Mock Test Paper - Series I: July, 2024

Date of Paper: 31st July, 2024

Time of Paper: 10.30. A.M. to 1.30 P.M.

FOUNDATION COURSE

PAPER 2: BUSINESS LAWS

ANSWERS

1. (a) (i) Section 73 of Indian Contract Act, 1872 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, compensation for any loss or damage caused to him thereby, which naturally arose in the usual course of things from such breach, or which the parties knew, when they made the contract, to be likely to result from the breach of it. But such compensation is not to be given for any remote and indirect loss or damage sustained by reason of the breach.

In the instant case, Mr. Chetan filed the suit against Himalayan Travels Pvt. Ltd. for damages for the personal inconvenience, hotel charges and medical treatment for his wife.

On the basis of above provisions and facts of the case, it can be said that Mr. Chetan can claim damages for the personal inconvenience and hotel charges but not for medical treatment for his wife because it is a remote or indirect loss.

(ii) According to section 17 of the Indian Contract Act, 1872, mere silence as to facts likely to affect the willingness of a person to enter into a contract is not fraud, unless the circumstances of the case are such that, regard being had to them, it is the duty of the person keeping silence to speak, or unless his silence is, in itself, equivalent to speech. Hence, in the instant case,

(A) This contract is valid since as per section 17, mere silence as to the facts likely to affect the willingness of a person to enter into a contract is not fraud. Here, it is not the duty of the seller to disclose defects.

(B) This contract is not valid since as per section 17, it becomes Sahil's duty to tell Rohan about the unsoundness of the horse because a fiduciary relationship exists between Sahil and his son Rohan. Here, Sahil's silence is equivalent to speech and hence amounts to fraud.

(C) This contract is not valid since as per section 17, Sahil's silence is equivalent to speech and hence amounts to fraud.

(b) **(i)** As per Section 2(6) of the Companies Act, 2013, an Associate Company in relation to another company, means a company in which that other company has a significant influence, but which is not a subsidiary company of the company having such influence and includes a joint venture company.

The term "significant influence" means control of at least 20% of total voting power, or control of or participation in business decisions under an agreement.

In the given case, ABC Ltd. has allotted equity shares with voting rights to XYZ Limited of ₹ 15 crore, which is less than requisite control of 20% of total share capital (i.e. ₹ 100 crore) to have a significant influence of XYZ Ltd. Since the said requirement is not complied therefore ABC Ltd. and XYZ Ltd. are not associate companies as per the Companies Act, 2013.

(ii) **"Inactive company"** means a company which has not been carrying on any business or operation or has not made any **significant accounting transaction** during the last two financial years or has not filed financial statements and annual returns during the last two financial years. [Explanation (i) to Section 455 of the Companies Act, 2013]

"Significant accounting transaction" means any transaction other than—

(a) payment of fees by a company to the Registrar;

(b) payments made by it to fulfil the requirements of this Act or any other law;

(c) allotment of shares to fulfil the requirements of this Act; and

(d) payments for maintenance of its office and records.

[Explanation (ii) to Section 455 of the Companies Act, 2013]

In the instant case, MTK Private Limited was registered on 5th January 2022 and did not start its business till 31st July 2024. Since the Company has not started its business and a period of more than two years has already elapsed, it will be treated as an inactive company.

(c) **(i)** Partnership Vs. Co-Ownership or joint ownership i.e. the relation which subsists between persons who own property jointly or in common.

Basis of difference	Partnership	Co-ownership
1. Formation	Partnership always arises out of a contract,	Co-ownership may arise either from agreement or

	express or implied.	by the operation of law, such as by inheritance.
2. Implied agency	A partner is the agent of the other partners.	A co-owner is not the agent of other co-owners.
3. Nature of interest	There is community of interest which means that profits and losses must have to be shared.	Co-ownership does not necessarily involve sharing of profits and losses.
4. Transfer of interest	A share in the partnership is transferred only by the consent of other partners.	A co-owner may transfer his interest or rights in the property without the consent of other co-owners.

(ii) Personal Profit earned by Partners (Section 16 of the Indian Partnership Act, 1932)

According to section 16, subject to contract between the partners:

(a) If a partner derives any profit for himself from any transaction of the firm, or from the use of the property or business connection of the firm or the firm name, he shall account for that profit and pay it to the firm;

(b) If a partner carries on any business of the same nature and competing with that of the firm, he shall account for and pay to the firm all profits made by him in that business.

2. (a) According to Section 15 of the Sale of Goods Act, 1930, whenever the goods are sold as per sample as well as by description, the implied condition is that the goods must correspond to both sample as well as description. In case the goods do not correspond to a sample or description, the buyer has the right to repudiate the contract.

Further under Sale of Goods Act, 1930, when the buyer makes known to the seller, the particular purpose for which the goods are required and he relies on his judgment and skill of the seller, it is the duty of the seller to supply such goods which are fit for that purpose.

In the given case, Mr. Vivek informed Mr. Manoj that he wanted the washing machine for washing woollen clothes. However, the machine which was delivered by Mr. Manoj was unfit for the purpose for which Mr. Vivek wanted the machine.

Based on the above provision and facts of case, there is breach of implied condition as to sample as well as description, therefore Mr. Vivek

can either repudiate the contract or claim the refund of the price paid by him or he may require Mr. Manoj to replace the washing machine with desired one.

(b) **(i)** According to the decision taken in the case of *Salomon Vs. Salomon & Co. Ltd.,* a company has a separate legal entity. A company is different from its members. Further, according to the decision taken in the case of *Macaura Vs. Northern Assurance Co. Ltd.,* a member or creditor does not have any insurable interest in the property of the company. Members or creditors of the company cannot claim ownership in the property of company.

On the basis of the above provisions and facts, it can be said that Mr. Sooraj and CPL Private Limited are separate entities. Mr. Sooraj cannot have any insurable interest in the property of CPL Private Limited neither as member nor as creditor. Hence, the insurance company is not liable to pay to Mr. Sooraj for the claim for the loss of stock by fire.

(ii) Section 8 of the Companies Act, 2013 deals with the formation of companies which are formed to promote the charitable objects of commerce, art, science, education, sports etc. Such company intends to apply its profit in promoting its objects. Section 8 companies are registered by the Registrar only when a license is issued by the Central Government to them. Since, Alfa School was a Section 8 company and it had started violating the objects of its objective clause, hence in such a situation the following powers can be exercised by the Central Government:

(i) The Central Government may by order revoke the licence of the company where the company contravenes any of the requirements or the conditions of this sections subject to which a licence is issued or where the affairs of the company are conducted fraudulently, or violative of the objects of the company or prejudicial to public interest, and on revocation the Registrar shall put 'Limited' or 'Private Limited' against the company's name in the register. But before such revocation, the Central Government must give it a written notice of its intention to revoke the licence and opportunity to be heard in the matter.

(ii) Where a licence is revoked, the Central Government may, by order, if it is satisfied that it is essential in the public interest, direct that the company be wound up under this Act or amalgamated with another company registered under this section.

However, no such order shall be made unless the company is given a reasonable opportunity of being heard.

(iii) Where a licence is revoked and where the Central Government is satisfied that it is essential in the public interest

that the company registered under this section should be amalgamated with another company registered under this section and having similar objects, then, notwithstanding anything to the contrary contained in this Act, the Central Government may, by order, provide for such amalgamation to form a single company with such constitution, properties, powers, rights, interest, authorities and privileges and with such liabilities, duties and obligations as may be specified in the order.

(c) Designated Partner [Section 2(1)(j) of the LLP Act, 2008]: "Designated partner" means any partner designated as such pursuant to section 7.

According to section 7 of the LLP Act, 2008:

(i) Every LLP shall have at least two designated partners who are individuals and at least one of them shall be a resident in India.

(ii) If in LLP, all the partners are bodies corporate or in which one or more partners are individuals and bodies corporate, at least two individuals who are partners of such LLP or nominees of such bodies corporate shall act as designated partners.

(iii) *Resident in India*: For the purposes of this section, the term "resident in India" means a person who has stayed in India for a period of not less than 120 days during the financial year.

3. (a) Expulsion of a Partner (Section 33 of the Indian Partnership Act, 1932):

A partner may not be expelled from a firm by a majority of partners except in exercise, in good faith, of powers conferred by contract between the partners.

The test of good faith as required under Section 33(1) includes three things:

- The expulsion must be in the interest of the partnership.
- The partner to be expelled is served with a notice.
- He is given an opportunity of being heard.

If a partner is otherwise expelled, the expulsion is null and void.

(a) Action by the partners of M/s ABC & Associates, a partnership firm to expel Mr. P from the partnership was justified as he was expelled by approval of the other partners exercised in good faith to protect the interest of the partnership against the unauthorized activities charged against Mr. P. A proper notice and opportunity of being heard has to be given to Mr. P.

(b) The following are the factors to be kept in mind prior expelling a partner from the firm by other partners:

- the power of expulsion must have existed in a contract between the partners;

- the power has been exercised by a majority of the partners; and
- it has been exercised in good faith.

(b) **(i)** According to section 2(68) of the Companies Act, 2013, "Private company" means a company having a minimum paid-up share capital as may be prescribed, and which by its articles, except in case of One Person Company, limits the number of its members to two hundred.

However, where two or more persons hold one or more shares in a company jointly, they shall, for the purposes of this clause, be treated as a single member.

It is further provided that -

(A) persons who are in the employment of the company; and

(B) persons who, having been formerly in the employment of the company, were members of the company while in that employment and have continued to be members after the employment ceased,

shall not be included in the number of members.

In the instant case, Powertech Limited may be converted into a private company only if the total members of the company are limited to 200.

Total Number of members

(i)	Directors and their relatives	190
(ii)	5 Couples (5*1)	5
(iii)	Others	5
	Total	**200**

Therefore, there is no need for reduction in the number of members since existing number of members are 200 which does not exceed maximum limit of 200.

(ii) According to Section 2(87) of the Companies Act, 2013 “subsidiary company” in relation to any other company (that is to say the holding company), means a company in which the holding company—

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

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

In the present case, the total share capital of Popular Products Ltd. is ₹ 20 crores comprised of 20 Lakh equity shares.

Delight Products Ltd., Happy Products Ltd. and Cheerful Products Ltd together hold 8,50,000 shares (2,50,000+3,50,000+2,50,000) in Popular Products Ltd. Jovial Ltd. is the holding company of all above three companies. So, Jovial Ltd. along with its subsidiaries hold 8,50,000 shares in Popular Products Ltd., which amounts to less than one-half of its total voting power. Hence, Jovial Ltd. by virtue of shareholding is not a holding company of Popular Products Ltd.

Secondly, it is given that Jovial Ltd. controls the composition of directors of Popular Products Ltd., hence, Jovial Ltd. is a holding company of Popular Products Ltd. and not a subsidiary company.

(c) The Indian Contract Act, 1872 does not define the word 'Agency'. However, section 182 of the Indian Contract Act, 1872 defines Agent and Principal as:

Agent means a person employed to do any act for another or to represent another in dealing with the third persons and

The principal means a person for whom such act is done or who is so represented.

Duties and obligations of an Agent

(i) **Duty to follow instructions or customs:** According to Section 211, an agent is bound to conduct the business of his principal according to the direction given by the principal, or, in the absence of any such directions, according to the customs which prevails in doing business of the same kind at the place where the agent conducts such business. When the agent acts otherwise and any loss is sustained by the Principal, he must indemnify him, and, if any profit accrues, he must account for it.

(ii) **Duty of reasonable care and skill:** According to section 212, an agent is bound to conduct the business of the principal with as much skill as is generally possessed by persons engaged in similar business, unless the principal has notice of his want of skill.

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

(iii) **Duty to render proper accounts [Section 213]:** An agent is bound to render proper accounts to his principal on demand. Rendering accounts does not mean showing the accounts but the accounts supported by vouchers. *(Anandprasad vs. Dwarkanath)*

(iv) **Agent's duty to communicate with principal [Section 214]:** It is the duty of an agent, in cases of difficulty, to use all reasonable

diligence in communicating with his principal, and in seeking to obtain his instructions.

(v) **Duty not to deal on his own account**: Agent should not deal on his own account without first obtaining the consent of the principal, otherwise the principal may—

(a) repudiate the transaction, (Section 215)

(b) claim from the agent any benefit which may have resulted to him from the transaction. (Section 216)

(vi) **Duty not to make secret profits**: It is the duty of an agent not to make any secret profit in the business of agency. His relationship with the principal is of fiduciary nature and this requires absolute good faith in the conduct of agency**.**

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

(vii) **Duty not to delegate:** According to section 190, an agent cannot lawfully employ to perform acts which he has expressly or impliedly undertaken to perform personally, unless by the ordinary custom of trade a sub-agent may, or, from the nature of agency, a sub- agent, must be employed.

(viii) **Agent's duty to pay sums received for principal [Section 218]:** Subject to such deductions, the agent is bound to pay to his principal all sums received on his account.

(ix) Duty not to use any confidential information received in the course of agency against the principal.

4. **(a)** **(i)** Section 25 of Indian Contract Act, 1872 provides that an agreement made without consideration is valid if it is expressed in writing and registered under the law for the time being in force for the registration of documents and is made on account of natural love and affection between parties standing in a near relation to each other. In other words, a written and registered agreement based on natural love and affection between the parties standing in near relation to each other is enforceable even without consideration.

In the instant case, the transfer of house made by Mr. Om Kashyap on account of natural love and affection between the parties standing in near relation to each other is written but not registered. Hence, this transfer is not enforceable.

(ii) Equality of burden is the basis of Co-suretyship. This is contained in section 146 of the Indian Contract Act, 1872, which states that "unless otherwise agreed, each surety is liable to contribute equally for discharge of whole debt or part of the debt remains unpaid by debtor.

Accordingly, on the default of Pawan in payment, Tarun cannot escape from his liability. Both the sureties Suraj and Tarun are liable to pay equally, in absence of any contract between them.

(b) Difference between promissory note and bill of exchange:

S. No.	Basis	Promissory Note	Bill of Exchange
1.	**Definition**	"A Promissory Note" is an instrument in writing (not being a banknote or a currency-note) containing an unconditional undertaking signed by the maker, to pay a certain sum of money only to, or to the order of, a certain person, or to the bearer of the instrument.	"A bill of exchange" is an instrument in writing containing an unconditional order, signed by the maker, directing a certain person to pay a certain sum of money only to, or to the order of a certain person or to the bearer of the instrument.
2.	**Nature of Instrument**	In a promissory note, there is a promise to pay money.	In a bill of exchange, there is an order for making payment.
3.	**Parties**	In a promissory note, there are only 2 parties namely: i. the maker and ii. the payee	In a bill of exchange, there are 3 parties which are as under: i. the drawer ii. the drawee iii. the payee
4.	**Acceptance**	A promissory note does not require any acceptance, as it is signed by the person who is liable to pay.	A bill of exchange needs acceptance from the drawee.
5.	**Payable to bearer**	A promissory note cannot be made payable to bearer.	On the other hand, a bill of exchange can be drawn payable to bearer. However, it cannot be payable to bearer on demand.

(c) Meaning of Law: Law is a set of obligations and duties imposed by the government for securing welfare and providing justice to society. India's legal framework reflects the social, political, economic, and cultural aspects of our vast and diversified country.

The Process of Making a Law

- When a law is proposed in parliament it is called a Bill.
- After discussion and debate, the law is passed in Lok Sabha.
- Thereafter, it has to be passed in Rajya Sabha.
- It then has to obtain the assent of the President of India.
- Finally, the law will be notified by the Government in the publication called the Official Gazette of India.
- The law will become applicable from the date mentioned in the notification as the effective date.
- Once it is notified and effective, it is called an Act of Parliament.

5. **(a)** As per Section 4(3) of the Sale of Goods Act, 1930, where under a contract of sale, the property in the goods is transferred from the seller to the buyer, the contract is called a sale, but where the transfer of the property in the goods is to take place at a future time or subject to some condition thereafter to be fulfilled, the contract is called an agreement to sell and as per Section 4(4), an agreement to sell becomes a sale when the time elapses or the conditions are fulfilled subject to which the property in the goods is to be transferred.

(i) On the basis of above provisions and facts given in the question, it can be said that there is an agreement to sell between Simran and Jeweller and not a sale. Even though the payment was made by Simran, the property in goods can be transferred only after the fulfilment of conditions fixed between the buyer and the seller. As due to Ruby Stones, the original design is disturbed, bangles are not in original position. Hence, Simran has right to avoid the agreement to sell and can recover the price paid.

(ii) If Jeweller offers to bring the bangles in original position by repairing, he cannot charge extra cost from Simran. Even though he has to bear some expenses for repair; he cannot charge it from Simran.

(b) **(i)** **Mode of Settlement of partnership accounts:** As per Section 48 of the Indian Partnership Act, 1932, in settling the accounts of a firm after dissolution, the following rules shall, subject to agreement by the partners, be observed:-

(i) Losses, including deficiencies of capital, shall be paid first out of profits, next out of capital, and, lastly, if necessary, by the partners individually in the proportions in which they were entitled to share profits;

(ii) The assets of the firm, including any sums contributed by the partners to make up deficiencies of capital, must be applied in the following manner and order:

(a) in paying the debts of the firm to third parties;

(b) in paying to each partner rateably what is due to him from capital;

(c) in paying to each partner rateably what is due to him on account of capital; and

(d) the residue, if any, shall be divided among the partners in the proportions in which they were entitled to share profits.

(ii) (A) **When he becomes partner:** If the minor becomes a partner on his own willingness or by his failure to give the public notice within specified time, his rights and liabilities as given in Section 30(7) of the Indian Partnership Act, 1932, are as follows:

(a) He becomes personally liable to third parties for all acts of the firm done since he was admitted to the benefits of partnership.

(b) His share in the property and the profits of the firm remains the same to which he was entitled as a minor.

(B) **When he elects not to become a partner:**

(a) His rights and liabilities continue to be those of a minor up to the date of giving public notice.

(b) His share shall not be liable for any acts of the firm done after the date of the notice.

(c) He shall be entitled to sue the partners for his share of the property and profits. It may be noted that such minor shall give notice to the Registrar that he has or has not become a partner.

(c) A contract is discharged when the obligations created by it come to an end. A contract may be discharged in any one of the following ways:

(i) **Discharge by performance:** It takes place when the parties to the contract fulfil their obligations arising under the contract within the time and in the manner prescribed. Discharge by performance may be

(1) Actual performance; or

(2) Attempted performance.

Actual performance is said to have taken place, when each of the parties has done what he had agreed to do under the agreement. When the promisor offers to perform his obligation, but the promisee refuses to accept the performance, it amounts to attempted performance or tender.

(ii) **Discharge by mutual agreement:** Section 62 of the Indian Contract Act provides if the parties to a contract agree to substitute

a new contract for it, or to rescind or remit or alter it, the original contract need not be performed.

(iii) Discharge by impossibility of performance: The impossibility may exist from the very start. In that case, it would be impossibility ab initio. Alternatively, it may supervene. Supervening impossibility may take place owing to:

(a) an unforeseen change in law;

(b) the destruction of the subject-matter essential to that performance;

(c) the non-existence or non-occurrence of particular state of things, which was naturally contemplated for performing the contract, as a result of some personal incapacity like dangerous malady;

(d) the declaration of a war (Section 56).

(iv) Discharge by lapse of time: A contract should be performed within a specified period as prescribed by the Limitation Act, 1963. If it is not performed and if no action is taken by the promisee within the specified period of limitation, he is deprived of remedy at law.

(v) Discharge by operation of law: A contract may be discharged by operation of law which includes by death of the promisor, by insolvency etc.

(vi) Discharge by breach of contract: Breach of contract may be actual breach of contract or anticipatory breach of contract. If one party defaults in performing his part of the contract on the due date, he is said to have committed breach thereof. When on the other hand, a person repudiates a contract before the stipulated time for its performance has arrived, he is deemed to have committed anticipatory breach. If one of the parties to a contract breaks the promise the party injured thereby, has not only a right of action for damages but he is also discharged from performing his part of the contract.

(vii) Promisee may waive or remit performance of promise: Every promisee may dispense with or remit, wholly or in part, the performance of the promise made to him, or may extend the time for such performance or may accept instead of it any satisfaction which he thinks fit. In other words, a contract may be discharged by remission. (Section 63)

(viii) Effects of neglect of promisee to afford promisor reasonable facilities for performance: If any promisee neglects or refuses to afford the promisor reasonable facilities for the performance of his promise, the promisor is excused by such neglect or refusal as to any non-performance caused thereby. (Section 67)

(ix) Merger of rights: Sometimes, the inferior rights and the superior rights coincide and meet in one and the same person. In such

cases, the inferior rights merge into the superior rights. On merger, the inferior rights vanish and are not required to be enforced.

6. **(a)** (i) The question arising in this problem is whether the making of promissory note is complete when one half of the note was delivered to N. Under Section 46 of the N.I. Act, 1881, the making of a Promissory Note (P/N) is completed by delivery, actual or constructive. Delivery refers to the whole of the instrument and not merely a part of it. Delivery of half instrument cannot be treated as constructive delivery of the whole. So, the claim of N to have the other half of the P/N sent to him is not maintainable. M is justified in demanding the return of the first half sent by him. He can change his mind and refuse to send the other half of the P/N.

(ii) The promissory note is an unconditional promise in writing. In the above question, the amount is certain but the date and name of the payee is missing, thus making it a bearer instrument. As per Reserve Bank of India Act, 1934, a promissory note cannot be made payable to bearer - whether on demand or after certain days. Hence, the instrument is illegal as per Reserve Bank of India Act, 1934 and cannot be legally enforced.

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

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

Contracts of Insurance, indemnity and guarantee fall under this category.

Meaning of collateral Event: Collateral event is "an event which is neither a performance directly promised as part of the contract, nor the whole of the consideration for a promise".

Essentials of a contingent contract

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

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

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

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

(c) If the seller commits a breach of contract, the buyer gets the following rights against the seller:

1. **Damages for non-delivery [Section 57 of the Sale of Goods Act, 1930]:** Where the seller wrongfully neglects or refuses to deliver the goods to the buyer, the buyer may sue the seller for damages for non-delivery.

2. **Suit for specific performance (Section 58):** Where the seller commits breach of the contract of sale, the buyer can appeal to the court for specific performance. The court can order for specific performance only when the goods are ascertained or specific and where damages would not be an adequate remedy.

3. **Suit for breach of warranty (Section 59):** Where there is breach of warranty on the part of the seller, or where the buyer elects to or is forced to treat breach of condition as breach of warranty, the buyer is not by reason only of such breach of warranty entitled to reject the goods on the basis of such breach of warranty; but the buyer may –

   (i) set up against the seller the breach of warranty in diminution or extinction of the price; or

   (ii) sue the seller for damages for breach of warranty.

4. **Repudiation of contract before due date (Section 60):** Where either party to a contract of sale repudiates the contract before the date of delivery, the other may either treat the contract as:

   - subsisting and wait till the date of delivery, or
   - he may treat the contract as rescinded and sue for damages for the breach.

5. **Suit for interest:**

   (1) The buyer is entitled to recover interest or special damages, or to recover the money paid where the consideration for the payment of it has failed.

   (2) In the absence of a contract to the contrary, the court may award interest at such rate as it thinks fit on the amount of the price to the buyer in a suit by him for the refund of the price in a case of a breach of the contract on the part of the seller from the date on which the payment was made.