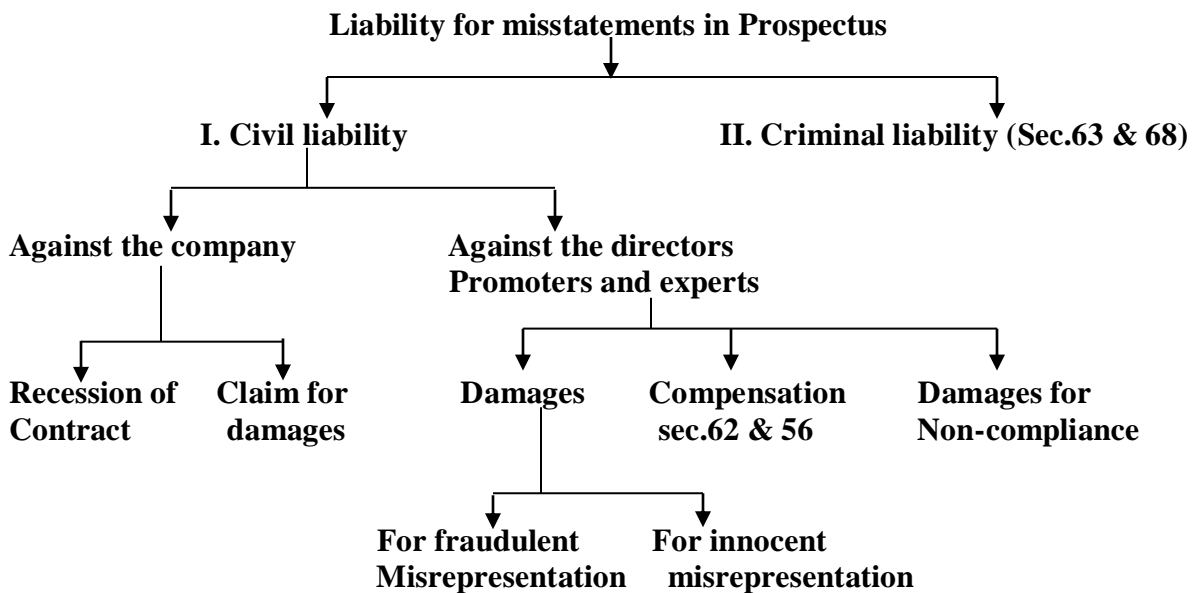
3. Statutory and other information

- Minimum subscription
- Expenses of the issue, fees structure etc.,
- Commission and brokerage
- Previous issue for cash
- Previous public issue- Date of allotment, closing date, date of refund etc.,
- Issue of shares otherwise than for cash

- g. Debentures and redeemable preference shares and other instruments issued by the company outstanding as on date of prospectus
- h. Options to subscribe
- i. Details of purchase of property
- j. Rights of members regarding Voting, dividend etc.,
- k. Restrictions, if any, on transfer of shares/ debentures
- l. Material contracts and inspections.

Misstatement in prospectus & their consequences

If there is any misstatement of a material fact in a prospectus, there may arise



I. Civil liability

A person who has been induced to subscribe for shares on the faith of a misleading prospectus has remedies against the company, promoters and experts.

1. Remedies against the company

If there is a misstatement or withholding of material information in a prospectus and if it induced, the share-holder can

- a. Rescind/ rescission of the contract
- b. Claim damages from the company, if the statement is fraudulent/ innocent

a. Rescission of the contract (Rescind the contract)

A person can apply to the court for the rescission of the contract, if such statements in the prospectus are false, fraudulent, or withholding of material information but he will have to surrender all the shares to the company. The contract can be rescinded in the following conditions are satisfied:

- i. The statement must be a material misrepresentation of fact

- ii. The statement must have induced the shareholder to buy them
- iii. The statement must be untrue
- iv. If the shares should not be purchased in open market (If so, recession is not possible)
- v. The omission of material fact must be misleading.

b. Damages for deceit (dishonesty)

- The affected person entitled to sue the company for damages
- He must prove the same matter
- He cannot both retain the shares and get damages against the company

2. Remedies against the Directors, promoters and experts – Their liabilities

a. Liability for damages for misstatement in prospectus – should pay the compensation.

Defenses of Directors:

- i. Withdrawal of consent
- ii. Absence of consent
- iii. Ignorance of untrue statement
- iv. Reasonable ground for belief
- v. Statement of experts

b. Liability for damages for omission

c. Liability under general law: If the mistake is done in the following nature

- Knowingly
- Without belief in its truth
- Recklessly, not caring whether it was true or false

II. Criminal Liability

Where a prospectus contains any untrue statement, every authorised person is punishable with imprisonment upto 2 years or fine upto Rs.50,000 or both.

Criminal activities:

- a. Issue and allotment of shares in fictitious names
- b. Fraudulently inducing persons to invest money
- c. Issuing application for shares without memorandum

DIRECTORS

Directors: A person having control over the direction, contact, management of the affairs of the company. Only an individual can be a director.

Powers of Directors

A. General powers of the board (Sec.291)

- Board of Directors is empowered to do all acts and things as the company is authorities to exercise and do.
- The Board shall not do any acts, which are to be done in company general meeting
- The Board shall exercise its power subject to the provision given in the companies act, MoA and AoA.

B. Powers to be exercised at Board meetings (Sec.292)

The directors are empowered to do the following as the resolution passed in the meeting.

- a. Make call on shareholders for unpaid shares
- b. Issue debentures
- c. Borrow money through public deposits (Except debentures)
- d. Invest the funds of the company and
- e. Make loans
- f. Can delegate the last three (c, d, & e) powers to a committee/ managers

C. Power to be exercised with the approval of company in general meeting (Sec.293)

- a. To sell, lease or dispose of the whole of the undertaking of the company
- b. To remit or give time for payment of any debt due
- c. To invest the compensation received by the co. for compulsory acquisition
- d. To borrow money
- e. To contribute to charitable and other funds, which are not directly relating to the business of the company

Duties of Directors

1. Fiduciary duties – as fiduciaries, the directors must
 - a. Exercise their powers honestly and bonafide for the benefit of the company
 - b. They should not make any secret profit
 - c. Should not involve any matters, which are against to the development of the company
 - d. Should not involve any matters of his personal interest
2. Duties of care, skill and diligence (Case: City equitable fire insurance Co. Ltd.)
 - Directors should carry out their duties with reasonable care, skill and diligence
 - The std. of care, skill and diligence is depends upon the nature of the company any circumstances, such standards of care depending upon the following:
 - * The type and nature of work
 - * Division of powers
 - * General usage and customs
 - * Directors work gratuitously or remuneratively

3. Other duties of directors:
 - a. To attend board meetings
 - b. Not to delegate his functions except to the extend
 - c. To disclose his interest regarding any contract

Liabilities of Directors

1. Liability to third parties

- a. **Under the act** – Directors are personally liable for the following activities as per the act
 - Failure to repay the application money (If minimum subscription is not attained)
 - Loss or damage is incurred due to irregular allotment of shares
 - Failure to repay the application money for which the stock exchange is not recognized
 - On failure by the company on pay a bill of exchange, pro-note, cheque etc., where the company is not mentioned in liable clause
- b. **Independently of the act**
 - Signing a negotiable instrument without mentioning the company's name
 - Any activity done in the name of the company

2. Liability to the company

- a. Ultra vires acts – The Directors is personally liable to the company for the any ultra vires act relating to payment of dividend, etc.
- b. Negligence – Personally liable for any loss/ damage arises due to negligence
- c. Breach of trust – liable to the company for any loss from breach of trust
- d. Misfeasance – (Willful misconduct) – Liable for willful misconduct

3. Liability for breach of statutory duties

Liable for the breach of statutory duties, ie., maintenance of proper accounts, filing of returns, observation of some statutory formalities, etc.

4. **Liability for acts of his co-directors:** A Director are not liable for the act of his co-directors provided he has no knowledge of that matter.

WINDING UP

According to Prof. Gower, winding up of a company is process whereby its life is ended and its property administered for the benefit of its creditors and members. Otherwise called Liquidation of a company or dissolving the company.

Modes of Winding up

There are Three modes of winding-up

1. Winding-up by the court i.e., Compulsory winding-up (Sec.433 to 483)
2. Voluntary winding-up (Sec.484 to 521)
 - a. Members' voluntary winding-up
 - b. Creditors' voluntary winding-up
3. Winding-up subject to supervision of court

1. Compulsory winding-up or winding-up by the Tribunal (Sec.433 to 483)

Winding-up of a company under the order of a Tribunal, such as

- a. Special resolution of the company
- b. Default in delivering the statutory report to the Registrar or in holding statutory meeting
- c. Failure to commence or suspension of business without proper reason
- d. Reduction in membership – Reducing the minimum members' strength (2 or 7)
- e. Inability to pay its debts
- f. Just and equitable – It means that the Tribunal has the power to winding-up of a company under judicial discretion depending upon the facts and circumstances, such as circumstances are as follows:
 1. When the substratum (Object or foundation) of a company is gone
That is the company failed to fulfill its objectives etc.,
 - a. Basis for the survival of the company is gone
 - b. Main objectives of the company has failed or impracticable
 - c. Carrying on its business at a loss and no hope for profit
 - d. Available assets are insufficient to meet the company debts
 2. Oppression (Domination) of minority shareholders
 3. There is deadlock in the management of the company
 4. Where public interest is likely to be prejudiced
 5. When the company carry out fraudulent or illegal business
 6. Where the company does not carry on any business or does not have any property
 7. Acting against the interest of the state (Govt.)
 8. Winding-up of a sick company

2. Voluntary winding-up (Sec. 484 to 520)

Winding-up by the member creditors of a company, without interference by the Tribunal. The members of creditors of a company settle their affairs without going to the Tribunal.

a. Members' voluntary winding-up

A declaration of solvency (Sec.488) is made by its members about winding-up in the Board meeting. The majority of the Directors at a Board meeting shall make the declaration about

the winding-up, at the time the company should not have any debt or able to clear all debts within 3 years from the commencement of winding-up.

- b. Creditors' voluntary winding-up:** The Company can be wound up by the resolution passed by the creditors at the general meeting.

Members' and Creditors' voluntary winding-up – a comparison

Particulars	Members'	Creditors'
1.Declaration of solvency	Issued by members	There is no such declaration
2.Control of winding-up	Members' control	Creditors' control
3.Meetings	No meeting with creditors	Meeting with creditors
4.Appointment of liquidator	Appointment by the company & remuneration fixed by company	Appointed by the Creditors & Remuneration fixed by the committee
5.Committee of inspection	There is no committee of inspection	There is committee for inspection
6.Powers of the Liquidator	Power is limited with the resolution passed in the company	Power is limited with the resolution passed in the committee or Tribunal.

Extra Question:

When does a private company become a public company?

1. Conversion by default

When a default is made by a private company in complying with the essential requirements of a private company.

- i.e., - Restriction on transfer of shares
- Limitation of the number of members to 50 etc.

2. Conversion by choice/ volition (freedom to decide)

A private company can become a public company by altering its articles. It should be informed/ filed to the registrar within 30 days, through prospectus.

And also:

- File a copy of the resolution altering the articles, with in 30 days to registrar
- Take steps to raise its membership to at least 07 and increase the number of directors
- Altering the regulations to essential for a public company

When does a Public company become a private company

- A special resolution should be passed in the board meeting and alteration should be made in the articles. Such alteration should be approved by central government.
- A print copy of such alteration shall be filed to registrar within one month of the date of receipt of approval.

Corporate Governance

It refers to “The process, mechanism, principles and structure by which the business and affairs of the company are directed and managed and governed effectively. Its goal is to enhance long term shareholder value through improving corporate performance and accountability while taking into account the interest of other shareholders”.

Corporate Governance is the system by which business corporations are directed and controlled. The Corporate governance structure specifies the distribution of rights and responsibilities among different participants in the corporation, such as the board, managers, shareholders and other stakeholders, and spells out the rules and procedures for making decisions on corporate affairs

The Corporate governance structure specifies the relations and the distribution of rights and responsibilities, among primarily three groups of participants, viz. the Board of directors, managers and shareholders.

Principal actors in corporate governance

Principal actors involved in corporate governance include the governing or regulatory body. This consist of:

Internal key actors – Chief Executive Officer, the Board of Directors,
Management & Shareholders and Employees.

External key actors – Suppliers, Creditors, Investors, Lenders, Customers, Society
and Government.

Stakeholders

The stake holders are the principal players in inception, sustainability, development and growth of any organisation. They are the Shareholders, Employees, Suppliers, Customers, Lenders, Investors, Banks, Government and Community at large.

4 P's of Corporate governance

People – Purpose – Process - Performance

Corporate governance has the integrated frame work, where the **people** are formally either trained or helped to develop to work for a definite and defined **purpose** in applying the systematic **processes** consistently to give the constant growth by better **performance**.

- **People** – Shareholders, Employees, Suppliers, Customers, Lenders, Investors, Society and Government
- **Purpose** – Established, Measurable, Actionable and Communicated
- **Process** – Established, Integrated, Documented, Automated, Implemented and Maintained
- **Performance** – Measured, Analyzed and Communicated

Principles / Elements of Corporate Governance

1. Rights and equitable treatment of shareholders

Organisations should respect the rights of shareholders and help shareholders to exercise those rights.

2. Interest of other stakeholders

Organisations should recognise that they have legal and other obligations to all legitimate stakeholders.

3. Role and responsibilities of the board

The board needs a range of skills, ability to understand various business issues and ability to challenge management performance

It needs to be of sufficient size and have an appropriate mix of executive and non-executive directors. The key roles of chairperson and CEO should not be held by the same person.

4. Integrity and ethical behaviour

Organisations should develop a code of conduct for their directors and executives that promotes ethical and responsible decision making

5. Disclose and transparency

Organisations should clarify and make publicly known the roles and responsibilities of board and management to provide shareholders with a level of accountability.

Contents of Articles

1. Share capital, rights of shareholders, payment of commissions etc.	10. General meetings and proceedings
2. Lien on shares (lien on a share means that the member would not be permitted to transfer his shares unless he pays his debt to the company.)	11. Voting rights of members, proxies
3. Calls on shares (demand made by the company on its share holders to pay whole or part of the balance remaining unpaid on each share at any time during the life time of a company")	12. Directors appointment, remuneration, qualification, powers, etc.
4. Transfer of shares (an existing shareholder <i>transfers</i> issued <i>shares</i> to another person)	13. Managers
5. Transmission of shares (passing of property in shares to the legal heirs. In the event of death of the shareholder)	14. Secretary
6. Forfeiture of shares (Shares may be forfeited if call is not paid within the stipulated time)	15. Dividend and reserves
7. Conversion of shares in to stocks	16. Accounts, audit and borrowing powers
8. Share warrants	17. Capitalisation of profits
9. Alteration of capital	18. Winding up

UNIT – III: LABOUR LEGISLATIONS

Introduction

The legislations formulated to protect the interest of the workers and also to provide them better working conditions/ environment.

Classifications

HRM functions

Staffing	Compensations & Rewards	Employee maintenance	Employee relations
1.Child labour prohibition & Regulation act 1986 2.The employment Exchange act 1959 3. The Apprentice Act, 1961 4.The contract Labour act, 1970 5.Bonded Labour system (Abolition) Act, 1976.	1. The Payment of wages act 1936 2.The minimum wages act, 1948 3. The payment of Bonus act, 1965 4. The Equal remuneration act, 1976.	1. The Factories act, 1948 2.The Mines act, 1952 3. The Employees provident fund & Miscellaneous provisions act, 1959 4.The Employees state Insurance act, 1948 5.Payment of Gratuity act, 1972 6. The Workmen's compensation act, 1923. 7. The Maternity Benefit Act, 1961.	1. The Trade Unions Act, 1926 2. The Industrial disputes act, 1947 3.The Industrial Employment (Standing Orders Act), 1946 4. <i>The Sales promotions Employees (conditions of Services) Act, 1976.</i>

Principles of Modern Labour Legislation

1.Principle of Protection- Example The Factories act, 1948, Child labour prohibition & Regulation act 1986, The Payment of wages act 1936, etc.,

2.Principle of social justice: Equality in social relationship, removing discrimination suffered by particular groups of labours. Certain group of labours having same sort of disabilities as compared to other groups. Eg. Indian slavery act, 1843, Equal remuneration act 1976.

3. Principle of Regulation: It regulates the relationship between employers and their associations. Eg. Trade union act 1926, The Industrial disputes act, 1947.

4. Principle of Welfare: Aims to provide certain welfare amenities to the workers and to ensure the provision of certain basic amenities to workers at their place of work. Eg. Beedi workers welfare fund act 1976.

5. Principle of Social security: Social insurance legislations and social assistance legislations. Eg. The Workmen's compensation act, 1923, The Maternity Benefit Act, 1961 and The Employees state Insurance act, 1948.

6. Principle of economic development: Improvement of physical working conditions, establishment of industrial peace.

7. Principle of International obligations: Accepted by ILO and UNO. Which are conventions and recommendations covered wide range of subjects – working conditions, employment of child labours, working hours, medical benefits, etc.

Types of Labour laws:

1. Protective Labour laws
2. Regulative Labour laws
3. Social security Labour laws
4. Welfare legislations.

OBLIGATIONS AND RIGHTS OF EMPLOYEES

Obligations: Under the Factories act, 1948, No workman in the factory is entitled to:

1. Interfere willfully or misuse any appliance, convenience or other things provided in a factory for the purpose of securing the health, safety and welfare of the factory workers.
2. Do willfully and without any reasonable cause anything likely to endanger himself or others.
3. Neglect willfully to make use of any appliance or other things provided in the factory for the purpose of securing the health and safety of factory workers.

4. Employees are expected to:

- * arrive at work on time
- * dress suitably for the job (wear safety equipment if required);
- * work to the best of their ability throughout their work day;
- * respect their employers, colleagues and customers;
- * take care of employer's property;
- * follow the employer's 'reasonable and lawful' instructions;

- * obey safety rules;
- * ask for help if they need it;
- * know what the employer expects the employee to do if the employee can't be at work for any reason;
- * not discriminate or harass others in the workplace; and
- * not act in a way that puts the employee – or others – at risk of injury in the workplace.

Rights of Employees: The workers enjoy the following rights under the Factories act, 1948.

1. They can claim minimum health and safety welfare facilities, annual leave, observance of working hours for adults, women and children.
2. They can refuse to work in contravention of provisions of the act and observe the statutory working hours, rest intervals, weekly holidays and overtime restrictions.
3. They can claim overtime payment at double the ordinary rates of wages, and also advance payment for annual leave if the period of leave is of not less than four days.
4. They can claim wages for the proportionate annual leave even before he puts in the qualifying service, if he/she is discharged or dismissed.
5. **Employees are entitled to:**
 - * be paid the right wage for the job they do;
 - * protection from unfair dismissal;
 - * sick leave, annual leave, public holidays, family leave and long service leave;
 - * have an unfair contract of employment which is not covered by an industrial award or a contract for services, amended or invalidated; and
 - * freedom to belong to or not belong to a union.

INDUSTRIAL LAW

THE FACTORIES ACT-1948

- It came in to force on 01.04.1949
- Its object is to regulate the conditions of work in manufacturing establishments which come within the definition of the term 'factory'.

Factory: A factory is a premise whereon 10 or more persons are engaged if power is used, or 20 or more persons are engaged if power is not used in a manufacturing process.

* Factory does not include: Mines, Railway running shed, a hotel & restaurant

Approval, Licensing & Registration of factories:

- The state govt. is empowered for giving approval, licensing and registration
- Application for permission to be sent to – Chief inspector or the State govt.

Occupier: The person who has ultimate control over the affairs of the factory

Labour welfare: The term 'Labour Welfare' refers to the facilities provided to workers in and outside the factory premises such as canteens, rest and recreation facilities, housing and all other services that contribute to the wellbeing of workers.

Health, Safety and Welfare

HEALTH

The Health of the workers in the conditions under which work is carried on in factories:

1. Cleanliness: - Free from effluvia and dirt
 - Dirt should be removed daily
 - Work room shall be cleaned at least once in a week
 - Effective means of drainage and use of disinfectants
2. Disposal of wastes and effluents:
3. Ventilation and temperature
4. Dust and fume - install exhaust appliances, it would be installed near the point of origin of the dust, fumes, or other impurity
5. Artificial humidification - cotton textile mills and in cigarette making factories.
6. Overcrowding should be avoided - The Chief Inspector of factories by order in writing shall fix the maximum member of workers to be employed
7. Lighting – sufficient and suitable lighting should be provided
8. Drinking water - Drinking points must be marked, away from urinal
 - Cooling water should be provided where more than 250 workers
9. Latrines and urinals – separate L & U for male and female and must be enclosed
 - cleaned at least once in every seven days with suitable detergents or disinfectants or with both.
10. Spittoons – The Persons shall not spit within the premises except in spittoons.

SAFETY

1. Fencing of machinery – dangerous part of machines to be securely fenced
2. Examination of machinery in motion by a trained adult male worker – restriction on women and young persons.
3. Restriction on young persons to work on dangerous machines
4. Striking gear and device for cutting of power
5. Self acting machines allowed within a distance of 45 centimeters
6. Casing (covering) of new machines
7. Prohibition of employment of women & young persons near cotton openers
8. hoist and lifts to be of good condition
9. Lifting machines, chains, ropes to be of good construction
10. Notice of maximum safe working speed to be kept near machine

11. Effective measures shall be taken to ensure safe working pressure
12. Floors, passage etc., should be properly constructed and maintained
13. Pits, sumps, openings in floors to be securely covered
14. Excessive weight – Workers should not be allowed to lift of excessive weight
15. Materials should be provided to protect eyes of the employees
16. Precautions against dangerous Furness
17. Precautions regarding the use of portable electric light
18. Precautions against explosives
19. Precaution in case of fire
20. Safety officers: must be employed if 1000 or more workers employed and manufacturing process carried on.

WELFARE

1. Washing allowance and facility
2. Facility for storing and drying clothing
3. Facilities for sitting
4. First aid appliances - one for every 150 workers
5. Shelters, rest rooms and lunch rooms should be provided
6. Crèches – If more than 50 women employees are working
7. Canteen – where more than 250 workers employed
8. Welfare officers – where more than 500 workers employed

Welfare facilities outside factory premises

In addition to providing welfare facilities in the factory premises, workers are also provided certain benefits and facilities outside the factory. These include:

- Maternity benefits;
- Gratuity, pension and provident fund benefits;
- Medical benefits;
- Educational facilities;
- Housing facilities;
- Recreational facilities including sports and cultural activities;
- Library and reading rooms;
- Holiday home and leave travel facilities;
- Consumers' cooperative stores and fair price shops;
- Vocational training; and
- Transportation facility to and from the place of work

EMPLOYMENT OF YOUNG PERSONS

Children: The age of children not completed 14 year shall not be allowed /employed in a factory

Young person (Adolescent): Who has completed the age of 14 years and not completed the age of 18 years

Adult : Who has completed the age of 18 years

Certificate of fitness (CoF):

It should be produced by young person before joining a duty or getting employment.

Apply : For getting CoF, the Young person by himself or guardian must apply for that

Validity : The CoF valid for 12 months from the date of issue, but it can be renewed.
Revocation of CoF: It can be revoked any time by the certifying surgeon.
Fees : Fees for getting CoF to be paid by the employer (at the time of renewal)

Working hours to Young persons:

- Not more than 4 1/2 hours per day
- Weekly holiday is must
- No young persons allowed to work in two factories
- Female young person to be allowed to work only between 8am to 7pm
- Display of notice of work of young person must be there
- Register of young person workers should be maintained by the manager.

EMPLOYMENT OF WOMEN

All provisions regarding employment of adult male worker is applicable to adult female worker, except the following:

1. Work on or near machinery in motion is not allowed
2. Prohibition of employment near cotton openers
3. Crèches
4. Maximum of 48 hours in a week and 9 hrs. per day
5. Working hrs. between 6am to 7pm
6. Certificate of fitness (CoF) is must
7. Restricting the employment of women in dangerous operations/ machines
8. Annual leave: One day for every 20/15 days (15 days for Female young person) and Maximum maternity leave 12 weeks

Provisions regarding Health of factory workers under Factories Act, 1948

To take care of the health of workers in factories, the Factories Act, 1948 has provided for certain measures which are stated below:

(i) Cleanliness of the factory premises

Every factory shall be kept clean and free from effluvia arising from any drain, privy or other nuisance. It is specifically provided that in a factory—

— accumulations of dirt and refuse shall be removed daily, by sweeping or any other method, from the floors and benches of work rooms and from stair cases and passages, and disposed off in a suitable manner;

— the floor of every room shall be cleaned. This shall be done at least once every week by washing, using disinfectant or by some other effective method;

— where a floor is liable to become wet in the course of any manufacturing process to such an extent as is capable of being drained, effective means of drainage shall be provided.

— all inside wall and partitions, all ceilings or tops of rooms and all walls, sides and tops of passages and staircases shall

- a) be painted or varnished, and repainted and re-varnished at least once in a period of five years; where they are painted or varnished, be cleaned at least once in a period of 14 months by such methods as may be prescribed by the Government.
- b) Where painting or varnishing is not required, be kept white washed or colour washed, and the white washing or colour washing shall be carried out at least once in every period of 14 months.

(ii) Disposal of Wastes and Effluents: Effective arrangement shall be made for the disposal of wastes and effluents arising out of manufacturing process in the factories.

(iii) Ventilation and Temperature: Provision to be made for ventilation and regulation of temperature in the factories. Effective and suitable measures shall be adopted for securing and maintaining in every room—

- adequate ventilation by the circulation of fresh air, and
- such a temperature as will secure to workers reasonable conditions of comfort, and prevent injury to health, and in particular the walls and roofs shall be of such material and so designed that such temperature shall not exceed but kept within reasonable limits.

The state government shall prescribe the standards of adequate ventilation and reasonable temperature for any factory or part thereof.

(iv) Dust and Fume: In every factory, where due to manufacturing process, dust or fume or other impurity arise which is likely to be injurious to the health of workers employed, effective measures shall be taken to prevent its inhalation, and accumulation in any workroom. If it is necessary to install exhaust appliances, it would be installed near the point of origin of the dust, fumes, or other impurity. Measures shall be taken to enclose such points.

(v) Artificial humidification: Artificial creation of humidity is employed in India in cotton textile mills and in cigarette making factories. In respect of factories, where humidity of the air is artificially increased, it is provided to make rules—

- prescribing standard of humidification;
- regulating the methods used for artificially increasing the humidity of the air;
- directing prescribed tests for determining the humidity of the air to be correctly carried out and recorded, and
- prescribing methods to be adopted for securing adequate ventilation and cooling of the air and the work rooms.

(vi) Over-crowding

No room in any factory shall be overcrowded to such an extent which becomes injurious to the health of the workers employed therein. The Chief Inspector of factories by order in writing shall fix the maximum member of workers to be employed in each room in the factory.

(vii) Lighting

The Factories Act provides for sufficient and suitable lighting, natural or artificial where workers are working or passing through. Provision of cleaning of inner and outer surface is provided for all glazed windows and skylights used for the lighting of the workrooms. In every factory, effective provision shall be made for the prevention of

- a) glare, either directly from a source of light or by reflection from a smooth or polished surface;
- b) the formation of shadows to such an extent as to cause eyestrain or the risk of accident to any worker.

(viii) Drinking Water

In every factory, effective arrangement shall be made at suitable places for sufficient supply of wholesome drinking water. Such places shall be legibly marked 'Drinking Water' in a language understood by a majority of the workers employed in the factory. In case of factories employing more than 250 workers, provisions shall be made for cooling drinking water during hot weather by effective means, and for its distribution.

(ix) Latrines and Urinals

The Factories Act requires that provision should be made for —

- a) Sufficient latrine and urinal accommodation conveniently situated and accessible to workers while they are in the factory;
- b) Separate enclosed accommodation for male and female workers;
- c) Such accommodation being adequately lighted and ventilated;
- d) All such accommodation being maintained in a clean and sanitary condition;
- e) Sweepers being employed to clean latrines, urinals and washing places;

Where the number of workers in a factory is more than 250

- i) Latrines and urinals shall be of prescribed sanitary types;
- ii) The floor and internal walls of the latrines and urinals shall be laid with glazed tiles;
- iii) Floors and walls and the sanitary pans of latrines and urinals shall be thoroughly washed and cleaned at least once in every seven days with suitable detergents or disinfectants or with both.

(x) Spittoons

Sufficient number of spittoons must be provided in every factory and maintained in clean and hygienic condition. No person shall spit within the premises of a factory except in the spittoons. A notice containing this provision and the penalty for its violation shall be prominently displayed at suitable places in the factory premises.

Welfare provisions in the factories

(i) Washing facilities: The Factories Act provides for —

- a) Adequate and suitable facilities for washing for the use of workers in the factories. The workers who live in crowded areas have inadequate facilities for washing at their homes, and bathing facilities add to their comfort, health and efficiency.

- b) Separate and adequately screened washing facilities for the use of male and female workers.
- c) Such facilities being conveniently accessible, and being kept clean.

(ii) Facilities for storing and drying clothes:

A suitable place for keeping clothes not worn during working hours shall be provided in every factory. Facilities shall also be provided for the drying of wet clothes.

(iii) Facilities for sitting:

For workers who are to work in a standing position, suitable arrangement for sitting shall be provided in the factories. This is to enable workers to take advantage of any opportunity for rest which may occur in the course of their work.

(iv) First-aid appliances:

First-aid boxes or cupboards equipped with the required contents should be provided for workers in every factory. This should be readily accessible to them during all working hours. The number of such first aid boxes shall not be less than one for every 150 workers employed in the factory. Such first-aid box shall be kept in the charge of a responsible person who is trained in first-aid treatment and who shall be available during the working hours of the factory.

In factories employing more than 500 workers, there shall be an ambulance room. It should contain the prescribed equipments, and be in the charge of such medical and nursing staff as may be prescribed.

(v) Canteens:

In factories employing more than 250 workers, there shall be a canteen for the use of workers. The government may prescribe the rules in respect of the

- food stuff to be served in the canteen;
- charges to be made;
- constitution of a managing committee for the canteen ; and
- representation of the workers in the management of the canteen.

(vi) Shelters, restrooms and lunch rooms:

Adequate and suitable shelters, rest rooms, and lunch rooms with drinking water facility shall be made in factories employing 150 workers or more. Workers can eat meals brought by them in such rooms. Rest and lunch rooms shall be sufficiently lighted and ventilated. It shall be maintained in cool and clean conditions.

(vii) Creches:

In every factory, where more than 50 women workers are employed, provision shall be made for suitable and adequate room for the use of children under the age of six years of such women. Such a room shall be adequately lighted and ventilated. It shall be maintained in clean and sanitary conditions under the charge of a woman trained in the care of children and infants.

(viii) Welfare Officer:

The factories Act also provides for employment of welfare officers with prescribed qualification to look into the implementation of various facilities provided for. Such a provision exists in every factory employing more than 500 workers.

Welfare facilities outside factory premises

In addition to providing welfare facilities in the factory premises, workers are also provided certain benefits and facilities outside the factory. These include:

- Maternity benefits;
- Gratuity, pension and provident fund benefits;
- Medical benefits;
- Educational facilities;
- Housing facilities;
- Recreational facilities including sports and cultural activities;
- Library and reading rooms;
- Holiday home and leave travel facilities;
- Consumers' cooperative stores and fair price shops;
- Vocational training; and
- Transportation facility to and from the place of work.

THE PAYMENT OF WAGES ACT – 1936

It was passed to regulate the payment & unauthorized deductions of wages to certain classes of persons employed in a factory or industry.

Time of payment of wages (Rules):

1. Wages to be paid before 7th or 10th day of every month
 - Less than 1000 persons 7th day
 - More than 1000 persons 10th day
2. Wages in case of termination of employment
 - To be paid before the expiry of the 2nd working day from the date of termination
3. Wages to be paid on a working day only

Deductions from wages

1. Deductions for fines:
 - No fine – before showing cause and completed age of 15 years
2. Deductions for absence from duty
3. Deductions for damages or loss
4. Deductions for services provided by the employer

5. Deductions for recovery of advances
6. Deductions for recovery of loans
7. Deductions for payment to co-operative societies and insurance schemes
8. Other deductions:
 - Deductions of income tax
 - Deductions by order of court
 - Deductions for payment to co-op societies advances
 - Deductions for provident fund
 - Deductions for insurance premium
 - Deductions made with written authorization of the employee to donations

Note: The total deduction shall not exceed 75% of such wages

Maintenance of Registers & Records

The employer shall maintain the following registers and records

1. The work performed by them
2. The wages paid to them
3. Deductions made from their wages
4. The receipts given by them

Penalty for offences under the Act (To employer)

1. Penalty for delaying payment of wages within prescribed period
2. Penalty for not paying wages on a working day or in current coins or currency
3. Penalty for failure to maintain / furnish/ return records
4. Penalty for obstructing inspectors/ officials

THE PAYMENT OF BONUS ACT – 1965

Bonus – Something to the good

This act is to provide for the payment of bonus to persons employed in certain establishments for their contribution in profit.

- To impose statutory liability upon an employer
- To define principles of payment of bonus
- To provide minimum & maximum bonus
- To provide machinery for enforcement of the liability for payment of bonus
- A minimum bonus of 8.33% of the wage or salary is payable, whether the establishment has made profit or loss.
- Liability for bonus is a statutory liability

*** Application of the Act**

- Every factory coming under Factories act 1948
- Every other establishment, there employees strength more than 20 persons

Act not applicable to the following categories of employees:

- Employees of LIC
- University & other educational institutions
- Seamen
- Employed through contractors

- Employed by NABARD, UTI, SIDBI
- Employees of red-cross society & its branches
- Any other financial institutions (other than banking company)
- RBI employees

*** Power of exemption for giving bonus**

The appropriate Govt. alone empowered to give exemption to the establishment for giving bonus, based on its financial position and other relevant circumstances by notification in the official Gazette.

The order of exemption can be refused by affected parties and apposed through Quasi-Judicial with proper reasons.

*** Eligibility & Distribution for Bonus:**

Eligibility (U/S.8): Every employee shall be entitled to receive bonus, if he works not less than 30 working days in a financial year.

If he worked less than 30 days, the bonus could be reduced proportionately

*** Disqualification (U/S: 9):**

The employee shall be disqualified from receiving bonus, if he is dismissed from service for: Fraud, Violent behaviour, Theft and Sabotage of any property of factory.

DETERMINATION OF BONUS

- Bonus can not be claimed by workers as a matter of right

The following is the procedure for determining bonus for two different establishments, namely Banking Company and others.

1. Determination of Gross Profit(GP) – For Banks and Others
2. Determination of available surplus
3. Allocable surplus
4. Proportionate reduction in bonus in certain cases
5. Adjustment of interim bonus paid
6. Time limit for payment of bonus
7. Recovery of bonus

1. Determination of Gross Profit (GP):

At first we have to Determine GP from given Net Profit, GP can be calculated as follows:

- A) For a Banking Company – First schedule - Computation of GP from NP

Particulars	Amt.	Amount (in Rs.)
Net Profit (from P&L account)		xxxx
ADD: Items to be added back to NP-(A)		
- Provision for bonus	xxxx	
- Provision for depreciation	xxxx	
- Any reserves	xxxx	

- Any gratuity paid/given	XXXX	
- Donations in excess of admissible for IT	XXXX	
- Capital expenditure and Capital losses	XXXX	
- Losses from business situated out side india	<u>XXXX</u>	<u>XXXX</u>
		XXXX
LESS: Items to be deducted from NP – (B)	XXXX	
- Capital receipts	XXXX	
- Profit of any business situated outside India	XXXX	
- Refund of any excess direct tax paid	<u>XXXX</u>	<u>XXXX</u>
- Cash subsidy given by Govt.		
Gross Profit for Bonus		XXXX

A) For Other Companies – First schedule

- Computation of GP form NP

Particulars	Amt.	Amount (in Rs.)
Net Profit (from P&L account)		XXXX
ADD: Items to be added back to NP-(A)		
- Provision for bonus	XXXX	
- Provision for depreciation/ Direct taxes	XXXX	
- Any reserves	XXXX	
- Any gratuity paid/given	XXXX	
- Donations in excess of admissible for IT	XXXX	
- Capital expenditure and Capital losses	XXXX	
- Losses from business situated out side india	<u>XXXX</u>	<u>XXXX</u>
		XXXX
LESS: Items to be deducted from NP – (B)	XXXX	
- Capital receipts	XXXX	
- Profit of any business situated outside India	XXXX	
- Refund of any excess direct tax paid	<u>XXXX</u>	<u>XXXX</u>
- Cash subsidy given by Govt.		
Gross Profit for Bonus		XXXX

2. Determination of available surplus: After determining the GP, the establishment should determine the available surplus as under.

Particulars	Amt.	Amount (in Rs.)
Gross Profit (Calculated as above)		XXXX
Less: Items to be deducted	XXXX	
- Any depreciation admissible	XXXX	
- Any amount spent for development	XXXX	
- Any direct taxes paid	XXXX	
- Amount specified in 3rd Shedule*	<u>XXXX</u>	<u>XXXX</u>
Available surplus		XXXX

* The items specified in 3rd Schedule:

- Dividend payable to preference share holders
- 8.5/ 7.5% of its paid up equity share capital for commencement of Business
- 6% of it reserves
- Remuneration payable to the partners of the firm
- Rs. 48,000 or remuneration paid to employees which ever is less.

3. Allocable surplus:

After determining the available surplus, the employee's share is called allocable surplus. The allocable surplus is the workers' share in the available surplus.

a. The amount of bonus:

- Mini.. bonus: **8.33%** of the salary earned during the accounting year (U/s.10) **OR**
Rs.100 p.m.(Rs.60 in case of below 15 years)w.e.is Higher.
- Maximum Bonus: (U/s. 11): It is possible only the allocable surplus exceeds the minimum bonus – i.e **20%** of salary.

b. 'Set on' & 'Set off' of allocable surplus (u/s.15):

The rule set-on and set-off is applicable on the allocable surplus.

- (i) 'Set on' : Where the allocable surplus for any accounting year exceeds the maximum bonus amount, the excess shall be carried forward to next/succeeding years. It should be utilized only for payment of bonus (the year in which there is no allocable surplus)
- (ii) 'Set- off': In an accounting year, if the allocable surplus is not available to pay minimum bonus, the unpaid amount is set-off to next year.

Ex. The 4th schedule.

Minimum bonus: Rs.1,04,167

Maximum bonus: Rs.2,50,000

Year	Allocable surplus	Bonus	Set-off / Set-on	Total C/f
1	1,04,167	1,04,167	Nil	Nil
2	6,35,000	2,50,000	2,50,000 (maxi)	
3	2,20,000	2,50,000 (30000 from 2 nd year)	-	2,20,000
4	Nil	1,04,167	1,15,833	Nil

4. Proportionate reduction in bonus in certain cases: If any employee has not worked for all the working days in an accounting year, the minimum bonus will be reduced proportionately.

5. Adjustment of interim bonus paid: If any interim bonus paid during that accounting year, that shall be reduced from actual bonus.

6. Time limit for payment of bonus: - With in a month from the date on which the settlement comes into operation. - Or with in a period of 8 months, from the close of the accounting year.

7. Recovery of bonus: In case of any due in payment of bonus, the affected person can recover them through Government.

THE INDUSTRIAL DISPUTES ACT- 1947

This act is amended for the prevention and settlement of industrial disputes, through 2 new institutions namely Works committee and Industrial Tribunals.

Objectives:

1. To secure industrial peace (A state in industrial relations in which both employer and employees abstain (withhold) from industrial action, such as strikes and lockouts.)
2. By preventing & settling industrial disputes between employer and workmen
3. To maintain good relations through external machinery (Conciliation, Courts, Industrial Tribunals etc.)
4. To ameliorate (improve) the condition of workmen in the industry
5. By redressal of grievances of workmen in industry
6. By providing job security

Extent of the act: Applicable to whole of the India, to all industries (Private/Public).

Industry:

U/s.2 (j) of Industrial disputes act, Industry is “any systematic activity carried on by Co-operation between on employer and his workmen.

What is not an Industry:

- Any agricultural operation
- Hospitals/dispensaries
- Khadhi and village industry
- activities of any associations
- Educational, scientific, research, training institutes.

Industrial disputes:

Any dispute/differences between – Employers & Employees, Employers & Workmen and Workmen & Workmen.

Generally it means a dispute between the Workmen and the Management.

Three ingredients of Industrial disputes:

1. There should be real dispute
2. Dispute between Employer & Workmen
3. Dispute connected with employment or non-employment

Types of Industrial disputes

- a) Individual disputes: Any dispute between that workmen & employer connected with dismissal, termination or retrenchment of that workmen.
- b) Collective dispute – effected all the workmen relating to
 - Wages, bonus, compensation, hours of work, leave, Holidays, Rules of discipline, closure of organization, Retrenchment ect.,

LAY – OFF (U/s.2(kkk))

Lay-off means, the failure, refusal or inability of an employer to give employment to a workmen due to – shortage of coal, power, raw material or the accumulation of stocks or the breakdown of machinery or natural calamity.

LOCK-OUT (U/s.2(l))

It means the temporary closing of a place of employment or suspension of work or refusal by an employer to any number of employees

- Lock-out is a weapon available to employer
- Strike is a weapon available to employees.

Differences between Lay-off and Lock out

Lay- off	Lock-out
1. Employer refuses to give employment due to shortage of resources	1. Due to closing of a place of employment
2. Due to trade reasons, beyond the control of the employer	2. It is a weapon used by the employer influencing workmen to accept his demand
3. No way connected with Industrial dispute	3. It is connected with Industrial dispute

RETRENCHMENT (U/s.2 (OO))

The termination by the employer of the service of a workman for any reason otherwise than as punishment by way of disciplinary action.

Retrenchment not include: -Voluntary retirement - Retirement due to reaching the R'age
- Termination due to non-renewal of contract.

STRIKE U/s.2 (q)

- a. A cessation of work by a body of persons employed in any industry acting in combination
- b. A concerted refusal of any number of employees
- c. Refusal under a common understanding of any number of employees

UNFAIR LABOUR PRACTICE (U/s.2(ra))

It means any of the practices specified in the 5th schedule on the part if employer, trade unions and on the part of workmen.

UNFAIR LABOUR PRACTICE (LISTED IN 5TH SCHEDULE)

I. On the part of employer & Trade unions of employers

- 1. To interfere with/coerce workmen in the exercise of their right to organize/form/joint activities for collective bargaining
 - a. Threatening workmen with dismissal
 - b. Threatening a lock-out/closure
 - c. Granting wage increase without consulting Trade unions
- 2. To dominate the activities of Trade unions
 - a. The employer taking an active interest in organizing Trade unions
 - b. Employer showing partiality to one of the trade unions
- 3. To establish employer – sponsored trade unions of workmen
- 4. To encourage/discourage membership in any trade unions
 - a. Punishing workman (WM) to join in a Trade union
 - b. Dismissing WM for taking part in legal strike

- c. Changing seniority of WM due to active participation in Trade union activities
- d. Refusing promotion for showing interest in Trade union
5. To discharge or dismiss workmen
 - a. by way of victimization
 - b. not in good faith
 - c. by falsely evidence
 - d. for misconduct of a minor/technical character
6. To abolish the work of a regular nature
7. Transferring a workmen
8. Showing partiality to one set of workers
9. To employ workmen as 'badlis', casuals/temporaries for long period
10. To recruit workman during legal strike
11. Failure to implement award
12. To indulge in acts of violence
13. Proposing/continuing a lock-out

II. On the part of Workmen & Trade unions of workmen

1. To advise/actively support illegal strike
2. To coerce workmen to join a Trade union
3. To indulge in acts of violence
4. Squatting on the work premises after working hours
5. 'Gherao' of any of the managerial or staff members
6. To stage demonstration at the residence of the employer
7. Damaging properties of establishment

Workman

Any person (including an apprentice) employed in any industry to do any manual, unskilled, skilled, technical, clerical or supervisory work for hire or reward.

Who are not workmen:

- Employed in Police service/ Employee of prison
- Employed in managerial/ administrative work
- Supervisors drawing wages exceeding Rs.1600 per mensem

Procedure for settlement of Industrial disputes & Authorities under the act

Setting up authorities for prevention, investigation and settlement of Industrial disputes, they are:

1. Works committees (Sec.3)
2. Conciliation officers (Sec.4)
3. Boards of Conciliation (Sec.5)
4. Courts of inquiry (Sec.6)
5. Labour courts (Sec.7)
6. Industrial Tribunals (Sec.7-A)
7. National Tribunals (Sec.7-B)

3 modes of settlement of disputes under this act

A. Voluntary settlement and conciliation

- B. Adjudication
- C. Arbitration

[A] CONCILIATION MACHINERY

Which include Works committees, Conciliation officers, Board of Conciliation and Courts of Inquiry. They can only make inquiry about the disputes, but can not make any awards.

1. Works committees (WC): (Sec.3)

- Where 100 or more workmen are employed, the WC must be constituted
- Members: The employer & employees should be the members of the committee, the employees strength should not be less than the employer's representatives in the committee.

Powers & Duties

- Securing & preserving amenity or good relations between employers and workmen
- Comment upon matters of their common interest
- Compose any material difference of opinion in welfare, wages, holidays etc.

2. Conciliation officers (Sec.4)

The appropriate Government through notification in Official Gazette appoint Conciliation officers. Their duty is to mediate and promote the settlement of Industrial disputes.

Duties:

- a. To hold conciliation proceeding s- where any disputes exists.
- b. To investigate the dispute
- c. To send a report & memorandum of settlement to appropriate Govt.
- d. To send a full report about their efforts for settlement, to the Govt. in case no settlement is arrived.
- e. Report should be submitted within 14 days of the commencement of the conciliation proceedings or within the time period fixed by Govt.

Powers:

1. Power to enter premises
2. Power to call for and inspect documents

3. Boards of Conciliation (Sec.5)

The appropriate Govt. constitutes this board and appoints its members through official gazette.

Members:

It consist of a Chairman (An independent person) & 2 or 4 other members. The other members appointed to represent the disputed parties on the recommendation of them.

Duties:

- a. To Bring about a settlement of the dispute
- b. To send a report & memorandum of settlement to appropriate Govt.
- c. To send a full report about their efforts for settlement, to the Govt. in case no settlement is arrived.

- d. To communicate reasons to the parties, if no further reference made.
- e. To submit report within 2 months.

Power:

1. Power to enter premises
2. Power of Civil court
 - Enforcing attendance
 - Compelling the submission of document
 - Issuing notice for the examination of witnesses.

4. Court of enquiry

It is for inquiring into any matter appearing to be connected with or relevant to an industrial dispute.

Duties:

- It should inquire into the matters referred to it.
- To send report of Govt. within 6 months.
- The reports should be in writing & signed by all the members.
- It should record any minutes of recommendations in report

Power:

1. Power to enter premises
2. Power of Civil court
 - Enforcing attendance
 - Compelling the submission of document
 - Issuing notice for the examination of witnesses.
3. This court may appoint any person having special knowledge of the matter under consideration.

[B] ADJUDICATION MACHINERY

Sec.7 to 9, explain the adjudication authorities are:

1. Labour court (Sec.7)
2. Industrial Tribunal (Sec.7-A)
3. National Tribunal (Sec.7-B)

1. Labour court (Sec.7)

The appropriate Govt. may constitute one or more labour courts for adjudication of Industrial disputes specified in the 2nd schedule.

Matters within the Jurisdiction of Labour court (The 2nd Schedule)

- a. The legality of an order passed by an employer
- b. Discharge and dismissal of Workman
- c. Withdrawal of any customary concession or privilege
- d. Illegality of strike and lock-out

* The Labour court should consist of only one person, to be appointed by the appropriate Government.

Qualification of the Authority: - The person should be,

- a. The Judge of High court
- b. District judge or Additional district judge (Not less than 3 years of service)
- c. Presiding officer of Labour court (Not less than 7 years of service)

Duties:

- a. To adjudicate upon Industrial disputes, specified in 2nd schedule
- b. To give award within the specified period
 - Award to be in writing & signed and its published

Power:

- a. Power to enter premises
- b. Power of Civil court
 - Enforcing attendance
 - Compelling the submission of document
 - Issuing notice for the examination of witnesses.

2. Industrial Tribunal (Sec.7-A)

Constituted for the adjudication of industrial disputes specified in the 2nd & 3rd schedule.

Matters within the Jurisdiction of Industrial Tribunal (The 3rd Schedule)

- a. Wages, including the period or modes of payment
- b. Compensatory & other allowances
- c. Hours of work and rest intervals
- d. Leave with wages & holidays
- e. Bonus, PF, Gratuity, etc.
- f. Shift working
- g. Classification of grades
- h. Rules of discipline
- i. Rationalization
- j. Retrenchment of workmen & Closure of establishment

Qualification of the Authority: - The person should be,

- a. The Judge of High court
- b. District judge or Additional district judge (Not less than 3 years of service)
- c. Presiding officer of Labour court (Not less than 7 years of service)

Duties:

- a. To adjudicate upon Industrial disputes, specified in 2nd schedule
- b. To give award within the specified period
 - Award to be in writing & signed and its published

Power:

- a. Power to enter premises
- b. Power of Civil court
 - Enforcing attendance
 - Compelling the submission of document
 - Issuing notice for the examination of witnesses.
- c. Power to appoint assessors (Specialists of a particular field)
- d. Power to award cost

3. National Tribunal (Sec.7-B)

It is constituted for the adjudication of industrial disputes which, in the opinion of the central Govt. considered as National importance or the disputes of industrial establishment situated in more than one state.

* Qualification, Duties and Power of the Authorities are as same in Labour court and Industrial tribunal.

Award and Settlement

Award: An interim or final determination of any industrial dispute framed by Labour court, Industrial tribunal or National Tribunal or Arbitrators.

Settlement: - A settlement arrived at in the course of conciliation proceedings
- A written agreement between the employer & workmen arrived during the course of conciliation proceedings.

Differences between Awards and Settlements

AWARDS

1. Definition of Award
2. Enforceable on expiry of 30 days from its publication
3. Rejection/ modification of award is possible within 90 days
4. Period of operation of award is 1 year
5. Report should be published
6. An award can be arrived through Labour court, Industrial Tribunal and National Tribunal

SETTLEMENTS

1. Definition of Settlement
2. Enforceable on the date in which the agreement is signed
3. At any time
4. The period agreed or for 6 months
5. Need not be published
6. The settlement is arrived through Conciliation.

* **Distinction between Lay-off and Retrenchment.**

Strike & Lock-out

Prohibition of Strike and Lock-out in the following cases: (Sec.22 & 23)

1. Strike in a Public utility services:

- a. Without giving to the employer notice of strike, within 6 weeks before striking
 - b. Within 14 days of giving such notice
 - c. Before the expiry of the date of strike
 - d. During any conciliation proceedings & 7 days after the conclusion
- A strike notice is valid only for 6 months.

2. Lock-outs in a Public utility services:

- a. Without giving to the employer notice of strike, within 6 weeks before striking
 - b. Within 14 days of giving such notice
 - c. Before the expiry of the date of strike
 - d. During any conciliation proceedings & 7 days after the conclusion
- A Lock-out notice is valid only for 6 months.



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3. Strike and Lock out in an Industrial establishment

- a. During the course of any conciliation proceedings & 7 days after the conclusion
- b. During the pendency of proceeding before LC, IT and NT
- c. During the pendency of proceeding before arbitration
- d. During the period in which a settlement or award is in operation.

Unit – IV
Corporate Tax Planning

Tax Planning

Tax planning can be defined as an arrangement of one’s financial and economic affairs by taking complete legitimate benefit of all deductions, exemptions, allowances and rebates so that tax liability reduces to minimum.

Direct Taxes

Direct taxes are those which a person pays directly from his income, wealth, or estate. It is paid after the income or benefit reaches the hands of the person, which are Income tax, wealth tax, corporate tax and gift tax.

Indirect Taxes

Which are not directly charged from the persons, which are collected in the form of excise duty, customs duty and sales tax.

Taxable Turnover

It means the turnover on which a dealer shall be liable to pay tax as determined after making such deductions from his total turnover and in such manner as may be prescribed.

Tax Avoidance

Tax avoidance is reducing or negating tax liability in legally permissible ways and has legal sanction. Tax avoidance is sound law and certainly not bad morality for anybody to so arrange his affairs in such a way that the brunt of taxation is the minimum. This can be done within the legal framework even by taking help of loopholes in the law.

Tax Evasion

All methods by which tax liability is illegally avoided are termed as tax evasion. Tax evasion may involve an untrue statement knowingly, submitting misleading documents, suppression of facts, not maintaining proper accounts of income earned (if required under law), omission of material facts on assessment.

Tax Planning Vs. Tax Management

Tax Planning	Tax Management
The objective of tax planning is to reduce the tax liability to the minimum.	The objective of tax management is to comply with the provisions of law.
Tax planning is futuristic in its approach.	Tax management relates to past (i.e., assessment proceedings, rectification, revision, appeals etc.), present (filing of return of income on time on the basis of updated records) and future (corrective action).

Tax planning is very wide in its coverage and includes tax management.	Tax management has a limited scope, i.e., it deals with specific activities such as filing of returns of income on time, drafting appeals, deduction of tax at source on time, updating records from time to time, etc.
The benefits arising from tax planning are substantial particularly in the long run.	As a result of effective tax management, penalty, penal interest, prosecution, etc., can be avoided.

Tax Avoidance Vs. Tax Evasion

Tax Avoidance	Tax Evasion
Any planning of tax which aims at reducing tax liability in legally recognised permissible ways, can be termed as an instance of tax avoidance.	All methods by which tax liability is illegally avoided is termed as tax evasion.
Tax avoidance takes into account the loopholes of law.	Tax evasion is an attempt to evade tax liability with the help of unfair means/methods.
Tax avoidance is tax hedging within the framework of law	Tax evasion is tax omission.
Tax avoidance has legal sanction	Tax evasion is unlawful and an assessee guilty of tax evasion may be punished under the relevant laws.
Tax avoidance is intentional tax planning before the actual tax liability arises	Tax evasion is intentional attempt to avoid payment of tax after the liability to tax has arisen

Causes of Tax evasion

1. Multiplicity of tax laws
2. Complicated tax laws
3. Higher rate of taxation
4. Inadequate information as to sources of tax revenue
5. Investment in real property
6. Ineffective tax enforcement
7. Deterioration of moral standard

Remedies for evasion

1. Through overhauling of tax laws
2. Reduction in tax rates
3. Replacement of sales tax & excise duties
4. Tax on agricultural income
5. Maintenance of proper accounts
6. Introduction of expenditure tax

7. Tightening of tax enforcement

Types of tax planning

There are four types of tax planning open to a business.

ILLEGAL	LEGAL		
Tax evasion	No tax planning	Basic tax planning	Advance tax planning
		Tax bills reduced by 5%-20%	Tax bills reduced by 50% – 100%

(1) Tax evasion

All methods by which tax liability is illegally avoided are termed as tax evasion. Tax evasion may involve an untrue statement knowingly, submitting misleading documents, suppression of facts, not maintaining proper accounts of income earned (if required under law), omission of material facts on assessment.

(2) No tax planning

This is what many businesses do by default. They simply complete their tax returns and send them off to the taxman, having taken no prior action to arrange their affairs in such a way to legally pay less tax.

(3) Basic tax planning

Most businesses do this since it is what most of the accountants advising them are good at. Basic tax planning such as incorporating the business, taking dividends rather than salaries and timing when they spend money can often reduce tax bills by 5% to 20%.

Various Basic methods of Tax Planning as follows :

a) **Short Term Tax Planning:** Short range Tax Planning means the planning thought of and executed at the end of the income year to reduce taxable income in a legal way.

b) **Long Term Tax Planning:** Long range tax planning means a plan at the beginning or the income year to be followed around the year. This type of planning does not help immediately as in the case of short range planning but is likely to help in the long run ;

c) **Permissive Tax Planning :** Permissive Tax Planning means making plans which are permissible under different provisions of the law, such as Planning of taking advantage of different incentives and deductions, planning for availing different tax concessions etc.

d) **Purposive Tax Planning:** It means making plans with specific purpose to ensure the availability of maximum benefits to the assessee through correct selection of investment, making suitable programme for replacement of assets, varying the residential status and diversifying business activities and income etc.

(4) Advanced tax planning

Historically this has really only been available to the richest entrepreneurs. Indeed it has helped them become even richer as it can reduce tax bills by 50% to 100%. In recent years this has changed, and now all good accountants (including One Accounting) can access a range of advanced tax planning solutions on behalf of their clients.

Central Sales Tax Act 1956 (CST Act 1956)

Central Sales Tax (CST): It a tax on Inter-state sale of goods, where the buyer and seller are in different state. CST will be chargeable under the CST Act, 1956 passed by Central Govt. in parliament.

Scope of CST

1. To regulate or determine the sales in case of interstate trade or commerce
2. To levy tax on sale of goods in the course of Inter-state trade
3. To declare certain goods to be of special importance in the course of Inter-state trade.
4. To specify the restrictions and conditions in respect of Inter-state trade

Sale

Sale means transfer of property in goods by one person to another in the course of business for cash, deferred payment or other valuable consideration and includes:

- Transfer of property in goods
- Work contract
- Hire purchase
- Right to use
- Supply of goods by unincorporated association
- Supply of food as part of any service

Dealer: Any person carrying on the business of buying, selling or distributing goods directly or indirectly for cash, deferred payment, commission or any remuneration.

- Business: Any trade, commerce or manufacture with or without a profit motive
- Sale: Transfer of property from one person to another for a valuable consideration.
- Goods: All materials, articles, commodities except newspapers, shares, money, claims
- Rate: As prescribed in the Act.

Essential elements of sale:

- Goods should be transferred
- General property in good should be transferred
- Price must be paid
- There must be a seller and a buyer
- There must be a valid consent of both buyer and seller

Declared Goods [Section 2(C)]

It includes those goods which are considered to be of special importance in interstate trade or commerce under section 14. Some of these goods is –

• Cereals	• Cotton	• Jute	• Pulses
• Coal	• Crude Oil	• Oilseeds	• Sugar

Goods [section 2(d)]

This includes all material articles or commodities and all kind of movable property excluding newspapers, actionable claims, stocks, shares, and securities.

If newspapers are sold as scrap then, it will be charged to central sales tax if it is an inter- state sale.

Important Features of this Act

1. It extends to the whole of India.
2. Every dealer who makes an inter-state sale must be a registered dealer and a certificate of registration has to be displayed at all places of his business.
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 - Other goods.

The rates of tax on declared goods are lower as compared to the rate of tax on goods in the second category.

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Scope of CST

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2. To levy tax on sale of goods in the course of Inter-state trade
3. To declare certain goods to be of special importance in the course of Inter-state trade
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Principles for determining Inter-State Sales Tax

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- Occasions the movement of goods from one state to another or
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Exceptions to CST

- Sale of electric energy
- Sale to an exporter for the purpose of export (penultimate sale)
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 - a) To registered Dealer or
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Types of Goods

- Declared goods or goods of special importance: These are goods mentioned U/S 14 of CST (e.g.. Cereals, Coal, Cotton etc)
- Undeclared goods

Central Sales Tax rates

Types of goods	Sale to Govt.	Sale to regd. dealer	Sale to un regd. dealer
Declared goods	0% or State sales tax rate, whichever is lower. Form: D	0% or State sales tax rate, whichever is lower. Form: C	TWICE the general sales tax rate. (8%)
Undeclared goods	5% - 28 %	5% - 28 %	5% - 28 % or sales tax whichever is less

Penalties

- Penalties in the form of prosecution/ fine U/S 10
- Penalties in lieu of prosecution U/S 10
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Form C: The sale is from one registered dealer to another registered dealer

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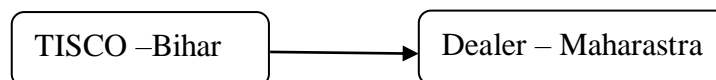
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Incidence of CST

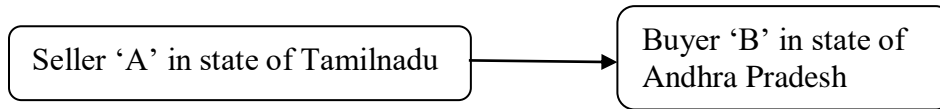
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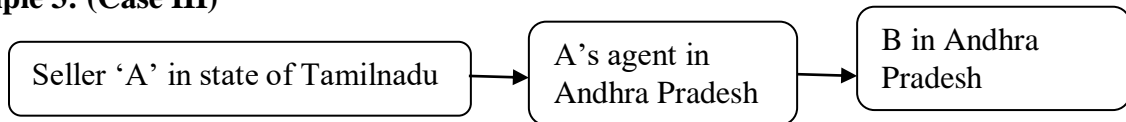
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- f. Mode of transfer is immaterial. It may be aircraft, rail, ship, post, motor vehicle, etc.
- g. Sale is not a Inter-state sale, if movement of goods are not related to contract for sale
- h. If movement of goods starts from one state and ends in the same state is not an Inter-state trade. Even if during transit goods passes through other state.

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Document of title of goods: When the goods are handed over to carrier, the carrier gives a receipt to the seller. The seller sends the receipt to the buyer then the buyer gets delivery of goods on submission of that receipt to the carrier.

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Transfer of document is a symbolic delivery of goods to the buyer. It carries with its full ownership of goods. Delivery of document of title is also an Inter-state sale, liable for CST.

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 - It should be submitted to Registering authority
 - A demand draft should be enclosed for the amount specified by the authority
3. ***Documents to be enclosed with Form D***
- 2 recent passport size photographs
 - Identity to prove his existence like passport/family card/bank pass book/driving license/VAO certificate
 - Copy of MOA and AOA in case of company
 - Copy of Partnership deed in case of partnership
 - Form XI of TNGST act signed by applicant and manager
 - Form A showing the estimated turnover for the year
4. ***Security money***
- The Registering authority may demand security equal to 50% of the tax due as estimated
 - In all cases Rs.2500/- has to be collected by way of security at the time of new registration
5. ***Issue of registration certificate***
- The commissioner issues certificate within 7days
 - If no notice been made with ref to the application within 20 days the dealer is deemed to be registered
 - Registration certificate should be renewed every yr. by paying 500 before 31st march without penalty.
 - Collection of tax by registered dealer
 - The registered dealer may collect the tax by issuing a bill in respect of every sale, in duplicate
 - One copy of the bill should be retained by the dealer to be checked by officials

Amendment (Modification) to certificate of registration

- Where the dealer has altered the name, place and nature of business
- Where the dealer has changed the class or classes of goods in which he carries on his business
- Where there is change in ownership in business and Cancellation of registration
- Under section 21(4) when he proves that his turnover in each of the 2 consecutive years immediately preceding the application was less than Rs.75000
- Cancellation or amendment by the prescribing authority

- Cancellation by the authority due to failure on the part of dealer to pay tax or penalty, declaration of false information, failure to provide security etc.,

Duties of a registered dealer

- Shall keep at the place of business, the certificate of registration, books of accounts.
- Shall notify the registering authority about the change in place of business
- Shall send bill of sale or delivery note or such documents along with the goods
- Shall furnish the returns before the due dates prescribed

VALUE ADDED TAX (VAT)

VAT is a tax on turnover and is added at every stage of manufacture or process, based on the value added at each stage.

VAT may be defined as “a tax to be paid by the manufacturers or traders of goods and services on the basis of value added by them”.

It is not a tax on the total value of the commodity being sold but on the value added to it by the manufacturer or trader. They are not liable to pay tax on the entire value of the commodity. But they have to pay the tax only on the Net value added by them in the process of production or distribution.

In this tax, the seller will collect the tax only on the value added by him towards his produced goods by excluding the tax on purchase paid by him. The VAT is payable by seller who is termed as a ‘dealer’.

The VAT works on the principle that when raw material passes through various manufacturing stages and manufactured product passes through various distribution stages, tax should be levied on the ‘Value Added’ at stage and not on the gross sales price.

Basically, VAT is multi-point tax, with provision for granting set off (Credit) of the tax paid at the earlier stage. Thus, tax burden is passed on when goods are sold. This process continues till goods are finally consumed. Hence, VAT is termed as ‘Consumption type’ tax with ‘destination principle’. VAT works on the principle of ‘tax credit system’.

Scope of VAT: the following transactions are subject to VAT

- The supply of goods and provision of services with a place of supply in India;
- The import of goods into India;
- Intra-Community acquisition of goods in India by a taxable person;
- The supply of goods or services specified in the India VAT Act, if the taxable person has opted for taxation of those.

Cascading effect of tax

In modern production technology, raw material passes through various stages and processes continues till a final product emerges. This product then goes to distributor/wholesaler, who sells it to retailer and then it, reaches the ultimate consumer. If tax is based on selling price of a product, the tax burden goes on increasing as raw material and final product passes from one stage to other.

The Output of the 1st manufacturer becomes input for 2nd manufacturer who carries out further processing and supply it to 3rd manufacturer. This process continuous till the final product emerges. If a tax base is on the selling price of the product, the tax burden goes on increasing as raw material and final product passed one stage to other.

Each subsequent purchaser has to pay tax again and again on the material that has already suffered tax. This is called cascading effect. This VAT scheme permits manufacturers to obtain complete reimbursement of excise duty/ sale tax paid on the component or raw materials used as input in the manufacturing of final products.

Example: Manufacture 'A' supplies his output to 'B' at Rs.100. Thus, 'B' gets the material at Rs.110, inclusive of tax @ 10%. He carries out further processing and sells his output to 'C' at Rs.150. While calculating his cost, 'B' has considered his purchase cost of materials as Rs.110 and added Rs.40 as his conversion charges. While selling product to 'C', 'B' will charge tax again @10%. Thus 'C' will get the item at Rs.165 (150+10% tax). In fact, 'Value added' by 'B' is only Rs.40 (150-110). As stages of production and/or sales continue, each subsequent purchaser has to pay tax again and again on the material which has already suffered tax. Tax is also paid on tax. This is called Cascading effect.

At VAT, VAT = Tax base (Value added by them) x Rate of Tax
 = Rs.110 – 10 = 100 (Less sales tax paid on RM)
 = 100 + 40 (Processing charge) = Rs.140, rate of tax is 10%
Therefore, 140 + (140x10/100)
 = 140 + 14 = Rs.154.

Method of Calculation of VAT

Purchase Price	Rs.100
Tax paid during purchase	Rs.10 (Input tax)
Selling price	Rs.150
Tax collected during resale	Rs.15
Input tax credit (Tax paid during purchase)	Rs.10
VAT payable (Out tax – Input tax)	Rs.5
Total tax collected by Government (At the time of purchase by dealer – Rs.10, At the time of resale by the dealer – Rs.5)	Rs.10
Total tax (Rs.10+5)	Rs.15

Details	With Sales Tax	With VAT
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	A	B	A	B
Purchases price	-	110 (with 10% input tax)	-	100
Value added	100	40	100	40
Sub total	100	150 (100+10+40)	100	140
Add Tax @ 10%	10	15	10	14
Total Sales price	110	165	110	154
Assume A & B are manufacturers. Tax revenue with Sales Tax Rs.25, with VAT Rs.14				

Explanation:

1. 'B' will purchase goods from 'A' @ Rs.110, which is inclusive of duty of Rs.10.
2. Since, 'B' going to get credit of duty of Rs.10, he will not consider this amount for his costing.
3. He will charge conversion expense of Rs.40 and sell his goods at Rs.140.
4. He will charge, 10% tax and raise invoice of Rs.154 to 'C' (140 + tax @ 10%)
5. In the invoice prepared by 'B', duty shown will be Rs.14. But, 'B' will get credit of Rs.10 paid on the Raw material purchased by him from 'A'.
6. Thus, effective duty paid by 'B' will be only Rs.4.
7. 'C' will get the goods at Rs.154 and Not at Rs.165, which he would have got in absence of VAT.
8. Thus, in effect, 'B' has to pay duty only on Value Added by him.

Practical implications of VAT

1. Goods purchased from unrecognized dealer, VAT cannot be imposed
2. VAT is tremendous paper work and record keeping
3. VAT system can work only if record keeping is proper and reliable
4. Bogus (Fake) Invoices on which tax credit is availed
5. Acquisition fraud (missing trade fraud) is possible - 'A' dealer imports goods and makes sale within the country. The dealer collects the tax from innocent buyer. 'A' does not pay tax (collected from buyer) to the Govt.
6. Carousel (round about) fraud - 'A' imports goods without tax. He sells goods to 'B' and charge VAT. 'B' avails credit of tax shown by 'A' in his Invoice.

Unit – IV
Corporate Tax Planning

Tax Planning

Tax planning can be defined as an arrangement of one’s financial and economic affairs by taking complete legitimate benefit of all deductions, exemptions, allowances and rebates so that tax liability reduces to minimum.

Direct Taxes

Direct taxes are those which a person pays directly from his income, wealth, or estate. It is paid after the income or benefit reaches the hands of the person, which are Income tax, wealth tax, corporate tax and gift tax.

Indirect Taxes

Which are not directly charged from the persons, which are collected in the form of excise duty, customs duty and sales tax.

Taxable Turnover

It means the turnover on which a dealer shall be liable to pay tax as determined after making such deductions from his total turnover and in such manner as may be prescribed.

Tax Avoidance

Tax avoidance is reducing or negating tax liability in legally permissible ways and has legal sanction. Tax avoidance is sound law and certainly not bad morality for anybody to so arrange his affairs in such a way that the brunt of taxation is the minimum. This can be done within the legal framework even by taking help of loopholes in the law.

Tax Evasion

All methods by which tax liability is illegally avoided are termed as tax evasion. Tax evasion may involve an untrue statement knowingly, submitting misleading documents, suppression of facts, not maintaining proper accounts of income earned (if required under law), omission of material facts on assessment.

Tax Planning Vs. Tax Management

Tax Planning	Tax Management
The objective of tax planning is to reduce the tax liability to the minimum.	The objective of tax management is to comply with the provisions of law.
Tax planning is futuristic in its approach.	Tax management relates to past (i.e., assessment proceedings, rectification, revision, appeals etc.), present (filing of return of income on time on the basis of updated records) and future (corrective action).

Tax planning is very wide in its coverage and includes tax management.	Tax management has a limited scope, i.e., it deals with specific activities such as filing of returns of income on time, drafting appeals, deduction of tax at source on time, updating records from time to time, etc.
The benefits arising from tax planning are substantial particularly in the long run.	As a result of effective tax management, penalty, penal interest, prosecution, etc., can be avoided.

Tax Avoidance Vs. Tax Evasion

Tax Avoidance	Tax Evasion
Any planning of tax which aims at reducing tax liability in legally recognised permissible ways, can be termed as an instance of tax avoidance.	All methods by which tax liability is illegally avoided is termed as tax evasion.
Tax avoidance takes into account the loopholes of law.	Tax evasion is an attempt to evade tax liability with the help of unfair means/methods.
Tax avoidance is tax hedging within the framework of law	Tax evasion is tax omission.
Tax avoidance has legal sanction	Tax evasion is unlawful and an assessee guilty of tax evasion may be punished under the relevant laws.
Tax avoidance is intentional tax planning before the actual tax liability arises	Tax evasion is intentional attempt to avoid payment of tax after the liability to tax has arisen

Causes of Tax evasion

1. Multiplicity of tax laws
2. Complicated tax laws
3. Higher rate of taxation
4. Inadequate information as to sources of tax revenue
5. Investment in real property
6. Ineffective tax enforcement
7. Deterioration of moral standard

Remedies for evasion

1. Through overhauling of tax laws
2. Reduction in tax rates
3. Replacement of sales tax & excise duties
4. Tax on agricultural income
5. Maintenance of proper accounts
6. Introduction of expenditure tax

7. Tightening of tax enforcement

Types of tax planning

There are four types of tax planning open to a business.

ILLEGAL	LEGAL		
Tax evasion	No tax planning	Basic tax planning	Advance tax planning
		Tax bills reduced by 5%-20%	Tax bills reduced by 50% – 100%

(1) Tax evasion

All methods by which tax liability is illegally avoided are termed as tax evasion. Tax evasion may involve an untrue statement knowingly, submitting misleading documents, suppression of facts, not maintaining proper accounts of income earned (if required under law), omission of material facts on assessment.

(2) No tax planning

This is what many businesses do by default. They simply complete their tax returns and send them off to the taxman, having taken no prior action to arrange their affairs in such a way to legally pay less tax.

(3) Basic tax planning

Most businesses do this since it is what most of the accountants advising them are good at. Basic tax planning such as incorporating the business, taking dividends rather than salaries and timing when they spend money can often reduce tax bills by 5% to 20%.

Various Basic methods of Tax Planning as follows :

a) **Short Term Tax Planning:** Short range Tax Planning means the planning thought of and executed at the end of the income year to reduce taxable income in a legal way.

b) **Long Term Tax Planning:** Long range tax planning means a plan at the beginning or the income year to be followed around the year. This type of planning does not help immediately as in the case of short range planning but is likely to help in the long run ;

c) **Permissive Tax Planning :** Permissive Tax Planning means making plans which are permissible under different provisions of the law, such as Planning of taking advantage of different incentives and deductions, planning for availing different tax concessions etc.

d) **Purposive Tax Planning:** It means making plans with specific purpose to ensure the availability of maximum benefits to the assessee through correct selection of investment, making suitable programme for replacement of assets, varying the residential status and diversifying business activities and income etc.

(4) Advanced tax planning

Historically this has really only been available to the richest entrepreneurs. Indeed it has helped them become even richer as it can reduce tax bills by 50% to 100%. In recent years this has changed, and now all good accountants (including One Accounting) can access a range of advanced tax planning solutions on behalf of their clients.

Central Sales Tax Act 1956 (CST Act 1956)

Central Sales Tax (CST): It a tax on Inter-state sale of goods, where the buyer and seller are in different state. CST will be chargeable under the CST Act, 1956 passed by Central Govt. in parliament.

Scope of CST

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Sale

Sale means transfer of property in goods by one person to another in the course of business for cash, deferred payment or other valuable consideration and includes:

- Transfer of property in goods
- Work contract
- Hire purchase
- Right to use
- Supply of goods by unincorporated association
- Supply of food as part of any service

Dealer: Any person carrying on the business of buying, selling or distributing goods directly or indirectly for cash, deferred payment, commission or any remuneration.

- Business: Any trade, commerce or manufacture with or without a profit motive
- Sale: Transfer of property from one person to another for a valuable consideration.
- Goods: All materials, articles, commodities except newspapers, shares, money, claims
- Rate: As prescribed in the Act.

Essential elements of sale:

- Goods should be transferred
- General property in good should be transferred
- Price must be paid
- There must be a seller and a buyer
- There must be a valid consent of both buyer and seller

Declared Goods [Section 2(C)]

It includes those goods which are considered to be of special importance in interstate trade or commerce under section 14. Some of these goods is –

• Cereals	• Cotton	• Jute	• Pulses
• Coal	• Crude Oil	• Oilseeds	• Sugar

Goods [section 2(d)]

This includes all material articles or commodities and all kind of movable property excluding newspapers, actionable claims, stocks, shares, and securities.

If newspapers are sold as scrap then, it will be charged to central sales tax if it is an inter- state sale.

Important Features of this Act

1. It extends to the whole of India.
2. Every dealer who makes an inter-state sale must be a registered dealer and a certificate of registration has to be displayed at all places of his business.
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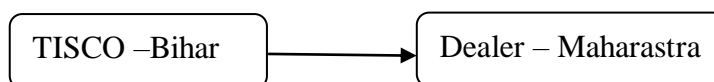
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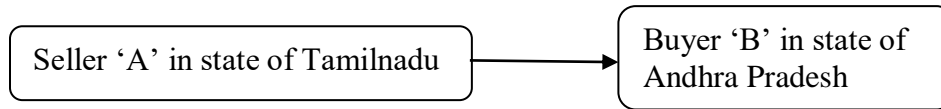
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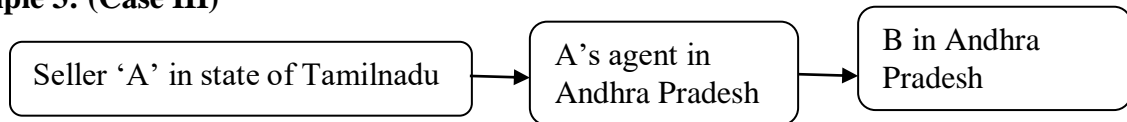
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3. ***Documents to be enclosed with Form D***
- 2 recent passport size photographs
 - Identity to prove his existence like passport/family card/bank pass book/driving license/VAO certificate
 - Copy of MOA and AOA in case of company
 - Copy of Partnership deed in case of partnership
 - Form XI of TNGST act signed by applicant and manager
 - Form A showing the estimated turnover for the year
4. ***Security money***
- The Registering authority may demand security equal to 50% of the tax due as estimated
 - In all cases Rs.2500/- has to be collected by way of security at the time of new registration
5. ***Issue of registration certificate***
- The commissioner issues certificate within 7days
 - If no notice been made with ref to the application within 20 days the dealer is deemed to be registered
 - Registration certificate should be renewed every yr. by paying 500 before 31st march without penalty.
 - Collection of tax by registered dealer
 - The registered dealer may collect the tax by issuing a bill in respect of every sale, in duplicate
 - One copy of the bill should be retained by the dealer to be checked by officials

Amendment (Modification) to certificate of registration

- Where the dealer has altered the name, place and nature of business
- Where the dealer has changed the class or classes of goods in which he carries on his business
- Where there is change in ownership in business and Cancellation of registration
- Under section 21(4) when he proves that his turnover in each of the 2 consecutive years immediately preceding the application was less than Rs.75000
- Cancellation or amendment by the prescribing authority

- Cancellation by the authority due to failure on the part of dealer to pay tax or penalty, declaration of false information, failure to provide security etc.,

Duties of a registered dealer

- Shall keep at the place of business, the certificate of registration, books of accounts.
- Shall notify the registering authority about the change in place of business
- Shall send bill of sale or delivery note or such documents along with the goods
- Shall furnish the returns before the due dates prescribed

VALUE ADDED TAX (VAT)

VAT is a tax on turnover and is added at every stage of manufacture or process, based on the value added at each stage.

VAT may be defined as “a tax to be paid by the manufacturers or traders of goods and services on the basis of value added by them”.

It is not a tax on the total value of the commodity being sold but on the value added to it by the manufacturer or trader. They are not liable to pay tax on the entire value of the commodity. But they have to pay the tax only on the Net value added by them in the process of production or distribution.

In this tax, the seller will collect the tax only on the value added by him towards his produced goods by excluding the tax on purchase paid by him. The VAT is payable by seller who is termed as a ‘dealer’.

The VAT works on the principle that when raw material passes through various manufacturing stages and manufactured product passes through various distribution stages, tax should be levied on the ‘Value Added’ at stage and not on the gross sales price.

Basically, VAT is multi-point tax, with provision for granting set off (Credit) of the tax paid at the earlier stage. Thus, tax burden is passed on when goods are sold. This process continues till goods are finally consumed. Hence, VAT is termed as ‘Consumption type’ tax with ‘destination principle’. VAT works on the principle of ‘tax credit system’.

Scope of VAT: the following transactions are subject to VAT

- The supply of goods and provision of services with a place of supply in India;
- The import of goods into India;
- Intra-Community acquisition of goods in India by a taxable person;
- The supply of goods or services specified in the India VAT Act, if the taxable person has opted for taxation of those.

Cascading effect of tax

In modern production technology, raw material passes through various stages and processes continues till a final product emerges. This product then goes to distributor/wholesaler, who sells it to retailer and then it, reaches the ultimate consumer. If tax is based on selling price of a product, the tax burden goes on increasing as raw material and final product passes from one stage to other.

The Output of the 1st manufacturer becomes input for 2nd manufacturer who carries out further processing and supply it to 3rd manufacturer. This process continuous till the final product emerges. If a tax base is on the selling price of the product, the tax burden goes on increasing as raw material and final product passed one stage to other.

Each subsequent purchaser has to pay tax again and again on the material that has already suffered tax. This is called cascading effect. This VAT scheme permits manufacturers to obtain complete reimbursement of excise duty/ sale tax paid on the component or raw materials used as input in the manufacturing of final products.

Example: Manufacture 'A' supplies his output to 'B' at Rs.100. Thus, 'B' gets the material at Rs.110, inclusive of tax @ 10%. He carries out further processing and sells his output to 'C' at Rs.150. While calculating his cost, 'B' has considered his purchase cost of materials as Rs.110 and added Rs.40 as his conversion charges. While selling product to 'C', 'B' will charge tax again @10%. Thus 'C' will get the item at Rs.165 (150+10% tax). In fact, 'Value added' by 'B' is only Rs.40 (150-110). As stages of production and/or sales continue, each subsequent purchaser has to pay tax again and again on the material which has already suffered tax. Tax is also paid on tax. This is called Cascading effect.

At VAT, VAT = Tax base (Value added by them) x Rate of Tax
 = Rs.110 – 10 = 100 (Less sales tax paid on RM)
 = 100 + 40 (Processing charge) = Rs.140, rate of tax is 10%
Therefore, 140 + (140x10/100)
 = 140 + 14 = Rs.154.

Method of Calculation of VAT

Purchase Price	Rs.100
Tax paid during purchase	Rs.10 (Input tax)
Selling price	Rs.150
Tax collected during resale	Rs.15
Input tax credit (Tax paid during purchase)	Rs.10
VAT payable (Out tax – Input tax)	Rs.5
Total tax collected by Government (At the time of purchase by dealer – Rs.10, At the time of resale by the dealer – Rs.5)	Rs.10
Total tax (Rs.10+5)	Rs.15

Details	With Sales Tax	With VAT
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	A	B	A	B
Purchases price	-	110 (with 10% input tax)	-	100
Value added	100	40	100	40
Sub total	100	150 (100+10+40)	100	140
Add Tax @ 10%	10	15	10	14
Total Sales price	110	165	110	154
Assume A & B are manufacturers. Tax revenue with Sales Tax Rs.25, with VAT Rs.14				

Explanation:

1. 'B' will purchase goods from 'A' @ Rs.110, which is inclusive of duty of Rs.10.
2. Since, 'B' going to get credit of duty of Rs.10, he will not consider this amount for his costing.
3. He will charge conversion expense of Rs.40 and sell his goods at Rs.140.
4. He will charge, 10% tax and raise invoice of Rs.154 to 'C' (140 + tax @ 10%)
5. In the invoice prepared by 'B', duty shown will be Rs.14. But, 'B' will get credit of Rs.10 paid on the Raw material purchased by him from 'A'.
6. Thus, effective duty paid by 'B' will be only Rs.4.
7. 'C' will get the goods at Rs.154 and Not at Rs.165, which he would have got in absence of VAT.
8. Thus, in effect, 'B' has to pay duty only on Value Added by him.

Practical implications of VAT

1. Goods purchased from unrecognized dealer, VAT cannot be imposed
2. VAT is tremendous paper work and record keeping
3. VAT system can work only if record keeping is proper and reliable
4. Bogus (Fake) Invoices on which tax credit is availed
5. Acquisition fraud (missing trade fraud) is possible - 'A' dealer imports goods and makes sale within the country. The dealer collects the tax from innocent buyer. 'A' does not pay tax (collected from buyer) to the Govt.
6. Carousel (round about) fraud - 'A' imports goods without tax. He sells goods to 'B' and charge VAT. 'B' avails credit of tax shown by 'A' in his Invoice.